CHILD DEVELOPMENT PROGRAMS ADVISORY COMMITTEE—Continued

the calendar year. School administrators report substantial variability in the degree to which the child care needs of students attending year-round schools are being met while these children are on vacation ("off-track") during the school year. (In a typical year-round school, students may have four three-week vacations during the year.) Most principals report that a majority of students have working parents and are without any formal supervision while they are "off-track," and, in many communities, recreational and other programs traditionally offered during the summer months have not been expanded to serve children throughout the year.

At a time when the Legislature is encouraging school districts to adopt year-round education programs as a means of mitigating the need to construct new school facilities, we believe that it should have more information about the child care needs created by such programs and the options available to meet those needs. Accordingly, we recommend that the Legislature adopt the following supplemental report language:

"The Child Development Programs Advisory Committee shall study and make recommendations regarding the child care needs of children in year-round schools and the degree to which these needs are being met by services currently available. The committee shall consider services provided by the Office of Child Development, local community programs, and private providers, and shall identify regulations or procedures which create unnecessary barriers to the provision of child care services to children in year-round schools. The committee shall report its findings to the Joint Legislative Budget Committee and the legislative fiscal committees no later than November 1, 1984."

Health and Welfare Agency

DEPARTMENT OF HEALTH SERVICES

Item 4260 from the General Fund and various other funds — Budget p. HW 37

Requested 1984–85	$3,130,521,000
Estimated 1983–84	3,113,942,000
Actual 1982–83	3,214,338,000
Requested increase (excluding amount for salary increases) $16,579,000 (+0.5 percent)	
Total recommended reduction	59,734,000
Recommendation pending	2,120,496,000

1984–85 FUNDING BY ITEM AND SOURCE

Item	Description	Fund	Amount
4260-001-001	Department support	General	$91,996,000
4260-001-014	Department support	Hazardous Waste Control	10,146,000
4260-001-044	Department support	State Transportation	298,000
4260-001-203	Department support	Genetic Disease Testing	12,565,000
4260-001-335	Department support	Sanitarian Registration	81,000
4260-001-455	Department support	Hazardous Substances	9,645,000
4260-001-456	Department support	Hazardous Substances Compensation	355,000

4260-001-890—Department support	Federal	(251,193,000)
4260-001-898—Department support	County Health Services	806,000
4260-001-900—Department support	Local Health Capital Expenditure	217,000
4260-101-001—Medi-Cal local assistance	General	2,009,305,000
4260-101-001—Medi-Cal local assistance (provision 2)	Federal	(51,821,000)
4260-101-890—Medi-Cal local assistance		(2,016,932,000)
4260-105-001—Medi-Cal abortions	General	13,687,000
4260-106-001—Cost-of-living adjustment	General	28,531,000
4260-106-890—Cost-of-living adjustment	Federal	(19,247,000)
4260-111-001—Preventive health local assistance	General	949,869,000
4260-111-890—Preventive health local assistance	Federal	(23,374,000)
—County health projects		2,200,000
—Family repayments		820,000
Total		$3,130,521,000

SUMMARY OF MAJOR ISSUES AND RECOMMENDATIONS

DEPARTMENT OF HEALTH SERVICES—Continued

ceipt of the proposed implementing legislation and additional information regarding the proposal.

9. County Medical Services Program (CMSP) Hospital Contracts. Recommend adoption of legislation allowing the CMSP to reimburse hospitals that contract with Medi-Cal at Medi-Cal contract rates. 885

10. ***Local Health Capital Expenditures. Increase General Fund Reversions by $441,000.*** Recommend that at budget hearings, the department (a) explain why $10,829,000 in unused medically indigent services funds are not proposed for expenditure through the Local Health Capital Expenditure Account (LHCEA) and (b) develop a spending plan for LHCEA funds. Further recommend that (a) LHCEA funds be appropriated through the Budget Bill to assure greater legislative control of expenditures and (b) $441,000 in interest income in the LHCEA be reverted to the General Fund in accordance with current law. 889

11. ***California Children's Services (CCS) Cost-of-Living Adjustment (COLA). Reduce Item 4260-106-001 by $272,000.*** Recommend a reduction of $272,000 to correct errors in the calculation of CCS COLAs. 893

12. ***CCS Inpatient Utilization Review. Reduce Item 4260-111-001 by $389,000, Item 4260-101-001 by $111,000, and Item 4260-101-890 by $110,000.*** Recommend Budget Bill language requiring Medi-Cal field offices to review treatment authorization requests for extended lengths of stay for all CCS hospital inpatients. Further recommend a reduction of $389,000 in the CCS budget and $221,000 ($111,000 General Fund) in the Medi-Cal budget to reflect savings attributable to these reviews. 894

13. CCS Contracting for Hospital Inpatient Services. Recommend that by April 14, 1984, the California Medical Assistance Commission report to the Legislature on the feasibility and potential effects of implementing a hospital contracting program for CCS hospital inpatient services. 896

14. ***CCS Pharmaceutical Purchasing Policy. Reduce Item 4260-111-001 by $249,000.*** Recommend reduction to reflect savings in the purchasing of pharmaceuticals attributable to stricter adherence to state guidelines. 898

15. CCS Recoveries for Liable Third Parties. Recommend legislation to insure that CCS is notified of legal action related to liability for injuries treated by CCS. 898

16. ***Genetically Handicapped Persons' Program. Reduce Item 4260-106-001 by $26,000.*** Recommend a reduction of $26,000 to correct for overbudgeting. 901

17. Genetic Disease Program. Recommend that prior to budget hearings, the department submit (a) an updated budget change proposal for the Neural Tube Defects project that reflects revisions in the implementation schedule and staffing estimates and (b) a revised fund condition statement for the Genetic Disease Testing Fund. 902

18. Primary Care Clinics Program. Recommend that 903

DEPARTMENT OF HEALTH SERVICES—Continued

Medi-Cal Program 943

001) and $2,125,134,000 (Items 4260-101-890 and 4260-106-890), pending May revision of expenditure estimates.

40. Additional Federal Fund Revenue to Medi-Cal Program. Recommend Department of Finance include in May revision information regarding outstanding federal funding disputes and an estimate of probable 1984–85 revenue if these disputes are resolved in the state's favor. 958

41. ***Federal Matching Reduction. Reduce Item 4260-101-001 by $23,319,000 and increase Item 4260-101-890 by $23,319,000.*** Recommend that the budget provide for a reduction in the federal matching share based on the President's budget (3 percent) rather than a "worst-case" assumption (4.5 percent). 960

42. Prudent Purchasing Projects. Recommend that the department advise the Legislature during budget hearings regarding plans for implementation of prudent purchasing of drugs and other health care products. 977

43. ***Peer Group Rates. Reduce Item 4260-101-001 by $24,311,000 and Item 4260-101-890 by $23,032,000.*** Recommend budget reflect savings due to court settlement. 980

44. ***Claims Processing Improvements. Reduce Item 4260-101-001 by $1,425,000 and Item 4260-101-890 by $1,425,000.*** Recommend reduction to reflect savings anticipated due to two improvements in Medi-Cal claims processing. 982

45. Dental Contract Procurement Schedule. Recommend that prior to budget hearings, the department advise the Legislature on the schedule for and status of the dental contract reprocurement. 984

46. Prepaid Health Plan Rates. Recommend that prior to budget hearings, the department provide (a) 1983–84 prepaid health plan (PHP) rates, (b) comparable fee-for-service costs, (c) a description of the methods used to determine these rates, and (d) a schedule for developing 1984–85 rates. 986

47. Prepaid Health Plan Rate Establishment. Recommend that during budget hearings, the department advise the Legislature on the reasons for the delay in establishing PHP rates during the current year. 986

48. Notification of Rule Changes. Recommend adoption of Budget Bill language requiring that the Legislature be notified of Medi-Cal rule changes expected to cost $1,000,000 or more. 987

49. Augmentations to Medi-Cal Categories. Recommend adoption of Budget Bill language (a) forbidding expenditures in excess of 3 percent of the amount appropriated for any of the three Medi-Cal local assistance categories and (b) requiring legislative notification of augmentations to these categories. 987

50. Corrective Action Plan. Recommend that the department report to the Legislature during budget hearings on the status of corrective action plans to reduce quality control errors in 16 counties and two Los Angeles County Hospitals. 992

51. County-Specific Error Rates. Withhold recommenda- 993

DEPARTMENT OF HEALTH SERVICES—Continued

tion on $1,312,000 in Item 4260-001-001 and $1,312,000 in Item 4260-001-890, pending receipt of the department's proposal for (a) determining county-specific payment error rates and (b) utilizing these rates to pass along federal error rate sanctions and assess state sanctions.

52. Salary and Benefit Increase. Recommend (a) transfer of $5,165,000 from Item 4260-101-001 to Item 4260-106-001 and $4,968,000 from Item 4260-101-890 to Item 4260-106-890 to fund a 1984–85 cost-of-living adjustment for county administration, (b) adoption of Budget Bill language contained in the 1983 Budget Act limiting state funding for county salary and benefit increases to the amount specified in the 1984 Budget Act, and (c) that the Legislature authorize state support for salary and benefit increases provided to county employees in 1984–85 up to the percentage increase approved for state employees in the 1984 Budget Act. 995

53. ***Past Salary and Benefit Increase Calculation. Reduce Item 4260-101-001 by $1,614,000 and Item 4260-101-890 by $1,613,000.*** Recommend reduction to correct technical budgeting error in calculating the cost of providing state support for county employee salary and benefit increases approved in prior years. 1000

54. ***Claims Processing Cost Reimbursements. Reduce Item 4260-101-001 by $201,000 and Item 4260-101-890 by $595,000.*** Recommend that cost-based reimbursements to claims processing contractor reflect reductions anticipated from implementation of a new contract. 1006

55. ***State Controller Audits. Increase Item 4260-101-001 by $185,000 and Item 4260-101-890 by $186,000.*** Recommend funding State Controller audits of Medi-Cal checkwrites as part of Medi-Cal administration so that the federal government shares in these costs. (Savings to the General Fund: $186,000.) 1007

56. ***Treatment Authorization Review Staff. Reduce Item 4260-001-001 by $221,000 and Item 4260-001-890 by $524,000.*** Recommend a reduction of 21 positions due to reduced workload as a result of the 1982 Medi-Cal reforms. 1009

57. Field Services Vacancies. Recommend department advise the fiscal committees during hearings on the 1984 Budget Bill regarding (a) the administration's plans for filling vacant treatment authorization review positions and (b) the effects of high vacancy rates on the state's review of these requests. 1010

58. ***Direct County Input. Reduce Item 4260-101-001 by $1,220,000 and Item 4260-101-890 by $1,080,000.*** Recommend reduction to reflect receipt of anticipated but unbudgeted recoveries resulting from county participation in health coverage identification. 1015

59. ***Child Support Referrals. Reduce Items 4260-101-001 and 4260-101-890 by $525,000 and increase Items 4260-001-001 and 4260-001-890 by $25,000.*** Recommend increase for processing additional child support referrals and reduction 1016

to reflect associated savings.

60. Contract Extension. Recommend adoption of supplemental report language directing the department to (a) extend the privately contracted recoveries pilot project until June 1985 and (b) provide an analysis of costs of and benefits from privately contracted recoveries. 1018

61. Earnings Clearance System. Recommend department advise the Legislature by April 1, 1984, regarding the status of the earnings clearance system. 1019

62. Insurance Company Contracts. Recommend adoption of supplemental report language directing the department to submit to the Legislature by January 1, 1985, estimates of costs and expenditure reductions resulting from pilot contracts with insurance companies. 1019

63. Real Property. Recommend department advise the Legislature during budget hearings regarding staffing of increased recovery workload associated with real property liens. 1020

64. ***State Share of Recoveries. Reduce Item 4260-101-001 by $2,000,000 and increase Item 4260-101-890 by $2,000,000.*** Recommend General Fund reduction and federal fund increase to correct underbudgeting of state savings. 1021

65. ***Uncleared Recoveries. Reduce Item 4260-101-001 by $689,000 and Item 4260-101-890 by $611,000.*** Recommend uncleared recoveries be reflected in the budget. 1022

66. ***CHAMPUS Match. Reduce Item 4260-101-001 by $1,329,000 and Item 4260-101-890 by $1,261,000.*** Recommend budget be revised to reflect savings from a recent match between Civilian Health and Medical Program of Uniformed Services (CHAMPUS) and Medi-Cal eligibility files. 1023

Department of Health Services
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DEPARTMENT OF HEALTH SERVICES—Continued

GENERAL PROGRAM STATEMENT

The Department of Health Services has responsibilities in two major areas. First, it provides access to health care for California's welfare and medically needy populations through the Medi-Cal program. Second, the department administers a broad range of public health programs, including (1) programs that complement and support the activities of local health agencies controlling environmental hazards, preventing and controlling disease, and providing health services to populations that have special needs and (2) state-operated programs such as those that license health facilities and certain types of technical personnel.

The department has 4,313.1 authorized positions in the current year.

OVERVIEW OF THE BUDGET REQUEST

The budget proposes expenditures of $5,581,629,000 from all funds, including federal funds and reimbursements, for support of Department of Health Services programs in 1984–85. This is an increase of $64,089,000, or 1.2 percent, above estimated current-year expenditures.

The budget proposes departmental expenditures of $3,093,388,000 from the General Fund in 1984–85, which is an increase of $50,301,000, or 1.7 percent, above estimated current-year expenditures. This increase will grow to the extent any salary or staff benefit increases are approved for the budget year.

The budget proposes changes in expenditures (all funds) in each of the four major budget categories, as follows:

- Support: up $4,043,000 (2 percent).
- Special projects: up $14,536,000 (7 percent).
- Preventive health local assistance: up $26,784,000 (2.8 percent).
- Medi-Cal local assistance: up $18,726,000 (0.5 percent).

The $39.6 million reduction in funding from the Hazardous Substances Account is primarily caused by a technical change in the way outside funding received for cleaning up contaminated hazardous waste sites is accounted for in the budget. These funds are now counted as federal funds and reimbursements, rather than as revenues to the account.

The budget proposes the following significant changes in the budget year:

- An increase of $3 million and 62 positions for the Hazardous Waste Management program so that permits can be issued to all hazardous waste facilities within five years and so that inspections can be increased in order to ensure compliance with hazardous waste laws.
- The deletion of 24.5 positions in the Family Planning program to reflect the transfer of family planning responsibilities to local governments.
- The deletion of 83.2 positions to reflect the establishment of the Public Health Enhancement program that transfers funding and responsibilities for various public health programs to local governments.
- An increase of $2.7 million and 27.5 positions in the Genetic Disease and Health Protection programs to increase the department's prevention activities.

Table 1 shows the proposed budget, by major program category.

Table 1
Department of Health Services
Expenditures and Funding Sources
1982–83 through 1984–85
(in thousands)

	Actual 1982–83	*Estimated 1983–84*	*Proposed 1984–85*	*Change*	
				Amount	*Percent*
Department support	$185,719	$206,244	$210,287	$4,043	2.0%
Special projects	106,557	204,142	218,678	14,536	7.1
Preventive health local assistance	552,446	958,895	985,679	26,784	2.8
Medi-Cal local assistance	4,724,610	4,148,259	4,166,985	18,726	0.5
Totals	$5,569,332	$5,517,540 [a]	$5,581,629	$64,089	1.2%
General Fund	*$3,182,929*	*$3,043,087 [a]*	*$3,093,388*	*$50,301*	*1.7%*
Federal funds	*2,234,587*	*2,337,155 [a]*	*2,362,567*	*25,412*	*1.1*
Hazardous Substances Account	*6,811*	*49,600*	*10,000*	*−39,600*	*−79.8*
Hazardous Waste Control Account	*4,601*	*6,828*	*10,146*	*3,318*	*48.6*
Genetic Disease Testing Fund	*9,288*	*10,295*	*12,565*	*2,270*	*22.0*
County Health Services Fund	*2,960*	*2,200*	*3,006*	*806*	*36.6*
Local Health Capital Expenditure Account	*1,386*	*204*	*217*	*13*	*6.4*
Reimbursements	*126,407*	*66,443*	*88,541*	*22,098*	*33.3*
Other funds	*363*	*1,728*	*1,199*	*−529*	*−30.6*

[a] The total expenditures for 1983–84 are $6,773,000 less than the amount shown in the Governor's Budget. The budget schedules do not reflect the following adjustments: (1) a federal fund increase of $4,036,000 for the California Children's Services program, (2) General Fund savings of $10,235,000 from county recoupment reversions, and (3) General Fund savings of $574,000 from reduced caseload estimates for the Child Health and Disability Prevention program.

ANALYSIS AND RECOMMENDATIONS

1. DEPARTMENT SUPPORT

Department support is proposed at $211,077,000 (all funds) in 1984–85 and accounts for 3.8 percent of the department's budget.

The department proposes support for 4,135 positions in the budget year (excluding those assigned to special projects), a decrease of 178, or 4.1 percent, below the number of positions in the current year. This decrease results primarily from general position reductions in department administration and medical assistance. Reductions in preventive health positions due to the proposed public health enhancement and family planning block grant programs have been offset by increases in other preventive health divisions, especially in the Toxic Substances Control Division. The reduction also reflects a decrease of 36.5 positions due to the Governor's "3 percent reduction." Our calculations indicate that the "3 percent reduction" is, in fact, 1 percent of both support costs and personnel-years.

Table 3 illustrates the main components of the increase proposed in the department's support budget, excluding special projects.

DEPARTMENT OF HEALTH SERVICES—Continued

Table 2

Department of Health Services Support Positions and Expenditures—All Funds 1982–83 through 1984–85 (dollars in thousands)

	Actual 1982–83	Estimated 1983–84	Proposed 1984–85	Change Amount	Change Percent
Positions					
Preventive health	1,174.8	1,336.8	1,266.8	−70.0	−5.2%
Toxic substances control	141.8	184.0	245.5	61.5	33.4
Medical assistance	929.4	1,059.4	1,000.4	−59.0	−5.6
Licensing and certification	192.6	228.3	217.3	−11.0	−4.8
Audits and investigations	429.8	496.0	496.0	—	—
Administration and Director's office	980.8	1,008.6	909.0	−99.6	−9.9
Totals	3,849.2	4,313.1	4,135.0	−178.1	−4.1%
Expenditures[a]					
Preventive health	N/A	$61,396	$63,137	$1,741	2.8%
Toxic substances control	N/A	17,645	18,555	910	5.2
Medical assistance	N/A	49,120	49,569	449	0.9
Licensing and certification	N/A	12,598	12,918	320	2.5
Audits and investigations	N/A	18,239	19,243	1,004	5.5
Administration and Director's office	N/A	48,021	47,655	−366	−0.8
Totals	$188,065	$207,019	$211,077	$4,058	2.0%

[a] Data on 1982–83 support expenditures are not available by department unit.

Attorney Reductions

The *Supplemental Report to the 1983 Budget Act* requires that the Legislative Analyst report to the Legislature on any reductions made by the administration in attorney positions in the Health and Welfare Agency either by vetoes to the 1983 Budget Act or proposed reduction in the 1984 Budget Bill.

In acting on the 1983 Budget Act, the Governor vetoed funds for 7.5 positions in the Office of Legal Services, including five attorneys. The reductions were accomplished without lay-offs by not filling vacancies and transferring staff to other departments. The department informs us that the reduction has caused no major changes in its program. Nevertheless, we have found that it takes more time for the department to respond to routine requests, and more work is being referred to the Attorney General.

The 1984–85 budget does not propose any further reductions in attorney positions.

2. LICENSING AND CERTIFICATION

The Licensing and Certification program develops, implements, and enforces state standards to promote quality health care in approximately 3,800 hospitals, clinics, long-term care facilities, home health agencies, and adult day health centers. In addition, the program performs certification reviews for the federal government at facilities that seek to qualify for Title XVIII (Medicare) or Title XIX (Medi-Cal) funding. Program activities related to Medicare certifications are 100 percent federally funded. Activities related to Medi-Cal certifications are approximately 75 percent federally funded.

Expenditures and funding for the Licensing and Certification program are summarized in Table 4.

The budget proposes (1) a decrease of 20 positions in this program during 1984–85, due to "changing departmental needs" and (2) an increase of 9 positions due to additional workload related to new activities.

Table 3

Department of Health Services Support
Proposed Budget Changes
(in thousands)

	General Fund	*All Funds*
1983–84 expenditures (adjusted base budget)	$91,603	$241,622
Baseline adjustments		
A. Increase in existing personnel costs		
1. Dental benefits	62	115
2. Merit salary adjustments	877	1,615
3. Retirement	−44	−81
4. Health benefits	295	551
5. OASDI	183	337
6. Full-year funding of 1983–84 salary increase	3,910	7,208
B. Increases in operating expenses and equipment		
1. Six percent price increase	1,367	3,165
C. One-time adjustments		
1. Travel reallocation	60	—
2. Limited-term positions	−883	−2,310
3. Department of Personnel Administration	18	34
4. Positions abolished per Government Code Section 12439	−11	−30
5. Reimbursement funding adjustment	633	—
6. Medi-Cal funding adjustments	−1,512	—
7. Superfund adjustment	—	−40,500
8. Reorganization funding adjustment	−59	—
9. Adjustment in federal funds for expenditures in other departments	—	−1,412
10. Social services refugee reimbursement	—	2,510
11. Cannery contract	—	104
12. McColl remedial action	—	−1,500
13. Professional Standards Review Organizations	—	1,105
14. Pro-rata increase	—	555
Program change proposals		
1. Preventive health services	−2,203	−1,198
2. Medical assistance	−615	−1,614
3. Audits and investigations	−282	110
4. Licensing and certification	−172	−294
5. Administration	−1,071	−1,897
6. Toxic substances control	−34	2,716
Miscellaneous adjustments	−126	166
1984–85 expenditures (proposed)	$91,996	$211,077
Change from 1983–84:		
Amount	−$393	−$30,545
Percent	0.4%	−12.6%

Table 4

Licensing and Certification Expenditures
(dollars in thousands)

	Actual 1982–83	*Estimated 1983–84*	*Proposed 1984–85*	*Change*	
				Amount	*Percent*
All funds	$12,065	$14,011	$14,385	$374	2.7%
General Fund	*$6,531*	*$8,280*	*$8,242*	*−$38*	*−0.5%*
Federal funds	*5,534*	*5,731*	*6,143*	*412*	*7.2*

DEPARTMENT OF HEALTH SERVICES—Continued

Department Appeals Court's Prohibition on Collection of Licensing Fees

Chapter 327, Statutes of 1982 (SB 1326, the companion bill to the 1982 Budget Act), revised health facility licensing fees and established a mechanism for annually adjusting the fees through the budget process. At the time the measure was enacted, the fees were expected to produce approximately $7.1 million in General Fund revenue during 1982–83, as a partial offset to the estimated $8 million in General Fund expenditures for the licensing program in that year. To date, however, none of the additional funds that the Legislature anticipated have been collected by the department. This is because the Los Angeles County Superior Court has ruled that the department will be in contempt of the court's 1982 judgment in the CAREX case if it attempts to collect any fees.

The department has appealed the court's decision to the Court of Appeal, Second Appellate District. The required briefs were filed in January 1984, and oral arguments will be scheduled in the spring. The department indicates that it is unlikely that a decision in this case will be reached before the start of the 1984–85 fiscal year.

The department has obtained approval from the Health and Welfare Agency and the Department of Finance to propose an offer to settle this case. The department presented an offer to the plaintiffs in October 1983. On January 12, 1984, the plaintiffs' attorney submitted a counteroffer, which the department is now reviewing.

License Fees for 1984–85

We withhold recommendation on licensing and certification fees proposed for 1984–85, pending receipt of a fee schedule from the department.

Chapter 327, Statutes of 1982, requires the department to submit a proposed health facility licensing fee schedule to the Legislature as part of its annual budget request. The act requires the department to set the licensing fees at a level sufficient to provide revenues in an amount equal to (1) the General Fund appropriation to the program as specified in the annual Budget Act *plus* (2) the federal funds budgeted in the preceding fiscal year *less* (3) the actual federal funds received in the preceding fiscal year.

Chapter 1597, Statutes of 1982 (AB 2841), requires the department to submit an alternative fee schedule proposal that bases fees for each category of facility on the number of violations and the accumulated actual time spent by the department in licensing and monitoring facilities in that category. Our analysis of the department's alternative fee schedule in April 1983 revealed several problems with the proposed schedule. Consequently, the Legislature adopted language in the *Supplemental Report to the 1983 Budget Act* directing the department to submit a revised report by November 1, 1983. The revised report was received by the Legislature in December 1983.

At the time this *Analysis* was prepared, the department had not submitted to the Legislature the fee schedule required by Chapter 327. Consequently, we have no basis at this time for evaluating (1) the proposed level of fees under the Licensing and Certification program nor (2) the merits of the alternative fee schedule relative to the basic fee schedule. Accord-

ingly, we withhold recommendation on the level of fees proposed for 1984–85, pending receipt of the fee schedule that the department is required to submit.

Budget Request Is Inconsistent

We recommend that the department explain in budget hearings how it intends to cover the additional licensing and certification workload that will result from the termination of abbreviated surveys.

On October 31, 1983, the abbreviated surveys of skilled nursing facilities previously allowed by the federal government on a demonstration basis were terminated. The abbreviated surveys allowed California to adjust to reduced federal support for licensing and certification by reducing the number of survey requirements for certification of skilled nursing facilities. Under this approach, a survey team could complete a survey in less than one-half the time required by a full survey—two to two and one-half days, compared to five to seven days. The federal government, however, has determined that the abbreviated surveys were of limited value and thus discontinued their use. As a result, the department estimates that 25.5 new positions may be required to support the workload that will result from returning to full surveys for skilled nursing facilities.

The budget request for licensing and certification in 1984–85 does not request any additional funding or positions for this workload. In fact, the budget proposes a *decrease* of 20 positions, or 10 percent of the number authorized in the current year, due to "changing departmental needs." The department has not identified how it will absorb the additional workload that will result from returning to full surveys for skilled nursing facilities in the budget year.

Because adequate surveys of health facilities are critical to (1) assuring the health and safety of patients and (2) the maintenance of federal funding for long-term care, we recommend that in budget hearings the department explain to the Legislature how it will cover the additional workload that will result from returning to full surveys of health facilities.

Travel Expense Reductions Are Not Budgeted

We recommend the deletion of ~~$112,000~~ ($65,000 General Fund and ~~$47,000~~ federal funds) from department support to reflect savings in travel costs resulting from staff reductions.

The budget proposes to reduce 20 positions from the Licensing and Certification Division due to "changing departmental needs." The positions include 13 professional and 7 clerical positions. The budget fails to recognize the reduced travel costs that will result from the reduction in the professional staff. The department normally budgets $8,600 for travel per position. Accordingly, we recommend the reduction of $112,000 to reflect savings in travel expenses associated with the reduction of 13 professional staff.

Need for Proposed New Positions and Funds is Overstated

We recommend a reduction ~~of $22,000 from the General Fund and three~~ positions to more accurately reflect expected needs due to workload increases.

The budget proposes an increase of $242,000 and nine field survey staff to accommodate workload related to new licensing and certification activities. The new workload includes (1) reviewing hospitals for compli-

DEPARTMENT OF HEALTH SERVICES—Continued

ance with Medi-Cal contracts and investigating alleged instances of noncompliance, (2) surveying small intermediate care facilities for developmentally disabled persons, (3) surveying chemical dependency services and hospitals, and (4) certifying Short-Doyle mental health and substance abuse clinics.

Our analysis indicates that the need for additional positions and funds is overstated, for two reasons. First, the General Fund share of the workload related to certifying Short-Doyle clinics is reimbursed through an interagency agreement with the Departments of Mental Health and Alcohol and Drug Programs. Consequently, the funding requested for this activity is overstated by $23,000 (General Fund). Second, the budget request does not consider the fact that one-third of the additional workload will be incurred by the Los Angeles County Department of Health Services, rather than by the department. Los Angeles County conducts licensing and certification activities for the department under a contract. As a result, while the department will need the funds it has requested, it will not need three positions, or one-third of the nine positions requested. Accordingly, we recommend the reduction of three positions and $23,000 from the General Fund to more accurately reflect the expected additional needs.

3. AUDITS AND INVESTIGATIONS

The Audits and Investigations program conducts financial audits of Medi-Cal and public health providers, investigates allegations of provider or beneficiary fraud in the Medi-Cal program, performs post-payment reviews of the appropriateness of Medi-Cal health care services and payments, conducts quality control reviews of the accuracy of county eligibility determinations, and reviews and audits hospitals and prepaid health plans. The department estimates that 97 percent of all audits and investigations activities and expenditures are attributable to the Medi-Cal program.

The budget proposes a net increase of $1.1 million ($200,000 General Fund) for audits and investigations in 1984–85. In addition, it proposes (1) 20 new positions to perform financial audits covering county expenditures of AB 8 county health services funds and (2) reductions for other programs amounting to 20 positions. The increase in funds is primarily due to the full-year effect of the salary and benefit increases provided on January 1, 1984, and a 6 percent increase in operating expenses to offset the effects of inflation.

Position Reductions

We recommend that the proposed reduction of 14 positions be approved.

The proposed reduction of 20 positions in the budget year reflects (1) consolidation of certain administrative support functions (9 positions), (2) reductions in the workload related to medically indigent adults (3 positions), (3) a reduction in staff devoted to quality control reviews of county eligibility determinations (6 positions), and (4) the elimination of staff currently used to (a) evaluate state third-party collection and (b) conduct non-cost-beneficial reviews of optometrists, dentists, and podiatrists who receive Medi-Cal reimbursements (2 positions).

In our analysis of Medi-Cal eligibility determinations, we withhold rec-

ommendation on the proposed reduction of 6 positions related to quality control reviews. With regard to the remaining 14 positions proposed for elimination, we have not been able to establish that these positions are needed to perform the department's statutory duties. On this basis, we recommend that the proposed reduction be approved.

Audit Unit for AB 8 Expenditures w|drawn 4|23

We recommend (1) a reduction of $111,000 to correct for overbudgeting, (2) that the department report at budget hearings on the status of AB 8 recoupment appeals and the amount of potential reversions to the General Fund in 1984–85, and (3) adoption of supplemental report language requiring the department to audit county medically indigent services allocations concurrent with audits of AB 8 allocations.

The budget proposes $694,000 from the County Health Services Fund to establish an ongoing program to audit county AB 8 health services expenditures. These funds would provide support for 20 two-year limited-term positions. During the initial two years of the audit program, the department intends to audit all counties and other local jurisdictions that received AB 8 funding for the period July 1979 through June 1982. Thereafter, audits of AB 8 county expenditures would be conducted by existing Audit and Investigations Division personnel.

Based on results of a five-county pilot project completed in 1982–83 (auditing 1979–80 expenditures), the department estimates that the AB 8 audit program will recover up to $10 million annually. Existing law provides that funds recovered within three years of the initial appropriation are deposited in the County Health Services Fund. Funds recovered after three years revert to the General Fund.

The department states that a full-scope audit program would also (1) contribute to more accurate records of health-related expenditures, revenues, and net county costs by ensuring the use of proper accounting procedures, (2) ensure that AB 8 funds are used only for expenditures authorized by AB 8, and (3) improve the state's on-site scrutiny of the accuracy of financial data reports from counties.

Positions Will Not Be Filled Until October 1, 1984. The requested level of funding for salaries and operating expenses assumes that all 20 positions will be occupied for all of 1984–85. The department estimates, however, that the full 20 positions will not be filled prior to October 1, 1984—three months into the budget year. Assuming that seven positions are filled on August 1, seven are filled on September 1, and the remaining six are filled on October 1, we estimate that the department has overbudgeted 1984–85 costs by 16 percent. We therefore recommend a reduction of $111,000 in Item 4260-001-898 to correct for this overbudgeting.

Budget-Year Reversions Not Identified. The department estimates that recoupments resulting from the five-county pilot project completed in 1982–83 will total $1,506,000. Thus far, $60,000 has been collected, $33,000 is under appeal, and the remaining audit claims will, in all probability, be appealed. These appeals should be completed during the current fiscal year. The 1984–85 budget, however, does not identify any reversions to the General Fund resulting from the pilot projects. We therefore recommend that at budget hearings, the department report on the status of these appeals and the amount available for reversion to the General Fund in 1984–85.

Audits of County Medically Indigent Services (MIS) Programs. During the initial two years of the new AB 8 audit program, the depart-

DEPARTMENT OF HEALTH SERVICES—Continued

ment intends to audit AB 8 allocations from 1979–80 through 1982–83. We believe the scope of these audits should be expanded.

Since January 1, 1983, counties have received medically indigent services (MIS) allocations to assist them in providing health services to indigent persons. Counties may use MIS funds for many of the same purposes as AB 8 funds, and planning, budgeting, accounting, and reporting requirements for the two programs often are similar. In fact, it may be difficult to audit expenditures from these two funding sources by some counties on a separate basis. Consequently, we conclude that it would be prudent and cost-effective for the AB 8 program audit unit to also audit expenditures of MIS funds. Accordingly, we recommend that the Legislature adopt the following supplemental report language:

"The department shall audit MIS expenditures concurrent with the auditing of AB 8 expenditures."

4. PREVENTIVE HEALTH SERVICES

The Preventive Health Services program provides state support for California's public health programs. To administer these public health programs, the department maintains five divisions with the following responsibilities:

1. ***The Office of County Health Services and Local Public Health Assistance*** (a) distributes funds appropriated by AB 8 (Ch 282/79) to local health agencies, (b) distributes funds to counties for care of medically indigent persons, (c) administers state and federal subvention programs that provide funds for the support of local public health activities, (d) distributes funds for capital outlay projects to local health agencies, and (e) provides technical assistance in funding matters to local health departments.

2. ***The Community Health Services Division*** addresses the special needs of women and children through the Family Planning, Maternal and Child Health, Genetic Disease, California Children's Services, Genetically Handicapped Persons', and Child Health and Disability Prevention programs.

3. ***The Rural Health Division*** is responsible for improving the quantity and quality of health services available to underserved rural, farmworker, and Indian populations through the provisions of public health services in small rural counties and the funding of primary health care clinics.

4. ***The Environmental Health Division*** operates programs to protect public health by controlling food, drugs, water supplies, vectors, noise, and unnecessary exposure to ionizing radiation.

5. ***The Health Protection Division*** is responsible for (a) preventing and controlling infectious and chronic disease, (b) conducting epidemiological studies including the health effects of toxics in the environment and the workplace, and (c) operating public health laboratories.

In addition, preventive health services staff administer a number of special projects. These projects, which are shown separately in the budget, are studies or demonstration projects that are 100 percent funded by the federal government, other state agencies, or other organizations.

Budget Proposal

Department Support. The budget proposes $75,835,000 (including overhead costs) for department support attributable to preventive health programs in 1984–85. This amount excludes funding for special projects. The requested amount is $2,005,000, or 2.7 percent, more than estimated current-year expenditures. The increase reflects:

- A proposal to consolidate all or part of five preventive health services categorical programs into the Public Health Enhancement program (PHEP), effective January 1, 1985. Under the proposal, the PHEP would be administered primarily by the counties, although some administrative responsibilities for programs of regional significance would remain with the state. The budget proposes a net reduction of 83 positions and a transfer of $822,000 ($163,000 General Fund) in support funds that were associated with administering the former preventive health programs to local assistance.
- A proposal to transfer the administration of family planning services to the counties, beginning January 1, 1985. In conjunction with this transfer, the budget proposes to eliminate 24.5 positions from the Office of Family Planning and transfer $445,000 in support expenditures to local assistance.
- An increase of $2,746,000 for support of the neural tube defects unit.

Table 5 and Chart 1 display staffing and operating support for each preventive health program in the current and budget years.

Table 5

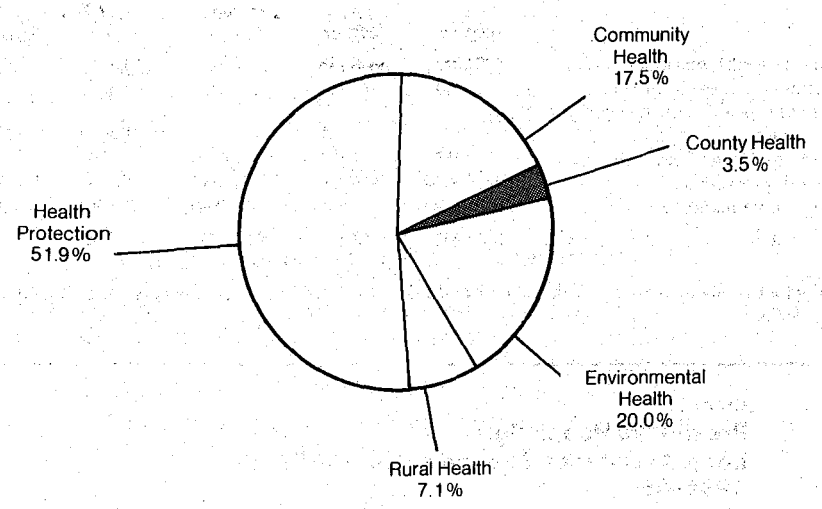
Preventive Health Support
Positions [a] and Expenditures—All Funds
1983–84 and 1984–85
(dollars in thousands)

	Positions			*Expenditures*		
	Estimated 1983–84	*Proposed 1984–85*	*Percent Change*	*Estimated 1983–84*	*Proposed 1984–85*	*Percent Change*
County health services	47.5	43.5	−8.4%	$2,163	$2,209	2.1%
Community health services	276.6	238.1	−13.9	11,014	11,055	0.4
Rural health services	115.4	101.4	−12.1	4,841	4,483	−7.4
Environmental health	300.7	286.2	−4.8	12,549	12,604	0.4
Health protection	596.6	597.6	0.2	30,829	32,786	6.3
Subtotals	1,336.8	1,266.8 [b]	−5.2%	$61,396	$63,137	2.8%
Distributed overhead	318.0	281.9	−11.4	12,434	12,698	2.1
Subtotals	1,654.8	1,548.7	−6.4%	$73,830	$75,835	2.7%
Special projects	779.3	892.6	14.5	166,042	218,678	31.7
Totals	2,434.1	2,441.3	0.3%	$239,872	$294,513	22.8%

[a] Position counts do not reflect salary savings.
[b] Includes 104 half-year positions (93 in community health services and 11 in health protection) scheduled to be phased out in conjunction with the Public Health Enhancement program and the family planning grant program.

DEPARTMENT OF HEALTH SERVICES—Continued

Chart 1
Preventive Health Services
Department Support Expenditures[a]—All Funds
1984–85



[a] Excludes administrative overhead.

Local Assistance. The budget proposes $991,397,000 in local assistance for preventive health services. This is an increase of $20,810,000, or 2.1 percent, above estimated current-year expenditures. The increase primarily reflects:

- A $10,410,000 increase to provide a 2 percent cost-of-living adjustment (COLA) for most preventive health services programs.
- A decrease of $10,235,000 in recoupment reversions from county health services funds for 1984–85.
- A $5,507,000 increase to reflect (1) increased utilization in the California Children's Services, Genetically Handicapped Persons', and Child Health and Disability Prevention programs and (2) a population adjustment for county health services subventions under AB 8.
- A $1,267,000 increase in local assistance funds available for family planning services and the Public Health Enhancement program resulting from the transfer of support to local assistance.
- An increase of $650,000 to restore funds for primary care clinics vetoed by the Governor in 1983–84.
- The elimination of $350,000 for adult day health care matching grants.
- A $209,000 revision to the county health services base budget resulting from Tehama County opting out of the rural health services contract-county program.

Table 6 and Chart 2 present local assistance expenditures for 1982–83 through 1984–85.

Table 6
Preventive Health Local Assistance
Expenditures—All Funds
1982–83 through 1984–85
(in thousands)

	Actual 1982–83	*Estimated 1983–84*	*Proposed 1984–85*	*Change*	
				Amount	*Percent*
County health services	$424,247	$838,278	$857,094	$18,816	2.2%
Community health services	114,754	107,793	117,200	9,407	8.7
Public health enhancement program	—	—	(14,460)	(14,460)	N/A
Rural health services	7,787	7,595	7,947	352	4.6
Health protection	5,635	5,229	3,438	−1,791	−34.3
Legislative mandates [a]	23	(136)	(86)	(−50)	(−36.8)
Totals	$552,446	$958,895	$985,679	$26,784	2.8%

[a] Legislative mandates not included in totals for 1983–84 and 1984–85. These amounts are included in Item 9860.

Chart 2
Preventive Health Services
Local Assistance Expenditures—All Funds
1984–85

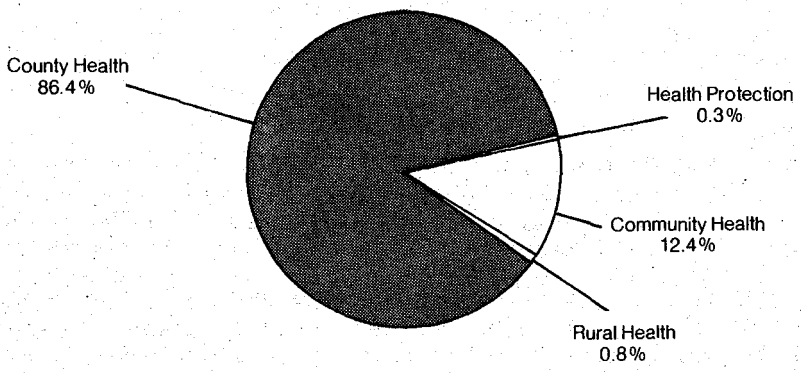


Table 7 displays the budget changes proposed in the preventive health local assistance programs.

DEPARTMENT OF HEALTH SERVICES—Continued

Table 7
Preventive Health Local Assistance
Proposed Budget Changes
(in thousands)

	General Fund	*All Funds*
1983–84 expenditures (Budget Act)	$942,865	$963,117
Baseline adjustments, 1983–84		
1. Adult day health care (Ch 1208/83)	350	350
2. Child health and disability prevention (CHDP)	−574	−574
3. California children's services utilization increase	—	4,036
4. Special needs and priorities expenditures	—	2,200
5. Recoupment reversion	—	−10,235
1983–84 expenditures (adjusted base budget)	$942,642	$958,895
Baseline adjustments, 1984–85		
1. Adult day health care	−350	−350
2. County health services—decrease in recoupment reversions	—	10,235
3. Rural health opt-out	209	209
Caseload and cost adjustments:		
1. Local government fiscal relief population increase	994	994
2. California children's services (CCS)—utilization increase	4,144	3,541
3. CCS—family repayment decrease	—	−150
4. Genetically handicapped persons—program utilization increase	398	398
5. CHDP—utilization increase	574	574
Cost-of-living adjustments (2 percent):		
1. Health protection	67	67
2. Community health services	1,819	1,819
3. County health services	7,378	7,378
4. Rural health services	152	152
Program change proposals:		
1. Family planning transfer of support funds to local assistance	445	445
2. Public health enhancement proposal transfer of support funds to local assistance	163	822
3. Restoration of primary care clinic reductions	650	650
1984–85 expenditures (proposed) [a]	$959,287	$985,679

[a] Details may not add to totals due to rounding.

Cost-of-Living Adjustments in Preventive Health Local Assistance Programs

The budget requests $9,416,000 for a 2 percent cost-of-living adjustment (COLA) for most preventive health local assistance programs. Of this amount, $7,378,000 is proposed for the AB 8 local government fiscal relief program, $1,819,000 is proposed for various community health programs, and $219,000 is proposed for health protection and rural health programs. The budget proposes no COLA for county health programs serving medically indigent persons. If the Legislature chooses to provide a 2 percent COLA for county medically indigent services, it will have to augment the General Fund budget by $9,549,000.

Assembly Bill 8 provided for automatic increases in the annual appropriation to the County Health Services Fund for local government fiscal relief, based on a formula that recognizes population increases and inflation. The measure bases that part of the increase intended to compensate for inflation on the December-to-December change in the average of the Los Angeles and San Francisco consumer price indices for all urban consumers. Under the provisions of AB 8, a 5.55 percent COLA is required for 1984–85.

We estimate that the adjustments required to comply with the provisions of AB 8 would result in a $21,469,000 increase in expenditures for

fiscal relief above the current-year level ($994,000 for population and $20,475,000 for inflation). The budget provides for an increase of $8,372,000 ($994,000 for population and $7,378,000 for inflation). Thus, in order to provide a full population and cost-of-living adjustment, as required by AB 8, the Legislature would have to augment the budget by $13,097,000.

A. PUBLIC HEALTH ENHANCEMENT PROGRAM

The budget proposes to consolidate all or part of five preventive health categorical programs into a block grant called the Public Health Enhancement program (PHEP), effective beginning January 1, 1985. The PHEP would be administered by the counties. The programs proposed for consolidation are Maternal and Child Health (MCH), Child Health and Disability Prevention (CHDP), Preventive Health Care for the Aging, Children's Dental Disease Prevention, and Immunization Assistance.

For the period January 1, 1985, through June 30, 1985, the budget proposes $14,460,000 for PHEP local assistance, including $7,637,000 from the General Fund and $6,823,000 in federal funds. The amount of local assistance funding is $1,259,000, or 9.5 percent, greater than the sum of estimated expenditures for the individual categorical programs during a comparable time period in the current year. This increase is the result of (1) a transfer of $822,000 from support to local assistance to reflect state administrative savings resulting from the consolidation, (2) an increase of $287,000 to reflect workload increases in the CHDP, and (3) an increase of $150,000 to provide a 2 percent cost-of-living adjustment (COLA) for the General Fund share of PHEP.

The budget proposes the deletion of 83.2 positions currently associated with the categorical programs proposed for inclusion in the PHEP. This represents 30 percent of the existing positions. The reduction includes 4.7 positions in department administration. The department estimates that administrative savings associated with the elimination of these positions will be $822,000 in 1984–85 and $2,318,000 in 1985–86, the first full year in which the new program will be in operation. These funds are proposed for transfer to local assistance. The budget proposes to retain 51.9 positions currently associated with the categorical programs to (1) continue performing functions not proposed for transfer to the counties and (2) monitor and review PHEP allocations.

Table 8 displays proposed funding for the PHEP in 1984–85. The table also shows estimated PHEP expenditures in 1985–86, when the program will be implemented for a full year.

On page 31 of the budget summary, the Governor indicates that as part of the legislation implementing PHEP, the administration "will support . . . . an augmentation of $1.25 million to assist in [the transfer of responsibilities to local government] and to provide local government with the ability to expand in areas of high need." *This $1.25 million is not reflected in the department's budget schedules.*

The budget proposes to consolidate all or part of the following five categorical programs into the PHEP.

Maternal and Child Health (MCH). The MCH program addresses the health care needs of women and children by (1) subsidizing prenatal care for low-income women, (2) developing services for newborn infants in areas with high concentrations of high-risk patients, (3) supporting regional systems of maternity and newborn care, and (4) supporting outreach efforts to populations with a high percentage of high-risk pregnancies. The target population consists of pregnant women and newborn children, particularly low-income women and women with high-risk pregnancies.

DEPARTMENT OF HEALTH SERVICES—Continued

Table 8

Public Health Enhancement Program
Support Adjustments and Local Assistance Expenditures
1984–85 and 1985–86
(dollars in thousands)

		Proposed 1984–85 (One-half Year)		*Estimated 1985–86 (Full Year)* [a]	
	Positions [b]	*Support Adjustments* [b]	*Local Assistance Expenditures*	*Support Adjustments*	*Local Assistance Expenditures*
Health protection					
Preventive health care for the aging	−5.0	−$103	($621)	−$206	($1,240)
Dental health	−4.0	−73	(765)	−146	(1,530)
Immunization assistance	−2.0	−53	(510)	−105	(1,020) [c]
Community health					
Maternal and child health (MCH)	−40.5	−830	(7,805)	−1,662	(15,603)
MCH grants	—	—	(6,063)	—	(12,127)
Infant dispatch	—	—	(111)	—	(221)
Perinatal access	—	—	(402)	—	(803)
High risk infant follow-up	—	—	(488)	—	(971)
Perinatal health	—	—	(741)	—	(1,481)
Child health and disability prevention	−40.0	−802 [d]	(3,937)	−1,603 [d]	(7,874)
Administration	−4.7	−82	—	−248	—
Transfer of support funds to local assistance	—	—	(822)	—	(2,318)
PHEP administration section	13.0	589	—	589	—
PHEP local assistance	—	—	14,460	—	29,585
Totals	−83.2	−$1,354	$14,460	−$3,381	$29,585
General Fund	—	*−$163*	*$8,234*	*−$999*	*$17,258*
Federal funds	—	*−1,191*	*6,226*	*−2,382*	*12,327*

[a] Estimates based on budget change proposal submitted by the department. These estimates assume a 2 percent COLA on 1983–84 General Fund local assistance expenditures.
[b] The budget proposes to establish the PHEP administrative section July 1, 1984, and implement the position reductions on January 1, 1985.
[c] Excludes $378,000 proposed to be continued as categorical funding.
[d] Includes federal funds totaling $532,000 in 1984–85 and $1,063,000 in 1985–86.

The entire MCH program is proposed for inclusion in the PHEP. The budget proposes to eliminate 40.5 positions currently associated with the program. The remaining staff of 13 positions would continue administering local assistance funds that the budget proposes to set aside for programs of regional or statewide significance.

Child Health and Disability Prevention (CHDP). The CHDP program funds comprehensive health assessments for the early detection and prevention of disease and disabilities in children. The target population for services is (1) Medi-Cal eligible children up to age 21 and (2) low birth weight infants and children entering school whose family incomes fall below 200 percent of the Aid to Families with Dependent Children in-

come standard. Health assessments for Medi-Cal eligible children are mandated under the federal Early Periodic Screening, Diagnosis, and Treatment (EPSDT) program. The department estimates that 772,000 health assessments will be provided in the current year, of which 653,000 will be provided to Medi-Cal eligible children and 119,000 will be provided to children paid for with state funds.

The entire CHDP program, except for functions associated with administering the EPSDT program, is proposed for inclusion in the PHEP. The budget proposes to eliminate 40 of the 65 positions currently associated with the program. The remaining 25 positions are in the Child Health Information and Claiming (CHIC) Unit. These positions process Medi-Cal (EPSDT) and non-Medi-Cal (state-funded) provider claims.

Children's Dental Disease Prevention. The dental health program promotes dental disease prevention programs, provides consultation on dental disease, and administers the school-based Dental Disease Prevention program established by Ch 1134/79 (SB 111). In 1981–82, 231,000 children participated in this program, which includes daily in-class brushing and flossing, weekly fluoride rinsing, and dental health and nutrition education.

Five of eight positions and $1.5 million in local assistance funds are proposed for inclusion in the PHEP. The remaining dental health staff of three positions will continue functions that cannot be carried out by individual counties.

Immunization Assistance. The immunization unit oversees the distribution to local health departments of vaccines and local assistance for immunization of children and senior citizens. State staff assist counties in reviewing children's school immunization records, train county personnel in vaccine preventable diseases and control techniques, and respond to disease outbreak situations.

Two of five positions and $1 million of $1.4 million in local assistance funds are proposed for inclusion in the PHEP. The remaining three positions will provide technical assistance to counties in the event of emergencies.

Preventive Health Care for the Aging. The Preventive Health Care for the Aging program funds city and county health departments to provide public health nurses for health appraisals, counseling, referrals and follow-up, and other preventive health services to older adults in senior citizen centers housing projects, congregate meal sites, and community clinics.

Five positions and $1,216,000 in local assistance funds currently associated with the Preventive Health Care for the Aging program are proposed for inclusion in the PHEP.

Public Health Enhancement Program Proposal

Under PHEP, responsibility for provision of services, as well as funds currently spent on the five categorical programs and $822,000 in state administrative savings, would be transferred to the counties. Counties would have significant flexibility in designing their own programs. Details of the proposal are discussed below.

Restrictions on Use of Funds. Each county would be required to submit an application for funds that includes (1) a description of the populations and localities to be served, (2) a statement of goals and objectives, and (3) a description of services to be provided. Prior to submission of the application, each county would have to hold a public hearing con-

DEPARTMENT OF HEALTH SERVICES—Continued

cerning its application for funds. Counties would have to use the funds for activities that would qualify for funding under one of the five programs consolidated into the PHEP, although they could establish different funding levels for the individual programs and could eliminate programs entirely. Federal funds would have to be used in accordance with guidelines and regulations associated with the federal maternal and child health block grant.

County Funding Allocations. State administrative savings would be allocated to counties on a per-capita basis, using population estimates developed by the Department of Finance. Each county, however, would receive a minimum allocation of $7,500 ($15,000 in 1985–86). Local assistance funds would be allocated based upon the proportion of total funds received by the county and other public or private agencies located in the county from the five categorical programs from July 1, 1980, through June 30, 1984.

The department proposes to set aside $2 million ($4 million for 1985–86) of PHEP local assistance funds to continue specific programs of statewide or regional significance. These funds would be administered by the state. Table 9 displays the programs and the funding levels for each during the current year.

Table 9

Programs of Regional or Statewide Nature
Proposed for Funding Through $4 Million Set-Aside Funds
Public Health Enhancement Program

	Estimated 1983–84
Maternal and child health data base	$357,000
Demonstration projects (7 projects)	2,254,000
Prematurity prevention (3 projects)	
Diabetic pregnancy outcome (2 projects)	
Training (2 projects)	
Infant dispatch	217,000
Perinatal access	787,000
High-risk infant follow-up	956,000
	$4,571,000

Source: Department of Health Services.

Because the amount proposed for the set-aside ($4 million for a full year) is less than the amount of estimated expenditures in the current year ($4,571,000) shown in Table 9, reductions in the number or scope of some projects would have to be made.

Eligibility for Services. Eligibility guidelines for services provided with federal MCH block grant funds would be consistent with federal regulations. Each county could establish its own eligibility guidelines for the use of state funds.

Reporting, Audit, and Oversight Requirements. State staff would review each county's statement of intended expenditures to determine whether the proposals comply with federal block grant requirements. Counties would have to (1) use funds only for purposes specified in the statement of intended expenditures, (2) establish fiscal control and fund accounting procedures to assure proper disbursement and use of funds,

and (3) submit reports of expenditures and services. Counties would be audited to assure compliance with rules concerning the use of federal maternal and child health block grant funds. The state could withhold funds if the county does not comply with federal regulations.

State Responsibilities. The department proposes to establish a PHEP unit (13 positions) and an MCH unit (13 positions) in the Community Health Services Division. This staff would be responsible for (1) providing or contracting for services to carry out projects of regional or statewide significance or to meet a critical or unanticipated need for such services, (2) establishing procedures for submission and review of each county's statement of intended expenditures, and (3) adopting regulations and procedures necessary to (a) implement the PHEP and (b) assure compliance with federal MCH block grant regulations. The department proposes to continue 25 positions in the Child Health Information and Claiming Unit. These positions process Medi-Cal (EPSDT) and non-Medi-Cal (state-funded) provider claims.

More Information Needed

We withhold recommendation on the PHEP proposal, pending receipt of the proposed implementing legislation and additional information regarding the proposal.

Our review of the PHEP indicates that the proposal has merit. For example, under the new program:

- Responsibility for establishing funding levels for local health programs would be vested with that level of government most familiar with, and most responsive to, local needs.
- Responsibility for administering local health programs and selecting local providers would be assigned to that level of government best able to oversee program operations.
- Administration of health programs at the local level could be centralized and streamlined, because counties would not need to comply with state program regulations and separate reporting and auditing requirements that apply to individual categorical programs.
- The state would experience savings because not as many state staff would be needed to administer local programs. The funds for this staff would be allocated to counties, making it available for additional services.

We cannot, however, recommend approval of the PHEP at this time for three reasons: (1) the proposed legislation that would implement the program was not available at the time this *Analysis* was written, (2) the Legislature needs additional information in order to evaluate the proposal, and (3) our review has identified significant problems related to administration of the federal EPSDT program and options for small counties that need to be resolved before the new program is authorized.

Additional Information Needs. In order to facilitate legislative review of the PHEP proposal, we recommend that the department submit to the fiscal committees, by April 1, 1984, a response to the following questions:

1. ***Will increased local costs to administer the PHEP reduce the level of dollars available for services?*** Some counties might have difficulty providing the services now provided by state staff because they lack the resources needed to perform certain administrative functions effectively. For example, depending on how they organize their programs, counties

DEPARTMENT OF HEALTH SERVICES—Continued

would be required to develop and negotiate contracts, establish a claims payment system, and develop reporting and auditing requirements for the local agencies with whom they contract. Under the PHEP proposal, state administrative savings of $822,000 in 1984–85 and $2,318,000 in 1985–86 would be transferred to counties. We have no basis for determining whether these additional funds would fully offset increased county administration costs. Consequently, we cannot determine whether there would be an increase, decrease, or no change in the current level of service dollars.

2. ***Will the program's reporting and auditing requirements be sufficient to (a) provide adequate information for legislative decision-making and (b) assure that funds are spent according to legislative intent?*** The proposal indicates that the department will require reports from county programs and will audit expenditures by counties in accordance with federal requirements. The proposal does not provide any details on the requirements associated with the expenditure of state funds.

The Legislature needs information from county programs to determine how effectively and efficiently General Fund resources are being used and to set future policy directions. Without audits of how state funds are used, the Legislature cannot be assured that PHEP funds are being spent according to legislative intent or that unused or improperly used funds will be recovered by the state.

3. ***What workload and responsibilities will the 26 positions proposed for continuation at the state level have?*** The budget proposes to create a PHEP unit consisting of 13 positions and a MCH unit consisting of 13 positions. The department has not provided a detailed workload analysis supporting its proposal.

Problems with the Proposal. Our review has identified two significant problems with the proposal that should be overcome prior to legislative action. We recommend that the department address these problems when it submits additional information regarding the proposal.

1. ***Enforcement of Federal Guidelines for the EPSDT Program.*** Approximately 85 to 90 percent of the health assessments now provided by the CHDP program are funded by Medi-Cal under federal EPSDT program regulations. To receive these funds, the state is required to fulfill federal reporting and auditing requirements.

Currently, 36 positions (27.5 professional and 8.5 clerical) in three state offices (Los Angeles, Berkeley, and Sacramento) administer the program. The 27.5 professional positions include (1) 6 public health nurses, 1 nutritionist, and 13 analysts who receive and review county CHDP program plans and budgets, make recommendations on those applications, and provide technical assistance, (2) 4 policy analysts who work with the federal government to assure that changes in federal regulations are implemented in the state and county programs, and (3) 3.5 positions to prepare federal and state reports and provide information to the counties regarding the reporting requirements.

Under the PHEP proposal, these functions would be the responsibility of the 13-position PHEP unit. In addition, the unit would have other responsibilities related to administering county PHEP allocations. Accordingly, we recommend that the department explain how federal reporting and auditing requirements will be met within the level of staffing proposed in the budget.

2. ***No Options for Small Counties.*** Under a number of state public

health programs, including Rural Health Contract Counties, California Children's Services (CCS), and Medically Indigent Services, small counties may contract with the state for administration and provision of services. These counties have been given this option either because they lack trained county personnel or because the county is too small for cost-efficient management of the programs. Currently, there are 14 counties participating in the rural health contract counties program, 33 counties opting for state administration of their CCS program, and 30 counties participating in the Medically Indigent Services contracting program. Some small counties may not be able to provide quality services in a cost-efficient manner under the PHEP proposal and might choose state administration if it was available. This type of arrangement may also be warranted for administration of the PHEP. The department should address this issue when it submits additional information on the proposal to the Legislature.

Federal Funds for PHEP Department Support

We recommend a reduction of $391,000 from the General Fund to reflect the availability of federal funds for administrative support of the Public Health Enhancement program.

The budget requests $589,000 from the General Fund for support of the Public Health Enhancement program administration section. The primary function of this unit would be to monitor local EPSDT programs to assure that they meet federal requirements. In the current year, approximately 66 percent of the funds available to support these functions are federal funds.

Because the functions of the PHEP unit will be basically the same as administrative functions associated with the CHDP program in the current year, we see no reason why the department cannot continue to claim Medi-Cal funds for administrative support. Accordingly, we recommend (1) a General Fund reduction of $391,000 in the support appropriation for the PHEP administrative unit and (2) a corresponding increase in federal funds.

Federal Maternal and Child Health Block Grant

The budget proposes maternal and child health (MCH) block grant expenditures of $24,340,000 in 1984–85. Of this amount, $9,922,000 is budgeted for California Children's Services (CCS). The remainder will be spent on (1) state maternal and child health programs for the first six months of 1984–85 and (2) the Public Health Enhancement program (PHEP) during the second half of the budget year.

Table 10 displays estimated current-year and proposed budget-year expenditures from MCH block grant funds. Most of the changes shown in the table result from including MCH block grant funds in the PHEP. The table shows that the department proposes to decrease federal fund expenditures for CCS local assistance by $603,000, or 5.7 percent. The table also shows that there will be no carry-over funds available to fund expenditures in 1985–86, except for the reserve needed to fund the program July 1, 1984, to September 1, 1984, the last quarter of the federal fiscal year.

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Table 10
Federal Maternal and Child Health (MCH) Block Grant
Allocation of Funds
1983–84 and 1984–85
(in thousands)

	Estimated 1983–84	*Proposed 1984–85*	*Change Amount*	*Change Percent*
Funds available				
Carry-over from prior fiscal year	$10,599	$4,795	−$5,804	−54.8%
Block grant award	19,227	19,545 [a]	318	1.7
Total available	$29,826	$24,340	−$5,486	−18.4%
Expenditures				
Support	1,965	1,432	−533	−27.1
MCH grants	11,924	6,063	−5,861	−49.2
Special project (infant botulism)	200	—	−200	−100.0
High-risk infant follow-up	200	100	−100	−50.0
Public health enhancement program	—	5,722	5,722	N/A
Regional/statewide MCH programs	—	1,000	1,000	N/A
Agency task force & audit withhold	217	101	−116	−53.5
California children's services	10,525	9,922	−603	−5.7
Total expenditures	$25,031	$24,340	−$691	−2.8%
Carry-over to next fiscal year	4,795	—	−4,795	−100.0

[a] Excludes $4,886,000 for July 1, 1985, to September 30, 1985.

B. FAMILY PLANNING GRANT PROGRAM

The budget proposes to transfer responsibility for the family planning program to counties, effective January 1, 1985. Currently, the family planning program funds contraceptive, sterilization, information, and education services. The target population for the services is low-income persons whose incomes are higher than the Medi-Cal eligibility limit. The information and education projects that have been funded in the past have included education programs intended to improve parent and child communication about sexuality, training programs for family planning providers, and educational programs promoting male involvement in contraceptive decision-making.

The budget proposes $29,758,000 for support of family planning services in 1984–85, excluding administrative overhead. This amount is $618,000, or 2.1 percent, above estimated current-year expenditures. The funding change is primarily due to a 2 percent cost-of-living increase proposed for local assistance. The budget proposes to eliminate 24.5 of 29.5 positions currently associated with the program and transfer the savings associated with deleting these positions—$445,000 in 1984–85 and $890,000 in 1985–86, when the program is effective for the full year—to augment the local assistance appropriation.

On page 31 of the budget summary, the Governor states that "an augmentation of $4.75 million to the level of funding contained in this budget will be included in the proposed legislation to assist in transferring family planning to local government and to provide local government with the ability to expand in areas of high need." *This $4.75 million is not reflected in the department's budget schedules.*

Current-Year Funding Reductions. The current-year allocation for family planning reflects gubernatorial vetoes of $9.5 million in local assistance and $458,000 in state support. As a result of the reduction in local assistance funds, the Office of Family Planning instituted or raised fees for

certain family planning services and reduced services provided for (1) the treatment of gynecological and sexually transmitted diseases and (2) emergency medical services for contraceptive-related complications.

The reduction in support funds required the elimination of 11 positions and caused a reduction in the (1) level of technical assistance provided to counties and (2) collection of information and monitoring of family planning services provided in the state.

Family Planning Grant Program Proposal

Currently, the state Office of Family Planning contracts with counties and private nonprofit local agencies to provide family planning services. In the current year, counties received 34 percent of local assistance funds. The remaining funds were awarded to private nonprofit agencies. Contractors bill the state on a per-visit basis for contraceptive and sterilization services provided to eligible persons. In addition, contractors bill the state for the actual cost of providing information and education services. State staff award and monitor contracts and provide technical assistance to local agencies.

Under the administration's family planning grant program proposal, the responsibility for providing family planning services would be transferred to the counties. The proposal gives each county the flexibility to design its own family planning program. Details of the proposal are discussed below.

Restrictions on Use of Funds. Each county desiring to participate in the family planning grant program would have to submit an application for funds that includes (1) a narrative description of the population eligible to receive state-funded family planning services, (2) a description of services to be provided, (3) a statement of program goals and objectives, (4) a funding formula for allocating state funds (first four years only), and (5) a summary of a public hearing on the proposed allocation of funds within the county. All state funds received by counties under this program would have to be used to provide family planning services.

County Funding Allocations. Each county would receive a funding allocation based on a four-year (1980–81 through 1983–84) historical pattern of state family planning expenditures within that county. Counties would be responsible for either providing services directly or contracting with local agencies to provide services. During the first two years of the grant program (1984–85 and 1985–86), counties could not increase the percent of state funds allocated for services provided directly by the county. In 1986–87 and 1987–88, a county could increase its own share of state funding by 35 percent. For example, if a county had received an average of $20,000 to provide family planning services between 1980–81 and 1983–84, and local nonprofit agencies in the county had received an average of $20,000 during the same four-year period, the county could spend only 50 percent of its allocation to provide services directly in the initial two years of the grant program. The county would be required to use the remaining 50 percent of its allocation of state funds to contract with other agencies for the provision of services. For the following two years, the county could use 67.5 percent (50 percent plus 35 percent times 50 percent) of state funds to provide services directly. Counties would have complete discretion over the use of funds beginning in 1988–89.

Provision for Small Counties. Any county that has a population under 40,000 (currently, 16 counties) or that does not receive state family planning funds on the date the proposed legislation is enacted (currently 6 counties) could choose to not accept state funds. In such cases, the department could use that county's share of state funds to contract for

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family planning services in that county.

Eligibility for Services. Counties would be required to provide family planning services to all persons eligible for Medi-Cal benefits. Each county could determine its own eligibility standards for family planning services provided to non-Medi-Cal eligible persons.

Reporting and Audit Requirements. Each county would have to maintain records available for audit by the state and submit reports to the state containing "minimal data" regarding the program.

State Staff. The department proposes to continue five positions at the state level needed to implement the family planning grants. State staff would include one half-time nurse consultant, one health planning analyst, one half-time research analyst, one statistical clerk, one account clerk, and a typist.

More Information Needed

We withhold recommendation on the family planning grant proposal pending receipt of the proposed implementing legislation and additional information regarding the grant proposal.

Our review of the family planning grant program indicates that the concept has merit. For example, under the new program:

- Responsibility for administering local family planning programs and selecting local providers would be assigned to that level of government best able to oversee program operations.
- Counties would be able to reallocate funds to or from direct services or redistribute funds among geographic areas to meet local needs.
- Local family planning programs could be integrated with other local maternal and child health programs to achieve administrative savings and better program coordination, because counties would not need to comply with state program regulations.
- Reporting and auditing requirements would be reduced.
- The state would experience savings in administrative expenditures because not as many state staff would be needed to administer programs. These funds would be allocated to counties where they would be available for additional services.

We cannot, however, recommend approval of the proposal at this time, for three reasons: (1) the proposed legislation that would implement the program was not available at the time this *Analysis* was prepared, (2) the Legislature needs additional information in order to evaluate the proposal, and (3) our analysis identified significant problems related to the proposed allocation methodology and current family planning program activities that have statewide significance and should be resolved before legislative action. Consequently, we withhold recommendation on the proposal, pending review of the proposed legislation and receipt of additional information. We recommend that the department submit to the Legislature additional information that clarifies the proposal and addresses the problems that our review has identified.

Additional Information Needs. In order to facilitate legislative review of the family planning grant program proposal, we recommend that the department submit to the fiscal committees, by April 1, 1984, a response to the following questions:

1. ***Will increased local costs to administer the grant program reduce the level of dollars available for services?*** Some counties might experi-

ence difficulties providing services now provided by state staff because they lack the resources needed to perform certain administrative functions effectively. For example, depending on how they organized their programs, counties would be required to develop and negotiate their own contracts, establish claims payment systems, and develop reporting and auditing requirements for the local agencies with whom they contract. Under the grant proposal, state administrative savings of $890,000 (full year) would be transferred to the counties. This amount represents 3.1 percent of total state expenditures on family planning services. We have no basis for determining whether these additional funds would fully offset increased county administration costs. Consequently, we cannot determine whether the proposal would result in an increase, decrease, or no change in the level of dollars available for services.

2. ***Will the state's fiscal interests be protected under the family planning grant proposal?*** The current target populations for state-funded family planning services are women aged 15–44 whose family income falls below 180 percent of the federal poverty level and sexually active teenage women with higher family incomes. Under the grant proposal, counties would establish their own eligibility requirements and specify the scope of services to be provided. Because family planning services may be unpopular in some areas, some counties might choose to impose restrictive eligibility requirements or reallocate funds to county administration rather than direct services. In this case, the state might experience increased Medi-Cal, welfare, and other costs associated with unwanted pregnancies.

3. ***Will the program's reporting and auditing requirements be sufficient to (a) provide adequate information for legislative decision-making and (b) assure that funds are spent according to legislative intent?*** The proposal indicates that the department will require reports from county programs and will audit expenditures by counties. The proposal does not provide any details on the contents of the reports or the purposes of the audits. The Legislature needs information from county programs to determine how effectively and efficiently General Fund resources are being used and to set future policy directions. Without audits, the Legislature cannot be assured that the family planning funds are being spent in accordance with legislative intent or that unused or improperly used funds will be recovered by the state.

4. ***What workload and responsibilities will the five positions proposed for continuation at the state level have?*** The budget proposes to create a family planning unit consisting of five positions in the Community Health Services Division. Because we do not know (a) the number of counties that would choose not to administer their own programs and (b) the level of reporting requirements and state administrative review that would be required under the proposal, we do not know if this level of staffing would be sufficient to meet the requirements of the program.

Problems with the Proposal. Our review has identified two significant problems with the proposal that should be resolved prior to legislative action. We recommend that the department address these problems when it submits additional information regarding the proposal.

1. ***Funding Allocations.*** Our review of the proposed plan for allocating family planning funds to counties shows that allocations based on historical spending levels, as proposed by the department, are not consistent with the distribution of estimated need among counties. As a measure of estimated need, we used the number of women aged 15 to 44 whose

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family income falls below 180 percent of the federal poverty level, plus the number of sexually active teenage women at higher income levels estimated in the "Office of Family Planning Statistical Report, 1979 and 1980." We calculated allocations to counties based on the distribution of the target population among counties and compared these allocations to the allocations proposed by the department. We then calculated the ratio between the proposed allocations and the allocations based on "need," for each county.

Table 11 shows the distribution of the funding ratios for the 58 counties. Seven counties would receive allocations that are more than 150 percent of the amount they would receive based solely on target population. Twelve counties would receive allocations that are less than 51 percent of the amount they would receive based solely on target population. These numbers increase slightly when federal and private funds are considered.

Table 11

Family Planning Grant Proposal Funding Allocations
Ratio of Amount Received Under Department's Proposal to Amount Received Based on Percent of Target Population

Amount Received Under Department's Proposal As a Percentage of the Amount Received Based on Share of Target Population	*Number of Counties*		
	State and State Funds	*Federal and Federal[a] Funds*	*State Private Funds*
0–50 percent	12	13	13
51–90 percent	20	15	15
91–110 percent	8	9	11
111–150 percent	9	12	9
151 percent and over	7	7	8
Totals[b]	56	56	56

[a] Federal funds reflect federal Title X allocations. Private funds reflect Planned Parenthood grants and fundraising.

[b] There are 58 counties in California. Del Norte/Humboldt and Yuba/Sutter (until 1982–83) combine to provide public health services.

The differences between the proposed allocation (based on the historical allocation of funds) and the allocation based on each county's share of the target population are due to two factors:

- Existing allocations of service dollars do not always reflect need, due to differences in the availability of providers and other factors.
- Information, education, and certain other programs are provided on a regional basis. Consequently, a county's historical allocation may reflect funds not used to provide direct services.

2. ***Programs of Statewide Significance.*** Under the grant proposal, funds currently used for specialized family planning programs that are provided most efficiently on a statewide or regional basis would be eliminated. For example, the state funds a nurse practitioner training program to increase the number of trained staff available to contractors. The state is also establishing a program to purchase contraceptive supplies and pharmaceuticals in volume, thereby making additional dollars available for services. Termination of these programs could cause reductions in the quality, and an increase in the costs, of services under the program.

As part of the Public Health Enhancement program proposal, the department proposes continued state administration of funds for certain regional programs. A similar arrangement may be warranted for the family planning program.

C. COUNTY HEALTH SERVICES

The budget proposes $859,303,000 (all funds) for support of the Office of County Health Services and Local Health Public Assistance, excluding administrative overhead. This is an increase of $18,827,000, or 2.2 percent, above estimated current-year expenditures. Local assistance is proposed in the amount of $857,094,000, which is $18,781,000, or 2.2 percent, higher than estimated current-year expenditures. Department support is proposed in the amount of $2,209,000, which is $46,000, or 2.1 percent, above estimated current-year expenditures. Table 12 displays proposed local assistance expenditures.

Table 12
County Health Local Assistance
Expenditures and Funding Sources
1982–83 through 1984–85
(in thousands)

	Fund	Actual 1982–83	Estimated 1983–84	Proposed 1984–85[a]	Change Amount	Change Percent
Local government fiscal relief (AB 8)	General	$364,728	$367,708	$376,289	$8,581	2.3%
County public health projects (SNAP)	CHSF	2,863	2,200	2,200	—	—
Reversions	—	−5,200	−10,235	—	10,235	N/A
Local health capital expenditures	LHCEA	1,000	—	—	—	—
Public health subvention	General	705	705	705	—	—
	Federal	470	466	466	—	—
Subtotals	All	$364,566	$360,844	$379,660	$18,816	5.2%
Medically indigent services	General	$259,681	$477,434	$477,434	—	—
Los Angeles County payment delay	General	−200,000	—	—	—	—
Totals	All	$424,247	$838,278	$857,094	$18,816	2.2%
General Fund		*$425,114*	*$845,847*	*$854,428*	*$8,581*	*1.0%*
Federal funds		*470*	*466*	*466*	—	—
County Health Services Fund		*2,863*	*2,200*	*2,200*	—	—
Local Health Capital Expenditure Account		*1,000*	—	—	—	—
Reversions		*−5,200*	*−10,235*	—	*10,235*	*N/A*

[a] Does not include repayment of $200 million to Los Angeles County pursuant to Ch 1594/82, which is reflected in Item 9660.

The local assistance increase proposed for 1984–85 is due to three factors:

- An increase of $8,372,000 for AB 8 local fiscal relief to reflect increased population and provide a 2 percent cost-of-living adjustment.
- An increase of $10,235,000 because reversions of AB 8 funds in the current year will not occur in the budget year.
- A transfer of $209,000 from department support to AB 8 local fiscal relief.

The budget proposes a staffing level of 38.9 positions for the Office of

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County Health Services and Local Public Health Assistance—a decrease of 3.6 positions from the current year. The reduction in staffing reflects (1) the deletion of 2 public health nurse positions in the Local Public Health Assistance Unit and (2) the termination of 1.6 limited-term positions.

Local Government Fiscal Relief (AB 8)

Enactment of AB 8 in 1979 put in place a new program providing fiscal relief to local agencies as a means of replacing property tax revenues lost by these agencies as a result of Proposition 13 (1978). A portion of this fiscal relief is appropriated to the County Health Services Fund, which was created by the act, for distribution by the department to support local health services. The funds are distributed as follows:

1. Three dollars per capita, adjusted for inflation, is allocated to counties that submit a plan and budget to the department.
2. An amount up to 50 percent of 1977–78 net county costs for health services above $3 per capita, adjusted for inflation, is allocated to counties that sign an agreement with the department director. The agreement commits the county to (a) match state funds on a dollar-for-dollar basis and (b) spend funds in general accordance with the county's health services plan and budget.
3. If a county's proposed expenditures are less than the amount required to obtain the maximum allocation, additional funds can be allocated if the county demonstrates that it did not detrimentally reduce its health services. Counties cannot receive matching funds that exceed 60 percent of budgeted county costs above the per capita allocation, unless that county is experiencing severe financial hardship, as determined by the director of the department in consultation with the Department of Finance.
4. Unspent funds are (a) reallocated to counties in accord with guidelines established by the Legislature in Budget Act language, (b) deposited in the Local Health Capital Expenditure Account for purposes of local health capital outlay projects, or (c) reverted to the General Fund, depending on the source and amount of the unused funds.

The annual inflation adjustment specified by AB 8 is the percentage increase in the California Consumer Price Index during the prior calendar year (December to December).

Assembly Bill 8 Population and Cost-of Living Adjustments

The companion bills to the Budget Bill, AB 2314 and SB 1379, include sections deleting the provisions of AB 8 that establish the appropriations level for county health services. In lieu of the statutory amount, the budget proposes an appropriation of $376,289,000 for these services. This is $8,581,000, or 2.3 percent, above estimated current-year expenditures. The proposed amount for 1984–85 reflects the following assumptions:

1. ***Population Adjustment.*** The budget includes $994,000 for a projected 2 percent increase in population.
2. ***County Opt-Out Adjustment.*** The budget shows an increase of $209,000 in the maximum allocation available to Tehama County under AB 8. These funds were transferred from the contract counties program, through which the state provides public health services directly for small rural counties. Section 1157.5 of the Health and Safety Code allows counties participating in the contract counties program to receive funds in lieu of state-funded positions.

3. *Cost-of-Living Adjustment (COLA).* The budget proposes $7,378,000 to provide a 2 percent COLA. We estimate that a 5.55 percent increase is required by existing law (AB 8) given the rate of inflation between December 1982 and December 1983. The cost of providing a 1 percent increase in the base expenditure level proposed in the budget (that is, 1983–84 expenditures plus increases for population and the opt-out adjustment) is $3,689,000. Consequently, we estimate that the cost of providing county fiscal relief at the statutory level would be $389,570,000 in 1984–85. This is $13,097,000 more than the amount proposed in the budget.

County Share Reductions

Under current law, a county may receive AB 8 funds on a 60 percent state, 40 percent county basis, instead of a 50 percent state, 50 percent county basis, if it demonstrates that it did not detrimentally reduce its health services. A county proposing to reduce its matching ratio must hold a public hearing to determine (1) whether the reduction is detrimental to the health needs of the public in the case of public health services or detrimental to the health care needs of indigents in the case of outpatient or inpatient health services and (2) whether the reduction would impair the county's ability to fully implement its county health services plan. The county must then determine that the reduction is not detrimental, based on the public hearing, and transmit its findings to the department Director for final review. If the Director concurs with the county, the county may receive AB 8 funds at the reduced matching ratio. Through 1982–83, the Director had concurred with the counties' findings in 48 out of 49 cases.

A county may also reduce its matching ratio if the Director of Health Services, in consultation with the Department of Finance, determines that the county is in extreme financial distress. Thus far, no county has proposed to reduce its allocation under this provision.

Medically Indigent Services

The 1982 Medi-Cal reform legislation eliminated the medically indigent adult (MIA) category of Medi-Cal recipients, effective January 1, 1983. Eligibility for state-funded benefits, however, was continued for (1) refugees with up to 18 months of residency, (2) women with confirmed pregnancies, and (3) adults residing in skilled nursing or intermediate care facilities. Under Welfare and Institutions Code Section 17000, health care for persons previously classified as MIAs is now a county responsibility. Counties with a population under 300,000 *may* administer their own programs or contract with the County Medical Services program (CMSP) in the Office of County Health Services for program administration ("CMSP counties"). Counties with a population over 300,000 *must* administer their own programs ("independent counties").

The reform legislation established subventions to assist counties in providing health care services to medically indigent persons. The amount available for subventions is determined annually in the Budget Act. Each county's share of available state funds is determined by the county's percentage of total statewide Medi-Cal expenditures for MIAs during 1979–80, 1980–81, and 1981–82. The funds are distributed to counties on a monthly basis through the Medically Indigent Services (MIS) Account, a special account of the County Health Services Fund. To receive MIS payments, a county must (1) expand its county health services plan (required under AB 8) to include information on the criteria and procedures it uses in

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determining a person's eligibility for services and the types of services provided and (2) spend no less for county health services than the amount required to obtain the county's maximum AB 8 allocation.

Budget Proposal. The budget proposes $477,434,000 from the General Fund for support of the Medically Indigent Services (MIS) program. This is the same level of expenditures estimated for the current year. The Governor does not propose to provide a cost-of-living adjustment (COLA) to the MIS program because "the current level of funding is sufficient to meet the projected demand in 1984–85." A 2 percent COLA, consistent with other preventive health COLAs, would increase MIS expenditures by $9,549,000.

Currently, 31 counties operate independent programs and 27 counties participate in the CMSP. Under current allocation procedures, the 31 independent counties will receive $441.9 million, or 93 percent, of the proposed budget-year appropriation. The 27 CMSP counties will receive $34.4 million, or 7 percent, of the total amount.

Program Status—Independent Counties

The department currently is compiling a "fact book" that will document in detail the scope and level of services now being provided in each county's MIS program. The department intends to complete the fact book by March 1984.

To be able to advise the Legislature on matters related to the MIA transfer, we visited the MIS programs in seven independent counties that are receiving approximately 55 percent of total MIS funding in the current year. Our review of the MIS programs in these seven counties left us with three main impressions:

1. Program utilization in the first 10 months of implementation was significantly lower than originally anticipated.
2. County programs vary tremendously in design and operation.
3. The differences in program implementation and operation will make it difficult, if not impossible, for the Legislature to obtain comparable information from the counties on the number of persons served and the level and scope of medical services provided.

Utilization Lower than Anticipated. Based on reports from counties, utilization of county health services by medically indigent persons during the initial 10 months of the program was significantly lower than originally anticipated. Our analysis indicates that there are two primary reasons for the lower-than-anticipated utilization levels:

- ***Medi-Cal Estimates Not Transferable.*** At the time of the transfer, the department provided information on the number of MIAs historically served by the Medi-Cal program in each county. Most counties used these numbers as the basis for estimating their own MIS program needs. The Medi-Cal estimates, however, had a number of shortcomings that resulted in the counties overestimating utilization. For example, the Medi-Cal data (1) included categories of MIAs that remained eligible for Medi-Cal and (2) did not account for a number of persons that remained eligible for Medi-Cal pending hearings on their termination from the program.
- ***Provider Choice Restricted.*** Under Medi-Cal, MIAs had a choice of service providers. Under the county programs, indigent persons do not have free choice of provider. Instead, counties utilize their own

hospitals or, where necessary, contract with a limited number of providers. In some cases, these contracts do not include providers that previously had served a large number of Medi-Cal MIA patients.

Apparently, the restrictions on provider choice have caused many indigent persons to reduce or delay utilization of services or obtain the resources needed to pay the provider of choice for services. It is also possible that the amount of bad debt incurred by private hospitals and other providers has increased due to the MIA transfer.

Utilization of the MIS program has increased in recent months. It is too soon to tell if it will reach the originally projected levels.

Program Design and Operation. Our review of the MIS program has shown a number of differences in the MIS program design and operations among counties. We discuss these differences below.

- ***Extent of Integration with Existing County Programs.*** Prior to the MIA transfer, the range of medical services provided to the indigent population varied by county. A similar variation in service availability has arisen under the MIS program. In some areas, such as San Francisco and Los Angeles, the MIS program has been integrated into the existing mechanisms for providing health care to indigents under Section 17000 of the Welfare and Institutions Code. Other counties, such as San Diego and Merced, maintain separate programs for the provision of MIS services.
- ***Financial Eligibility.*** Many counties require a financial eligibility screening to determine ability to pay and then bill for services according to that determination. In some cases, persons eligible for MIS support were separately identified. In other counties, they were not separately identified or were separately identified only after the patient failed to pay his or her bill. We also found that financial screenings are often significantly more extensive for inpatients than outpatients. Depending on the county, the financial screening may be performed by (1) the county health department, (2) the county welfare department, or (3) an individual provider.
- ***Prior Authorization for Treatment.*** The extent to which different MIS programs require prior authorization for service provision varies among counties. Merced, for example, has a medical review board that authorizes all inpatient services other than emergency services. Other counties employ varying degrees of prior authorization requirements, often depending on the type of service.
- ***Risk Agreements.*** Independent counties are at risk for overexpenditures in their MIS programs. Some counties have put health care providers at risk through contracts. For example, in contracting out for 100 percent of MIS program services, San Diego has transferred all risk to the contractors. Conversely, counties providing all services in their own facilities are entirely at risk for program overexpenditures.
- ***Program Records.*** Maintenance of detailed program records varies among counties, generally depending on how the program has been implemented. Counties that fully integrate their MIS programs with existing health care services may not have the capability to separately tabulate data on MIS patients. This is true in San Francisco. Other counties, such as Merced, keep separate counts of MIS patients. Counties that contract for services may require such information from their contractors for billing, monitoring, or audit purposes.

DEPARTMENT OF HEALTH SERVICES—Continued

- *Scope of Services.* The scope of medical services available varies significantly among counties. In some areas, MIS funds are used for services provided only in life-threatening situations as defined by the county or, in some cases, individual (contracted) providers. In contrast, other counties provide a broad range of services, including extensive outpatient services. In some counties, all potential MIS patients are screened for medical eligibility (as determined by the county). In other counties, medical eligibility screening, as financial screening, may be vastly different for outpatient and inpatient services.

Requirements for Legislative Decision-Making. Many counties have integrated their MIS programs with other health programs that provide similar or complementary services, for administrative and fiscal reasons. Due to this integration of records and fiscal information, it is difficult, if not impossible, to obtain comparable information across counties on the number of persons served and the level and scope of medical services provided. As a result, the information that will be available to the Legislature will be of limited value when the Legislature makes decisions on (1) the basic policy direction for the program, (2) any funding changes that may be required by increases in workload, (3) the size of the cost-of-living increases that should be granted, and (4) the allocation of funding among counties.

Program Status—Counties Participating in the CMSP

The County Medical Services program (CMSP) provides health services to persons formerly classified as MIAs in counties with a population below 300,000 that choose to contract with the state. MIS payments to counties participating in the CMSP are deposited directly in the CMSP Account in the County Health Services Fund. The original legislation provided that the state would be at risk for any costs above the amounts deposited in the account until June 30, 1983. As a condition for accepting the risk, the state may require that participating counties adopt uniform eligibility criteria and benefits. Chapter 530, Statutes of 1983 (AB 490), extended the period under which the state would remain at risk until June 30, 1984. Consequently, the participating counties will be at risk for any costs in excess of the amounts deposited in the special account, beginning in 1984–85.

The department, in consultation with the counties, decided to model the CMSP on the Medi-Cal program. Specifically, the CMSP (1) determines eligibility using an eligibility determination process similar to Medi-Cal's, (2) provides services through Medi-Cal providers, and (3) uses the Medi-Cal claims processing system.

Six Counties Change Original Choices. Thirty-four of the 43 counties with populations under 300,000 originally chose to contract with the state to administer their MIS programs. Since that time, three counties (Lake, Santa Barbara, and Placer) chose to administer independent programs beginning July 1, 1983, two counties (Santa Cruz and Mendocino) chose independence beginning October 1, 1983, and one county (Sutter) chose to participate in the CMSP beginning October 1, 1983.

CMSP Reserve. The Medi-Cal reform legislation allows the Governor to use any unexpended funds in the CMSP Account to establish an operating reserve for the purposes of the program, provided he displays

these funds as a separate line item in the budget. The 1984–85 budget identifies operating reserves of $2.1 million on June 30, 1983, $3.3 million on June 30, 1984, and $4.5 million on June 30, 1985. These figures are based on the department's preliminary estimates of the amounts of unexpended funds remaining from the 1982–83, 1983–84, and 1984–85 appropriations after all service liabilities are liquidated. The figures could change significantly because (1) the program is new and consequently utilization estimates could be incorrect and (2) due to billing lags, complete expenditure data are not available until 18 months after the close of the fiscal year in which services are provided.

Providers Reimbursed at 100 Percent. In 1982–83, the amount available for health care services provided through the CMSP was approximately 70 percent of projected state expenditures for health care provided under Medi-Cal to MIAs. To insure that the CMSP would stay within its budget, the department, in consultation with participating counties, developed a package of service benefit and provider rate reductions designed to achieve the necessary savings. As part of this plan, the CMSP originally anticipated reimbursing providers at 85 percent of Medi-Cal rates. Because utilization of the program has been lower than initially estimated, however, the CMSP has been able to continue to reimburse CMSP providers at the same level as Medi-Cal. The program will continue this level of reimbursement until such time as it determines reductions are necessary to keep within authorized funding levels.

Contracting for Hospital Inpatient Services

We recommend the enactment of legislation allowing the CMSP to reimburse hospitals that contract with Medi-Cal at Medi-Cal contract rates.

We estimate that the CMSP annually pays for approximately 27,000 days of hospitalization for eligible persons, at a cost of approximately $16 million. Claims for these services are reimbursed by the Medi-Cal fiscal intermediary, based on *cost-based rates* established by the Medi-Cal program.

Our review of CMSP hospital inpatient expenditures indicates that significant savings could be achieved by reimbursing hospitals that contract with Medi-Cal using the *contract rates* instead of the cost-based rates. We found that 25 percent of these expenditures, or approximately $4 million, are made to hospitals currently under contract with Medi-Cal. We also determined that had the CMSP reimbursed these hospitals using contract rates rather than cost-based rates, there would have been a savings of approximately 15 percent, or $615,000 annually.

We therefore recommend the adoption of legislation allowing the CMSP to reimburse hospitals under contract with Medi-Cal at Medi-Cal contract rates. Any savings resulting from this change would remain in the CMSP Account and be available to pay for other services provided by the program.

Unused County Health Services Funds

Savings that occur in county health services funds are recouped by the state. Formerly, unused funds were allocated to counties according to "special needs and priorities" (SNAP), as determined by the department Director. Under Ch 323/83, unused funds (1) may be appropriated by the Legislature in the annual Budget Act for one-time county public health projects, (2) may be appropriated by the Legislature in the annual Budget Act for state administration related to the one-time projects, (3) are trans-

DEPARTMENT OF HEALTH SERVICES—Continued

ferred to the Local Health Capital Expenditure Account (LHCEA) for local capital outlay projects, or (4) revert to the General Fund, depending on the source and amount of funds.

Savings occur in the following circumstances:

1. ***AB 8 Funds.*** Savings can occur because counties fail to apply for their full AB 8 allocations or counties do not spend their full allocations. These savings are identified by the department (a) during review of the county's AB 8 plan and budget, (b) following AB 8 hearings, (c) during review of the county's "estimated actual" expenditure report, (d) during review of the county's final expenditure report, or (e) through department audits. Funds recovered after three years are reverted to the General Fund and are not available for reallocation.

The department has recently completed a pilot project involving audits of five independent counties. In these counties, $1.5 million in potential recoupments were identified. As a result of the success of the pilot project, the department proposes in the budget to establish an AB 8 audits unit to audit all county AB 8 expenditures from 1979–80 through 1982–83. The department estimates recoupments from these audits of up to $10 million annually. We discuss this proposal under the Audits and Investigations program.

For counties operating independent medically indigent services (MIS) programs, it is unlikely that any savings will occur from AB 8 funds appropriated in 1982–83 or later because the counties must receive their full AB 8 allocations in order to receive MIS funds.

2. ***MIS Funds—County Medical Services Program (CMSP) Counties.*** Savings can occur when the CMSP does not fully expend the allocations made to it on behalf of participating counties. Due to billing lags, complete expenditure data are not available until 18 months after the end of the fiscal year in which the funds were appropriated.

3. ***MIS Funds—Independent Counties.*** Savings occur when counties do not spend their full allocations. MIS program savings are identified by the department in its reviews of county expenditures, concurrent with AB 8 reviews.

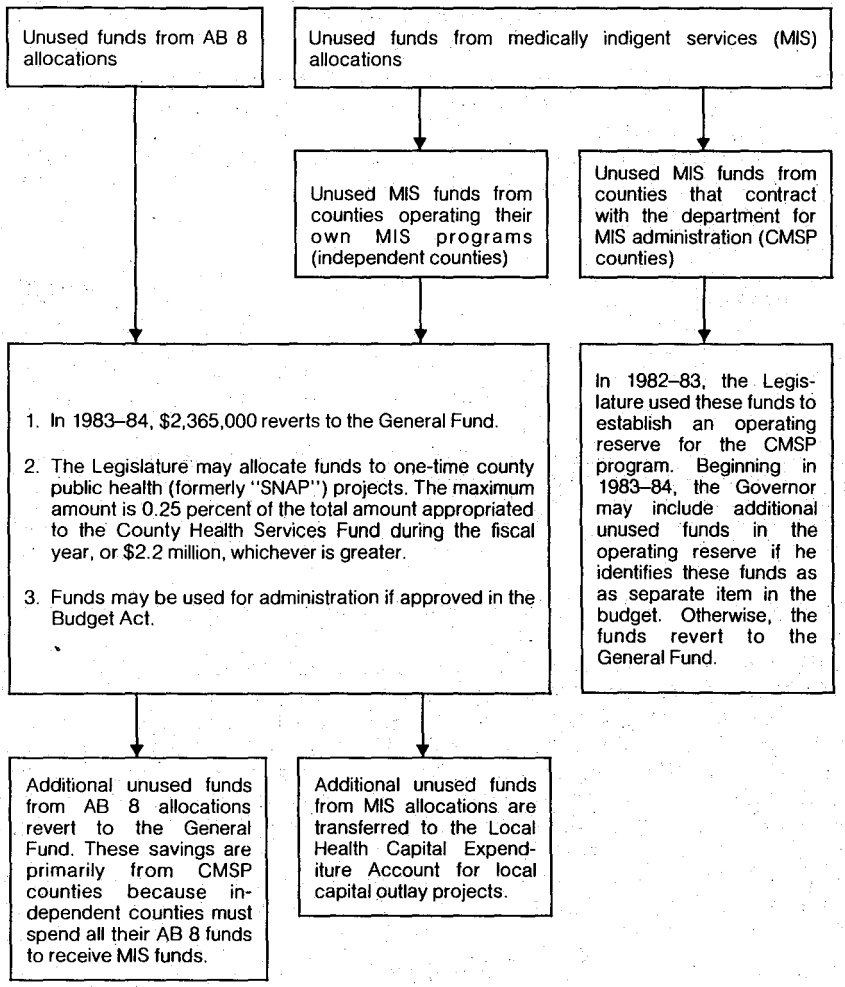
During any given year, the department may identify unused funds originating from appropriations in several different fiscal years. Chart 3 displays the procedure for determining how unused funds identified in any fiscal year are allocated.

Recoupment and Allocation of Unused County Health Services Funds

Since the enactment of AB 8, the department has allocated a total of $46,193,000 in unused county health services funds. This amount includes (1) *actual* recoupments of $23.3 million from appropriations made in 1979–80 through 1981–82 and (2) *estimated* unused funds of $22.9 million from appropriations made in 1982–83 through 1984–85. It does not include recoveries of MIS or AB 8 funds from the 1984–85 appropriation other than $1.2 million in estimated unused CMSP funds.

It is likely that additional funds will be recouped as a result of (1) additional expenditure reports submitted by counties and (2) the activities of the proposed audit unit. Recoveries from these audits are estimated at up to $10 million annually.

Chart 3
Procedure for Allocating Unused County Health Services Fund Monies [a]



[a] This procedure is followed each fiscal year to allocate funds identified in that year. The identified funds originate from appropriations made in that year and earlier years.

DEPARTMENT OF HEALTH SERVICES—Continued

Table 13 shows recoupments, by year of appropriation, and allocations, by year of allocation.

Table 13
Allocation of Unused County Health Services Funds
Identified as of January 24, 1984 [a]
1979–80 through 1984–85
(in thousands)

	Actual 1979–80	*Actual 1980–81*	*Actual 1981–82*	*Actual 1982–83*	*Estimated 1983–84*	*Proposed 1984–85*	*Totals*
1. Unused county health services funds, by year of appropriation	$3,615	$9,037	$10,634	$11,758	$9,926	$1,223	$46,193
As percent of appropriation	1.1%	2.9%	3.0%	1.9%	1.2%	0.1%	1.4%
2. Allocation of unused county health services funds, by year of allocation							
County public health projects	—	$876	$1,799	$2,863	$2,200	$2,200	$9,938
Department administration	—	—	651	97	—	806	1,554
LHCEA	—	—	—	—	4,329	6,500	10,829
CMSP operating reserve	—	—	—	2,058	1,226	1,223	4,507
General Fund reversions	—	—	—	8,324	11,041	—	19,365
Totals	—	$876	$2,450	$13,342	$18,796	$10,729	$46,193

[a] The table reflects actual recoupments except for the following estimates: (1) $9 million from 1982–83 appropriation identified in 1983–84, (2) $8 million from 1983–84 appropriation identified in 1984–85, and (3) amounts available for CMSP operating reserve identified in same year as appropriation. It is likely that additional monies will be recouped as a result of (1) submission of additional county expenditure reports and (2) the activities of the proposed AB 8 audit unit.

County Public Health Projects—Formerly "Special Needs and Priorities" (SNAP)

Under current law, expenditures from unused funds for county public health projects are limited to 0.25 percent of the amount appropriated to the County Health Services Fund, or $2.2 million, whichever is greater. The law provides that the department shall allocate these funds according to priorities established by the Legislature in the annual Budget Act. Counties must match these funds on a one dollar county-one dollar state basis, except in public health emergencies and for projects involving distressed county hospitals.

Table 14 presents the expenditure categories established in the law and the amount specified for each in the 1983 Budget Act and the 1984 Budget Bill.

Table 14
Expenditures for County Public Health Projects
1983–84 and 1984–85

Public health emergencies	$500,000
Distressed county hospitals	350,000
Refugee health programs	450,000
Computerization of county information processing	250,000
County-clinic linkage projects	250,000
Elderly care projects	400,000
Total	$2,200,000

Local Health Capital Expenditures

We recommend that the department (1) explain at budget hearings why $10,829,000 in unused MIS funds are not proposed for expenditure through the Local Health Capital Expenditure Account (LHCEA) per current law and (2) develop a spending plan for LHCEA funds. We recommend that the Legislature appropriate these funds through the Budget Bill to assure greater legislative control of expenditures. We further recommend that $441,000 in interest income in the LHCEA be reverted to the General Fund.

Chapter 1351, Statutes of 1980 (AB 3245), established a program to (1) provide financial assistance to local jurisdictions to fund capital expenditures for local health facilities and equipment and (2) defray the department's administrative costs in providing technical assistance to local jurisdictions relative to financing such capital improvements. The act appropriated $25 million from the Special Account for Capital Outlay to the LHCEA, which was created by the act, for purposes of the program.

Due to delays in hiring staff, developing criteria, and selecting projects, no grants or loans were awarded until November 1981, when 79 projects were selected for funding. Of these projects, 61 will be completed by 1983–84, 15 will be completed during 1984–85, and 3 will be completed during 1985–86. The budget indicates that $24 million of the $25 million appropriation was allocated to counties in 1981–82 and that the remaining $1 million was allocated in 1982–83.

New Funds for Capital Outlay. Beginning in the current year, a portion of unspent county health services funds is allocated to the LHCEA for county capital outlay projects. The LHCEA fund condition statement included in the budget shows a 1984–85 surplus in the LHCEA of $11,053,000. This amount includes $10,829,000 transferred from the Medically Indigent Services (MIS) Account ($4,329,000 in 1983–84 and $6,500,000 in 1984–85) and $441,000 in interest income from LHCEA investments, less $217,000 proposed for administrative expenditures in 1984–85. The budget indicates that there will be no expenditures of LHCEA funds for local assistance in either the current year or the budget year.

Under current law, funds recouped from unspent MIS allocations to independent counties above a certain amount are required to be deposited in the LHCEA and used for new projects or related department administration. Funds earned from interest or income on LHCEA funds are required to be reverted to the General Fund. We recommend that at budget hearings the department (1) explain why $10,829,000 in unused MIS funds in the LHCEA are not proposed for expenditure and (2) develop and present a spending plan for LHCEA funds.

We recommend that the funds in the LHCEA not utilized for administrative expenses be appropriated through the Budget Bill in Item 4260-111-900 and that funds in the LHCEA utilized for administrative expenses be appropriated through the Budget Bill in Item 4260-001-900. This would not increase state spending but would increase legislative control and oversight of this fund. We further recommend that $441,000 in interest income earned on LHCEA funds be reverted to the General Fund.

DEPARTMENT OF HEALTH SERVICES—Continued

Los Angeles County Payment Delay

The budget reflects expenditures of $200 million for payment to Los Angeles County in June 1985, pursuant to the Medi-Cal reform legislation (Ch 1594/82). This allocation is not reflected in the department's expenditure totals but is included under a new item, Item 9660.

As a means of providing transition funding for the MIA transfer, Chapter 1594 granted $200 million to Los Angeles County, payable in June 1985, in lieu of $200 million in AB 8 and medically indigent services (MIS) payments that the state would otherwise have had to make to Los Angeles County in 1982–83. The act authorized Los Angeles County to sell grant anticipation notes using the state grant as security. Funds raised from the sale of the notes were to be used to replace the AB 8 and MIS funds. The act further required the state to make its AB 8 and MIS payments to Los Angeles County in July of the fiscal years 1983–84 and 1984–85 instead of throughout the fiscal year.

D. COMMUNITY HEALTH SERVICES

The budget proposes expenditures of $128,255,000 for community health services programs, excluding administrative overhead. This is an increase of $9,448,000, or 8 percent, above estimated current-year expenditures of $118,807,000.

Support expenditures are proposed at $11,055,000, which is $41,000, or 0.4 percent, more than estimated current-year expenditures. This change reflects an $861,000 decrease in personal services expenditures and a $902,000 increase in operating expenses. The personal services decrease stems largely from the reduction of 83 positions in connection with the implementation of the Public Health Enhancement program (PHEP) and the Family Planning Grant program. The increase in operating expenses primarily reflects the proposed implementation of the Neural Tube Defects program, which involves extensive contracts and equipment.

Local assistance is proposed at $117,200,000, which is an increase of $9,407,000, or 8.7 percent, above estimated current-year expenditures. This increase is primarily the result of (1) increased utilization in California Children's Services and the Genetically Handicapped Persons' and Child Health and Disability Prevention programs ($4,514,000), (2) a 2 percent cost-of-living adjustment for most community health services programs ($1,819,000), (3) the transfer of Health Protection program local assistance funds to the PHEP ($1,858,000), (4) the restoration of funds for the Primary Care Clinics program ($450,000), and (5) the transfer of support funds to local assistance under the PHEP and family planning grant proposals ($1,267,000).

Table 15 displays community health services local assistance program expenditures.

In this section, we discuss California Children's Services, the Genetically Handicapped Persons' program, and the Primary Care Clinics program. The Public Health Enhancement program and the Family Planning Grant program are discussed earlier in the analysis.

Table 15
Community Health Local Assistance
Expenditures and Funding Sources
1982–83 through 1984–85
(in thousands)

	Fund	Actual 1982–83	Estimated 1983–84	Proposed 1984–85	Change Amount	Change Percent	Funds Included in PHEP
A. Family planning	General	$37,627	$28,138	$29,155	$1,017	3.6%	—
B. Maternal and child health (MCH)	All	15,507	16,043	8,760	−7,283	−45.4	$8,279
Infant dispatch	General	217	217	111	−106	−48.8	111
Perinatal access	General	706	787	401	−386	−49.0	401
High-risk infant follow-up	General	756	756	386	−370	−48.9	386
	Federal	200	200	100	−100	−50.0	100
Perinatal health	General	1,412	1,452	741	−711	−49.0	741
Primary care clinics	General	940	504	958	454	90.1	—
MCH grants	Federal	11,276	12,127	6,063	−6,064	−50.0	6,063
C. Genetic disease	General	1,568	1,570	1,601	31	2.0	—
Sickle cell	General	503	503	513	10	2.0	—
Prenatal counseling	General	611	612	624	12	2.0	—
Tay-Sachs	General	454	455	464	9	2.0	—
D. California children's services							
Genetically handicapped persons	All	4,968	5,403	5,916	513	9.5	—
	General	4,895	5,333	5,846	513	9.6	—
	Repayments	73	70	70	—	—	—
California children's services	All	46,267	49,143	53,371	4,228	8.6	—
	General	37,663	37,718	42,699	4,981	13.2	—
	Federal	7,704	10,525	9,922	−603	−5.7	—
	Repayments	900	900	750	−150	−16.7	—
E. Adult day health care	General	250	350	—	−350	−100.0	—
F. Child health and disability prevention	General	8,567	7,146	3,937	−3,209	−44.9	3,937
G. Public health enhancement program	All	—	—	14,460 [a]	14,460	N/A	
	General	—	—	7,637	7,637	N/A	
	Federal	—	—	6,823	6,823	N/A	
Totals		$114,754	$107,793	$117,200	$9,407	8.7%	
General Fund		*$94,601*	*$83,971*	*$93,472*	*$9,501*	*11.3%*	
Federal funds		*19,180*	*22,852*	*22,908*	*56*	*0.2*	
Family repayments		*973*	*970*	*820*	*−150*	*−15.5*	

[a] Includes $1,895,000 previously included in health protection programs and $822,000 proposed for transfer from support to local assistance.

California Children's Services

The California Children's Services (CCS) program manages and funds specialized care and rehabilitation services for physically handicapped children whose families are unable to pay the full cost of these services. The target population for services is persons under 21 years of age with specific catastrophic or severely handicapping conditions whose disabilities may be arrested, improved, or corrected. Services provided under the program include diagnostic evaluations, treatment services, physical and occupational therapy, orthopedic and pediatric clinic services, and medical case management. A family's need for financial assistance is determined based on the total cost of recommended treatment, the ability of the family to pay the cost, and the availability of program funds. Families with an annual income of $40,000 or more are ineligible for services.

DEPARTMENT OF HEALTH SERVICES—Continued

The department estimates that CCS case managers will follow 92,960 patients in the current year and that the program will provide medical services to 28,570 children. Of the children receiving medical services, 8,890 will be funded by the Medi-Cal program and 19,680 will be funded by CCS.

The CCS program is administered jointly by the state and the counties. The state is responsible for overall administration and for establishing program and financial eligibility guidelines. All counties with a population over 200,000 are required to administer their own CCS programs. These counties, called "independent counties," are responsible for case management, claims payment, case finding, and financial eligibility determination. Counties with populations of less than 200,000 may administer the program as an independent county, or may contract with the state for case management and payment of provider claims. The "dependent" counties retain responsibility for case finding and financial eligibility determination. There are 25 independent and 33 dependent counties.

State staff perform three functions: (1) to approve providers used by the program, (2) to allocate funds to counties and process county claims for services funded by CCS, and (3) to perform case management and provider payment functions for the dependent counties. Funds are allocated to counties based on the level of funding provided by the county, workload estimates, and the amount of funds available.

Budget Proposal. The budget proposes $55,316,000 (excluding county funds) for support of the CCS program in 1984–85, excluding administrative overhead. This is an increase of $4,299,000, or 8.4 percent, above estimated current-year expenditures. Local assistance is proposed in the amount of $53,371,000, which is $4,228,000, or 8.6 percent, higher than estimated current-year expenditures. Department support is proposed at $1,945,000, which is $71,000, or 3.8 percent, above estimated current-year expenditures.

Based on assumptions contained in the department's November 1983 estimates, the increase in local assistance funding is primarily due to increases of:

- $820,000 to provide a 6.9 percent adjustment in funding for therapy services, due to increased county costs.
- $2,521,000 to provide a 6.8 percent adjustment in funding for treatment services, due to inflation and increased utilization of services.
- $837,000 to provide a 2 percent cost-of-living increase on General Fund expenditures.

The budget proposes a staffing level of 60.5 positions for CCS, which is the same number of positions authorized for the current year.

Growth in California Children's Services Expenditures

The California Children's Services (CCS) program has experienced significant increases in expenditures in recent years. During the period 1978–79 to 1984–85, CCS local assistance expenditures will grow from $26,425,000 to $53,371,000, an increase of 102 percent. In contrast, total General Fund local assistance expenditures during the same period will grow by 45 percent. The increase is attributable to the following factors:

Inflation. Inflation has increased the costs of all goods and services since 1978–79. The rise in the costs of medical services, however, has exceeded the general rate of inflation. Since 1967, the Consumer Price

Index for medical care has significantly outpaced inflation for all other goods and services with the exception of energy products and home ownership. Approximately 70 percent of CCS expenditures currently are for inpatient and outpatient medical costs.

Technology. A second factor that has had a significant impact on CCS expenditures is the development of new medical treatments. Where many premature babies in the past did not survive their first week of life, new technology has greatly extended the potential life span of such babies today. Currently, bone marrow transplants and liver transplants are experimental treatments that soon may be routinely financed by the CCS program. In fact, the Governor recently authorized CCS payment for a single bone marrow transplant that is estimated to cost approximately $100,000. The development of new technology has had a particularly dramatic impact on CCS expenditures, because the program pays primarily for specialty care and covers virtually all catastrophic diseases affecting children. It is no longer unusual to have daily expenditures for neonatal intensive care unit patients of $5,000 per day or to incur costs of $300,000 to $600,000 for one child. Orange County determined that the number of individual cases costing in excess of $40,000 increased from four in 1980–81 to 12 in 1982–83, a three-fold increase in just two years.

Current-Year Deficit

The budget document and the department's November estimate indicate that if current-year expenditure trends continue, CCS expenditures will exceed available funds by $4,036,000 in 1983–84. The department intends to use federal maternal and child health (MCH) block grant monies to fund this shortfall. At the time this *Analysis* was prepared, the Legislature had not received official notification that increased federal funding had been authorized for CCS, as required under Section 28 of the 1983 Budget Act.

The budget for the current year, as introduced, contained $43,987,000 for CCS—$37,816,000 from the General Fund and $6,171,000 from federal block grant funds. In the May revision, the Department of Finance proposed an increase in this amount of $4,641,000, due to caseload and cost increases partially offset by savings resulting from a new policy of requiring all CCS participants to apply for Medi-Cal. To fund the additional amount, the Department of Finance proposed to increase federal funds by $4,739,000 and reduce the General Fund appropriation by $98,000. The federal funds represented one-time money carried over from prior fiscal years and PL 97-377 (the "jobs bill") funds.

The Legislature rejected the department's proposal and, instead, augmented the CCS General Fund appropriation by $3,248,000—the amount we estimated would be needed to fully fund the CCS program—and used the $4.7 million in federal block grant funds to augment perinatal programs. The Governor vetoed both the General Fund augmentation for CCS and the federal funds for perinatal programs. In his veto message, the Governor stated that the federal funds "should be used to meet caseload increases in the CCS program."

Cost-of-Living Adjustment

We recommend a reduction of $272,000 in Item 4260-106-001 to correct errors in the calculation of CCS cost-of-living increases.

The budget proposes a General Fund increase of $837,000 to provide a 2 percent cost-of-living adjustment (COLA) for CCS expenditures sup-

DEPARTMENT OF HEALTH SERVICES—Continued

ported by the General Fund. The budget proposes no COLA for CCS expenditures supported by federal funds.

Our analysis indicates that for hospital inpatient and therapy expenditures, inflation adjustments were included in calculations of the "base budget" amount for 1984–85. Consequently, no additional COLA on these expenditures is needed. A COLA is not included in the base budget amount for the remaining category, outpatient services. Our calculations indicate that $565,000 is the amount needed to provide a 2 percent COLA for *both* state and federal expenditures for outpatient services. Since federal funds are capped, the entire amount of this adjustment would have to come from the General Fund. This amount is higher than the amount included in the budget because the budget amount is based solely on the General Fund portion of outpatient services expenditures.

Thus, the amount proposed in the budget ($837,000) is $272,000 more than the amount needed ($565,000). Consequently, we recommend a reduction of $272,000 to correct for (1) overbudgeting of COLA funds for hospital inpatient and therapy services and (2) underbudgeting of COLA funds for outpatient services.

The details of our analysis are as follows:

Therapy Services. The budget includes $12,713,000 (all funds) for therapy services in 1984–85, excluding the 2 percent COLA. This is $820,000, or 6.9 percent, above estimated current-year expenditures. The increase is due to projected utilization and cost increases. Our analysis indicates that the 6.9 percent increase already accounts for inflation in the costs of services. Consequently, an additional COLA for these expenditures is unnecessary.

Inpatient Services. The budget includes $11,593,000 (all funds) for inpatient services in 1984–85, excluding the 2 percent COLA. This amount includes $718,000 for a 6.6 percent increase to account for the effects of inflation on hospital costs. Thus, the proposed amount already includes an inflation adjustment, and an additional COLA is unnecessary.

Outpatient Services. The budget includes $28,228,000 (all funds) for outpatient services in 1984–85, excluding the 2 percent COLA. This amount is based on utilization trends. It does not include any funds for increases associated with inflation. A 2 percent COLA on this amount is $565,000.

Inpatient Utilization Review

We recommend (1) Budget Bill language requiring Medi-Cal field offices to review treatment authorization requests for extended lengths of stay by CCS hospital inpatients and (2) a reduction of $389,000 in CCS General Fund expenditures and $221,000 ($111,000 General Fund) in Medi-Cal expenditures to reflect one-half year savings resulting from implementation of these reviews.

The department estimates that expenditures for CCS hospital inpatient services will total almost $11.6 million in 1984–85. In our *Analysis of the 1983–84 Budget Bill,* we noted that county CCS offices have different policies regarding utilization reviews for those inpatients requiring extended hospitalization stays. As a first step toward strengthening utilization reviews, the 1983 Budget Act required the department to promulgate regulations that require county CCS programs to implement utilization review procedures established by Los Angeles County. Specifically, the

regulations require counties to (1) make on-site visits during extended hospitalizations at intervals of 30 to 60 days and (2) utilize length-of-stay criteria developed by Los Angeles County.

To examine current utilization review procedures by CCS, we contacted 11 independent county programs. Of the 11, one county provides on-site utilization review. The remaining 10 counties provide no on-site review, primarily because they lack qualified personnel. One of the 10 programs routinely grants requests for extensions of seven days. One other program reviews inpatient charts at 30-day intervals. The remaining eight counties have no formal policy for review of length-of-stay extension requests. Because hospitalization costs of $1,500 per day or $50,000 per month are not uncommon under the program, we believe that neither 30-day intervals between reviews nor routine seven-day extensions are fiscally prudent.

There are two potential methods for strengthening utilization review in this program. First, the state could require counties to implement additional utilization review procedures for all hospital inpatients. Our analysis indicates that this method probably would not be successful. First, there may not be sufficient workload for many counties to maintain their own utilization review personnel. In addition, travel time beween small counties and specialized hospitals utilized for CCS services may be prohibitively long. This is especially true for many northern California counties whose CCS patients receive inpatient services in the San Francisco area. Second, counties are reluctant to hire additional staff because the state does not finance increased administrative costs. Third, the state has been unsuccessful in enforcing current utilization review policies. Thus, there is no reason to believe that timely utilization review would occur under new policies, either. Consequently, we would not recommend that counties be required to perform this function.

A second method for strengthening utilization review is to have state personnel perform this service. Our analysis indicates that utilizing Medi-Cal field office personnel to review treatment authorization requests (TARs) for length-of-stay extensions requested on behalf of CCS hospital inpatients would (1) allow CCS to retain its basic case-management function through the initial hospital authorization, (2) alleviate a portion of workload now required of county programs, (3) assure effective, timely utilization review of CCS hospital inpatients, (4) result in significant savings to the state, and (5) add minimal additional workload to the field offices because field office staff routinely visit most hospitals to perform Medi-Cal utilization reviews.

Savings. The department estimates that reviews of length-of-stay extension requests under Medi-Cal result in an average savings of $178 for each hospital inpatient stay. Applying this estimated savings per inpatient stay to CCS inpatient expenditures, we estimate that these reviews would result in an annual savings of $983,000 to the CCS program (state and county funds) or $737,000 in state CCS expenditures. Savings of $737,000 in health care services costs result in total state savings of $778,000, because administrative allocations are based on service dollars.

Our analysis indicates that there would also be significant savings for Medi-Cal funded CCS hospital inpatients. Under current procedures, county CCS staff review utilization of Medi-Cal funded CCS patients. According to counties, Medi-Cal funded patients receive as little, or even less, utilization review than do CCS funded patients.

The department does not have data on Medi-Cal expenditures for CCS

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case-managed patients. Of children receiving medical services, however, approximately 31 percent are funded by Medi-Cal. Based on this percent, and assuming expenditures for Medi-Cal patients, at the very least, follow the same pattern as expenditures for other CCS patients, we estimate that field office review of length-of-stay extensions for CCS case-managed patients would result in annual savings to the Medi-Cal program of approximately $442,000 ($221,000 General Fund).

Field Office Workload. To provide on-site review for all CCS (Medi-Cal and non-Medi-Cal) patients would require a total of approximately 1.3 additional full-time equivalent staff positions for Medi-Cal field offices around the state. This assumes an average of one extension per hospital inpatient stay and approximately 5,526 CCS inpatients per year. Our analysis indicates this workload could be absorbed by the current staffing of Medi-Cal field offices. The budget proposes 430 positions for these field offices.

Recommendation. Medi-Cal field office review of length-of-stay extension requests would (1) save significant state dollars and (2) not impair the case-management function of the CCS program. Consequently, we recommend adoption of Budget Bill language requiring Medi-Cal field offices to review length-of-stay extension requests for CCS inpatients. The language would also (1) require the department to establish procedures governing exchange of information between county CCS programs and Medi-Cal field offices and (2) specify that state funds may not be used to pay for hospital days that are disapproved by the field offices.

There could be significant lead times involved in implementing this proposal because the field offices would be required to establish procedures for exchanging information with the different counties. Consequently, we recommend deleting funds from the CCS and Medi-Cal appropriations to reflect half-year savings. These amounts are $389,000 from the CCS appropriation and $221,000 ($111,000 General Fund) from the Medi-Cal appropriation. We recommend the following Budget Bill language:

"The department shall (1) require Medi-Cal field office personnel to review treatment authorization requests (TARs) for any extended lengths of stay beyond the length of stay specified in CCS length-of-stay criteria for all CCS case-managed hospital inpatients, (2) establish procedures governing exchange of information between county California Children's Services (CCS) programs and Medi-Cal field offices, and (3) require that no state funds may be used to pay for hospital days that are disapproved by the Medi-Cal field offices."

Contracting for Hospital Inpatient Services

We recommend that by April 15, 1984, the California Medical Assistance Commission report to the Legislature on the feasibility and potential effects of implementing a hospital contracting program for CCS hospital inpatients.

The costs for hospital inpatient services have risen dramatically in recent years. As a means of reducing the rate of increase in these costs, the Legislature enacted legislation in 1982 that requires hospitals wishing to participate in the Medi-Cal program to contract with the state. Noncontracting hospitals may receive Medi-Cal reimbursement only for emergency services. Specific hospitals, including children's hospitals, are

exempt from contracting until July 1984. The California Medical Assistance Commission (CMAC) directs the negotiations of Medi-Cal hospital inpatient contracts.

Our review of the Medi-Cal hospital contracting program shows that the program has reduced Medi-Cal hospital expenditures by approximately 15 percent. Due to the success of Medi-Cal's hospital contracting effort, we examined the possibility of contracting for hospital inpatient services provided under the CCS program. Our review indicates that contracting could result in significant savings to the CCS program, as well. The program currently spends approximately $11.6 million per year on hospital inpatient costs.

Program Implementation. Hospital contracting in the CCS program would only apply to CCS funded patients. Medi-Cal funded patients are already restricted to Medi-Cal contract, or specifically exempted, hospitals. Hospital claims for these patients are paid by the Medi-Cal fiscal intermediary. We see no advantages to disrupting the current method of service provision for Medi-Cal funded patients.

Implementation of a CCS hospital contracting program could take one of two principal forms:

- Combine with the Medi-Cal contracting program. Under this alternative, CCS hospital inpatients would receive services under Medi-Cal contracts and county CCS programs would reimburse contract hospitals at Medi-Cal rates. Because current Medi-Cal contracts may not allow the state to (1) include CCS patients under the contracts and (2) do not permit release of contract rates to counties, this alternative would require amendments to existing Medi-Cal contracts. Contract renegotiations could result in separate contract rates for CCS patients and/or changes in existing Medi-Cal rates.
- Establish an independent CCS hospital contracting program. Under this alternative (1) CCS funded patients might be subject to different restrictions than Medi-Cal funded patients and (2) the state might have less leverage in negotiating contracts.

Savings from Contracting. Under either administrative arrangement, savings from implementing a hospital contracting program for CCS could be significant, particularly in geographic areas in which specialized services for CCS hospital inpatients could be provided by more than one facility. The exact amount of savings would depend on the extent to which hospitals that provide specialized children's care would participate in a contracting program at lower reimbursement rates than those currently paid by CCS.

Analyst's Recommendation. Due to the potentially significant savings that the state would realize by implementing some form of CCS hospital contracting, we believe further study of this alternative is appropriate. The California Medical Assistance Commission (CMAC) has given some attention to contracting for specialized children's services in connection with a report on the children's hospital exemption that is due to the Legislature in February 1984. Consequently, we recommend that the CMAC report to the Legislature by April 15, 1984, on the feasibility and likely effects of hospital contracting for CCS hospital inpatient services. Specifically, the report should address:

1. Statutory changes needed to implement a CCS hospital contracting program.

2. Recommendations on whether it is preferable to establish a separate contracting program or combine CCS contracting with Medi-Cal contract-

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ing, and specifically how each type of program would be administered.

3. Steps involved in establishing a CCS contracting program and determining related administrative procedures.

4. Changes needed in the current CCS data collection system to allow effective contracting.

5. Potential dollar savings to the state.

CCS Pharmaceutical Purchasing Procedures

We recommend a reduction of $249,000 to reflect savings in the purchase of pharmaceuticals that can be realized from stricter adherence to state policy guidelines.

Current CCS policy guidelines require that reimbursement for prescription drugs, medical supplies, or devices shall be made in accordance with the Medi-Cal drug formulary and medical supplies listing. Currently, Medi-Cal reimburses for pharmaceutical purchases at one of the following rates, whichever is least costly:

1. Maximum allowable ingredient cost plus current professional fee ($3.60 dispensing fee).
2. Maximum allowable cost plus current professional fee.
3. Estimated acquisition cost plus current professional fee.
4. Average wholesale price plus current professional fee.
5. Charge to the general public.

Our review of CCS county programs indicates that these procedures are not strictly followed. In fact, in a survey of five independent CCS counties representing over 40 percent of CCS expenditures, *not one of the five followed the formulary.*

The department estimates that utilization of the Medi-Cal drug formulary results in a savings of 13 percent on pharmaceutical costs for the Medi-Cal program. Our review of the CCS program indicates a similar savings could be achieved if local CCS offices followed state CCS policy guidelines and utilized the Medi-Cal drug formulary. In 1982–83, CCS paid $4,428,000 for pharmaceuticals. Of this amount, $2,006,000 was covered by third-party payors. Thirteen percent of the remaining amount is $315,000. Consequently, we estimate that an annual savings of $315,000 to the CCS program could be achieved if state policy guidelines were followed. This consists of $236,000 in state funds and $79,000 in county funds. Savings of $236,000 in state pharmaceutical costs would result in total savings of $249,000, because administrative allocations are based on service dollars.

Accordingly, we recommend a reduction of $249,000 in CCS state funds to reflect state savings resulting from strict adherence to CCS state policy guidelines.

Recoveries from Liable Third Parties

We recommend that legislation be enacted to insure that CCS is notified of legal action related to liability for injuries treated by CCS.

The CCS pays medical expenses, sometimes including extensive rehabilitative care, for children injured during accidents such as automobile or diving accidents. In a portion of these cases, parents or guardians take legal action on behalf of the child against liable third parties to recover costs and collect damages. Parents and guardians are required to notify the CCS program of lawsuits and reimburse CCS for its costs when they receive monetary awards, but they do not routinely comply with this

requirement. As a result, counties that attempt to identify such cases in order to obtain reimbursement must rely on local newspapers for information.

Under current law, attorneys representing Medi-Cal clients, their guardians, or their estates must notify the department of legal actions involving liability for injuries. As a result of these requirements, Medi-Cal recoveries in cases involving legal action by Medi-Cal clients have increased.

We believe that CCS could achieve savings if it received information about pending lawsuits in a systematic fashion. Notification requirements established under the Medi-Cal program appear to be an effective method for obtaining information. Consequently, in order to insure that CCS is aware of legal actions involving liability for injuries treated under the CCS program, we recommend enactment of legislation pertaining to CCS that is similar to that contained in Section 14124.74–14124.83 of the Welfare and Institutions Code and Section 700.1 of the Probate Code.

Financial Eligibility and Repayment Report

The *Supplemental Report to the 1983 Budget Act* required the department to report by August 1, 1983, on alternatives for a new repayment system for CCS and the Genetically Handicapped Persons' Program (GHPP). At the time this *Analysis* was prepared, the report had not been submitted. Our comments on the current system follow.

Current Repayment System. In 1980–81, CCS and GHPP implemented a new system for determining financial eligibility for program services and the amount of repayments that service recipients are required to make. Prior to 1980–81, CCS determined the amount of repayment due from a family by (1) assessing the family's income and resources, (2) adjusting the amount for family size, (3) comparing the adjusted amount to an income standards table, and (4) requiring the family to pay one-half of the cost of services above the amount specified in the table. The system frequently was criticized for being ineffective and complicated. Prior to 1980–81, the GHPP did not have a repayment system.

The new system, called the Simplified Repayment System (SRS), uses state income tax information to determine financial eligibility and establish maximum repayment obligations. Individuals or families with incomes of $40,000 or less are eligible for services. Under SRS, an individual or family's maximum payment for services equals 200 percent of the family's state income tax liability in the prior year. For example, if a family paid $450 in state income tax for 1981, the family's maximum repayment obligation would be $900 ($450 times 2). If the cost of care received by a family member in 1982 was $1,000, and the family's medical insurance paid $300 of this amount, the family's actual repayment obligation would be $700 (total costs of $1,000 minus the insurance payment of $300). The programs permit individuals or families to reduce their repayment obligations in special circumstances, upon appeal.

The department exempts from repayment obligations (1) families with adjusted gross incomes less than 200 percent of the poverty level (plus an allowance for the cost of maintaining a disabled person in the household) and (2) families that have adopted a handicapped child. Families are not required to repay the state for diagnostic or therapy services.

Analyst's Comments. Our analysis indicates that the repayment system should be revised. Specifically, we have identified the following problems with the current system:

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- ***Tax Liability is a Poor Indicator of Ability to Pay.*** We see no consistent relationship between a family's tax liability and its ability to pay for medical care. Some families with high incomes successfully shelter their incomes, resulting in very low tax payments.
- ***Assets Should be Considered When Determining Eligibility and Ability to Pay.*** By excluding assets from these determinations, families in comparable economic circumstances may be treated differently, and vice versa. A family with $500,000 in property, $25,000 in the bank, and an annual income of $35,000 would have the same repayment obligation as a family with no property, $100 in the bank, and the same income. To minimize the administrative costs associated with determining assets, it may be possible to require more detailed financial screening for those clients whose estimated cost per case exceeds a certain level.
- ***Repayments Continually Dropping.*** Due to changes in financial eligibility, repayments in 1984–85 are estimated at $750,000. This is $150,000, or 17 percent, below current-year estimates. Our analysis indicates that the department should consider turning the responsibility for collecting family repayments over to providers. The CCS and GHPP could determine each family's repayment obligation, deduct the repayment amount from the amount the program owes the provider, and inform the provider of the amount owed by the family. The provider, which already has extensive resources allocated for collections, could then bill the family. This would also reduce county administrative workload.

CCS Regulations on the Way

The *Supplemental Report to the 1981 Budget Act* required the CCS program to develop regulations governing program operations. The CCS program has, in the past, operated through "program letters," which have the same effect as regulations but are not subject to public review. The department informs us that a draft of the regulations currently is under review and that these regulations should be completed by June 1985.

Genetically Handicapped Persons' Program

The Genetically Handicapped Persons' Program (GHPP) funds specialized medical care and rehabilitation services for adults with certain genetic diseases who are unable to pay the full cost of these services. The specific services provided under the GHPP are the same as those provided under the California Children's Services (CCS) program. Similarly, an individual's need for financial assistance under the GHPP is determined using the same method as that used under CCS. The department estimates that GHPP case managers will follow 1,840 patients in the budget year, of whom 770 will be Medi-Cal funded and 1,070 will be funded by the GHPP program.

Department support is proposed at $271,000 in 1984–85, which is $14,000, or 4.8 percent, below estimated current-year expenditures. This decrease reflects the elimination of one office technician position and increases to cover the added costs of benefits, merit salary adjustments, and operating expenses. Local assistance is proposed at $5,916,000, which is an increase of $513,000, or 9.5 percent, above current-year expenditures. This change is the result of $398,000 for increased workload and $115,000 to provide a

2 percent cost-of-living increase. Table 16 shows 1984–85 projected caseload and local assistance costs and funding sources for the GHPP.

Table 16
Genetically Handicapped Persons' Program
Projected 1984–85 Caseload and Costs

Condition	*Caseload*	*Cost Per Case*	*Total Costs*
Hemophilia	500	$6,728	$3,364,000
Cystic Fibrosis	210	6,193	1,301,000
Sickle Cell	170	5,170	879,000
Huntington's and related conditions	190	1,354	257,000
Totals	1,070	$5,421	$5,801,000 [a]
General Fund			*$5,731,000*
Family repayments			*$70,000*

[a] Excludes 2 percent cost-of-living increase.

Cost-of-Living Increase Double-Budgeted

We recommend a reduction of $26,000 in the proposed cost-of-living adjustment for the GHPP because these funds are double-budgeted.

The budget proposes $115,000 to provide a 2 percent cost-of-living adjustment (COLA) for the GHPP. This amount is based on estimated program costs of $5,731,000 in the budget year. Approximately 23 percent, or $1,318,000, of these funds are for hospital inpatient services. In estimating hospital inpatient costs, the department has already added a 6.6 percent COLA to the base amount. It is therefore inappropriate to provide a 2 percent COLA for this portion of the program. Accordingly, we recommend a $26,000 reduction in the amount proposed for a COLA for the GHPP in Item 4260-106-001 (General Fund).

Genetic Disease

The Genetic Disease Section administers programs that are designed to reduce or prevent genetic disease through early detection, consultation with professionals, and counseling. Programs administered by the Genetic Disease Section include the Newborn Screening program, which is supported by the Genetic Disease Testing Fund, and the Sickle Cell, Tay-Sachs, and Prenatal Counseling programs, which are supported by the General Fund.

The budget proposes department support expenditures of $12,081,000 for the Genetic Disease program, which is an increase of $3,474,000, or 40 percent, over estimated current-year expenditures. Local assistance is proposed at $1,601,000, an increase of $31,000, or 2 percent, above current-year estimated expenditures.

The increase in support expenditures is largely the result of an increase of 24.5 positions and $2,246,000 requested to begin implementation of the Neural Tube Defects program and the addition of nine positions and $669,000 for increased workload in the Newborn Screening program. The increase in local assistance results entirely from the provision of a 2 percent COLA for the unit's local assistance programs.

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Budget Proposal for Neural Tube Defects Program Needs to be Revised

We recommend that prior to budget hearings, the department submit (1) an updated budget change proposal for the Neural Tube Defects project that reflects revisions in the implementation schedule and staffing estimates and (2) a revised fund condition statement for the Genetic Disease Testing Fund that (a) presents updated reserve estimates and (b) reflects expenditures for the Neural Tube Defects project that reconcile with the revised schedule.

Background. In response to interest from professional and lay groups, the Legislature authorized the department to develop regulations for a demonstration program providing prenatal screening for neural tube defects. Neural tube defects are birth defects that cause damage to the brain or spinal cord. The most common neural tube defect is spina bifida (open spine). The demonstration program is designed to ensure the quality of laboratory testing, accuracy with which results are interpreted, timeliness, and availability of all necessary counseling and diagnostic services.

The 1982 Budget Act included funds to support six positions for the purpose of developing regulations for the Neural Tube Defects program. Due to the Governor's hiring freeze, only one of the six positions was filled, and no regulations for the program were developed. The 1983 Budget Act again provided funds for the program and permanently established the six positions. In Ch 323/83, the trailer bill to the 1983 Budget Act, the Legislature mandated the department to promulgate regulations for the program by June 30, 1984. At the time this *Analysis* was prepared, however, five of the six positions required to complete the regulations had still not been filled, again due to a hiring freeze. The demonstration project cannot begin until the regulations are completed.

Budget Proposal. The budget proposes to add 24.5 positions and $2,746,000 from the Genetic Disease Testing Fund for implementation of the Neural Tube Defects program. The funding level assumes that the regulations will be completed by June 30, 1984, and the demonstration project will begin on July 1, 1984. Based on the department's progress in the current year, we do not believe this schedule can be met. The department cannot tell us (1) when the five positions will be filled, (2) when the regulations will be completed, or (3) when the demonstration project will actually begin testing pregnant women.

In addition, estimates of carry-over reserves provided by the department are inconsistent with those contained in the budget. The budget shows reserves of $3,718,000 on June 30, 1984, $4,241,000 on June 30, 1984, and $4,743,000 on June 30, 1985. Estimates provided by the department show reserves of $6,000, $743,000, and $1,243,000, respectively. Without accurate account balances, the Legislature will not have adequate information on which to review the department's proposed fees.

In view of these problems, we recommend that prior to budget hearings, the department submit a revised budget change proposal for implementing the Neural Tube Defects project. The revised proposal should detail proposed positions and operating expenses and equipment that will actually be required in the budget year, and the dates by which each will be needed. We also recommend that the department submit a revised fund condition statement for the Genetic Disease Testing Fund that (1)

presents updated reserve estimates and (2) reflects expenditures for the Neural Tube Defects project that reconcile with the revised schedule.

Primary Care Clinics Program

The Primary Care Clinics program provides grants to nonprofit primary care clinics in order to stabilize the clinics' financial condition or fund innovative clinic programs. Grant amounts are limited to $60,000 per year. In the current year, the department has funded 34 community clinics and 7 clinic associations.

The budget proposes $1,387,000 for primary care clinic grants and loans, an increase of $659,000, or 90 percent, above estimated current-year expenditures. Of this amount, $958,000 is included in the Community Health Services Division budget and $429,000 is included in the Rural Health Division budget. The increase reflects (1) $650,000 that is proposed to restore funds vetoed by the Governor from the 1983 Budget Act and (2) $9,000 to provide a 1.2 percent cost-of-living adjustment (COLA) for the program. Apparently, the COLA amount is based on a portion of the proposed funding. Provision of a 2 percent COLA consistent with other community health and rural health services programs would require an additional $5,000.

Budget Bill Schedules in Error

We recommend that $200,000 inappropriately included in the community health services appropriation be rescheduled for rural health services.

The Budget Bill includes the proposed $650,000 increase for primary care clinics in the allocation for community health services. The budget narrative, however, states that the restoration of funds includes $450,000 in community health services and $200,000 in rural health services. This would accurately reflect the amounts vetoed from each program in the current year. We therefore recommend that the Budget Bill schedules be amended to reflect the intended increases.

E. RURAL HEALTH SERVICES

The Rural Health program (1) provides public health services in those counties with populations of 40,000 or less that choose to contract with the state, (2) funds health clinics and other health services for migrant and seasonal farmworkers and rural and urban Indians, and (3) provides technical assistance to rural hospitals and clinics. The target population for these services is California residents living in rural, medically underserved areas, particularly Indians and farmworkers. In 1981–82, clinics funded through the Rural Health program received 316,414 visits from patients. Of the total, 123,772 were Indians, 80,005 were farmworkers, and 112,637 were other persons residing in rural areas.

The budget proposes $12,431,000 (all funds) for support of the Rural Health Division in 1984–85, excluding administrative overhead. This is a decrease of $6,000, or less than 1 percent, below current-year levels. Department support is proposed at $4,484,000, which is $358,000, or 7.4 percent, below estimated current-year expenditures. The decrease in support results primarily from (1) a reduction of 10 positions to streamline the administration within the Rural Health Division and (2) the transfer of $209,000 to Tehama County's allocation from the County Health Services Fund because the county now exceeds the 40,000 population ceiling for receiving state-provided public health services under the contract counties program.

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Local assistance is proposed in the amount of $7,947,000, which is an increase of $352,000, or 4.6 percent, over estimated current-year expenditures. This increase is the result of a 2 percent cost-of-living increase and a proposed increase of $200,000 for primary care clinics vetoed by the Governor in 1983–84. Table 17 shows local assistance expenditures for the three Rural Health Division programs from 1982–83 through 1984–85.

Table 17
Rural Health Local Assistance Expenditures—General Fund 1982–83 through 1984–85 (in thousands)

	Actual 1982–83	*Estimated 1983–84*	*Proposed 1984–85*	*Change Amount*	*Change Percent*
Rural health					
Rural health	$3,597	$3,605	$3,677	$72	2.0%
Primary care clinics	424	224	429	205	91.5
Indian health	2,797	2,797	2,853	56	2.0
Farmworker health	969	969	988	19	2.0
Totals	$7,787	$7,595	$7,947	$352	4.6%

Budget Reductions

We recommend approval.

The budget proposes to eliminate 10 positions from the Rural Health Division. These reductions are spread throughout the division and include two positions that have been vacant since 1981–82. The department indicates that the workload associated with the positions proposed for elimination can be absorbed by the remaining personnel in the division. Our review of the program indicates that this assumption is reasonable, based on the current workload of the division. Therefore, we recommend that the reductions be approved.

F. ENVIRONMENTAL HEALTH

The budget proposes $12,604,000 (all funds) for support of the Environmental Health Division in 1984–85, excluding administrative overhead. This is an increase of $55,000, or 0.4 percent, above estimated current-year expenditures. The division currently contains five branches: sanitary engineering, vector biology and control, radiological health, food and drug, and local environmental health. The budget proposes 286.2 positions for 1984–85, a decrease of 14.5 positions and 20 positions from the current-year and 1982–83 levels, respectively. Nine of the positions being eliminated are from the Sanitary Engineering Branch and 7.5 are from the Food and Drug Branch.

Drinking Water Program Workload Increasing

We recommend that the department report at budget hearings on (1) the adequacy of standards for chemicals contaminating drinking water, (2) the state's ability to respond to problems identified by the new inventory process, and (3) the impact of the new inventory-related workload on ongoing program responsibilities.

The drinking water program in the Sanitary Engineering Branch (1) inspects and regulates water systems with more than 200 service connec-

tions, (2) investigates and institutes corrective actions as needed, (3) monitors organic chemical contamination, and (4) coordinates state enforcement of the federal Safe Drinking Water Act. The branch anticipates continuing to receive a special project grant of $704,000 in federal Safe Drinking Water Act funds from the Environmental Protection Agency (EPA).

The budget proposes reductions of (1) $321,000 and 7 positions due to the expiration of the Safe Drinking Water Bond program and (2) 10 positions funded by the EPA grant.

These reductions are occurring at the same time as the branch's workload is increasing due to passage of Ch 881/83 (AB 1803). This act requires the department to survey water systems to identify and develop an inventory of organic chemicals contaminating drinking water supplies. The act further requires the department to establish a sampling strategy for large water systems, review local plans, evaluate testing reports, and work with system operators to design ongoing monitoring plans as needed. The act also establishes a detailed schedule for completing these steps for large water systems and requires the department to develop a systematic water analysis program for small water systems by January 1, 1985.

When the act was being considered by the Legislature, the department indicated that it could absorb the workload without an increase in resources. The Legislature included $300,000 for this program in the department's budget for 1983–84, but the Governor vetoed the funds from the 1983 Budget Act.

Our review has identified several problems with the way this program is being implemented. First, our analysis indicates that the inventory is diverting staff from ongoing efforts to inspect, permit, and advise water system operators. These efforts had already been reduced by federal funding cutbacks and the reduction in positions associated with the state bond program. Second, the department lacks enforceable standards for most organic chemicals to determine whether levels found in test samples are a problem. Third, for those cases where a standard exists and a problem can be confirmed, the department has no resources to assist operators in correcting the condition, now that the bond program has expired. The drinking water inventory will probably generate enforcement and mitigation needs that will divert additional staff from ongoing activities.

We recommend that the department report at budget hearings on (1) the adequacy of currently available standards applying to chemical contamination in drinking water for reviewing and interpreting testing results received by water system operators and (2) the department's and system operators' ability to respond to problems that are identified during the inventory process. The report should also identify the amount of staff time assigned to the drinking water inventory and standard setting activities, and the impact of redirections on basic program activities in the current and budget years.

X-ray Inspections Reduced by 30 Percent

We recommend that the department report at budget hearings on its reasons for allowing a 36 percent vacancy rate for X-ray inspections.

The Radiologic Health Branch operates programs to protect the public and workers from unnecessary radiation. A major activity of the branch is inspecting X-ray machines. Our analysis indicates that recent hiring freezes imposed by the Governor led to a 30 percent reduction in X-ray machine inspections during calendar year 1983. Moreover, at the time this

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Analysis was prepared, 9 of 25 inspection positions, or 36 percent, were vacant. This level of vacancies limits the ability of the program to accomplish its basic mission, which is to protect the public from excess radiation produced by malfunctioning machines. In addition, the inspection program is supported by fees paid by machine operators and deposited in the General Fund. If program services are not being provided, it is not appropriate to continue charging fees at the current levels, and these fees should be reduced.

We recommend that the department explain at budget hearings why it is allowing a vacancy rate of 36 percent for X-ray inspections. It should also be prepared to comment on whether it intends to refund fees collected by the program.

Information Needed on Low-Level Radioactive Waste Disposal Site

We recommend that the department and the Resources Agency report jointly at budget hearings on their progress in developing a permanent site in California for the disposal of low-level radioactive wastes.

Chapter 95, Statutes of 1982 (AB 1513), and Ch 1177/83 (SB 342) established a procedure for establishing a low-level radioactive waste disposal site and designated the department as the lead agency for selecting a site operator and location. The statutes require the Resources Agency to develop a site directly if, by August 13, 1984, the department has received no acceptable applications from private parties to operate such a site.

In our analysis of the Resources Agency budget (Item 0540), we discuss the potential budget-year cost if the state has to develop and operate the site directly, as well as the Legislature's need for more complete information on this matter. On this basis, we recommend that the department and the Resources Agency report jointly at budget hearings on the status of efforts to implement this legislation. The report should include (1) an assessment of the department's ability to meet the statutory time schedule, (2) the number of applications received and/or anticipated to be received, and (3) a description of the activities and an estimate of the costs in 1984–85 if the Resources Agency is required to develop and operate a low-level radioactive waste disposal site.

G. HEALTH PROTECTION

The budget proposes $36,224,000 (all funds) for support of the Health Protection Division in 1984–85, excluding administrative overhead. This is an increase of $99,000, or 0.2 percent, above estimated current-year expenditures. Department support is requested in the amount of $32,786,000, an increase of $1,957,000, or 6.3 percent, above estimated current-year expenditures. Local assistance is proposed in the amount of $3,438,000, a decrease of $1,791,000, or 34 percent, below estimated current-year expenditures. These amounts do not include $3,429,000 in federal funds from the preventive health services block grant, administered by the division, that are budgeted in the special projects item.

The budget also proposes 591.6 positions for this program in 1984–85, a net reduction of 5 positions from the current year.

The division's functions include laboratory services, infectious and chronic disease control, preventive medical services, and epidemiological and toxicological studies. The division has been reorganized in the current year. The vital statistics program was transferred from health protection

to the Administration Division ($2,839,000 and 101 positions). In addition, the epidemiology and laboratory functions related to toxic substances were transferred to health protection from the Toxic Substances Control Division ($11,127,000 and 163 positions).

Department Support Changes. The net reduction of 5 positions proposed for the budget year reflects increases of 22 positions and decreases of 27 positions. Most of the increase is for laboratory positions supporting the Toxic Substances Control Division (4 positions) and the Genetic Disease Section (14 positions). The major decreases are due to (1) redirections to other programs (9 positions), (2) reductions in the amount of reimbursements received from other departments (9 positions), (3) implementation of the Public Health Enhancement program (5.5 positions), and (4) deletion of the Acquired Immune Deficiency Syndrome program (1.5 positions).

Local Assistance Changes. The budget proposes to include three health protection programs in the Public Health Enhancement program (PHEP), which is discussed in detail earlier in this analysis. The three programs are Preventive Health Care for the Aging, Dental Health, and a portion of Immunization Assistance. The consolidation would occur on January 1, 1985; consequently, the health protection budget includes only the half-year costs of the consolidated programs ($1,896,000). The budget proposes $29,000 for a 2 percent cost-of-living adjustment (COLA) for the local assistance expenditures not included in PHEP ($1,513,000). Proposed local assistance expenditures are shown in Table 18.

Table 18
Health Protection
Local Assistance Expenditures
General Fund
1982–83 through 1984–85
(in thousands)

	Actual 1982–83	*Estimated 1983–84*	*Proposed 1984–85*	*Change*	
				Amount	*Percent*
Adult health					
Preventive health care for the aging	$1,216	$1,216	$621 [a]	−$595	−49%
Health education/risk reduction	592	—	—	—	—
Lupus erythematosus research	684	720	734	14	2
Dental health	1,500	1,500	765 [a]	−735	−49
Immunization assistance	1,345	1,371	888 [a]	−483	−35
Tuberculosis control	398	422	430	8	2
Totals	$5,635	$5,229	$3,438	−$1,791	−34%

[a] The budget proposes to transfer these programs, excluding $378,000 in Immunization Assistance, to a new Public Health Enhancement program, effective January 1, 1985. These amounts reflect half-year costs.

Acquired Immune Deficiency Funding Eliminated

The budget proposes to eliminate $500,000 in General Fund support added by the Legislature in the current year for educational services and research related to Acquired Immune Deficiency Syndrome (AIDS). In the current year, the department is supporting (1) 15 contracts with local agencies for information and outreach programs designed to help prevent AIDS among high-risk populations, (2) 1.5 positions to operate the program, and (3) administrative and travel costs for the Task Force on AIDS,

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which was created by the department, and the AIDS Advisory Committee, which was created by Ch 1257/83 (SB 910). The department does not propose to continue the staff or contracts. The department has not determined how it will support travel and per-diem costs for the statutory advisory committee in 1984–85.

The $500,000 augmentation in the department's budget was accompanied by a $2.9 million augmentation to the University of California's budget for basic medical and scientific research on AIDS. The UC budget proposes $3,074,000 to continue the program in 1984–85, consisting of the current-year amount plus an inflation adjustment.

Hazardous Materials Laboratory Workload Increase

We recommend approval.

The budget requests four new positions and $151,000 from the Hazardous Waste Control Account to respond to increased workload resulting from current-year and proposed budget-year increases in Toxic Substances Control Division (TSCD) permitting and enforcement staff.

The current-year budget increased the TSCD permitting and enforcement staff by 29 positions but did not increase the laboratory staffing to perform additional tests requested by the new staff. The first TSCD quarterly report in 1983–84 showed that the laboratory increased its productivity and exceeded its planned number of determinations on samples by 470 percent for site mitigation and 93 percent for surveillance and enforcement. Large increases in the volume of samples submitted by the field staff, however, inundated the laboratory. As a result, only 38 percent of requested surveillance and enforcement determinations were completed.

The budget requests 62 new positions in the permitting and enforcement functions in 1984–85. The four new positions in the hazardous materials laboratory would cover workload generated by these 62 positions and the 29 positions established in the current year. In addition to requesting the staff augmentation, the department is investigating the feasibility and cost of contracting with private laboratories to analyze samples requiring routine determinations. The budget does not, however, propose additional funds for contract services.

Our analysis indicates that without the augmentation, the laboratory will continue to be unable to fulfill requests for laboratory work from the TSCD. Consequently, we recommend approval of the four new positions.

Hazardous Materials Laboratory Certification

We recommend approval.

The budget requests $107,000 from the Hazardous Waste Control Account for two positions to certify private and local government laboratories to do hazardous waste testing. Regulations establishing standards and fee levels are being developed in the current year by 1.5 limited-term positions. The two permanent positions requested in the budget will certify labs, conduct site visits, and review quality control procedures.

The positions are justified on a workload basis. Consequently, we recommend that they be approved.

Unjustified General Fund Buy-Out of Public Health Reimbursements

We recommend the reduction of $633,000 because the department has not justified increased General Fund support to replace reductions in reimbursements from other departments.

The budget proposes a General Fund increase of $633,000 in 1984–85 to compensate for reduced reimbursements received by the Air and Industrial Hygiene Laboratory ($278,000) and the Southern California Laboratory ($355,000) from the Department of Industrial Relations. The department contends that the increase is needed to compensate for a past budgeting error that inappropriately overestimated reimbursements and thereby reduced General Fund support for these programs.

The department was unable to provide us with any evidence supporting its claim. Nor was the department able to provide programmatic justification for a General Fund increase for these laboratories. Therefore, we recommend a reduction of $633,000 in the amount budgeted for these two laboratories.

Staff Resources for Toxic Air Contaminants Not Identified

We recommend that the department report at budget hearings on (1) the resources being utilized to support efforts by the Air Resources Board to assess toxic air contaminants in the current and budget years and (2) workload associated with this activity.

For a number of years, the Air Resources Board (ARB) has investigated toxic air contaminants and set exposure standards to limit negative health effects. The Department of Health Services, through the Epidemiological Studies Section, provides evaluations and recommendations on the health effects of toxic air contaminants to the ARB. Chapter 1047, Statutes of 1983 (AB 1807), establishes procedures for setting standards for control of toxic air contaminants. Costs of the program will depend on the number of contaminants for which standards are developed.

The ARB budget requests an additional $889,000 (various funds) and 5.7 personnel-years to increase the ARB efforts in regulating these substances. For each substance studied by the ARB, the department is required to contribute a detailed health effect analysis and toxicological review. The department's budget does not request new staff or funding or indicate the existing program activities that will be reduced in order to support the additional workload generated by the ARB augmentations. The non-air-pollution-related activities in the Epidemiological Studies Section include Superfund program health effect studies and consultation, pesticide health effects, birth defects monitoring, cluster investigation, and statistical environmental epidemiology.

The department was unable to identify the resources allocated to the toxic air contamination activities in the current and the budget years or the extent to which resources are being redirected from other activities to respond to increased workload generated by the ARB. We recommend that the department report at budget hearings on the staff it is allocating to toxic air contamination issues in the current year and on the workload anticipated in the budget year. The report should also identify any activities that will be reduced or eliminated in order to accommodate the new workload.

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Public Health Fees Adjustment

We recommend that the Legislature increase the adjustment for public health fee rates proposed in the Budget Bill from 4.2 percent to 6 percent in order to accurately reflect the change in program costs and to increase revenues to the General Fund.

Chapter 1012, Statutes of 1980, provides for automatic annual adjustments of certain fees assessed by the department, including laboratory license and vital statistics fees. The amount of the annual increase is set based on language in the Budget Act. The 1984 Budget Bill proposes a 4.2 percent increase, effective January 1, 1985. The proposed increase is a weighted average of a 3 percent increase in personal services expenditures and a 6 percent increase in operating expenses. The 3 percent personal services increase is intended to approximate the cost increase in 1984–85 resulting from the full-year effect of current-year salary and benefit increases (that is, the cost of these increases for an additional six months over and above the six-month cost attributable to the last half of 1983–84).

Our analysis indicates that this methodology understates the increase in personal services costs because it does not account for the 3 percent increase in personal services that took place in the current year. The fee increase of 2.05 percent approved in the 1983 Budget Act was a weighted average of a 5 percent increase in operating expenses and no personal services increase. When the final Budget Act was amended to provide a 3 percent increase, the public health fee adjustment was not corrected to reflect that change.

We therefore recommend that the adjustment factor for 1984–85 be changed to 6 percent to reflect the actual cost of the personal services cost-of-living increase from the time the fee adjustment was calculated to the beginning of the budget year. Without this change, fee revenues deposited in the General Fund will lag behind actual program cost increases, thereby resulting in a greater General Fund subsidy for the programs supported by the fees. This recommendation will result in increased General Fund revenues of approximately $100,000 in 1984–85.

The amount of the adjustment should be further increased at such time as the personal services increase for 1984–85 is determined by the Legislature.

Public Health Fee Revenues and Expenditures Inadequately Monitored

We recommend the adoption of supplemental report language requiring the department to (1) establish a mechanism to periodically review revenues and expenditures for programs supported by public health fees, (2) submit by September 1, 1984, a description of that mechanism and a listing of the fees, current fee rates, current annual revenues from each fee, and current annual expenditures for programs supported by the fees, and (3) identify by December 1, 1984, those statutory or regulatory changes needed to adjust fees so that fee revenues are reasonably related to the costs of the program activity.

Current law establishes fees to support various public health regulatory activities and services provided by the department. Some of these services are charged to individuals, such as fees for vital statistics records, while others are primarily assessed on businesses, such as food and drug inspections and various laboratory certifications. Another type of fee is associated

with the registration of occupational specialties such as X-ray technicians and public health nurses. Most of the individual fee rates are set in statute or by regulation. Chapter 1012, Statutes of 1980, provides for automatic annual adjustment of many of these fee rates based on an adjustment factor included in the Budget Act.

The current adjustment method, with one annual adjustment affecting all fees, captures some of the changes in departmental costs, but it does not reflect unique changes in the costs of specific programs. More importantly, the department is unable to provide an analysis of the adequacy of individual fees to support related program expenditures. In fact, the department was unable to provide a list of the fees, the statutory authority for each fee, or the revenue anticipated for each fee in the current and budget years. The budget detail shows fee revenues of $9.6 million in the current year and $6.5 million in the budget year. The department's budget office, however, advises that these numbers were transposed and that the budget is incorrect. The department was unable to provide any documentation to validate the accuracy of the fee collection amounts. The current lack of information makes it impossible for the Legislature to review the existing fee systems.

Our analysis indicates that currently the department cannot insure that (1) programs established by the Legislature to be self-supporting collect an adequate amount of revenue to support expenditures, (2) fee rates do not overcharge fee payers for the services provided, and (3) the Legislature has the opportunity to reevaluate fee rates that do not fully recover program costs.

In order to improve the fee assessment and monitoring system, we recommend the adoption of the following supplemental report language:

"The Department of Health Services shall conduct an in-depth review of existing public health fees and the activities funded by the fees. First, the department shall establish a mechanism to periodically review revenues and expenditures for specific fees. Second, by September 1, 1984, the department shall submit to the fiscal committees and the Joint Legislative Budget Committee (JLBC) a description of the mechanism it has established and listing of specific fees, current fee rates, annual revenues from each fee, and expenditures for each related program. Third, by December 1, 1984, the department shall submit to the fiscal committees and the JLBC its recommendations for statutory changes and a plan for regulatory changes needed to adjust fees so that fee revenues are reasonably related to the cost of the program activity. These recommendations shall also identify existing non-fee-supported public health programs that could be supported by fees."

Legislative Mandates

We recommend approval.

The budget proposes a General Fund appropriation of $86,000 in Item 9680-101-001 for state-mandated local programs. This amount is $50,000, or 37 percent, below current-year estimated expenditures. The entire reduction reflects reduced workload in activities carried out pursuant to Ch 102/81 and Ch 1163/81, related to death notices for Medi-Cal beneficiaries.

The mandating legislation and the estimated costs contained in the Governor's Budget for the budget year are:

1. Chapter 453, Statutes of 1974 (Sudden Infant Death Syndrome)	$6,000
2. Chapter 842, Statutes of 1978 (TB exams for school bus drivers)	5,000

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3. Chapters 102 and 1163, Statutes of 1981 (Medi-Cal beneficiary death notices)	75,000
Total	$86,000

The proposed expenditures are reasonable and consistent with amounts claimed by local governments in the past.

H. SPECIAL PROJECTS

The special projects line item includes 187 public health services, demonstration, research, and training projects. The projects typically are of short duration and are administered by various sections in the department. Most of the projects are federally funded.

The budget proposes expenditures of $218,678,000 for these projects in 1984–85, including $175,493,000 in federal funds and $43,185,000 in reimbursements from other state agencies or private parties. This is an increase of $52,636,000, or 32 percent, above current-year expenditures. Most of the increase is explained by the inclusion in this line item of $38.1 million in federal and private funds for cleaning up hazardous waste sites. These funds were displayed in the contracts line item in the current year. We discuss these expenditures in our analysis of the Superfund program in the Toxic Substances Control Division.

The budget proposes 893 positions for support of special projects (563 supported by federal funds and 330 by reimbursements). This is an increase of 114 positions, or nearly 15 percent, over estimated current-year levels. Many of these proposed positions will never be established because the federal government will not fund many proposed projects. Only 266 positions were actually filled in 1982–83, compared to 694 estimated a year ago.

Special Supplemental Food Program for Women, Infants, and Children (WIC). The WIC program provides food vouchers to nutritionally at-risk infants, children, and pregnant and breast-feeding women. It is 100 percent funded by the federal Department of Agriculture. WIC is the largest proposed special project, and it is estimated to use $129,385,000, or 59 percent, of the special projects funds in 1984–85.

The department indicates that the budget understates available funds by $6 million. Table 19 shows updated estimates of WIC expenditures in the current and budget years.

Table 19

Women, Infants, and Children Program Expenditures[a]
1983–84 and 1984–85
(in thousands)

	Estimated 1983–84	*Proposed 1984–85*
Food vouchers	$97,209	$106,930
Personal services	1,432	1,575
Other	18,982	20,880
Totals	$117,623	$129,385

[a] Based on department estimates as of January 20, 1984.

5. TOXIC SUBSTANCES CONTROL

The budget proposes expenditures of $58,122,000 (all funds) for the Toxic Substances Control Division in 1984–85, including program support, administrative overhead, and special projects. This is an increase of $986,000, or 1.7 percent, above estimated current-year expenditures. Programs administered by the division regulate hazardous waste management, clean up sites that have been contaminated by toxic substances, and encourage the development of treatment and disposal facilities as alternatives to waste disposal onto land. The budget proposes 245.5 positions for this program in 1984–85, which is an increase of 61.5 positions above the current-year authorized staffing level.

The 1.7 percent increase in expenditures proposed for the budget year follows an increase of $44.1 million, or 340 percent, in the current year. Most of this increase—$38.1 million—is for Superfund site cleanups paid for by the federal government or private parties who are responsible for the contamination. It is unlikely, however, that the full $38.1 million will be received by the department or spent in the current year. The remainder of the increase estimated for the current year—$6 million—reflects two factors: (1) spending in 1982–83 was below authorized levels and (2) 29 positions have been added to the regional offices for permitting, surveillance, and enforcement during 1983–84.

Table 20 displays the expenditures and funding sources for programs in the Toxic Substances Control Division in the prior, current, and budget years.

Table 20
Toxic Substances Control Division
Expenditures and Funding Sources
1982–83 through 1984–85
(in thousands)

	Actual	*Estimated*	*Proposed*	*Change*	
	1982–83	*1983–84*	*1984–85*	*Amount*	*Percent*
Support	$13,012	$57,136	$20,022	−$37,114	N/A
Special projects	—	—	38,100	38,100	N/A
Totals	$13,012	$57,136	$58,122	$986	1.7%
Hazardous Substances Account (HSA)	*$4,792*	*$10,053*	*$7,959*	*−$2,094*	*−20.8%*
Hazardous Substance Compensation Account	—	*355*	*355*	—	—
Repayment of General Fund loan	*1,178*	—	—	—	—
Hazardous Waste Control Account (HWCA)	*3,354*	*5,377*	*8,245*	*2,868*	*53.3*
General Fund	*30*	*44*	*13*	*−31*	*−70.5*
Federal Resource Conservation and Recovery Act (RCRA)	*2,937*	*2,852*	*3,450*	*598*	*21.0*
Energy and Resources Fund	*721*	*355*	—	*−355*	*−100.0*
Federal Superfund	—	*16,900*	*16,900*	—	—
Responsible parties	—	*21,200*	*21,200*	—	—

Multiple Funding Sources

The Toxic Substances Control program is currently supported by seven different funding sources. The funds and the programs supported by each fund are:

1. ***The Hazardous Substances Account*** **(HSA)**, established pursuant to Ch 756/81, is supported by taxes paid by generators of hazardous substances. The budget proposes to use the account to fund (a) cleanup of

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hazardous waste sites, (b) emergency response to releases of hazardous substances, (c) health effect studies, and (d) associated administrative costs. The tax was collected for the first time in 1982. The Hazardous Substances Compensation Account, an HSA subaccount, supports victim compensation claims.

2. ***The Hazardous Waste Control Account*** (HWCA) is supported by fees paid by operators of hazardous waste disposal facilities. These fees were first collected in 1974. The account funds the ongoing regulatory activities of the division, including permitting, inspections, transportation, manifesting, resource recovery, alternative technology assessment, designation of hazardous waste property, public participation, and program administration. It also supports laboratory support services and health effect studies conducted by the Health Protection Division and regulatory activities performed by the State Water Resources Control Board.

3. ***Federal Resource Conservation and Recovery Act*** (RCRA) funds are awarded to California by the federal Environmental Protection Agency (EPA) to support the state's Hazardous Waste Control program. The federal program supports many activities that are also funded by the HWCA.

4. ***The Federal Superfund*** (Comprehensive Environmental Response, Compensation, and Liability Act) finances the costs of cleaning up major uncontrolled hazardous waste sites on a 90 percent federal, 10 percent state basis. The EPA has designated 19 sites in California as eligible for this program.

5. ***The General Fund*** provides support for review of asbestos contamination problems. The budget proposes to eliminate separate funding for this program because the workload has been absorbed by other programs.

6. ***The Energy and Resources Fund*** (ERF) supports siting activities and alternative technology assessment. The budget proposes supporting these activities from the HWCA because authorization for the ERF is expiring.

7. ***Responsible parties*** are private companies or individuals that reimburse the state for the cost of cleaning up hazardous waste sites.

Organizational Changes

The Toxic Substances Control Division (TSCD) was created in October 1981 to consolidate existing departmental activities and provide a higher level of management attention. The division has been reorganized twice during the current year. In July 1983, the department transferred the laboratory, epidemiology, and toxicology staff back to the Health Protection Division (HPD) where they were located prior to October 1981, in order to separate the scientific and health effect assessment functions from the regulatory aspects of toxic substances control. In effect, this reorganization left the TSCD as a hazardous waste management unit. All non waste toxics activities, such as health assessments related to toxic air contaminants, occupational exposures, and pesticides, were transferred to the HPD. The department also added an additional top management position by splitting the responsibilities of the existing deputy director/division chief position into two separate jobs.

The second reorganization has not yet been completed. In this reorganization the department is eliminating the hazardous waste management branch office; upgrading the three regional offices to the section level; consolidating the Permit, Surveillance, and Enforcement Section and the Site Cleanup and Emergency Response Section into a new Program Man-

agement Section; and decentralizing the Superfund program. The Alternative Technology and Policy Development Section and Procedures and Regulations Development Section are not affected by the reorganization. The second reorganization is intended to place more decision-making authority in the regional offices, rather than in headquarters. The department has not yet determined how much of the Superfund program staff and responsibilities will be decentralized.

New section chiefs were selected in October. Until that time, most program managers were operating on an acting basis. As a result of language in the *Supplemental Report to the 1983 Budget Act* directing the department to conduct a nationwide search before filling these positions, over 75 candidates were interviewed. Three section chiefs were hired from inside the department, two from out of state and one from the State Water Resources Control Board.

Budget-Year Proposals

The budget proposes limited changes in the Toxic Substances Control program during the budget year. Specifically, the budget proposes to (1) add 35 positions for permitting hazardous waste facilities, (2) add 27 positions for surveillance activities, (3) add 3.5 positions to review financial assurance and liability documents, (4) add 4 positions to operate the information system, (5) discontinue one-time or limited-term activities, and (6) delete 7 positions from lower-priority activities. Table 21 displays the components of the budget changes.

Table 21
Toxic Substances Control Division
Proposed Support Budget Changes

	Positions	*Amount*	*Fund*
1983–84 expenditures (revised)	184.0	$19,036,000	Various
Baseline adjustments			
1. Cost increases (price letter, merit salary adjustment, etc.)	—	600,000	Various
2. Deletion of limited-term positions and one-time programs	−1.0	−268,000	HWCA
3. Deletion of McColl reappropriation	—	−1,500,000	HSA
4. Decrease in Superfund program for pro-rata	—	−561,000	HSA
Subtotals	−1.0	−$1,729,000	Various
Program change proposals			
1. Permitting	35.0	$1,703,000	HWCA and RCRA
2. Surveillance	27.0	899,000	HWCA
3. Financial assurance and liability	3.5	122,000	HWCA
4. Hazardous waste information system (HWIS)	4.0	305,000	HWCA
5. Hazardous waste property evaluation	−1.0	−35,000	HWCA
6. Governor's "3 percent" reduction	−5.0	−181,000	HWCA, RCRA, and ERF
7. Reduced federal support for data system	—	−75,000	RCRA
8. Administrative reduction	−1.0	−23,000	Various
Subtotals	62.5	$2,715,000	Various
1984–85 expenditures (proposed)	245.5	$20,022,000	Various
Change from 1983–84			
Number/amount	61.5	986,000	
Percent	33.4%	5.2%	

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Hazardous Waste Management Council Expires. The budget reflects a reduction of $268,000 due to expiration of statutory authority for the Hazardous Waste Management Council (HWMC) on June 30, 1984. This amount includes $225,000 for the council's five-person staff and related expenses and $43,000 for one position in the department's Alternative Technology Section. The council was established in 1982 to examine the process for siting hazardous waste facilities. It issued a draft hazardous waste management plan in January 1984.

A. HAZARDOUS WASTE MANAGEMENT

The Hazardous Waste Management program enforces state and federal regulations governing the transportation, treatment, storage, and disposal of hazardous wastes through permitting, surveillance, and legal actions. Most of the program's permit, surveillance, and enforcement activities are assigned to the three regional offices. The hazardous waste regulatory activities are funded by the Hazardous Waste Control Account (HWCA) and the federal Resource Conservation and Recovery Act (RCRA).

Additional activities conducted under this program include administering abandoned site activities, conducting hazardous waste property evaluation, promoting resource recovery through the California Waste Exchange, encouraging high-technology treatment and disposal facilities as an alternative to land disposal, and hazardous waste hauler registration and monitoring.

A large part of the current hazardous waste management workload consists of developing regulations to implement recent legislation and to make the state program conform to federal RCRA requirements. In the current year, the department expects to complete regulations that: (1) revise the fee schedule that supports the HWCA, (2) establish rewards for informants who report illegal hazardous waste management practices, and (3) set standards for (a) site owners' financial responsibility and liability, (b) treatment, storage, and disposal facilities, (c) hazardous waste elements of county solid waste management plans, (d) transportation containers and driver's training, (e) site closure procedures, (f) hazardous waste and border zone property, and (g) infectious waste control.

Hazardous Waste Control Account Revenues and Fee Regulations

The Hazardous Waste Control Account (HWCA) was established in 1973 to support the department's Hazardous Waste Control program. The department is required to adjust the fee through regulation in order to generate sufficient revenue to support program expenditures and to provide for a reserve of 5 percent. During the last two years, fee rates have been adjusted by the Legislature in the budget trailer bill because (1) the department failed to develop regulations in a timely manner and (2) legislative budget augmentations necessitated fee increases.

Chapter 89, Statutes of 1982 (AB 1543), requires the department to establish a variable fee system based on the degree of hazard presented by different types of waste. The fee system established by the Legislature in last year's trailer bill (Ch 323/83, AB 223) met this requirement by establishing a two-tiered system. It set a fee rate of $6.40 per ton of hazardous waste disposed onto land for the first 2,500 tons per month per disposer. It set a fee of $18 per ton on certain types of hazardous wastes that will

be restricted from land disposal according to a schedule established in regulation. This system was adopted as an interim solution and will sunset on June 30, 1984.

Current-Year Revenues. The budget projects a current-year surplus of $2.6 million in the HWCA. The surplus resulted from (1) lower-than-anticipated expenditures due to the Governor's veto of $1.8 million in legislative budget augmentations and (2) greater-than-anticipated resources due to a carry-over of $654,000 from the prior year. This surplus will be carried over into 1984–85, and thus reduce the amount of tax collections needed to support the program in the budget year.

Proposed Fee Regulations. The department has developed draft HWCA fee regulations to (1) generate $9.2 million in revenue and (2) establish a variable fee schedule based on the degree of hazard of various wastes. In its fee schedule the department proposes utilizing the four waste categories established under the Superfund program. The fee rates proposed in the regulations range from $0.15 per ton for low-hazard waste to $29.26 per ton for extremely hazardous waste. The fee rate on most types of hazardous wastes is proposed at $14.63 per ton. The methodology is consistent with the current Superfund tax structure and will shift the tax burden to disposers of hazardous or extremely hazardous wastes and away from disposers of low-hazard wastes and wastes disposed into injection wells or by land farming.

The department states that it is drafting language for the trailer bill to implement these fees if the regulation package is not approved in time. Without new fee provisions in regulation or statute, the fee rate reverts to $1 per ton on July 1, 1984. That fee level would not generate sufficient revenue to support proposed expenditures in the budget year.

Changes Needed in the Fee Mechanism. The existing fee mechanism will need more extensive changes in the future. First, the fees currently are assessed only on wastes that are disposed on land. The department's hazardous waste control program, however, also regulates treatment facilities that recycle, incinerate, or condense hazardous wastes. Under current law, these facilities are subject to minor requirements to pay fees to the HWCA. As the recent regulations to ban land disposal of selected highly hazardous waste take effect during the next two years, the quantity of tonnage upon which the fee is assessed will decline. This will place a larger burden on those companies who continue to dispose on land.

Second, existing law requires monthly fee collections, which places an unnecessary administrative burden on both the state and the feepayers. The Legislature may wish to consider adopting a quarterly or annual payment mechanism, and expanding the tax base so that all types of hazardous waste facilities contribute to the cost of the regulatory program. For example, the Legislature could impose fees (1) on methods of treatment or disposal that are not currently assessed fees or (2) for operating permits.

Program Performance Improving

In our *Analysis of the 1983 Budget Bill,* we identified a number of serious management deficiencies within the department and concluded that the program had not produced results commensurate with the available funding and staff resources. Consistent with these observations, actual program results in 1982–83 were significantly below the department's stated goals. In the current year, however, the department has made progress in eliminating past deficiencies and improving program management.

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1982–83 Outputs Significantly Below Goals. The division failed to achieve many of its stated priority goals during 1982–83. The department had made a commitment to the Legislature to issue 50 permits during 1982-83. Only seven permits were issued. Existing law requires the department to issue regulations to implement specific program requirements. Few of the scheduled regulations were issued in 1982–83. According to data provided by the EPA, the department met 92 percent of its commitment for facility inspections but only 18 percent of its commitment to follow up on identified violations with administrative actions or court referrals.

Current-Year Improvement. The department has achieved a number of important accomplishments in the current year. After a national search, the department appointed six permanent section chiefs and reorganized its operations to give more authority to the regional administrators. It has signed memoranda of understanding with two counties for local inspection of waste generators and is negotiating with four additional counties. In September, the department released its first enforcement manual, which establishes uniform procedures for all inspections, follow-up activities, investigations, and referral to local law enforcement officers. The first quarterly report for 1984–85 indicated that the department was meeting most of its important output indicators, including permits and inspections.

Current-Year Problems. The major problem affecting the program in the current year is a substantial vacancy rate in new and existing positions. During the first half of the year, the permit, surveillance, and enforcement activities had up to 30 percent of the authorized positions vacant. The positions were left vacant to allow new managers to make the hiring decisions and to generate salary savings. Because the final appointments of the new section chiefs were delayed until mid-November, positions were vacant longer than originally intended. The department indicates that all positions should be filled by mid-February.

A secondary problem has been that the department has not completed negotiating a memorandum of understanding with the State Water Resources Control Board governing responsibilities of the two agencies in ground water monitoring and land disposal facility permitting.

The department's increased focus on enforcement has resulted in a reduction in the amount of attention given to waste reduction, recycling, and planning.

Federal Funding for Hazardous Waste Management. In last year's *Analysis*, we identified three problems in the department's management of federal funds provided by the Environmental Protection Agency (EPA) under the Resource Conservation and Recovery Act of 1976 (RCRA). Specifically, (1) the budget understated the amount of federal funds, (2) the department was consistently late in negotiating the annual contract with EPA, and (3) the timing of federal grant award precluded legislative review.

The department has improved in all three areas. The $3.7 million budgeted from RCRA in 1984–85 appears reasonable, given past funding trends. The department and the EPA concluded grant negotiations on time, and a grant was awarded on October 5, 1983. The EPA has agreed to change its grant period for this program from the federal fiscal year to a state fiscal year basis, as requested last year by the Legislature in the *Supplemental Report to the 1983 Budget Act.*

As these improvements are taking place, however, we have identified other potential federal funding problems. The EPA recently identified $203,000 of the 1982–83 grant expenditures that were not justified, based on the department's performance in meeting permit goals. At the time this analysis was written, the EPA had not yet determined whether it would require the department to return the funds or whether it would allow the state to carry forward the $203,000 into the current year. In addition, the EPA conditioned $1.85 million of its current-year grant on the completion of 13 specified key performance measures. If the department fails to meet some of these output goals, the EPA could withdraw funds and thereby create an additional liability to the HWCA.

Response to Legislative Reporting Requirements Improving. In past years we have criticized the department for failing to submit some legislatively mandated reports and for submitting others late. In the current year, the department has submitted three of six required reports on time, one report a month late, and one report three months late. As of February 1, 1984, it had not submitted the annual recycling program report, due on December 31, 1983, or any community relations plans for Superfund sites. No date had been specified for the submission of the plans.

Continued Reporting Needed

We recommend that the Legislature adopt supplemental report language requiring the department to submit (1) a comprehensive work plan for 1985–86, (2) quarterly reports on its 1984–85 accomplishments, and (3) compliance-based evaluation standards.

Although the department is improving its hazardous waste management program and meeting more of its key performance goals, we believe the existing planning and reporting requirements should continue.

Work Plan. One year ago, the Legislature required the department to develop a comprehensive work plan that displayed available staffing and funding and represented a commitment to accomplish specific quantifiable objectives during 1983–84. The Legislature required the work plan because the department had not met key performance goals, had moved resources from one activity to another, and had ignored recommendations made by the Auditor General. The Legislature also required that the department submit by March 31, 1984, a similar work plan for 1984–85.

Our analysis indicates that the work plan is a useful tool for the department in planning and managing its resources and for the Legislature, the EPA, and other interested parties in reviewing the department's priorities. In fact, the EPA accepted the state work plan as part of the RCRA grant application. This has meant that for the first time, the department has made the same performance commitments to both the Legislature and the EPA.

We recommend that the Legislature adopt supplemental report language to continue the planning requirement. We recommend, however, that the Legislature require the department to submit the work plan for 1985–86 on January 10, 1985, with the submission of the budget to the Legislature. Changing the date would allow the Legislature to evaluate the department's spending request for the budget year in the context of the state budget as a whole. The current March 31 date (1) is too late in the process to allow for a complete review and (2) does not facilitate comparisons of the department's budget to the budgets of other agencies.

Quarterly Reports. During the last three years, the Legislature required the department to submit quarterly reports on its toxic substances

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control activities. In the first two years, the department consistently submitted late reports that contained little useful information. In the current year, the Legislature adopted Budget Act language mandating the report and required submission of information on the department's progress in meeting specific commitments made in the work plan. The Legislature used the department's first report in the new format, issued prior to its due date, in an oversight hearing held in December 1983.

Due to the importance of the activities performed by the division, the past history of management deficiencies, and the usefulness of the reports in legislative oversight of the program, we recommend that the Legislature adopt supplemental report language continuing the quarterly reports in 1984–85.

Compliance-Based Evaluation System Needed. The information provided in the current work plan and quarterly reports provides an essential tool for the Legislature and the public to use in determining how the fiscal and personnel resources of the department are used. The information provides a count of the number of particular tasks performed, such as inspections. It does not, however, provide information to answer two important evaluation questions:

- What impact are the programs having on the regulated industries, the public health, and the environment?
- Are the program goals, priorities, and resources appropriate and adequate to protect the public health and the environment?

In order to provide answers to these two questions, we recommend that the Legislature require the department to (1) include in future work plans (a) a multi-year schedule for key performance measures and (b) compliance-based output indicators when appropriate and (2) report on a quarterly basis its progress in improving compliance with current law. For example, these indicators could reflect the percentage of inspected facilities complying with regulations, the amount of time needed to get facilities to comply, and the severity of violations. These compliance indicators would be in addition to the system for reporting frequency of current tasks such as inspections.

Recommended Language. Our recommended language requiring the department to continue the work plan and quarterly reports and to establish compliance-based evaluation measures follows:

"***Work Plan.*** The department shall prepare a work plan for the activities of the Toxic Substances Control Division (TSCD) in 1985–86 and shall submit that plan by January 10, 1985, to the chairpersons of the fiscal committees, the appropriate policy committees, and the Joint Legislative Budget Committee. The work plan should include the following: (1) quantitative goals and objectives for all sections, subunits, and regional offices of the TSCD and related units in the Health Protection Division, (2) identification of all program funding sources and positions by function, (3) workload standards for all staff assigned to the program, (4) a schedule for issuing program regulations, (5) a timetable of quarterly milestones, so that progress in meeting the goals set in the plan can be evaluated during the year, (6) specific changes in management or organizational structure that will be needed to achieve the goals of the plan, (7) clear priorities between various work goals and functions, (8) discussion of changes from the most recent work plan, (9) multi-year plans for activities that are scheduled for completion over an

extended time period, such as permitting and financial liability and closure plan review, (10) specific information on each Superfund site, and (11) compliance-based indicators to assess the department's impact on the regulated industries.

"Quarterly Reports. The department shall submit quarterly reports on the Toxic Substances Control Division's progress in meeting the objectives established in the 1984–85 work plan (including activities in related units located in the Health Protection Division). The report shall include (1) work-plan commitments achieved during that quarter, (2) changes to the work plan and justification for those changes, (3) filled versus authorized positions by activity, (4) summary information on enforcement actions undertaken against violators of hazardous waste laws and the division's success in achieving compliance, (5) the results of the inspection and regulation program for hazardous waste haulers, (6) status of the permit program including plans called in, draft permits prepared, final permits issued, and facilities that withdrew applications or requested exemptions or variances, and (7) site-specific expenditure data for each Superfund site. The report shall be due six weeks following the end of each quarter and shall be submitted to the chairpersons of the fiscal committees, the appropriate policy committees, and the Joint Legislative Budget Committee."

Permitting Augmentation of $1,703,000

We recommend approval.

The department issues hazardous waste facility permits to facilities that store, treat, or dispose of hazardous waste. The budget proposes an augmentation of 35 positions and $1,703,000 (25 positions and $867,000 from the Hazardous Waste Control Account, and 10 positions and $836,000 from federal RCRA funds) for this function.

Staffing levels for permitting have increased dramatically. The 1982 Budget Act authorized 25.5 positions. A mid-year EPA augmentation increased the number of positions to 43. Only 20.5 of the 43 positions, however, were actually filled. The 1983 Budget Act authorizes 35 positions. Since enactment of the Budget Act, the EPA has increased the department's grant award to fund 13 new positions and to provide a $500,000 augmentation for the State Water Resources Control Board. In December 1983, the Department of Finance notified the Legislature, pursuant to Section 28 of the 1983 Budget Act, that additional federal funds had been made available for expenditure by these entities.

The budget proposal for 35 new positions includes 25 new positions and 10 of the 13 positions administratively established in the current year as a result of the EPA grant augmentation. The augmentation will result in total permitting staff of 70 positions.

The augmentation would allow the department to complete issuing permits to all facilities regulated under federal law by June 30, 1988. The department's plan to complete the permitting process within five years is based on a number of assumptions about the actual number of facilities needing permits and the amount of staff time needed to issue the permits. The department currently estimates that 680 facilities will need permits, and that 95 permits will be issued by June 30, 1984, leaving 585 permits to be issued through 1988.

These estimates assume that many of the 1,100 facilities originally identified will choose not to apply for a final permit. A facility may drop out of the permitting process if it is unable to meet the rigorous requirements

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for a final permit. Other facilities may drop out of the permit process if they qualify for an exemption by changing their methods to reduce the time during which they store hazardous waste. The department assumes a drop-out rate of 50 percent for treatment and storage facilities and 33 percent for disposal sites. If fewer facilities drop out, more facilities will need permits. This may prevent the department from being able to complete all permits in five years. If more facilities drop out, the total number of permits issued will decline.

The department also makes assumptions regarding the number of permits that will be issued annually by each technical staff person. The workload standard for treatment and storage permits appear valid, based on the department's experience in 1983. It is more difficult to evaluate the standard for land disposal and complex treatment facility permits because the state has not tested this standard by issuing any of these permits. Major changes to this standard could also significantly affect the number of permits issued.

Our analysis indicates that the department's assumptions are the best available at this time and are reasonable. Therefore, we recommend approval of the augmentation. Additional information on the number of facilities to be permitted during 1984–85 will be available in the division's 1984–85 work plan, which is due to be submitted to the Legislature on March 31, 1984. We may have additional comments to offer the Legislature after reviewing the work plan.

Surveillance and Enforcement

We recommend approval.

The surveillance and enforcement units in the regional sections are responsible for inspecting hazardous waste facilities, investigating complaints, following up violations, developing enforcement cases, referring cases for court actions, and investigating problems in transportation manifests. The department's current staff of 55 positions includes 44 field staff and 11 supervisory and clerical personnel. Of the existing field staff, 14 positions conduct inspections at permittable facilities and hauler terminals. The remaining 30 field positions perform investigative activities. In the current year, they are attempting to eliminate a large backlog of unresolved cases.

The budget proposes 27 additional positions and $899,000 from the Hazardous Waste Control Account to increase the frequency of inspections. Of these positions, 20 are field inspectors, 3 are supervisors, and 4 are clerical staff.

The 1983–84 work plan estimates that the existing 14 inspectors will perform 500 storage, transfer, treatment, and on-site disposal facility inspections and 225 hauler terminal inspections in the current year. Next year, the current staff would be able to perform 790 inspections, or 65 more than in the current year, because positions would be filled with trained staff for the full year.

As part of its budget development process, the department evaluated the inspection frequency possible given current staffing and determined that it is inadequate. The department then developed a recommended minimum level of inspection frequency. Table 22 shows the recommended inspection frequency and required staffing. The proposed budget augmentation provides the staff needed to perform the recommend

"minimum" number of inspections. The department's request would allow for 2,108 inspections annually. The actual number of inspections conducted in 1984–85 will depend on the amount of time needed to hire and train the additional personnel. The department estimates that it may take as long as six months before the new personnel are fully productive.

Table 22
Department of Health Services
Recommended Inspection Frequencies and
Inspector Staffing Requirements for
Hazardous Waste Facilities

	Type of Facility			
	Storage, Transfer, or Treatment	*On-Site Disposal*	*Hauler Terminal*	*Totals*
Number of facilities	945	89	985	2,019
Workload standard (inspections per field inspector per year)	45	31	150	—
Inspection frequency (per year)				
1983–84 (estimated)	.43	1	.30	790
1984–85 (proposed)	1	2	1	2,108
Number of field inspectors				
1983–84 (estimated)	9	3	2	14
1984–85 (proposed)	21	6	7	34

We have reviewed the department's recommended inspection frequencies and associated staffing. It appears that one annual inspection is needed at most facilities, and that two inspections per year are needed at on-site disposal facilities. We therefore recommend approval of the 27 additional positions and $899,000.

Technical Support for Field Augmentations May Be Inadequate

We recommend that in its 1984–85 work plan, the department document the workload in the Alternative Technology and Policy Development Section related to providing technical support to the regional offices.

The budget proposes 26 positions and $1.6 million for the Alternative Technology and Policy Development Section. This is a reduction of 3 positions and $152,000 from the current year. This section is responsible for alternative technology development, technical determinations related to implementing the land disposal ban, resource recovery and waste exchange, facility siting, health and safety evaluations, and technical assistance to regional offices to support permitting and enforcement activities. Chemists, engineers, and geologists in the section are available to review technical questions that are beyond the ability of the regional program staff, including detailed review of plans for site closure and post-closure site maintenance. The 1983–84 work plan included very few workload indicators for any of these activities.

The budget proposes an increase of 62 additional field staff in 1984–85, which can be expected to generate increased requests to the Alternative Technology and Policy Development Section for technical assistance. No increased staff has been requested for this activity. When we asked about this potential problem, the department stated that it (1) was reviewing

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the workload in this section and (2) expects that some staff now developing regulations may become available in the future to provide technical assistance.

Before the Legislature approves the requested budget, we believe it needs the department's assurance that technical services will be available to adequately support the proposed new field staff positions. We therefore recommend that in its 1984–85 work plan, the department document the workload to provide technical services to the regional field staff. The documentation should identify the amount of additional workload that will be generated by the field staff augmentation and how the department intends to provide that level of support.

3/9/84 **Contract Funds are Excessive** recommend approval as budgeted. DHS provides justification

We recommend the deletion of $329,000 requested from the Hazardous Waste Control Account for contracts in the Alternative Technology and Policy Development Section because the department has no expenditure plan for the funds.

The budget proposes $438,000 in contracts for the Alternative Technology and Policy Development Section. We have reviewed the contracts and recommend approval of $109,000 for contracts involving (1) fish bioassay tests ($71,000) and (2) medical monitoring of field staff throughout the division ($38,000). Both of these contracts support the ongoing activities of the rest of the division.

We recommend deletion of $329,000 requested from the Hazardous Waste Control Account for contracts involving (1) the assessment of siting needs and alternative waste disposal methods ($284,000) and (2) market research for recyclers and alternative technologies ($45,000), because the department has not provided sufficient information to justify the need for these contracts. Specifically, the department did not provide a description of specific projects to be funded by the contracts, reasons why specific projects are needed, or a schedule for implementing these projects. In addition, we question whether the department actually intends to utilize these funds. In the current year, $118,000 available for siting and alternative technology purposes had not been encumbered at the time this analysis was written, and the department does not appear to have any specific plans for spending these funds.

We are unable to recommend approval of the funds requested for these contracts without better descriptions, justifications, and assurances from the department that the funds will indeed be used for the budgeted purposes. Consequently, we recommend deletion of the funds.

Financial Assurance and Liability Coverage

We recommend approval.

Chapter 90, Statutes of 1982 (SB 95), requires hazardous waste facility operators to (1) provide financial assurance of their ability to pay for the closure and maintenance of the facility at the end of its useful life and (2) maintain liability coverage for any damage caused by accidents or long-term contamination. The intent of these requirements is to prevent future uncontrolled sites contaminated by hazardous wastes of the type that currently are being cleaned up through the Superfund program. The Procedures and Regulations Development Section is responsible for reviewing the financial documentation and referring facilities that violate

regulations to the enforcement unit.

The budget requests an augmentation of 3.5 positions and $122,000 from the Hazardous Waste Control Account to review financial documentation expected to result from the 35 new positions in the department's permit staff. We recommend approval of this augmentation because financial reviews are needed to develop permits and to ensure that facilities are in compliance with existing law.

Data System Augmentation is Premature

We withhold recommendation on four positions and $305,000 requested from the Hazardous Waste Control Account for the purpose of augmenting the Hazardous Waste Information System until the administration completes its reevaluation of the computer system design.

The Hazardous Waste Information System (HWIS) is a computerized data base with subsystems that track (1) hazardous waste haulers, (2) hazardous waste transportation manifests, (3) permit, inspection, and enforcement activities, (4) waste generator and facility information, and (5) technical reference information. The department began designing the system in 1981. Currently, these subsystems are in various stages of implementation. The hauler system is fully operational and the technical reference files are virtually nonexistent. The existing staff of 8.75 positions is unable to implement and operate the system as currently designed. The manifest tracking system, in particular, is significantly behind schedule and is unable to guarantee "cradle-to-grave" control of hazardous wastes from generation and transportation to treatment and disposal.

The budget proposes an increase of four positions and $305,000 from the Hazardous Waste Control Account (HWCA) to improve the operation of the HWIS. The increase consists of $230,000 in new expenditures and a shift in funding source for $75,000 in ongoing program costs from federal funds to the HWCA because federal funds will not be available for this activity in the budget year.

At the time this analysis was prepared, the department was reevaluating its data needs. In December 1983, the division determined that a complete review of the HWIS was warranted because of ongoing operational problems with the system. The department has assembled a review team of data processing and program staff to review all components of the system and develop recommendations for changes in the design and use of the HWIS. The department anticipates that the team's report will be available by early March. We therefore withhold our recommendation on the HWIS augmentation until we are able to review the report and determine the impact of the report's recommendations on staffing needs.

Office of Public Information and Participation

We recommend that prior to budget hearings the department report to the Legislature on the expenditures by the Office of Public Information and Participation that are directly related to the Superfund program. We further recommend that the department include those costs in its revised expenditure plan for the Superfund program.

The budget proposes $462,000 and 4.5 personnel-years for the Office of Public Information and Participation (OPIP) in 1984–85. This office's duties include (1) insuring public participation in decisions regarding site cleanup at Superfund sites, regulations, and hazardous waste facility permitting, (2) responding to public inquiries, and (3) providing general public information on hazardous substances through newsletters and

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other means. The Hazardous Waste Control Account (HWCA) currently funds all of the office's costs.

The office supports a variety of the programs in the division, including the Superfund program, which is funded by the Hazardous Substances Account (HSA). When the office was first established, the department did not anticipate that activities related to Superfund sites would be the largest aspect of the program's workload, and therefore funded the offie entirely from the HWCA. The department had no experience upon which to distribute the costs between funds.

We believe that both the HWCA and the HSA should be used to support this office because OPIP serves Superfund supported activities as well as those related to ongoing hazardous waste management. We are unable to recommend a specific funding shift because the department was unable to provide workload estimates for the office showing the distribution of staff time between the two functions.

We recommend that the department report prior to budget hearings on the amount of OPIP expenditures directly related to the Superfund program. We also recommend that the department include that amount in its revised expenditure plan for the Superfund program. (The revised Superfund expenditure plan is discussed in detail later in this analysis.) An increase in HSA expenditures for this activity will result in a commensurate decrease in HWCA expenditures.

3/9/84 recommend approval as budgeted BOE changed workload estimates

Need to Adjust Payments to the Board of Equalization

We recommend an augmentation of $63,000 in the Hazardous Waste Control Account appropriation and a transfer of $101,000 within the Hazardous Substances Account appropriation from interagency agreements to remedial action contracts because payments to the Board of Equalization are misallocated between the two funds.

The Board of Equalization administers the fee and tax collection systems for the Hazardous Waste Control Account (HWCA) and the Hazardous Substances Account (HSA). On the basis of a workload analysis, the board's budget requests $346,000 in reimbursements from the Department of Health Services, including $179,000 from the HWCA and $167,000 from the HSA. The department's budget, however, proposes a total of $384,000, including $116,000 from the HWCA and $268,000 from the HSA (the budget document shows an appropriation of $346,000 from the Hazardous Substances Account, but the Department of Finance advises us that this is a technical error and that it should be $268,000). Thus, the department's budget proposes $63,000 too little from the HWCA and $101,000 too much from the HSA.

In order to correctly distribute the revenue collection costs between the two funds, we recommend an increase of $63,000 from the HWCA and a reallocation of $101,000 in HSA funds from the interagency agreement with the Board of Equalization to remedial action contracts. This recommendation will correctly distribute the $346,000 for the Board of Equalization's tax collection costs and result in an increase of $101,000 in the funds available to clean up hazardous waste sites.

Eliminate General Fund Support

We recommend a reduction of $13,000 in General Fund support for asbestos-related programs because the department was unable to provide any justification for these expenditures.

In 1980, the Legislature established one position supported by the General Fund to monitor asbestos contamination. The budget proposes to eliminate that position and $34,000 in General Fund support because the workload related to school contamination has been absorbed by the Department of Education and the workload related to general environmental exposures has been absorbed by the division's regional staff. Although this activity accounted for the only General Fund support in the division, the budget continues to show expenditures of $13,000 from the General Fund. The department was unable to provide any justification for the $13,000 expenditure. We therefore recommend deletion of the $13,000 from the General Fund.

B. SUPERFUND

The budget proposes $48.1 million for the third full year of the Superfund program. This amount consists of $10 million from the Hazardous Substances Account (HSA) and $38.1 million in the special projects listing. The $10 million requested from the HSA is the same as the current-year amount, and is based on the maximum amount of funds available in the HSA. The $38.1 million in special projects includes $16.9 million from the federal Superfund program and $21.2 million from parties responsible for past disposal of hazardous wastes. These amounts are also the same as the current-year amounts, which were based on the department's estimates of the costs to clean up specified sites from the 1983 Superfund site priority list. The amount actually received from these sources may be significantly less. The budget also proposes reappropriating up to $44.5 million in unexpended current-year funds for site cleanup.

The Superfund program, created in 1981, provides funding to (1) clean up hazardous waste sites that pose a threat to public health, (2) meet the state's obligation for a 10 percent match for funds received from the federal Superfund program, (3) support emergency response to the release of hazardous substances, (4) provide emergency response equipment to local jurisdictions, (5) compensate persons injured by exposure to releases of hazardous substances, and (6) perform health effects studies of people living near hazardous waste sites. Many of these functions are administered by the Toxic Substances Control Division. Other functions are performed by the Health Protection Division or by other departments or agencies.

Federal Superfund Program. The federal Superfund program was created by the Comprehensive Environmental Response, Compensation, and Liability Act of 1981 (CERCLA). This program will make available $1.6 billion over a five-year period to assist states to clean up contaminated sites. It is administered by the federal Environmental Protection Agency (EPA).

Hazardous Substances Account. The state Superfund program is supported by the Hazardous Substances Account (HSA), which receives revenues from taxes paid by *generators* of hazardous waste that is disposed of on land. The Board of Equalization is authorized to assess and collect up to $10 million in taxes from generators each year for 10 years.

Chapter 756, Statutes of 1981 (SB 618), established four categories of waste, based on the degree of hazard, and specified a base tax rate for each

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type of waste. The act requires waste generators to report annually to the board by March 1 on the amount of wastes produced in each of the four waste categories. The board then adjusts the base tax rates to generate enough revenues so that revenues plus specified unobligated funds expected to be available at the start of the budget year equal $10 million. The act authorized a loan in 1981–82 for program start-up. The department paid back the entire loan plus interest in 1982–83.

Recent Statutory Changes. Chapter 1044, Statutes of 1983 (AB 860), amended the original Superfund law to (1) exempt site mitigation contracts from certain review, (2) authorize multi-year contracts, (3) authorize prequalification of bidders for emergency response contracts, (4) allow the department to enter sites without the owner's permission, (5) authorize the department to clean up a site when responsible parties do not act promptly and to collect treble damages, and (6) establish procedures for public participation in department site mitigation decisions.

Chapter 1155, Statutes of 1983 (AB 1806), enables the department to request the Board of Equalization to recalculate and reassess taxes when the total taxes collected for the fiscal year are insufficient to reach the revenue target. This act was needed because the actual taxes collected by the Board of Equalization were below the amounts assessed for 1981 and 1982.

Significant Budget Changes. The budget proposes changes in some *categories* of spending but does not propose a major change in the total *level* of spending. Table 23 summarizes the actual 1982–83 expenditures, estimated current-year expenditures, and proposed budget-year expenditures.

The significant changes proposed in the budget year are as follows:

- ***Remedial action contracts,*** the largest single activity funded by the state Superfund program, would be reduced by $1.65 million. Most of this reduction reflects the deletion of $1.5 million in one-time funds for the McColl site cleanup. These funds were carried over from 1982–83 for expenditure in the current year. The balance of the reduction ($150,000) reflects increasing costs for staff, overhead, and other program activities that result in less funds being available for contracts.
- ***Statewide pro-rata charges*** will increase by $561,000. This amount represents the pro-rata charge for a two-year period because no funding was provided for this purpose in the current year.
- ***Interagency agreements*** would decrease by approximately $400,000, due to expiration of two projects established on a limited-term basis. The two agreements being eliminated are with (1) the California Highway Patrol, which provides hazardous materials training and curriculum development for first responders to emergency incidents ($263,000) and (2) the Department of Industrial Relations, which calls for the department to study health hazards experienced by emergency response personnel ($163,000).

Table 23
Superfund Expenditures
1982–83 through 1984–85
(in thousands)

	Actual 1982–83	Estimated 1983–84	Proposed 1984–85	Change Amount	Change Percent
A. Hazardous Substances Account (HSA)					
1. Remedial actions and response					
Cleanup contracts	$1,728	$6,127	$4,478 [a]	−$1,649	−26.9%
Department of Health Services support	1,283	1,713	1,677	−36	−2.1
Attorney General	90	104	110	6	5.8
Department of Water Resources	10	15	16	1	6.7
State Water Resources Control Board	—	35	37	2	5.7
Subtotals	$3,111	$7,994	$6,318	−$1,676	21.0%
2. Emergency response					
Emergency reserve	$521	$1,000	$1,000	—	—
Equipment	774	595	600	5	0.1
California Highway Patrol	292	263	—	−263	−100.0
Department of Industrial Relations	157	163	—	−163	−100.0
Office of Emergency Services	53	55	58	3	5.5
Subtotals	$1,797	$2,076	$1,658	−$418	−20.1%
3. Health effect studies	$114 [b]	$500	$500	—	—
4. Victim compensation					
Board of Control administration	55	43	43	—	—
Claims fund	—	312	312	—	—
Subtotals	$55	$355	$355	—	—
5. Board of Equalization tax collection	$243	$253	$268	$15	5.9%
6. Department of Health Services overhead	313	322	341	19	5.9
7. Statewide pro-rata	—	—	561	561	100.0
8. General Fund loan repayment	1,178	—	—	—	—
Subtotals, HSA	$6,811	$11,500	$10,000	−$1,500	−13.0%
B. Special projects					
1. Federal Superfund	—	16,900	16,900 [a]	—	—
2. Responsible parties	—	21,200	21,200 [a]	—	—
Subtotals	—	$38,100	$38,100	—	—
Totals	$6,811	$49,600	$48,100	−$1,500	−3.0%

[a] Amounts available in 1984–85 for remedial action contracts will be increased by reappropriation of up to $6.2 million from the HSA and up to $38.1 million in nonstate funds.
[b] Contracts only in 1982–83; staff costs and contracts in other years.

The Budget Proposal is Inaccurate and Incomplete

We withhold our recommendation on $10 million requested from the Hazardous Substances Account, $21.2 million from responsible parties, and $16.9 million in federal funds until the department submits (1) a revised budget proposal that corrects errors in the budget as submitted, (2) an updated site-specific expenditure plan for state, federal, and responsible party monies, and (3) a justification for 17 new positions for remedial action activities at specified certain sites.

Budget is Inaccurate. We identified numerous errors and discrepancies between the 1983 Budget Act, the fund condition statement, and the budget documents submitted to the Legislature. For example:

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- The amounts shown in the budget for three interagency agreements in 1983–84 (Board of Control, Board of Equalization, and Department of Industrial Relations) are inconsistent with the 1983 Budget Act and the budget justification provided by the department.
- The HSA fund condition statement appears to overstate the tax revenues for 1982–83 and the beginning reserves for all three fiscal years.
- The 1984–85 tax revenue amount assumes collection of the maximum $10 million authorized by Ch 756/81, despite significant carry-over reserves from prior years. Current law requires reductions in tax assessments by the amount of the unobligated balance.
- The budget shows a reserve at the end of 1984–85. The department has not explained why it has not planned to spend all available funds.

Budget is Incomplete. The budget lacks a detailed spending plan for the remedial action request. The budget proposes appropriations of $6,318,000 in state funds and $38,100,000 in federal and responsible party funds to clean up hazardous substances and mitigate the environmental and health effects of these substances. The budget also proposes reappropriations of up to $6.4 million in unexpended state funds and up to $38.1 million in unexpended federal and responsible party funds from the current year. The state fund appropriation includes (1) $4,478,000 for contracts with private firms to design and implement site cleanups, (2) $110,000 for legal services from the Attorney General, and (3) $1,677,000 to support department remedial action staff. The federal and responsible party fund appropriation would support additional remedial action contracts and 17 temporary positions. The reappropriations would support remedial action contracts.

At the time this *Analysis* was prepared, the department had not provided a site-specific spending plan for the state fund appropriation. The site-specific spending plan for the federal and responsible party fund appropriation is identical to the 1983–84 estimated expenditures. The department has not (1) reestimated the need for funds at each site, (2) reassessed the current status of efforts to acquire funds from these sources, or (3) justified 17 temporary-help positions proposed presumably to oversee expenditure of these funds on a site-specific basis. Nor does the department have a spending plan for the proposed reappropriation.

The department informs us that it intends to submit a revised budget proposal prior to budget hearings. We withhold recommendation on the Superfund budget request, pending receipt of the revised proposal.

The revised proposal should include:

- Site-specific spending plans for state, federal, and responsible party monies based on (1) the new site priority list released on January 10, 1984, (2) the department's estimate of the costs for remedial action, and (3) the likelihood of acquiring federal or responsible party funds.
- An estimate of the amount of the unencumbered balance for all sources of funds and a site-specific spending plan for the amounts proposed for reappropriation.
- Justification for the 17 new temporary-help positions proposed to be supported by federal funds and responsible parties.
- A corrected fund condition statement with revenue, expenditure, and carry-over reserve details for the three fiscal years.
- Revised amounts for interagency agreements with the Board of Control, Board of Equalization, and the Department of Industrial Relations for 1983–84 and 1984–85.

Underspending Will Probably Continue

When the Legislature created the Superfund program, it provided for annual expenditures and revenues of $10 million. In the first two years of the program, annual expenditures from tax revenues were significantly less than $10 million. In 1981–82, of the $2 million authorized, $843,000 was spent. In 1982–83, the first full year of the program, expenditures were $3.2 million less than the appropriation. This amount would have been $4.7 milllion if unbudgeted expenditures for department overhead and repayment of a General Fund loan had not reduced the net amount of underspending by $1.5 million. Our analysis indicates that the $4.7 million consisted of $2.4 million that was unspent due to circumstances within the control of the department and $2.3 million that was unspent due to statutory restrictions on the use of certain funds. The specific components of the $4.7 million are:

- $1.5 million set aside by the Legislature for the McColl site.
- $480,000 from the $1 million emergency reserve account.
- $300,000 for the Victims' Compensation program. These funds were not spent because there were no claims submitted.
- $2,420,000 of $6.1 million budgeted for remedial action personnel, contracts, and interagency agreements. The underspending here was due to (1) the freeze on hiring and contract awards, (2) an inefficient contract approval process, (3) the reduction of services rendered through interagency agreements, and (4) the absence of matching funds from the federal Superfund program.

We identified four causes for the underspending. First, the program has not yet emerged from a start-up phase that has been prolonged by the administration's hiring and contract freeze. This problem has been alleviated in the current year. The administration lifted the freeze on Superfund program hiring and site mitigation contracts, as directed by the *Supplemental Report to the 1983 Budget Act.* There have been efforts to improve the contract process, although it continues to be excessively long. The filling of positions, however, continues to be delayed. Second, some underspending in the early years of the program is a result of the unequal pattern of expenditures for sites. The total amount spent on sites each year will increase as the less expensive preliminary assessment and design phases are succeeded by the more expensive cleanup phase. Third, some underspending is due to statutory restrictions on funds, such as for emergency response and victims' compensation. A portion of these funds are likely to continue to be unspent in future years. Finally, some underspending may result from delays in specific site expenditures due to problems in obtaining federal matching funds or responsible party funds, or to late or incomplete information about the level of expenditures needed. This type of underspending is also likely to continue.

Remedial Action

The major purpose of the Superfund program is to implement remedial actions at uncontrolled hazardous waste sites in order to alleviate threats to the public health and the environment.

The budget proposes expending $6.3 million of the $10 million from the HSA, or 63 percent of available HSA funds, for this activity. Moreover, all of the $38.1 million that the department expects to receive from the EPA and responsible parties is budgeted for remedial action. Remedial action involves a complex sequence of activities that require increasingly larger

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commitments of resources. The sequence generally includes (1) discovery of an uncontrolled or abandoned site, (2) collection and analysis of data to determine the extent and type of contamination, (3) review of cleanup options to select the most cost-effective method and development of a detailed engineering design, (4) competitive bidding by contractors, (5) on-site cleanup work, and (6) monitoring or maintenance of the site after the cleanup if necessary.

Search for Uncontrolled Hazardous Waste Sites. The systematic search for uncontrolled hazardous waste sites in California began in 1980. By June 1983, initial surveys were completed in 28 counties. Almost 25,000 potential sites were identified. Of these, 20,300 were determined to be nonhazardous, 1,200 were referred to the regional offices for enforcement or other action, 105 were referred to the Superfund program for evaluation, and 3,000 need additional investigation. In the current year the department intends to investigate 900 of the 3,000 sites and to take samples at 60 sites using a $558,000 grant from EPA. The budget contains no funds to continue the abandoned site discovery or evaluation process after the federal grant expires.

Preliminary Assessment and Ranking. Each site is assessed to determine the hazards posed by ground water contamination, toxicity, and other factors. The department then ranks sites on a priority list published annually on January 10. The 1983 priority list contained 60 sites, and the 1984 list contains 93 sites. Many of the site rankings have changed from 1983 to 1984 due to (1) the addition of new sites, (2) reduction of hazards at a site through remedial action, and (3) changes in the ranking methodology designed to make the state methodology consistent with the methodology used by the federal EPA to develop its nationwide priority list.

Cleanup. Under current law, funds appropriated for remedial action must be expended in accordance with the priorities established by the ranking system. In general, state HSA expenditures for remedial activities have been limited to the top 18 sites. The department sometimes undertakes cleanup or investigative activities out of priority order, however, when (1) action at high-priority sites is delayed due to negotiations with the EPA or responsible parties or (2) the technical, legal, or financial issues involving a lower-priority site are relatively uncomplicated or (3) the EPA or responsible parties initiate remedial action.

At the time this *Analysis* was written, remedial action had been completed at two sites—Llano Barrels and Celtor. Llano Barrels was ranked number 35 and Celtor was number 14 on the 1983 priority list. Llano Barrels was a relatively simple cleanup, consisting of removing barrels and some spillage at a cost of $222,000. The potential for the further deterioration at the site required immediate action. The EPA took the lead in the Celtor cleanup, using one of its umbrella contracts to move quickly. The cleanup at Celtor cost approximately $340,000, with $34,000 from the HSA and $306,000 from the federal Superfund. As of January 1984, the Superfund program staff were negotiating with responsible parties for cleanup of three sites and with the EPA for cleanup of three sites. In addition, the department is negotiating with both the EPA and responsible parties for cleanup of Stringfellow and McColl. Staff of the Hazardous Waste Management program are negotiating with responsible parties for cleanup of some other sites on the Superfund list as part of enforcement activites.

Department Failed to Notify Legislature on Timely Basis

In the 1983 Budget Act, the Legislature authorized expenditure of $40.5 million from nonstate sources, even though it was uncertain that the state would actually receive these funds. The Legislature appropriated the funds in order to prevent unnecessary delays that would have occurred if the funds had not been included in the Budget Act. If the funds had not been appropriated, the department would have been required to seek a deficiency appropriation or wait 30 days after it received the funds, as Section 28 of the 1983 Budget Act requires. The Legislature adopted language in the *Supplemental Report to the 1983 Budget Act* requiring the department to notify the Legislature within 30 days when funds from nonstate sources are received in order to provide for legislative oversight without delaying remedial actions.

On August 18, 1983, the department accepted a $2.7 million EPA grant for the Stringfellow site. The department, however, did not notify the Legislature of the grant until December 19, 1983. The department and the Department of Finance indicate that confusion over the detail and the format of the notification resulted in the 90-day delay. The department has developed a procedure to correct the problem and states that it will provide future notifications within 30 days.

Rapid Program Changes and Increased Program Flexibility Necessitate Continued Reporting

We recommend approval of two technical changes proposed in the Budget Bill because these changes will increase program flexibility. We further recommend that the Legislature adopt supplemental report language requiring the department to report specified information about its planned and actual expenditures during the fiscal year.

The budget proposes two technical changes that will enable the department to respond to changing circumstances, and expedite the expenditure of site cleanup funds. Specifically, the budget proposes to (1) exempt reallocations of funds among sites from the Section 28 notification requirement and (2) budget federal and responsible parties' monies in the special projects line item instead of the contracts line item.

Site-Specific Expenditure Plan Will Always Be Subject to Change. Expenditure estimates for site cleanups are subject to wide margins of error due to uncertainty and changing information. To prepare the budget, the department estimates the cost of remedial action at certain sites on the site priority list in the upcoming year and the probability of obtaining federal or responsible party funds to support the remedial actions. As the year progresses, new information from site characterization studies, decisions on cleanup plans, and contractor bids may cause the department to change its cost estimates. The progress of negotiations with the federal Environmental Protection Agency (EPA) and responsible parties may cause the department to change its estimates of the funds available from these sources. Another factor affecting the department's expenditure plans is the site priority list. The department's cleanup priorities may change when the new list comes out in January or as new site information becomes available.

Provisions for Program Flexibility Are Justified Due to Rapid Program Changes. The Budget Bill proposes two changes to address uncertainties inherent in the budget proposal and to increase program flexibility:

- The Budget Bill contains language that would exempt reallocations

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among sites from the provisions of Section 28 of the Budget Act. This would expressly allow the department to reallocate funds among sites without legislative notification and a 30-day waiting period. The department may need to reallocate funds when (1) bids for contracts or actual costs are above or below the estimated cost and (2) federal funding—which requires matching by state funds—changes unexpectedly.

- The budget proposes inclusion of $38.1 million in federal and responsible party funds in the "special projects" line item. The budget also proposes 17 temporary-help positions in the special projects line item to perform site-specific monitoring functions. In the current year, these funds are budgeted in contracts. The department normally budgets funds in the special projects line item if (1) the amount of funds is uncertain and (2) the funds can easily be identified and managed independently of other department funds. The change in budget categories allows the department to rapidly establish temporary-help positions as federal and responsible party monies become available. Consequently, the size of the program staff can change as site cleanup funds fluctuate.

The provision for reallocation of funds among sites codifies current practice. We believe this practice is appropriate, given the department's need to respond rapidly to new situations that require fund reallocations.

Placement of the federal and responsible party funds in the special projects budget appears to be consistent with the department's normal budgeting practice. In concept, this appears to be appropriate. The department has not, however, explained how the new positions will be used. It is possible that the functions anticipated for the positions are inappropriate for placement in the special projects line item. We have withheld recommendation on the 17 positions and $38.1 million in the special projects line item, pending the receipt of a site-specific expenditure plan and justification for the positions.

Rapid Changes and Increased Flexibility Reduce Legislative Control. Due to the uncertainties surrounding the remedial action expenditure plan, the Legislature has no assurance that actual expenditures will be the same as the budgeted plan. The proposed technical changes increase the department's flexibility to respond to these changes with minimum delays. They tend to reduce further, however, the Legislature's ability to review and control program expenditures. To offset this loss of control, we recommend that the Legislature obtain regular reports on program status so that it is able to monitor changes in program direction and determine if the department is achieving planned objectives.

In the *Supplemental Report to the 1983 Budget Act,* the Legislature established requirements calling for the department to (1) notify the Legislature when nonstate funds are received from EPA or responsible parties and (2) submit quarterly reports describing the status of planned activities. We recommend consolidating the existing reporting requirements and expanding the categories of information in order to (1) track planned versus actual expenditures and receipts from federal and responsible parties *by site* and (2) evaluate the department's reasons for not making planned expenditures or for reallocating funds. To accomplish this, we recommend that the Legislature adopt the following supplemental report language:

"The department shall submit to the fiscal committees and the Joint Legislative Budget Committee, as part of its quarterly report, updates on its expenditures and related activities for the Superfund program from the Hazardous Substances Account, federal funds, or responsible party funds. The report shall include (1) amounts budgeted, spent, encumbered, or negotiated for each site, by funding source, (2) the steps taken to acquire funds from nonstate sources, and (3) comments adequate to track planned versus actual expenditures, and resources available."

Cleanup Funds Probably Are Inadequate

The total cost to clean up hazardous waste sites in California and the amount that the state will need to contribute towards the cleanups are difficult to determine. Any cost estimate depends on assumptions about the number of sites and the average cost per site. The state's share of the estimated cost depends on the amount available from the federal government and responsible parties. Nevertheless, our analysis indicates that the funds available from the state Hazardous Substances Account probably will be inadequate to meet the state's share of total cleanup costs.

After review of available data and discussions with the department and the federal Environmental Protection Agency (EPA), we have developed a series of cost estimates that are based on certain assumptions about the number of sites, the cost per site, and the availability of funds to support cleanups. The purpose of the estimates is to illustrate the *potential* magnitude of total costs, available resources, and additional funds needed.

Number of Sites. The 1984 Superfund site list contains 93 sites that pose a significant threat to the public health or the environment. The department expects to identify at least 100 additional sites through its abandoned site survey and ongoing enforcement activities. For the purposes of these calculations, we will use 200 sites as the likely total number of sites.

Cost Per Site. Site investigation and cleanup costs vary considerably, depending on the amount and type of contamination and the mitigation methods selected. The department cannot develop site-specific estimates at this time because it has not fully studied each site to determine the amount and type of contamination, nor has it selected a cleanup method for each site. The cost per site may range from $100,000 to over $40 million.

To develop estimates of cost per site, we first reviewed data on identified sites. We distributed the initial 100 sites into cost categories, based on these data. For example, we assumed that 25 percent of the sites will cost between $10 million and $40 million to investigate and clean up. These assumptions result in an average cost per site for the first 100 sites ranging from $4.7 million to $15.5 million. Second, we assumed that costs would be lower for the next 100 sites because the worst sites probably have been identified already on the current site priority list. With more of the sites occurring in lower-cost categories, we estimate that the average cost per site for the second 100 sites ranges from $3.5 million to $10.2 million. The combined average cost per site for the full 200 sites ranges from $4.1 to $12.9 million. The total estimated cost to clean up the 200 sites ranges from $820 million to $2.6 billion.

Availability of Nonstate Revenues. Currently, there are three sources of funds to finance the cleanup of hazardous waste sites: the state Hazardous Substances Account, the federal Superfund, and responsible

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parties. We assume that responsible parties will provide 50 percent of the total cost to clean up all sites and that EPA will award California 8 percent of federal Superfund monies.

Table 24 displays our estimates of costs and funds available for cleanups based on these assumptions. As the table shows, we estimate that the additional amount of state funds needed to clean up sites ranges from $220 million to $1.1 billion. The table also displays additional potential revenue if the federal Superfund program is extended for five more years at the current level of funding. If federal funds are available for an additional five-year period, the unmet need would range from $90 million to $970 million.

Table 24
Illustration of Potential Costs for Superfund Cleanups and Potential Need for Additional State Funds (in millions)

	Low	*Moderate*	*High*
Amount needed to clean up 200 sites	$820	$1,700	$2,580
Amount available under current law			
Responsible parties (50 percent of total costs)	410	850	1,290
State Superfund ($6 million per year for 10 years)	60	60	60
Federal Superfund (8 percent of national total)	130	130	130
Subtotals	$600	$1,040	$1,480
Additional state funds needed	$220	$660	$1,100
Amount available if federal Superfund legislation is extended 5 years	130	130	130
Additional state funds needed if federal Superfund legislation is extended 5 years	$90	$530	$970

Conclusion. Although our total cost estimates are based on a number of assumptions and have a wide margin of error, they illustrate the magnitude of the task facing the state if 200 hazardous waste sites are to be cleaned up. The actual amount of additional funds needed may vary significantly from the $660 million "mid-range" estimate. Even at the "low" estimate, and assuming that the federal Superfund is extended, an additional $90 million in new resources would be needed.

We do not recommend immediate legislative action to provide these funds. Clearly, many of the assumptions used in illustrating the potential need are based on incomplete data. Until the department determines more about the degree of contamination at specific sites, the likely cost of cleaning them, and the likelihood of identifying responsible parties or receiving federal funds, a specific recommendation for a long-term legislative response would be premature. Nevertheless, we recommend specific legislative changes to increase revenues in the short run, which are discussed later in this analysis.

General Obligation Bond Proposal. The Governor, on page 53 of the budget, proposes a $300 million general obligation bond issue that would provide funds to accelerate the rate at which hazardous waste sites are cleaned up. The full amount of the bonds plus interest would be paid back over a multi-year period from HSA taxes and payments from the federal government and responsible parties. At the time this *Analysis* was prepared, the proposed legislation and the department's cost projections

supporting the $300 million amount were not available. The $300 million bond proposal, however, does not appear to provide additional funds because it would be repaid by *existing* funding sources. If this is the case, it is not a solution to the long-term need for additional funds. We will be able to provide more complete comments on the proposal after the administration submits the proposed legislation and detailed cost estimates supporting the $300 million amount.

Reappropriation

We recommend:

1. ***Enactment of legislation to (a) alter the Superfund tax formula so that the full $10 million authorized by Ch 756/81 may be collected every year of the program and (b) delete provisions allowing funds appropriated for remedial action to be available for encumbrance after the close of the fiscal year for which the funds were appropriated.***

2. ***Deletion of the proposed reappropriation of unexpended state Hazardous Substances Account funds that were appropriated in the 1983 Budget Act for remedial action contracts.***

3. ***That the department include in its site-specific expenditure plan estimates of unobligated state funds from the current year and a plan for spending these funds, so that these funds may be added to the 1984–85 Superfund appropriation.***

The budget proposes to reappropriate all unexpended remedial action contract money remaining from the current-year appropriations of state Hazardous Substances Account (HSA), federal, and responsible party funds. The proposed language provides that the funds would be available for encumbrance until June 30, 1986. This would address the following two problems related to the treatment of unencumbered funds:

1. Under Ch 756/81 (SB 618), all unencumbered remedial action funds, as well as most other unencumbered funds, are included in the "unobligated balance" for purposes of calculating tax assessments. As a result, the level of tax assessments in the next year is reduced by the amount of the unobligated balance. The effect of the calculations involving the unobligated balance is to reduce the total amount of funds available for site cleanup during the 10-year life of the Superfund program.

2. Chapter 1044, Statutes of 1983 (AB 860), created a statutory inconsistency by making funds appropriated for remedial action available for encumbrance for three years after the close of the fiscal year in which the funds were appropriated. The act did not, however, remove these funds from the unobligated balance for the purposes of calculating tax assessments. Consequently, any unobligated funds carried over as a result of this provision would not increase the total funds available for cleanups in the next year. Instead, they would simply reduce the level of taxes assessed in the next year.

The reappropriation proposed by the budget would address both problems. By reappropriating remedial action contract funds it would remove them from the unobligated balance. Consequently, the level of taxes assessed in the next year would be higher. This would increase the total level of funds available for cleanups over the life of the Superfund program and clarify the statutory inconsistency.

Our analysis indicates that these two problems should be resolved. We recommend, however, a different solution to the problems. Specifically, we recommend:

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- Enactment of legislation to alter the tax assessment formula in order to eliminate the calculations involving the unobligated balance. This would allow all unobligated funds to be carried over into the next year without reducing the level of tax assessments. It would therefore increase the total amount of funds available for cleanup over the 10-year life of the program.
- Enactment of legislation to amend the statutory provision allowing funds for remedial action to be encumbered for three years. The amendment would delete the department's authority to encumber funds after the close of the fiscal year of the appropriation but continue the department's authority to enter into multi-year contracts if funds are encumbered during the year of the initial appropriation.
- Deletion of the proposed reappropriation of state HSA funds.
- An increase in the Superfund appropriation to reflect estimates of unobligated state funds that will be carried over from the current year. The amount of the increase would be determined after the department submits an expenditure plan identifying the estimated amount of unobligated funds and how they would be spent.

These recommendations would make additional funds available for cleanups, resolve the existing statutory inconsistency, and facilitate the Legislature's review of the department's annual spending plan. They would also avoid problems associated with tracking reappropriations. Our reasons for recommending these actions are discussed in detail below.

Need to Increase Funds Available for Cleanup. The Legislature designed the tax mechanism supporting the Hazardous Substances Account (HSA) to generate up to $10 million in revenues per year for 10 years. Collections may be less than $10 million in any year because the act requires the Board of Equalization to reduce tax assessments if the department estimates that there will be an unobligated balance in the account on June 30. The board calculates tax assessments so that the projected unobligated balance, called "M", plus total tax collections equal $10 million. Thus, the $100 million potentially available over the 10-year life of the program is reduced by the sum of unobligated balances carried over from one year to the next during the period.

Our analysis indicates that the program is likely to have an unobligated balance every year, due to (1) statutory restrictions on the use of funds (emergency response reserve and victims' compensation) and (2) delays in expenditures for specific sites. The delays at specific sites may result from problems in obtaining federal matching funds, unresolved technical or legal issues, or incomplete information. In addition, the program's capacity to expend funds may be low in the program's first few years, due to the relatively low cost of the early stages of remedial action (preliminary assessment, site characterization studies). The program's spending pace will increase in future years, due to (1) the development of the program's structure and procedures for cleanups as the department gains experience and (2) the higher costs of the latter stages of remedial action, which involve the actual site cleanup. These unencumbered balances could be large enough to significantly reduce the amount of funds available for cleanups over the life of the program.

As discussed in the previous section, the total amount of state monies needed to clean up hazardous waste sites may significantly exceed the $100 million potentially available from taxes deposited in the HSA. We do

not have a firm estimate of the amount that will be needed. Nevertheless, we believe it would be prudent for the Legislature to take action now to assure that potential revenues to the HSA envisioned when the account was established are utilized to the fullest extent possible. Consequently, we recommend adoption of legislation that would alter the tax assessment formula to allow the full $10 million to be collected each year, regardless of any balance in the fund that may be unobligated at the end of the prior year.

Specifically, the legislation would:

- Delete the calculations involving the unobligated balance ("M").
- Specify that the new tax assessment method shall be effective for taxes due July 1, 1984.

These actions would make additional state funds available for expenditure in 1984–85 and for the remaining years of the program. We recommend that the department include in its site-specific expenditure plan for the Superfund program (1) an estimate of the amount of unobligated funds at the end of the current year and (2) a plan for spending these funds, so that the Legislature can increase the HSA appropriation to reflect the additional amount that would be made available by enactment of the legislation we recommend.

Problems with Reappropriation and Allowing Multi-Year Availability of Unencumbered Funds. We have identified two problems with the budget proposal to reappropriate unexpended state funds and the statutory provision allowing unencumbered funds to be available after the fiscal year in which the appropriation was made. Specifically, the budget proposal and statutory provision:

1. ***Do Not Save All Unencumbered Funds.*** The reappropriation proposal and statutory provision each prevent a portion of the unobligated balances from reducing the total amount available for cleanups. They do not, however, prevent the entire unobligated balance from reducing tax assessments in the following year. The statutory provision allows the department to carry over unencumbered remedial action funds. The reappropriation proposal would allow the department to carry over only the remedial action *contract* funds. It does not allow staffing and other costs associated with remedial action to be carried forward. In addition, neither approach would allow carry-over of the entire unobligated balance. The unobligated balance may also include unobligated monies for interagency agreements, victims' compensation, and health effects studies.

2. ***Are Inappropriate Funding Mechanisms for Cleanup Projects Because They Prevent Legislative Review.*** The funds that the budget proposes to reappropriate would not be used for the type of projects usually associated with multi-year encumbrance authority and reappropriation. Normally, a multi-year encumbrance period is allowed for specific capital outlay projects when the project involves multiple stages with well-defined costs. Reappropriations normally are used to fund completion of specific projects when the project is delayed for some reason. In both of these cases, the Legislature does not need to review the expenditures during the latter years because the need for and the costs of the project are well-established.

In contrast, the state remedial action funds proposed for reappropriation in the budget are not for one specific site but for a group of sites. Moreover, the cleanup costs for each site included in the detailed justification for the original appropriation are subject to change due to improved information about the hazards and mitigation methods associated with

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each site. In addition, the original site list and expenditure plan might change when the new site priority list is issued annually on January 10 and during the year when the department obtains additional information.

Due to the potential changes in the department's spending plan for state funds after the initial appropriation, we believe the unencumbered state funds should not be reappropriated, nor made available for encumbrance after the initial year. Instead, the Legislature should reexamine the department's entire spending plan annually, including its spending plan for unencumbered funds remaining from the current year. If the department cannot spend funds appropriated for or reallocated to a certain site in the year funds were first available, there is nothing to preclude the department from including the site in the site-specific expenditure plan submitted in support of the following year's budget, if the site still appears on the Superfund priority list.

For these reasons, we recommend (1) deletion of the reappropriation provisions contained in the Budget Bill affecting state funds and (2) enactment of legislation to amend the provision allowing encumbrances over multiple years. This amendment would allow the department to encumber funds for a contract that extends over several years but delete the provision that makes funds for remedial action available for encumbrance for up to three years after the fiscal year for which the funds originally were appropriated.

Federal and responsible party funds are received for cleanup of particular sites. Consequently, the reappropriation of federal and responsible party funds is appropriate.

Contracting Process Is Inadequate

We recommend that prior to budget hearings, the department submit recommendations for enactment of legislation and/or descriptions of administrative remedies to streamline the Superfund contracting process.

The Superfund budget proposes $5.7 million for external consultant and professional services contracts. These contracts include $4,478,000 for remedial action, $1 million for emergency response, and $246,000 for health effects studies.

The division currently handles about 50 new contracts per year. Each contract must pass through 45 steps of development or approval. These steps occur in 16 different units or offices, including 13 units within the department.

Currently, it takes one to three months for contract development, which includes design specifications, a scope of work, and a formal request for proposal. Once the contract is developed, it takes four to six additional months for contractor selection and negotiation and approval by the department and by external agencies. Each of these steps can take additional time if revisions are required.

The lengthy process has contributed to the program's inability to spend appropriated contract monies. For example, in 1982–83 the department failed to encumber approximately $1.3 million in monies appropriated for remedial action contracts due to the lengthy contract process and the hiring freeze.

The Legislature adopted language in the *Supplemental Report to the 1983 Budget Act* requiring the department to streamline the contract process. The Legislature later passed Ch 1044/83 (AB 860) allowing multi-

year contracts and prequalification of bidders for emergency response, and exempting the program from certain provisions of the state contracting procedures. The changes were intended to accelerate contracting for remedial action.

During the first half of the current year, the department (1) established a tracking system for contracts and (2) contracted with the State Water Resources Control Board to use an existing computer program to establish schedules for the contracting process and contract expenditures. The department currently is developing a detailed descriptive analysis of the contracting process.

These steps are not sufficient to meet the legislative directive to streamline and accelerate the contract process. The department needs to evaluate the causes of the excessive length of the process and to develop recommendations to streamline it. For example, our analysis indicates that the staff has not been adequately trained in contracting procedures and that the department has not developed a contracting procedures manual.

We therefore recommend that prior to budget hearings, the department submit recommendations for statutory changes and/or descriptions of administrative remedies needed to streamline the Superfund program contract process. The report should discuss the causes and extent of delays, the staff training and workload for contracts, and options for improving the process.

The Department Has Not Developed Community Relations Plans as Required

We recommend that prior to budget hearings the department submit a community relations plan for each Superfund site funded in the current year. We further recommend that the Legislature adopt supplemental report language requiring the department to submit community relations plans by September 30, 1984, for each site funded in the budget year.

The purpose of the Superfund program is to control or clean up sites where contamination from hazardous materials poses a threat to the public health and the environment. In order to ensure that community residents are notified of and have an opportunity to participate in the department's decisions on how to clean up the site, the Legislature adopted language in the *Supplemental Report to the 1983 Budget Act* requiring the department to (1) submit to the Joint Legislative Budget Committee (JLBC) a community relations plan for each Superfund-supported site and (2) to offer to hold at least one public or community meeting for each site. Chapter 1044, Statutes of 1983 (AB 860), codified the requirement that the department provide an opportunity for community participation in the decision-making process and hold at least one public meeting. The act did not address community relations plans.

At the time this *Analysis* was prepared, the department had not submitted community relations plans for any of the sites funded for the current year. A draft plan for the Stringfellow site recently was developed to meet the requirement contained in a cooperative agreement with EPA, but the plan has not been officially submitted to the JLBC.

In order to ensure that the department fully consults with each community as intended by both the statute and the 1983 supplemental report we recommend that prior to budget hearings the department submit to the JLBC a community relations plan for each Superfund-supported site for which funding was provided in the current year. We further recommend that the Legislature adopt the following supplemental report language:

"The department shall submit to the chairpersons of the fiscal commit-

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tees and the Joint Legislative Budget Committee (JLBC), by September 30, 1984, a community relations plan for each Superfund-supported site for which funding is provided in the budget year."

Other Superfund Issues

Emergency Response

The budget proposes $1,658,000 for emergency response programs, including a reserve of $1 million for major emergencies, $600,000 for equipment purchased for local governments, and $58,000 for planning activities performed by the Office of Emergency Services. This is a decrease of $418,000 from current-year expenditures, reflecting the termination of two limited-term projects. The Department of Industrial Relations is completing its two-year study of the health hazards experienced by state and local emergency response personnel. Based on the results of this study, the department intends to set safety and exposure standards for these personnel. In addition, the California Highway Patrol will end its three-year training program for personnel responding to hazardous material spills. The curriculum package is available for local use, and it appears that community colleges, local jurisdictions, and professional safety associations will continue to provide training.

The *Supplemental Report to the 1983 Budget Act* required the department to develop a three-year plan for the improvement of state and local response to releases of hazardous substances. That report is due on March 1, 1984. We will make additional comments on the adequacy of the existing program at budget hearings, based on our review of this report.

Victims' Compensation Program Is Not Compensating Anyone

We recommend that the department explain at budget hearings its plan for ensuring that persons who are likely to be exposed to hazardous substance releases will be informed of the availability of victims' compensation.

The budget proposes $355,000 from the Hazardous Substances Compensation Account, including $312,000 for payment of claims and $43,000 for the Board of Control's administrative costs. These amounts are identical to the amounts appropriated in the current year.

Chapter 756, Statutes of 1981 (SB 618), provided for the payment, under specified circumstances, of compensation for out-of-pocket medical expenses and lost wages or business income caused by the release of hazardous substances. The law limits the amount of compensation to $15,000 per year. No claim for compensation may be presented for long-term exposure to ambient concentrations of air pollutants. The account is administered by the Board of Control.

No claims were filed in 1982–83 and only three claims have been filed in the current year. None of these claims has reached the board for judgment. There are three possible explanations for the lack of claims: (1) inadequate public outreach, (2) statutory restrictions, and (3) no one has incurred out-of-pocket medical expenses or lost wages or business income as a result of release of hazardous substances.

Inadequate Public Outreach. The board has issued press releases and notified physicians, medical facilities, and professional associations of the availability of the victims' compensation funds. The board, however, has not developed a program to notify residents living near hazardous

waste disposal sites or other persons with a probability of exposure to releases of a hazardous substance. Residents of communities located near disposal sites have complained at legislative hearings that despite months of attending hearings and meetings and receiving newsletters as part of the department's community relations activities, they were never informed about the victims' compensation program.

The board's failure to notify the public severely limits the ability of potentially eligible persons to apply for compensation. The department has drafted an interagency agreement that specifies in detail the responsibilities of the board in performing outreach functions. Under the agreement, the division's Office of Public Information and Participation (OPIP), which is responsible for a variety of public education and outreach activities related to toxic substances, would assist the board in developing its outreach program.

We therefore recommend that at budget hearings, the department describe its plan for ensuring that an adequate victims' compensation public outreach program is implemented. This should include a specific listing of proposed activities and expenditures to identify and inform populations that may be exposed to hazardous substances about the availability of victims' compensation.

Statutory Restrictions. Existing statutory restrictions may discourage individuals harmed by exposure to hazardous substances from applying for compensation. Current law requires that the claimant demonstrate that (1) the party responsible for the release cannot be determined, (2) the loss was not recoverable through court action, and (3) the financial or physical harm was directly caused by the release.

Last year the Legislature passed SB 1036, which would have made claimants eligible for compensation from the state account within 60 days of presenting a claim to the party believed liable. This would have made it unnecessary to exhaust judicial remedies before state compensation could be received. The state would have then imposed a lien on any future court settlement. This bill was vetoed by the Governor. In his veto message, the Governor said the bill was premature because the Hazardous Waste Management Council (HWMC) was reviewing legal issues related to financial liability and victims' compensation.

The HWMC draft plan was issued in January 1984. The plan recommends that the Legislature reevaluate the victims' compensation statutes in the areas of limited eligibility, coverage, and proof of causation.

Lack of Victims. It is possible that (1) the number of people that have been harmed by exposure to hazardous substances is significantly less than originally anticipated or (2) any losses due to releases of hazardous substances have been compensated by responsible parties or private insurance companies. We have no basis for determining to what extent these factors are responsible for the lack of claims.

6. CALIFORNIA MEDICAL ASSISTANCE PROGRAM (Medi-Cal)

Table 25 displays our recommended changes to the Medi-Cal budget. These changes reflect our analysis of where the budget contains funds that are in excess of the amount needed to fund the Medi-Cal program. Any funds released by these recommendations would be available for redirection by the Legislature to other high-priority health care needs or to other state-funded programs.

DEPARTMENT OF HEALTH SERVICES—Continued

Table 25

Summary of Legislative Analyst's Recommended Fiscal Changes in Medi-Cal Program (in thousands)

Issue	*General Fund*	*Federal Funds*[a]	*All Funds*
Federal matching reduction	−$23,319	$23,319	—
Peer group hospital rates	−24,311	−23,032	−$47,343
Claims processing improvements	−1,425	−1,425	−2,850
Past salary increase calculation	−1,614	−1,613	−3,227
Claims processing—cost reimbursements	−201	−595	−796
State controller audits	185	186	371
Health insurance recoveries—direct county input	−1,220	−1,080	−2,300
Child support recoveries	−500	−500	−1,000
State share of recoveries	−2,000	2,000	—
Uncleared recoveries	−689	−611	−1,300
CHAMPUS savings	−1,329	−1,261	−2,590
California Children's Services utilization review	−111	−110	−221
Treatment authorization review staff	−221	−524	−745
Total recommended changes	−$56,755	−$5,246	−$62,001
Withhold final action until May revision	$2,042,107	$2,125,134	$4,167,241
County-specific error rates—withhold	$1,312	$1,312	$2,624
Total amount on which recommendations withheld	$2,043,419	$2,126,446	$4,169,865

[a] Includes reimbursements and federal funds available for prior-year expenditures.

Program Summary

The California Medical Assistance program (Medi-Cal) is a joint federal-state program initially authorized in 1966 under Title XIX of the federal Social Security Act. The purpose of Medi-Cal is to assure the provision of necessary health care services to public assistance recipients and other individuals who cannot afford the costs of needed health care.

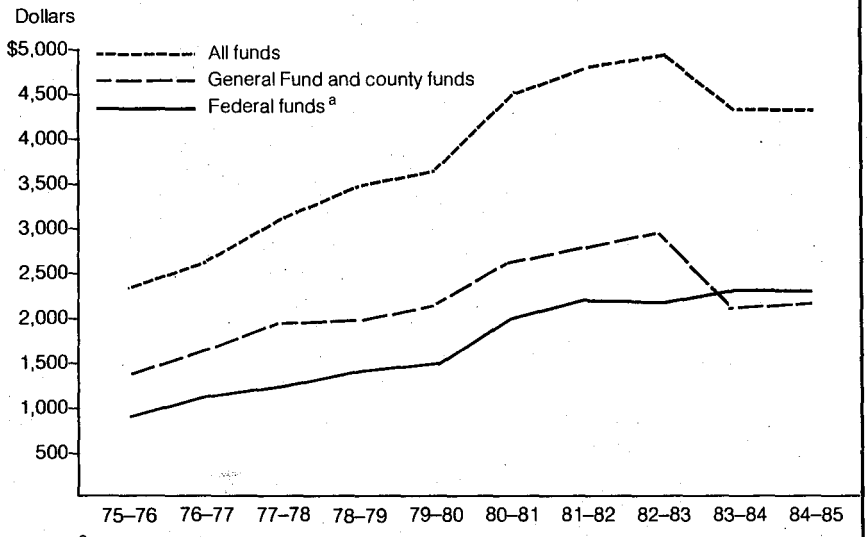
Public expenditures for the Medi-Cal program increased steadily and rapidly for many years. Due largely to the enactment of the 1982 Medi-Cal reforms (Ch 328/82, Ch 329/82, and Ch 1594/82), however, estimated Medi-Cal costs in the current-year will drop sharply. Moreover, the department expects only slight increases in Medi-Cal costs during 1984-85. Chart 4 displays federal, state, and county expenditures for Medi-Cal from 1975-76 to 1984-85.

Overview of the Medi-Cal Budget Request for 1984–85

The budget proposes Medi-Cal expenditures of $4,274 million ($2,081 million General Fund) in 1984–85, including $4,167 million ($2,042 million General Fund) for local assistance and $107 million ($39 million General Fund) for state administration. The total proposed level of General Fund expenditures for Medi-Cal in the budget year is $23 million, or 1 percent, more than estimated current-year expenditures.

Proposed General Fund local assistance expenditures in 1984–85 are $24 million, or 1 percent, above estimated current-year expenditures for this purpose. Medi-Cal local assistance expenditures are budgeted in Items 4260-101-001, 4260-105-001, and 4260-106-001 and include support for health care benefits, county eligibility determination activities, and claims processing.

Chart 4
Medi-Cal Expenditures by Funding Source 1975–76 through 1984–85 (in millions)



[a] Federal funds includes payments for health care provided to refugees and for amounts withheld during prior years.

Proposed General Fund state administration expenditures are $1 million, or 2 percent, below estimated current-year expenditures. Medi-Cal state administration expenditures are included in support items for the Department of Health Services (Item 4260-001-001), the Department of Social Services (Item 5180-001-001), and the California Medical Assistance Commission (Item 4270-001-001).

Table 26 shows Medi-Cal expenditures for 1982–83 through 1984–85. The proposed funding levels for Medi-Cal are discussed more fully in our analysis of the individual Medi-Cal program components.

Program Description

Federal, State, and County Responsibilities Under the Medi-Cal Program

The administration and funding of Medi-Cal are shared by the federal and state governments. Counties perform certain tasks on behalf of the state.

The state Department of Health Services (DHS) develops regulations, establishes rates of payment to health care providers, reviews requests for authorization of certain types of treatment prior to delivery, audits provider costs, recovers payments due from private insurance companies and other sources, reviews county eligibility determinations, and manages various contracts with private vendors for processing of provider claims. Other state agencies, including the California Medical Assistance Commission and the Department of Social Services, perform Medi-Cal-related functions under agreements with DHS.

DEPARTMENT OF HEALTH SERVICES—Continued

Table 26

Medi-Cal Expenditures and Funding Sources
1982–83 through 1984–85
(in thousands)

	Fund	Actual 1982–83	Estimated 1983–84	Proposed 1984–85	Percent Change
Health care services	General	$2,467,264	$1,953,752	$1,978,546	1.3%
	All	4,536,626	3,983,578	4,018,651	0.9
County administration	General	86,004	54,644	56,371	3.2
	All	146,873	126,189	119,816	−5.0
Claims processing	General	13,762	10,288	7,190	−30.1
	All	41,111	38,890 [a]	28,774 [a]	−26.0
Subtotals	General	$2,567,030	$2,018,684	$2,042,107	1.2%
	All	$4,724,610	$4,148,657	$4,167,241	0.4%
State administration	General	$38,969	$40,194	$39,353	−2.1%
	All	98,386	108,488	106,812	−1.5
Totals	General	$2,605,999	$2,058,878	$2,081,460	1.1%
	All	$4,822,996	$4,257,145	$4,274,053	0.4%

[a] Includes $397,000 in 1983–84 and $257,000 in 1984–85 in reimbursements from the County Medical Services Program for claims processing.

County welfare departments, and in Los Angeles County the county health department, determine the eligibility of applicants for Medi-Cal. In addition, many counties receive Medi-Cal reimbursements for services delivered to Medi-Cal-eligible individuals treated in county hospitals and outpatient facilities.

The federal Department of Health and Human Services, through its Health Care Financing Administration, provides policy guidance and financial support for the Medi-Cal program.

Eligibility

The department estimates that approximately 2.8 million persons, or about 11 percent of California's population, will be eligible for Medi-Cal benefits in each month during 1984–85. These eligibles fall into three major categories: categorically needy, medically needy, and medically indigent. The *categorically needy* (cash grant recipients) consist of families or individuals who receive cash assistance under the Aid to Families with Dependent Children (AFDC) or Supplemental Security Income/State Supplementary Payment (SSI/SSP) programs. The categorically needy automatically receive Medi-Cal cards. They pay no part of their medical expenses.

The *medically needy* include families with dependent children and aged, blind, or disabled persons who are ineligible for cash assistance because their income exceeds cash grant standards. These individuals can become eligible for Medi-Cal if their medical expenses require them to "spend down" their incomes to 133 percent of the AFDC payment level specified for their household size.

The *medically indigent* are those who are not categorically linked (that is, they do not belong to families with dependent children and are not aged, blind, or disabled) but who meet income and share-of-cost criteria that apply to the medically needy category. Effective January 1, 1983, coverage under the medically indigent program is limited to (1) persons who are under the age of 21, (2) pregnant women, and (3) persons residing in long-term care facilities. Table 27 summarizes Medi-Cal eligibility criteria.

Table 27
Medi-Cal Program
Selected Eligibility Criteria
1983–84

	Categorically Needy					*Medically Needy and Medically Indigent*		
	AFDC			*SSI/SSP*				
Non-income-related	Families with at least one child under 18 (including unborn children) and absent, deceased, or unemployed parent			Over 65, blind, or disabled		Medically needy: meets non-income-related criteria of either AFDC or SSI/SSP Medically indigent: under 21, pregnant, or residing in long-term care facility		
Maximum monthly income [a]	*Family Size*	*Maximum Net Income*	*Maximum Gross Income*	*Category*	*Maximum Net Income* [b]	*Family Size*	*Income Allowed After Spend-Down* *AFDC-Linked*	*Other*
	1	$258	$387	Aged and disabled		1	$459	$459
	2	424	636	Individual	$477	2	567	709 [c]
	3	526	789	Couple	886	3	709	—
	4	625	937	Blind		4	834	—
	5	713	1,069	Individual	535	5	959	—
				Couple	1,041			
Personal property	Combined personal and real property maximum: $1,000			Combined personal and real property maximum: $1,500 for individuals, $2,500 for couples		*Family Size*	*Maximum Value*	
						1	$1,500	
						2	2,250	
						3	2,300	
						maximum	3,000	
Real property	Home exempt			Home exempt		Home exempt Prior home exempt under specified conditions or if listed for sale and a lien is established		

[a] Maximum income levels may be increased in 1984–85, depending upon legislative action on SSI/SSP and AFDC cost-of-living adjustments. Net income does not include a $20 general income deduction allowed by the SSI/SSP program.
[b] These amounts are the SSI/SSP grant levels effective January 1, 1984.
[c] This higher income level for two-person adult households has been rejected by the federal government.

DEPARTMENT OF HEALTH SERVICES—Continued

Scope of Benefits

Medi-Cal recipients are entitled to a wide range of health services including physician, inpatient and outpatient hospital, laboratory, nursing home care, and various other health-related services. Many Medi-Cal services, however, require prior state authorization and may not be paid for unless the service is medically necessary. Not all services allowed in California are required by federal law.

Federal law *requires* states participating in the Medicaid program to provide a core of basic services, including hospital inpatient and outpatient; skilled nursing; physician services; laboratory and X-ray; home health care; early and periodic screening, diagnosis, and treatment (EPSDT) for individuals under 21; family planning; and rural health clinics (as defined under Medicare). In addition, the federal government provides matching funds for 32 *optional* services. California provides 30 of the 32 benefits—more than any other state except Minnesota.

Despite the wide range of health services covered by the Medi-Cal program, three service categories account for 80 percent of projected state and federal Medi-Cal expenditures in 1984–85. These services are (1) professional (physician, dental, and other medical), (2) hospital, and (3) long-term care (skilled nursing and intermediate care) facilities, including state hospitals.

Expansion of Capitated Health Systems

The department pays for the vast majority of Medi-Cal health care services on a per-service basis after the service is rendered. The Medi-Cal program contracts with a number of organizations for delivery of the remaining services on a prospective basis. In these cases, payments are provided at per-person (capitated) rates.

The "fee-for-service" payment mechanism has often been criticized for providing financial incentives to health care providers to provide unnecessary medical services. Many of these critics believe that prepaid, capitated health systems have the potential to control the costs of medical care through a combination of preventive health care and controls on utilization. This section discusses the current status of capitated health systems in the Medi-Cal program, the advantages and drawbacks of expanding the use of capitation contracts, and various issues regarding capitation that are now before the Legislature.

Budget Proposes Expansion of Existing Capitation Programs. The budget proposes $530 million (all funds) for capitated contracts with a variety of prepaid health plans and organized health systems. This amount is $158 million, or 42 percent, more than estimated expenditures for these programs during the current year. The major reasons for the proposed increase are (1) anticipated increases in enrollment in prepaid health plans and (2) the expected start-up of five new county organized health systems.

This increase for capitated programs does not translate into an overall increase in Medi-Cal spending. Instead, the care provided under Medi-Cal capitation programs would be substituted for care that otherwise would be reimbursed on a fee-for-service basis. As a result expenditures under the various capitation programs are proposed to increase from 9 percent of Medi-Cal expenditures in 1983–84 to 13 percent of all Medi-Cal expenditures in the budget year.

Table 28
Medi-Cal Capitation Programs
Enrollees and Expenditures
1983–84 and 1984–85

Program	Description	Enrollees 1983–84	Enrollees 1984–85	Expenditures—All Funds (in thousands) 1983–84	Expenditures—All Funds (in thousands) 1984–85
Prepaid health plans (14)	Provide comprehensive health services excluding long-term care. Payment levels are based on costs during the previous year but may not exceed the cost of comparable fee-for-service Medi-Cal benefits.	217,712	269,034	$173,442	$223,378
California Dental Services	Provides dental care to all Medi-Cal eligibles except some enrollees in other organized health systems. Contract on a sole source basis since 1974.	2,622,017	2,587,681	107,964	108,158
Redwood Health Foundation	Provides a comprehensive range of services to Medi-Cal beneficiaries in three northern California counties. Contract on a sole source basis since 1973.	43,637	43,637	38,741	41,730
County organized health systems (5)	Provide comprehensive health services, excluding long-term care.	46,524	131,012	51,595	156,985
Primary care case management	Individual providers or provider groups assume responsibility for case management. Any specialized services are available to beneficiaries only if referred by the case manager. As of January 25, 1984, one contract was in effect.	450	1,860	8	10
Expanded choice of health care plans	The 1982 Medi-Cal reform measures authorize California Medical Assistance Commission to enter into new pilot prepaid, capitated contracts with health care plans in at least two counties, in order to expand beneficiaries' choice of health plans. Medi-Cal beneficiaries would retain enrollment for at least six months. No contracts to date.	—	—	—	—
Totals		308,323 [a]	445,543 [a]	$371,750	$530,261
All Medi-Cal health care services		2,799,000	2,796,400	$3,983,578	$4,018,651
Percent of Medi-Cal health care services under capitation contracts		11.0% [a]	15.9% [a]	9.3%	13.2%

[a] Excludes California Dental Services.

DEPARTMENT OF HEALTH SERVICES—Continued

Table 28 displays current Medi-Cal capitation programs. The largest proposed expenditure is for health services provided by 14 prepaid health plans. The table shows that primary care case management and expanded choice contracts authorized by the 1982 Medi-Cal reforms have not yet been fully implemented.

The table does not include services provided under hospital contracts. These contracts are competitively bid and offer providers an incentive to reduce costs within contractually set per-day rates. The current hospital contracts, however, provide for flat payments per day of hospitalization, rather than flat payments per beneficiary. Therefore, hospital contracts are not considered capitation contracts.

Possible Benefits to Expansion of Capitation. A number of proposals have been made in recent years to expand the use of per-capita payments. The mechanisms that would be used to achieve this expansion range from contracting for a single Medi-Cal benefit (dental care or prescription drugs) or specified geographic areas (county health systems) to purchasing health care insurance for all Medi-Cal beneficiaries from private carriers. The principal benefits attributed to these proposals by proponents include:

- ***Reduced Costs.*** Because one organization is responsible for most, if not all, health care costs, and payments are limited to established rates per person, providers have an incentive to reduce health care costs under capitated payment systems. Whether or not expansion of such payment systems actually reduces state Medi-Cal expenditures would depend on the terms of specific contracts. Presumably, rates set for capitated health systems would be based on the actuarial value of benefits to be provided to recipients. If the systems provide the same scope of benefits, freedom of choice, and provider reimbursement as the current program, then costs would remain the same as they are under the current fee-for-service system. They might even be higher if contractors are allowed to build a profit into their rates. Medi-Cal costs would be reduced under capitation only if utilization of costly services is reduced *and* these cost reductions are passed on in the form of capitated rates that are lower than fee-for-service payments.
- ***Improved Health Care.*** Expansion of Medi-Cal capitation programs may result in improved health care for beneficiaries because the health care systems have a fiscal incentive for keeping the beneficiaries well. Consequently, the systems emphasize preventive health care to avoid the high costs of hospitalization. Under fee-for-service reimbursement, health care providers receive greater revenue for providing numerous high-cost health care services.

- ***Reduced State Administrative Costs.*** Under the fee-for-service method of reimbursement, the state incurs costs for processing claims for each service rendered and assuring that certain types of health care services are necessary. The need for these activities will be reduced if payments are based on per-person rates. These administrative savings would be offset to some extent by the costs involved in contracting and quality assurance reviews of capitated health systems.

Potential Drawbacks to Expansion of Capitation. Currently, Medi-Cal beneficiaries generally are not required to enroll in capitated health systems. In fact, they have little incentive to do so because Medi-Cal benefits under capitated health systems are identical to benefits under fee-for-service medical care. As a result, enrollments in existing prepaid health plans are lower than the maximum number allowed under the contracts. The department estimates that only 269,000, or 82 percent, of 330,000 contract slots in prepaid health plans will be filled in 1984–85. Consequently, any effective attempt to expand the use of capitated reimbursement would require either (1) improved marketing strategies to induce Medi-Cal beneficiaries to enroll in health care plans or (2) mandatory enrollment of some form.

The principal drawbacks from expanding capitated programs cited by various observers are:

- ***Restricted Access to Health Care Providers.*** If enrollment in a capitated health system is mandatory, beneficiaries may be denied access to health care providers of their choice. In fact, one of the chief benefits of capitated health systems is cost containment and improved case management through restriction of beneficiaries to a limited number of providers. The effect of this restriction on the quality of health care is uncertain.
- ***Lower Quality of Care.*** A portion of the savings gained by the shift from fee-for-service to capitation reimbursement might result from underutilization of health care services. This reduction in the intensity and quality of care is expected to result from provider efforts to reduce costs. It will be difficult to determine whether utilization controls under capitated health systems eliminate unnecessary health care or deny needed health care.
- ***Start-up Costs May Be High.*** Under the fee-for-service system, Medi-Cal providers bill the program after the service has been provided. Due to billing and payment delays, payment for some Medi-Cal services provided during the closing months of a fiscal year are not made until the following fiscal year. Because most capitation schemes involve payment before the service is delivered, Medi-Cal payments would be accelerated if capitation programs are expanded. As a result, there will be major one-time costs from any expansion of prospective payments. These costs could be spread over several years through phased implementation.

DEPARTMENT OF HEALTH SERVICES—Continued

Four Bills Propose Expansion of Capitation

Four separate measures now before the Legislature propose to expand capitation under the Medi-Cal program. These bills are similar in many respects. All four:

- Establish a statewide Medi-Cal reimbursement system based on capitated, at-risk contracts with a variety of health care delivery organizations.
- Include all Medi-Cal benefits except (1) long-term care, (2) mental health services, (3) dental services provided under a statewide contract, and (4) existing capitated pilot projects and prepaid health plans.
- Require that costs under the capitated health systems shall be less than estimated fee-for-service payments. Contractors would be at-risk for all health care costs for enrolled beneficiaries within specified risk limits.
- Discontinue fee-for-service reimbursement in specific geographic areas once contracts have been executed with capitated health systems having sufficient capacity to serve the Medi-Cal population within the area.
- Allow reimbursement to noncapitated providers only under limited circumstances.
- Allow beneficiaries to select a capitated health system and request reassignment (1) at any time for good cause or (2) on the anniversary day of enrollment. Beneficiaries who fail to choose a system will be assigned.
- Provide for phased implementation based on specified percentages of the statewide Medi-Cal population. The actual implementation schedule varies among the four bills.

Major Differences Among the Bills. Although the four measures are similar in many respects, they contain several differences. The major differences among the bills involve (1) the implementation schedule, (2) the range of services required under each individual contract, (3) the responsibilities of various state agencies, (4) licensure and certification requirements, and (5) non-capitation-related provisions. These provisions are summarized in Table 29.

General Medi-Cal Budget Issues

Estimates Will Be Updated in May

We withhold recommendation on $4,167,241,000 ($2,042,107,000 General Fund), pending review of revised Medi-Cal expenditure estimates to be submitted in May.

The $2,042,107,000 (General Fund) proposed for Medi-Cal local assistance in 1984–85 is based on expenditure estimates prepared by the depart-

Table 29

Major Differences of Four Proposed Capitated Health Systems Bills

Subject	*AB 516 (Filante) As Amended September 15, 1983*	*AB 1307 (Robinson) As Amended September 16, 1983*	*AB 1515 (Bronzan/Willie Brown) As Amended September 15, 1983*	*SB 667 (Maddy) As Amended September 15, 1983*
1. Implementation schedule	Pilot implementation in two phases: • During the first phase, beginning January 1, 1985, and concluding January 1, 1986, contracts will be awarded in geographic areas containing up to *25 percent* of Medi-Cal beneficiaries who receive public assistance payments. • During the second phase, ending January 1, 1988, capitated health systems will provide coverage to medically needy and medically indigent Medi-Cal beneficiaries, as well as those receiving public assistance payments. By the end of the second phase, contracts will be awarded in geographic areas containing up to *50 percent* of the state's Medi-Cal population. Implementation beyond the initial 50 percent may not proceed without additional authorizing legislation.	States intent to implement the capitated health systems statewide no later than five years after the effective date of the bill. Because the bill contains an urgency clause, statewide implementation would occur by sometime in 1989. Beginning on the effective date of the bill and ending January 1, 1986, contracts will be awarded in geographic areas containing up to *20 percent* of the state's Medi-Cal beneficiaries who receive public assistance payments. Implementation beyond the initial 20 percent may not proceed without express authority granted in the Budget Act.	Same as AB 1307.	Same as AB 516.
2. Range of services under each contract	An individual capitated health system need not provide or arrange for provision of the full range of covered services.	Each capitated health system must provide or arrange for provision of the full range of covered services.	Same as AB 1307.	Same as AB 516.

Table 29—Continued

Major Differences of Four Proposed Capitated Health Systems Bills

Subject	*AB 516 (Filante) As Amended September 15, 1983*	*AB 1307 (Robinson) As Amended September 16, 1983*	*AB 1515 (Bronzan/Willie Brown) As Amended September 15, 1983*	*SB 667 (Maddy) As Amended September 15, 1983*
3. Program administration				
a. Department of Health Services	The department shall be responsible for negotiating contracts and administering the program. Authorizes establishment of a special unit in the department to implement the Capitated Health Systems program. Transfers existing authority to contract with county health systems from the commission to the department.	The department shall perform various administrative tasks, including assignment of beneficiaries to health systems entering into contracts negotiated by the commission and evaluating the program.	Same as AB 1307.	Same as AB 516.
b. California Medical Assistance Commission	Transfers the commission's authority to negotiate contracts with county health systems to the department and deletes the commission's authority to negotiate contracts with expanded choice health plans. The commission will continue negotiating contracts with hospitals, including any contract amendments in cases where capitated health systems contracts affect hospitals' case mix. The Director of the department, currently one of two ex-officio nonvoting members of the commission, will become the eighth voting member. The Director of the Department of Finance will remain an ex-officio nonvoting member.	The commission shall negotiate contracts with capitated health systems in addition to negotiating contracts with hospitals, county health systems, and other expanded choice health plans.	Same as AB 1307.	Same as AB 516.
c. Other agencies	No major provisions.	Requires the Department of Finance to authorize the transfer of up to $2 million from the department's budget for support of the commission. Designates the Health and Welfare Agency as the "single state agency" for administration of the Medi-Cal program.	Same as AB 1307.	Same as AB 516.

4. Licensure and certification	Capitated health systems need not be licensed or certified by the Commissioners of Corporations or Insurance at the time of entering their initial contracts, but the system (a) must have the ability to meet requirements for certification and licensure, as determined by the department, and (b) must be certified or licensed, as appropriate, within 12 months of the initial contract effective date. The department shall not contract with a capitated health system whose application for certification or licensure has been denied. At least 30 days prior to the effective date of any contract, the department shall request a determination from either the Commissioner of Corporations or the Insurance Commissioner regarding the licensure/certification status and financial standing of the proposed contractor. These determinations shall be provided within 30 days.	Capitated health systems must be licensed, certified, or specifically exempt from licensure in order to enter into contracts under this program. At least 30 days prior to the effective date of any contract, the commission shall request a determination regarding the licensure/certification status of the proposed contractor. The Commissioner of Corporations and the Insurance Commissioner shall respond to such requests within 30 days.	Same as AB 1307.	Same as AB 516.
5. Provisions not related to the Capitated Health Systems program	None.	Requires the commission to negotiate an exclusive contract for provision of prescription drugs and related fiscal intermediary services.	States legislative intent to annually review the University of California health sciences program during consideration of the Budget Act. Places before the voters a $495 million state general obligation bond for capital expenditures for local health facilities.	Provides that the state cannot be the Medi-Cal fiscal intermediary.

DEPARTMENT OF HEALTH SERVICES—Continued

ment during October through December 1983. The estimates reflect "base program" costs and the costs of policy changes. The base program estimates are based on analyses of trends in the number of users, number of eligibles, cost per unit of service, and service mix. The most recent actual data used in the December estimate of base program costs are from Medi-Cal claims paid in August 1983.

Estimates of policy changes include the fiscal effects attributable to the 1982 Medi-Cal reforms and more-recent legislation and various court decisions. These estimates are based on assumptions that reflect the best information available at the time the estimates were prepared. Without actual data, however, there is considerable uncertainty associated with projecting the effects of these policy changes on Medi-Cal expenditures.

Due to this uncertainty, the Department of Health Services advises that actual 1984–85 Medi-Cal expenditures may be as much as $260 million ($162 million General Fund) higher or $194 million ($100 million General Fund) lower than the amount proposed in the budget. Thus, General Fund costs in 1984–85 may range from $1,942 million to $2,204 million.

Major Factors Affecting Estimate. Table 30 displays the major variables affecting the department's estimate of Medi-Cal expenditures. Later in this analysis, we recommend budget changes for those issues identified in Table 30 where our analysis indicates a change is appropriate. In other cases, we describe the reasons for uncertainty.

Table 30
Factors That May Alter Medi-Cal Budget Estimates
General Fund
(in thousand)

	1983–84	*1984–85*
Factors likely to reduce expenditures		
Lower federal matching reduction	—	−$23,319
Lower unemployment rate	−$4,000	−2,500
Hospital peer group rates	−20,986	−24,311
Property transfers *(Beltran* v. *Myers)*	unknown	unknown
Claims processing improvements	—	−1,626
Subtotals	−$24,986	−$51,756
Factors likely to inrease expenditures		
Copayment proposal	—	$6,400
Aid paid pending	unknown	unknown
Prudent purchase of products	$1,900	8,100
Abortion funding	15,700	15,700
Subtotals	$17,600	$30,200
Totals	−$7,386	−$21,556

Revised Estimates Due in May. The Department of Finance will transmit revised Medi-Cal expenditure estimates to the Legislature in May 1984. These estimates will be based on actual data through February 1984. Because more recent data will be available, the range of expenditures likely to occur in the budget year should be narrower than the range surrounding the December estimate.

In our analysis of proposed Medi-Cal local assistance expenditures, we recommend reductions of $56,559,000 from the General Fund and $4,747,000 in federal funds. The Legislature could properly take action on these recommendations prior to the May revision of expenditure estimates. We

withhold final recommendation on $4,167,241,000 ($2,042,107,000 General Fund) proposed for Medi-Cal local assistance until we have had an opportunity to review the more-accurate information on projected Medi-Cal expenditures that will be included in the May revision.

Unanticipated Revenue Totals $39 Million in 1983–84

Each year, the Medi-Cal program receives funds primarily from the federal government as payment for health care services expenditures made in prior years. The 1983 Budget Act provided that these past-year revenues would be used in two ways during 1983–84:

- Specific amounts up to $61 million identified as owed to the state offset the General Fund share of current-year Medi-Cal expenditures (Provision 2).
- Any amounts received in excess of this $61 million or received for purposes unrelated to those identified in the 1983 Budget Act are available to the Medi-Cal program to fund any anticipated deficiency. Amounts not required to fund Medi-Cal deficiencies are treated as revenue and deposited directly in the General Fund (Provision 3).

As of December 1983, a total of $99 million had been received during 1983–84 as payment for prior-year Medi-Cal expenditures. The budget does not identify any additional funds that may be received in the current year.

Most of the $99 million is federal repayments of funds withheld or deferred in past years. Of the $99 million, $60 million was anticipated by the 1983 Budget Act and, therefore, will be expended in the current year to offset General Fund expenditures. The remaining $39 million was not anticipated by the 1983 Budget Act. Of this unanticipated revenue, $5 million is required to fund an estimated deficiency in Medi-Cal local assistance; and $34 million will be deposited in the General Fund. Table 31 summarizes the payments received during the current year for prior-year expenditures.

Table 31
Deferred Federal Funds and Other Revenue Received During 1983–84
(in thousands)

	1983 Budget Act	*December 1983 Estimate*	*Difference*
Provision 2			
Refund of federal sharing reduction	$45,403	$45,019	−$384
Misclassified sterilization claims	7,266	7,266	—
Prior period refugee funds	8,621	8,179	−442
Totals	$61,290	$60,464	−$826
Provision 3			
Retroactive payments to date of application for disabled beneficiaries	—	$36,963	$36,963
Misclassified sterilization claims	—	283	283
County Medical Services program reimbursements	—	1,637	1,637
Totals	—	$38,883	$38,883
Needed for deficiency	—	5,164	5,164
Revenue to General Fund	—	$33,719	$33,719

DEPARTMENT OF HEALTH SERVICES—Continued

Additional Revenue Likely in 1984–85

We recommend the Department of Finance, as part of its May revision of Medi-Cal expenditure estimates, (1) identify all outstanding federal funding disputes, (2) indicate the nature of the dispute and the likely date on which it will be resolved, and (3) provide an estimate of 1984–85 revenue if these disputes are resolved in the state's favor.

Each year some amount of revenue is received due to resolution of outstanding Medi-Cal funding disputes between the state and the federal government. In the current year, the state received $37 million more in federal revenue than was anticipated by the 1983 Budget Act. In 1982–83 the state received $77 million more than anticipated.

$52 Million Anticipated in 1984–85. The budget projects that $51.8 million in federal funds will be received during 1984–85. These funds were withheld to achieve the federal sharing ratio reductions required by the Omnibus Budget Reconciliation Act of 1981, but for which the state has established its entitlement. The budget proposes to use these funds to offset the General Fund share of Medi-Cal expenditures during 1984–85.

Additional Amounts Likely. The budget does not reflect the fact that the department probably will receive additional federal funds during 1984–85 for past-year expenditures. Amounts in excess of the $51.8 million identified by the budget may be available to the state if outstanding disputes over federal funding are resolved in the state's favor prior to or during the budget year. For example, the state has identified $16 million in federal costs for sterilizations provided during the period April 1, 1981, to March 1, 1983. This amount has not been paid to the state, pending federal review of (1) the state's calculation of these costs and (2) documentation of beneficiary release forms. This issue could be resolved and payments made to the state during 1984–85.

In addition to payment for sterilizations, there are a number of other unresolved funding disputes that could result in revenue during 1984–85 in excess of the $52 million identified by the Department of Finance. Not reflecting this revenue overstates the need for General Fund support for the Medi-Cal program and, therefore, reduces the Legislature's spending options. In order for the Legislature to identify the true amount required from the General Fund for support of the Medi-Cal program, we recommend that the Department of Finance, as part of its May revision of Medi-Cal expenditure estimates, (1) identify all outstanding federal funding disputes, (2) indicate the nature of the dispute and the likely date by which it will be resolved, and (3) provide an estimate of the revenue that could be expected in 1984–85 if the dispute is resolved in the state's favor.

Federal Funding for Health Care Services and Administration

The federal government matches state payments for the cost of Medi-Cal administration and health care services that are provided in accordance with federal law. The federal share of costs for qualified components of California's Medi-Cal program ranges from 50 percent for health care services to 100 percent for certain licensing activities and health services provided to refugees. The state does not receive federal payments for the cost of health care services provided to individuals who are not eligible for subsidized services under federal law—notably, medically indigent adults.

The federal Omnibus Budget Reconciliation Act of 1981 (PL 97-35)

reduced federal sharing rates for Medicaid (Medi-Cal in California) expenditures by specified percentages for federal fiscal year 1982 (FFY 82), FFY 83 and FFY 84. Table 32 shows the effects of this reduction on the federal sharing ratios during each of the three federal fiscal years.

Table 32

Federal Sharing Ratios Under the Provisions of The Omnibus Budget Reconciliation Act of 1981 (PL 97-35) Federal Fiscal Years 1982, 1983, and 1984 [a]

Program Component	*Normal Federal Share of Costs*	*Federal Sharing Ratios Under PL 97-35*		
		FFY 82 (3% reduction)	*FFY 83 (4% reduction)*	*FFY 84 (4.5% reduction)*
1. Health care services to nonrefugees and most administrative costs	50.0% [b]	48.5%	48.0%	47.75%
2. Family planning, design of qualified claims processing systems, and fraud elimination	90.0	87.3	86.4	85.95
3. Operation of approved claims processing systems, specified administrative costs	75.0	72.75	72.0	71.63
4. Inspections of long-term care facilities	100.0	97.0	96.0	95.5
5. Health care services provided to refugees	100.0	100.0	100.0	100.0

[a] Federal fiscal years overlap state fiscal years. The three years included in this table begin October 1, 1981, and end September 30, 1984.

[b] Federal sharing for health care services in various states ranges from 50 percent to 83 percent, based on a formula that considers the relationship of per capita income in each state with national per capita income.

Federal Fund Sharing Losses Are Recouped in the Following Year. The provisions of PL 97-35 require the federal government to reimburse states for funds withheld due to the reduced sharing ratios if certain conditions are met. The reduction will be lowered by 1 percent (from 3 percent to 2 percent in FFY 82, for example) if the state (1) operates a qualified hospital cost review program, (2) has an unemployment rate that exceeds 150 percent of the national average, or (3) recovers at least 1 percent of total federal payments through a fraud and abuse elimination program. According to the Department of Health Services and federal officials, California's recovery program qualifies for the 1 percent offset.

More significantly, the reduction in federal sharing during any year will be reduced by the amount by which federal payments in the state are less than specified expenditure limits. Any refund based on this comparison with expenditure limits is made as a grant to the state during the first quarter of the federal fiscal year following the reduction.

Due largely to the implementation of the 1982 Medi-Cal reforms, California's expenditure total has been less than the federal limits for FFY 82 and FFY 83 and is expected to be well within the FFY 84 limit. As a result, the federal sharing reductions amount to a delay in federal payment from one state fiscal year to the next, rather than a permanent cost to the General Fund. For example, the budget estimates that the federal reduction in 1983–84 health care services expenditures will be $69.5 million. Of this amount, $17 million withheld in the period July to September 1983 will be returned during 1983–84. The budget anticipates that the remaining $52.5 million will be refunded in 1984–85.

DEPARTMENT OF HEALTH SERVICES—Continued

Reductions Expire September 30, 1984

We recommend a General Fund reduction of $23,319,000 and an increase in federal funds of the same amount based on a 3 percent federal sharing reduction rather than a 4.5 percent "worst-case" reduction.

The budget requests $54,411,000 from the General Fund in anticipation that the federal Medicaid sharing ratio reductions established by the Omnibus Budget Reconciliation Act of 1981 will be extended beyond FFY 84. Under current federal law, these reductions expire September 30, 1984. The $54.4 million assumes that the reductions will be extended at the FFY 84 level—4.5 percent, less 1 percent because California has a qualified recovery program.

The actual federal funding reduction after September 1984, if any, will not be known until Congress and the President act on the federal budget for FFY 85. Unfortunately, that will not happen until after the Legislature has completed its work on the state's 1984–85 budget. One indication of the likely federal action on these reductions, however, is the President's proposed budget. This document, released after the Governor's budget, proposes to continue the sharing ratio reductions at 3 percent.

Faced with this uncertainty, the Legislature's choices are to (1) assume extension of the maximum reduction (4.5 percent), as the budget has done, (2) plan for a moderate reduction, based on the President's budget proposal (3.0 percent), or (3) assume no extension of the federal funding reductions and budget for a return to full 50 percent federal support. It is unlikely that the federal government will return to full support, given the size of the federal deficit. We believe, however, that the 4.5 percent reduction assumed by the department is too pessimistic. Based on past experience, Congress is not likely to reduce the budget for Medicaid by more than what the President has proposed. Moreover, this pessimism carries a high price-tag, in that it reduces the Legislature's fiscal options by requiring a larger commitment to Medi-Cal from the General Fund than would be necessary if less pessimistic assumptions are made.

Our analysis indicates that the most reasonable strategy for the Legislature to follow is to assume extension of the reductions at the level proposed by President Reagan—3 percent. Given the performance of the state's recovery program, a reduction of this size would translate into a 2 percent reduction for California. Accordingly, we recommend that the Legislature reduce the amount budgeted from the General Fund by $23,319,000 to reflect the more moderate 3 percent federal sharing reduction and increase the appropriation of federal funds by the same amount. If the federal reduction is larger than what the President proposes in his budget, the balance can be appropriated from the fund established for this very purpose—the Reserve for Economic Uncertainties.

A. MEDI-CAL HEALTH CARE SERVICES

The budget identifies a 1983–84 General Fund deficiency of $7 million, or 0.4 percent, for health care services, partially offset by an estimated expenditure shortfall of $1.8 million in funds budgeted for county eligibility determination. The budget also identifies $39 million in unanticipated federal funds and reimbursements received during 1983–84 as repayment for health care services expenditures actually incurred in 1982–83 and earlier years. Of this total, $5 million is proposed to fund the estimated

deficiency in Medi-Cal health care services. The remaining $34 million will be deposited in the state General Fund.

For 1984–85, the budget proposes $1,979 million from the General Fund for Medi-Cal health care services. This is an increase of $25 million, or 1.3 percent, above estimated current-year expenditures. The proposed $25 million increase in General Fund expenditures is primarily due to a 2 percent rate increase for most providers.

The budget proposes a total of $4,019 million (all funds) for Medi-Cal health care services in 1984–85. This is $35 million, or 0.9 percent, more than estimated total expenditures in the current year. Table 33 summarizes the major adjustments to current-year and proposed budget-year expenditure levels.

1. Current-Year Deficiency May Not Materialize

The Department of Finance projects a current-year General Fund deficiency of $7 million, or 0.4 percent, more than the amount appropriated. The deficiency in health care services is partially offset by a net surplus of $1.8 million in county administration and claims processing. The Department of Finance proposes to fund the remaining $5.2 million deficiency with unanticipated federal funds.

This section discusses the major revisions in the current-year expenditure estimates that lead to the estimated deficiency and the reasons actual 1983–84 expenditures may vary significantly from the budget estimate.

Other Real Property—$35 Million Cost. The 1982 Medi-Cal reform legislation (Ch 328/82 and Ch 329/82) (a) reduced from $25,000 to $6,000 the equity a Medi-Cal beneficiary may have in real property other than an occupied home and (b) allowed persons whose homes are considered "other" real property (primarily nursing home residents) to continue receiving Medi-Cal benefits prior to selling the home only if the home is listed for sale and a lien is placed against the property for the cost of benefits. The 1983 Budget Act reflected savings of $73 million ($36 million General Fund) as a result of this revised treatment of other real property.

The budget now estimates that 1983–84 savings due to these provisions will total $3.0 million ($1.5 million General Fund). The $35 million reduction in projected General Fund savings is due to (a) reduction from 6,165 to 2,055 in the number of Medi-Cal beneficiaries estimated to possess other real property, based on more reliable information ($18 million), (b) court-ordered implementation delays ($17 million), and (c) enactment of Ch 323/83, the 1983 budget trailer bill, which expanded the definition of "principal residence" to exempt certain types of property from the $6,000 real property limit ($84,000). Assuming an implementation date of January 1984, the budget anticipates savings of $37 million ($18 million General Fund) in 1984–85 due to the lower property limits and collection on liens.

Prior-Year Refugee Costs—$13 Million Cost. The Medi-Cal program has claimed but not received $13 million in federal reimbursements through the department of Social Services for health care services provided to refugees prior to October 1, 1982. Until 1983–84, this $13 million has been funded by a special $45 million General Fund loan for Medi-Cal program emergencies. The nationwide federal appropriation for these past-year expenditures is exhausted. Unless Congress appropriates additional funds for this purpose, the $13 million owed California will remain

DEPARTMENT OF HEALTH SERVICES—Continued

Table 33

Medi-Cal Health Care Services
Proposed Budget Changes
(in millions)

	General Fund	*All Funds*
A. Funds available, 1983–84		
1. 1982 Budget Act	$1,951.9	$3,874.4
2. Refugee reimbursements	—	39.6
3. Federal funds and reimbursements received for prior-year expenditures	—	58.5
4. Increased federal funds	—	4.1
Subtotals	$1,951.9	$3,976.6
B. Unanticipated current-year expenditure changes		
1. Other real property—reduced savings		
a. Court cases	$16.7	$33.3
b. Revised estimate and Ch 323/83	18.1	36.3
2. Increased costs for court orders and settlements	4.5	9.0
3. Unreimbursed prior-year refugee costs	12.7	12.7
4. Hospital contracts—revised estimate	−22.2	−44.4
5. Reduced dental services rates	−6.5	−13.9
6. Liver transplants (SB 72)	2.1	4.3
7. Delayed county health systems implementation	−8.6	−16.5
8. Unbudgeted pharmacy fees	3.3	7.0
9. Net of all other changes	−13.1	−20.8
C. 1983–84 revised estimates	$1,958.9	$3,983.6
D. Projected current-year surplus/deficiency (−)	−$7.0	−$7.0
E. Proposed funding for deficiency		
1. Unbudgeted federal funds[a]	5.2	5.2
2. Transfer from county administration	(1.8)	1.8
F. Adjusted 1983–84 expenditures	$1,953.7	$3,983.6
G. Budget-year changes		
1. Other real property—increased savings	−$14.6	−$29.2
2. Full-year cost of 1983–84 court orders	7.8	15.8
3. Provider rate increases[b]	31.4	63.3
4. 2 percent beneficiary cost-of-living adjustment	5.4	10.8
5. New beneficiary copayments	−6.4	−12.8
6. Hospital contract savings	−28.0	−56.1
7. Reduced federal sharing ratio	12.0	—
8. Hospital inpatient cost-per-discharge limits	−4.5	−12.6
9. Accelerated payments due to tape-to-tape billing	9.6	19.2
10. Changes in caseload, units of service per user, and cost per unit of service	12.7	39.4
11. Deletion of one-time 1983–84 costs	−8.6	−13.7
12. Prudent purchasing of products—full-year savings	−6.1	−12.4
13. Liver transplants	3.5	7.1
14. County health systems start-up	4.9	9.7
15. Other expenditure adjustments	5.7	6.6
H. Proposed 1984–85 expenditures	$1,978.5	$4,018.7
I. Change from 1983–84 (adjusted):		
Amount	$24.8	$35.1
Percent	1.3%	0.9%

[a] Another $33.7 million in unbudgeted federal funds and reimbursements has been received as of December 1983. This amount is not required to support a deficiency and will, therefore, be deposited directly in the General Fund.

[b] Includes increases of 10 percent for noncontract hospitals, 7.4 percent for drug ingredients, and 2 percent for most other providers. No increase is included for contract hospitals.

a state liability. The budget reflects this liability as a 1983–84 General Fund expenditure.

Hospital Contracts—$22 Million Savings. The 1983 Budget Act anticipated savings of $136 million ($67 million General Fund) due to reduced hospital reimbursements under contracts negotiated pursuant to the 1982 Medi-Cal reform legislation. The budget estimates 1983–84 savings from these contracts will be $180 million ($89 million General Fund), an increase of $44 million ($22 million General Fund). The increased savings results from revisions in estimates of (a) costs per day for noncontract hospitals, (b) number of inpatient days in noncontract hospitals, and (c) costs for medical transportation.

Other Changes—$18 Million Savings. In addition to these major changes, a number of other factors result in net savings of $18 million. These other changes are the result of new court orders and settlements, legislation allowing Medi-Cal reimbursement for liver transplants, delayed implementation of county-organized health systems, and lower-than-anticipated rates for capitated dental services.

Reliability of Midyear Estimates of Current-Year Expenditures. Our analysis indicates the estimated 1983–84 deficiency may not materialize. The Department of Health Services advises that actual 1983–84 General Fund expenditures may be as much as $130 million higher or $84 million lower than the current estimate. Based on recent experience and our analysis of the current estimate, we believe it is more likely that actual expenditures will be lower.

In each of the past five years, the Department of Finance has overestimated the cost of Medi-Cal health care services in preparing its midyear (December) estimates. For example, the midyear estimate of 1982–83 expenditures was $102 million, or 4 percent, higher than actual expenditures. Even a 1 percent overestimate of Medi-Cal expenditures could result in actual expenditures being $20 million to $25 million less than the amount projected. Table 34 compares the December estimate with actual costs during the last five years.

Table 34

Reliability of Medi-Cal December Estimates
General Fund Expenditures for Health Care Services
1978–79 through 1982–83
(in millions)

	December Estimate	*Actual Expenditures*	*Difference*	
			Amount	*Percent*
1978–79	$1,907.4	$1,796.0	$111.4	5.8 %
1979–80	1,958.5	1,888.0	70.5	3.6
1980–81	2,353.1	2,300.8 [a]	52.3	2.2
1981–82	2,636.5	2,630.1 [b]	6.4	0.2
1982–83	2,569.2	2,467.3	101.9	4.0

[a] Includes $7.3 million of bills that could not be paid because sufficient funds were not available. These bills were paid in 1981–82.
[b] Includes $54.4 million of bills that were not paid in 1981–82. These bills were paid in 1982–83.

If the relationship between actual and estimated expenditures for 1983–84 is consistent with what it was during the previous five years (actual expenditures 3.3 percent less than estimated expenditures), 1983–84 expenditures will be $57 million *less* than the General Fund appropriation, rather than $7 million higher.

DEPARTMENT OF HEALTH SERVICES—Continued

In addition to the consistent pattern of overestimating Medi-Cal expenditures in the mid year estimate, there are two major factors that may cause General Fund expenditures in the current year to be less than the amount shown in the budget:

- ***Peer Group Settlement—$21 Million.*** The department advises that out-of-court settlements have been reached with all but one hospital to allow the use of hospital rates based on the costs incurred by groups of similar hospitals for payments dating back to December 1, 1982. Due to this settlement, it is likely that the Medi-Cal program will realize savings of $40 million ($21 million General Fund) as a result of the implementation of peer group rates in 1983–84.
- ***Pessimistic Unemployment Projection— —$4 Million.*** Current projections of the number of unemployed persons are 11 percent lower than the projections used by the department in estimating AFDC and medically needy Medi-Cal beneficiaries. This overestimate of Medi-Cal beneficiaries may overstate current-year General Fund costs by as much as $4 million.

While these factors may reduce current-year expenditures, other factors such as court orders and unanticipated program changes will undoubtedly increase General Fund costs during 1983–84. For example, the budget does not reflect the $15.7 million General Fund cost of providing unrestricted abortions pursuant to court rulings. In addition, the budget reflects General Fund savings of $1.9 million from implementation of prudent purchase of drugs and other products. This program was postponed indefinitely by the administration and probably will not result in savings in the current year.

Taking all of these factors into account, our analysis indicates that General Fund expenditures for Medi-Cal health care services in 1983–84 are likely to be slightly less than the amount available, rather than slightly higher, as projected by the Department of Finance.

2. Proposed 1984–85 Budget Adjustments

The budget proposes $4,019 million ($1,979 million General Fund) for Medi-Cal health care services in 1984–85. The General Fund request is $25 million, or 1 percent, above estimated current-year expenditures. Table 33 on page 962 summarizes the major funding changes reflected in the proposed level of expenditures. This section discusses the major factors accounting for the proposed increase in Medi-Cal expenditures.

Other Real Property—$15 Million Savings. The budget anticipates savings in 1984–85 of $16.3 million from implementation of the other real property provisions of the 1982 Medi-Cal reform legislation. These provisions require that specified Medi-Cal beneficiaries list their property for sale. The $16.3 million is $14.6 million more than estimated current-year savings. The increase primarily reflects the fact that these provisions are expected to be in effect for all of 1984–85, as opposed to only six months in the current year, and that there will be a six-month delay in the sale of the property. The projected savings are based on (a) lien collections for the cost of health care services provided prior to sale of the property and (b) 18 months of ineligibility for each of 2,055 Medi-Cal beneficiaries who will have excess income due to the sale of their other real property.

Full-Year Cost of Court Orders—$8 Million Cost. Court decisions on three major cases in 1983–84 will result in General Fund costs during

the budget year of $13.5 million, or $7.8 million more than during the current year.

Provider Rate Increases—$31 Million Cost. The budget proposes provider rate increases of 10 percent for noncontract hospitals, 7.4 percent for drug ingredients, and 2 percent for all other providers except contract hospitals for increased General Fund costs of $31 million. The budget proposes no COLA for contract hospitals.

Copayments—$6 Million Savings. The budget anticipates enactment of legislation to charge Medi-Cal beneficiaries for nonemergency use of hospital emergency rooms ($10), drug prescriptions valued at less than $10 ($1) and more than $10 ($2), and a variety of other Medi-Cal reimbursed services ($2). These copayments would be mandatory and would result in lower Medi-Cal payments to providers, for an estimated General Fund savings of $6.4 million.

Hospital Contracts—$28 Million Savings. The budget projects General Fund savings of $118 million, or $28 million more than current-year savings, from lower hospital rates paid under contracts negotiated pursuant to the provisions of the 1982 Medi-Cal reform measures. This increased savings is due primarily to a 10 percent increase in the costs Medi-Cal would pay for hospital care without these negotiated contracts.

Federal Fund Changes—$12 Million Cost. The budget reflects (a) lower 1984–85 refunds ($9 million) of federal funds withheld during 1983–84 than received in the current year for funds withheld in 1982–83 and (b) higher reductions in federal funds under the sharing ratio reductions of the Omnibus Reconciliation Act of 1981 during the budget year ($3 million). Because the reduction provisions expire September 1, 1984, it is not certain that these additional costs will materialize.

Caseload, Utilization, and Cost Per Patient—$13 Million Cost. The budget includes $13 million to cover the net increase in costs associated with caseload, utilization, and cost per beneficiary, not including the costs of proposed provider rate increases and savings due to hospital contracting and cost per discharge limitations. The budget assumes a 0.1 percent reduction in the total number of Medi-Cal beneficiaries and a 0.7 percent increase in the number of beneficiaries who actually use Medi-Cal services. The budget assumes, however, that fewer beneficiaries will use the more expensive services, such as hospital care, resulting in a General Fund savings of $45 million in 1984–85.

The budget also assumes that the number of units of service per user will decline, resulting in reduced General Fund costs amounting to $29 million. This savings is due primarily to reduced lengths of stay in community hospitals and intermediate care facilities. The intensity with which most other Medi-Cal services are used is expected to increase slightly.

Due to use of higher-cost services and general cost increases, the per-unit costs of Medi-Cal services are expected to rise ($87 million). These increases would be higher, however, if the various savings measures established by the 1982 Medi-Cal reforms were not in place or if provider rates are increased beyond the levels proposed by the Governor.

Estimate Vulnerable in Many Areas. The department advises that actual Medi-Cal health care services expenditures may be as much as $260 million ($162 million General Fund) higher or $194 million ($100 million General Fund) lower than the amount proposed in the budget. The range of uncertainty estimated by the department reflects (1) normal variation due to unanticipated changes and errors, (2) potential federal error rate sanctions, (3) possible court rejection of proposed restrictions on elective

DEPARTMENT OF HEALTH SERVICES—Continued

abortions, and (4) possible federal denial of a waiver necessary to implement proposed beneficiary copayments. We have identified a number of additional areas where actual Medi-Cal costs may vary significantly from the department's estimate.

- ***Beltran v. Myers***—retroactive costs. The department estimates that payments to 1,100 beneficiaries denied Medi-Cal eligibility prior to 1981 due to property transfers will cost $15.3 million ($7.6 million General Fund) during 1984–85. At the time the December estimate was prepared, notices had not been sent to the possible beneficiaries of this court decision. There is considerable uncertainty in this estimate because (1) notices must reach eligible persons and (2) in order to receive payment, the beneficiaries must submit documentation of health care costs incurred during the period, now more than three years' past.
- Liver transplants. The budget proposes $11.4 million ($5.7 million General Fund) for 34 liver transplants authorized by Ch 1173/83 and continued health care for 11 patients surviving such operations during the current year. Because this benefit was offered under Medi-Cal for the first time in 1983–84, no data exist on either the cost per patient or the number of patients who may require transplants and for whom a suitable organ is available. Moreover, the budget estimate does not reduce the costs of these procedures to reflect the fact that considerable Medi-Cal health care costs would have been incurred for treatment of these extremely ill persons in the absence of the transplant procedures.
- Reduced unemployment rate. The number of unemployed persons used in calculating the number of Medi-Cal beneficiaries exceeds current unemployment projections for 1984–85 by 14 percent. As a result, the department advises that the estimate of Medi-Cal eligibles is 17,500 too high and the expenditure estimate is $5 million ($2.5 million General Fund) too high.
- Prudent purchasing of products. The budget anticipates savings of $16.3 million ($8.1 million General Fund) based on implementation of volume purchasing agreements for prescription drugs, laboratory services, and eye appliances. On December 28, 1983, however, the Governor postponed indefinitely the implementation of the first of these arrangements, prescription drugs, pending further study. It is uncertain whether this program will be implemented and when Medi-Cal savings will occur.
- Aid paid pending. Upon being notified that their Medi-Cal eligibility was terminated, 22,000 medically indigent adults filed for fair hearings. These beneficiaries receive Medi-Cal supported health care pending resolution of the fair hearings and, in many cases, a disability determination. The budget anticipates that these fair hearings will be completed by December 1983. In January 1983, however, 5,700 cases remained on aid paid pending the resolution of their appeal, at an additional monthly General Fund Medi-Cal cost of $1.2 million. As a result, Medi-Cal aid pending expenditures will exceed the 1984–85 projection by an undetermined amount. In our analysis of the support budget for the Department of Social Services (Item 5180-001-001), which is responsible for fair hearings and disability evaluations, we recommend the Department of Social Services submit to the Legisla-

ture a revised schedule for resolving these 5,700 cases.

3. 1984–85 Medi-Cal Health Care Services Expenditures in Perspective

The budget proposes few major changes to eligibility rules or the range of benefits available to Medi-Cal recipients. This section describes the components of proposed 1984–85 Medi-Cal health care services program expenditures and compares the proposed expenditure level with earlier years.

Eligibles and Users. The budget projects that an average of 2,797,000 persons will be eligible for Medi-Cal benefits each month during 1984–85. This is 3,000 less than the number of beneficiaries eligible in the current year.

Of the eligible population, an average of 45 percent, or 1,261,000 persons, are expected to use Medi-Cal benefits each month during 1984–85. This is an increase of 9,000 persons, or 0.7 percent, above the number of monthly users in 1983–84. The largest increase in users, 13,000, is expected among those Medi-Cal beneficiaries who receive public assistance grants (categorically needy).

The percentage of eligibles who actually use Medi-Cal services varies among the eligibility categories. In 1984–85, for example, 44 percent of the categorically needy and 55 percent of the medically needy will use services each month. By contrast, only 37 percent of medically indigent beneficiaries will use Medi-Cal benefits during 1984–85. The medically indigent population historically has had the highest utilization rates. The 1982 Medi-Cal reform legislation, however, terminated Medi-Cal eligibility for most adults in the medically indigent group. Consequently, now 85 percent of the medically indigent population are children, many between 18 and 21 years of age. Because this group requires less health care on average than the medically indigent adult population, utilization for the medically indigent is expected to decline in 1984–85. Table 35 displays the number of Medi-Cal eligibles and users, by aid category, from 1982–83 to 1984–85.

Table 35
Average Monthly Medi-Cal Eligibles and Users as Percent of Eligibles By Eligibility Category 1982–83 through 1984–85 (in thousands)

	1982–83		1983–84		1984–85	
	Eligibles	Percent Users	Eligibles	Percent Users	Eligibles	Percent Users
Categorically needy						
AFDC	1,662	34.2%	1,665	34.4%	1,660	35.2%
SSI/SSP	677	68.1	674	66.6	672	66.7
Medically needy	322	62.4	339	55.1	345	54.5
Medically indigent	211	67.3	112	40.2	110	37.0
Other [a]	14	100.0	10	100.0	10	100.0
Totals	2,886	47.8%	2,800	44.9%	2,797	45.3%

[a] Includes renal dialysis patients and refugees.

Expenditures by Eligibility Category. Proposed 1984–85 expenditures are higher for categorically needy and medically needy categories

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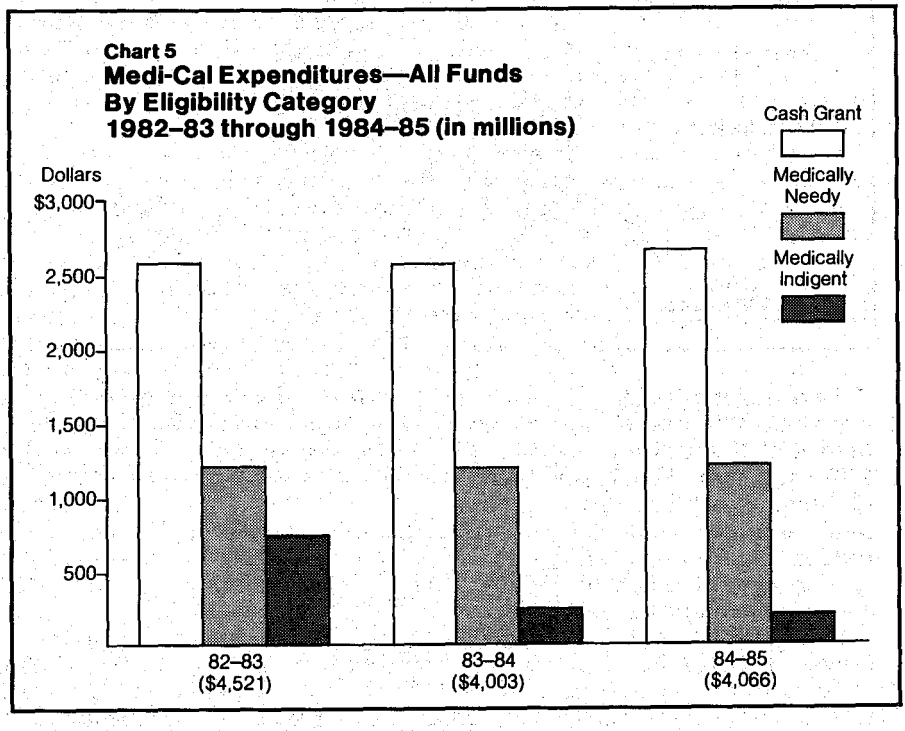
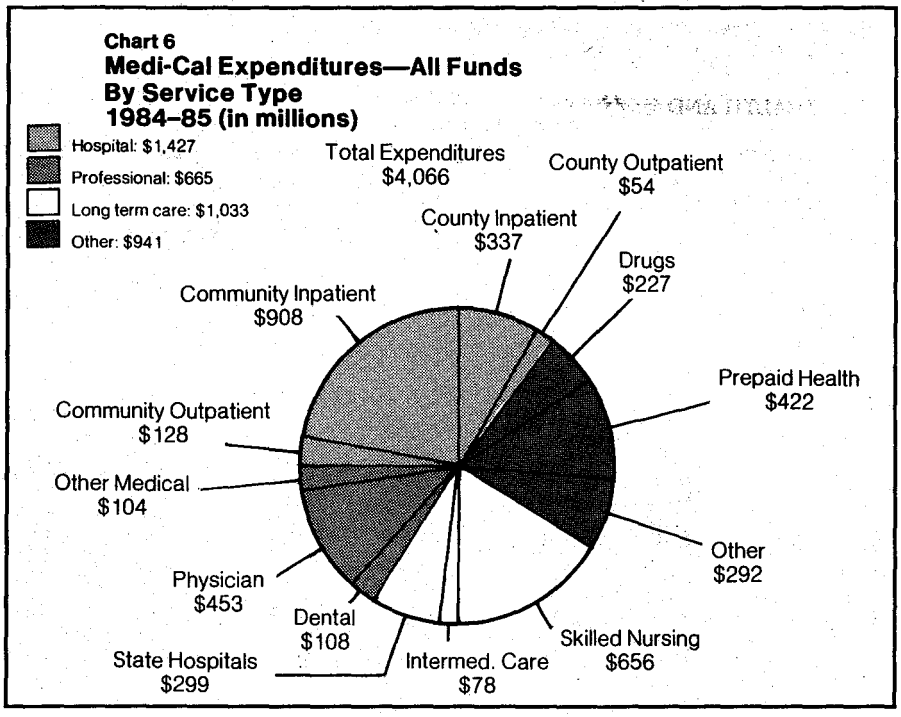
and lower for medically indigent beneficiaries than the levels of expenditures estimated for 1983–84. The major increase, $91 million, is expected in the categorically needy category. Chart 5 compares proposed expenditures, by aid category, with estimated current-year and actual 1982–83 expenditures. Chart 5 also shows that expenditures for medically needy persons account for 30 percent of total proposed Medi-Cal expenditures in 1984–85. Medically needy persons account for only 345,000 of the 2,797,000 eligibles, or 12 percent, of the total eligible population. The disproportionate expenditures for the medically needy are accounted for by higher than average use of services, especially high-cost services such as hospital and nursing home care, by those persons.



Expenditure by Service Type. Subject to various utilization controls, Medi-Cal beneficiaries may receive a wide range of health care services. The largest share of health care expenditures is accounted for by hospital care (35 percent). Chart 6 shows the proposed expenditures for major services in 1984–85.



Two major provider groups have experienced a reduction in income from the state due to the estimated $455 million decrease (all funds) in Medi-Cal expenditures since 1982–83. Hospital income has declined by $507 million, or 26 percent, primarily due to (a) negotiated contracts, (b) elimination of eligibility for most medically indigent adults, and (c) other new reimbursement methodologies. Physicians have experienced a $264 million, or 37 percent, reduction in income from the state due primarily to eligibility changes, restriction of benefits based on medical necessity, and rate reductions.

During the same period, expenditures for long-term care have increased by $81 million, or 8.5 percent, due primarily to slight increases in the length of stay and the cost per day of care. Expenditures for other services have increased by $288 million, or 31 percent, due primarily to increased prepaid health plan (PHP) enrollments. Increases in PHP expenditures over this period do not reflect increases in total Medi-Cal health care services expenditures. Instead, PHP expenditures replace expenditures for other types of service. Chart 7 displays the changes in expenditures for the three Medi-Cal service types with the highest total cost, from 1982–83 to 1984–85.

4. Legislative Changes Enacted During 1983

During 1983, the Legislature enacted two measures that are having and will continue to have significant fiscal and programmatic effects on the Medi-Cal program. The first of these measures, Ch 323/83, the 1983 budget trailer bill (AB 223), revised the treatment of other real property in Medi-

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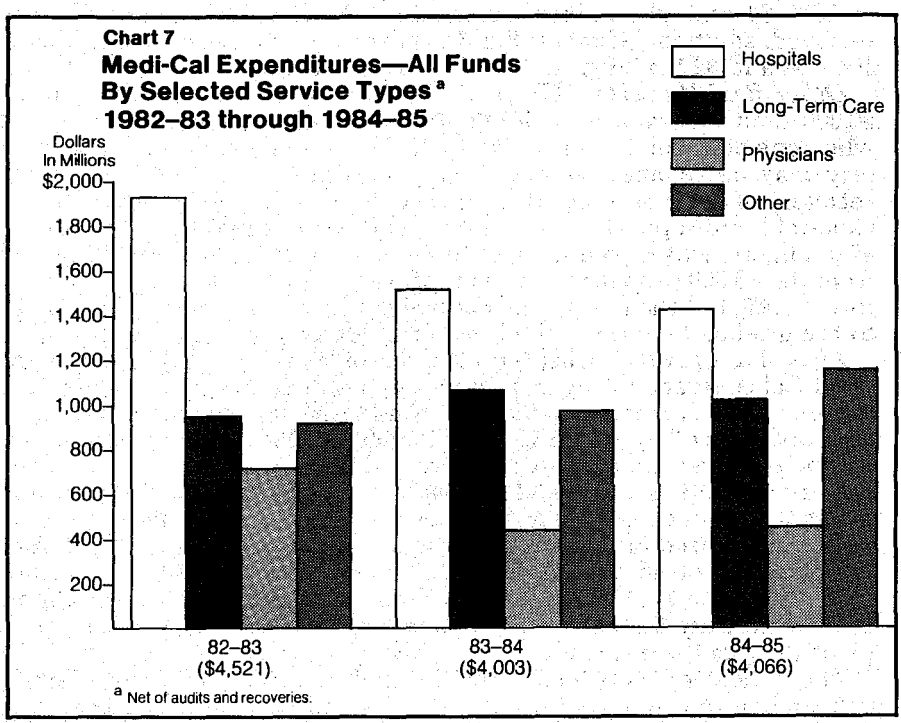

Cal eligibility determinations and increased the monthly income that Medi-Cal beneficiaries may retain for their living expenses. The other measure, Ch 1173/83 (SB 72), authorized Medi-Cal reimbursements for liver transplants. Previously, liver transplants were considered experimental, and therefore not eligible for reimbursement from Medi-Cal. The budget projects that these measures will cost $17 million (General Fund) in 1984–85.

Maintenance Need Levels. Chapter 323, Statutes of 1983 (AB 223), increased the maximum monthly income amounts (maintenance need level) that Medi-Cal beneficiaries may retain for their living expenses. Previously, maximum income levels were based on 133 percent of AFDC payment levels. This measure (1) sets maximum income levels for one-person households equal to 80 percent of the two-person income level, (2) sets maximum income levels for two-adult households equal to the income level for three-person families with children, (3) allows higher monthly incomes for Medi-Cal beneficiaries who share households with others and who reside in community care facilities, and (4) calculates income levels annually and then prorates the total to derive monthly amounts.

The department implemented these changes in September and October 1983. The changes were effective for eligibility determinations made beginning in July 1983. The department advises that the state's plan to increase the income level for two-adult households has been rejected by the federal Department of Health and Human Services. The department plans to appeal this ruling.

The department estimates these higher maintenance need levels will

increase General Fund-supported Medi-Cal expenditures by $6.2 million in 1983–84 and $9.3 million during 1984–85. If federal approval is not received, additional General Fund expenditures of at least $1.7 million in 1983–84 and $2.5 million in 1984–85 may be required.

Other Real Property. Chapter 323, Statutes of 1983, excludes from a $6,000 limit on property holdings the value of multiple dwelling units when one of the units is occupied by the Medi-Cal beneficiary. This property may be retained so long as liens are placed against its value for recovery of the cost of health care. The department estimates additional General Fund-supported Medi-Cal expenditures of $84,000 in 1983–84 and $2.0 million in 1984–85 due to exclusion of multiple family dwelling units from the $6,000 property limit. This provision was implemented effective July 1, 1983, but the full-year effect will not be realized until 1984–85, due to the gradual buildup in the number of affected cases.

Liver Transplants. Chapter 1173, Statutes of 1983 (SB 72), provides Medi-Cal coverage for liver transplant operations. Prior to enactment of this measure, liver transplants were considered experimental and, therefore, not covered by Medi-Cal. As of January 25, 1984, the department had authorized liver transplants for seven Medi-Cal beneficiaries and presurgery evaluation for four additional beneficiaries. The department estimates that 22 such procedures will be performed during 1983–84 and 34 will be authorized in 1984–85, at a cost of $375,000 per patient. In addition, the department advises that costs of continuing health care for these patients will be $125,000 during the second year after the operation and $63,000 annually thereafter. Thus, the five-year cost for a surviving transplant recipient is estimated to be nearly $700,000.

The budget projects total General Fund costs for these procedures of $2.1 million during 1983–84 and $5.7 million during 1984–85. The actual number of transplants and the costs of these procedures may differ significantly from the budget projection, depending on (1) availability of donor organs, (2) survival rates, and (3) actual health care costs for each operation.

Health Care Services Budget Issues

Court Decisions Will Cost General Fund $33 Million in 1984–85

The budget proposes $33 million from the General Fund to cover the costs of court decisions handed down in connection with five major and numerous minor lawsuits. The most costly of the five major decisions involves a delay in implementation of the other real property provisions of the 1982 Medi-Cal reform measures. Current-year General Fund Medi-Cal costs resulting from these decisions total $40 million, which is $23 million more than the amount anticipated by the 1983 Budget Act.

The budget estimates do not reflect costs resulting from a court ruling in a sixth major case. This ruling requires the department to continue financing those abortions for which Medi-Cal reimbursement was prohibited by the 1983 Budget Act. The department estimates that the costs to fully fund abortions in the current year will be $16 million more than the amount appropriated by the 1983 Budget Act. The budget assumes that abortion restrictions will *not* be overturned by the courts in 1984–85.

Thus, we find that costs resulting from court decisions handed down in 1983–84 will increase General Fund expenditures in the current year by $56 million, or $39 million more than the amount anticipated by the 1983 Budget Act.

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Table 36 shows the General Fund cost during 1983–84 and 1984–85 stemming from these decisions.

Table 36
Fiscal Effect of Medi-Cal Court Decisions and Settlements
1983–84 and 1984–85
General Fund
(in thousands)

	1983–84			
	1983 Budget Act	*Jan. 1984 Estimate*	*Difference*	*1984–85*
A. Health care services				
1. *Committee to Defend Reproductive Rights v. Rank*—payment for abortions [a]	—	$15,704	$15,704	—
2. *Bagley v. Dawson* and *Griffin v. Rank*—other real property	—	16,709	16,709	—
3. *Beltran v. Myers*—property transfers	$10,855	13,544	2,689	$20,788
4. *Lynch v. Rank*—social security payment increases	—	1,012	1,012	1,214
5. *Lopez v. Heckler*—disability determinations	—	717	717	4,292
6. *Turner v. Woods*—AFDC income deductions	6,187	6,187	—	6,187
7. Other cases	476	550	74	608
Subtotals	$17,518	$54,423	$36,905	$33,089
B. Eligibility determinations				
1. *Bagley v. Dawson* and *Griffin v. Rank*	—	$139	$139	—
2. *Beltran v. Myers*	$138	1,474	1,336	$311
3. *Lynch v. Rank*	—	457	457	37
Subtotals	$138	$2,070	$1,932	$348
Totals	$17,656	$56,493	$38,837	$33,437

[a] These costs are not reflected in the December estimates of Medi-Cal expenditures.

Elective Abortions. In this case, the San Francisco Appeals Court ordered the Department of Health Services, the State Controller, and the State Treasurer to "refrain from implementing those provisions of Items 4260-101-001 [the main Medi-Cal item] and 4260-105-001 [the special abortions item] of the 1983 Budget Act, which limit the funding of abortions sought by Medi-Cal recipients." The judge's temporary restraining order was issued on July 27, 1983. In response to this order, the department authorized expenditures from the special abortions item for all abortions, not just those funded by the 1983 Budget Act. In early January 1984, funds available in this special item were exhausted and the administration refused to certify payment for abortions. The appeals court issued a final ruling on January 24, 1984, (1) declaring unconstitutional the 1983 Budget Act restrictions on abortions and (2) requiring the state to fully fund the cost of abortions provided during 1983–84. As a consequence, the administration is currently authorizing payment for abortions. As a result of this ruling, General Fund Medi-Cal expenditures will exceed the amount appropriated in the 1983 Budget Act by $15,704,000.

Other Real Property. In a series of orders, the Los Angeles Superior Court has delayed implementation of the list-for-sale and lien collection provisions of the 1982 Medi-Cal reform measures for one full year. As a result, savings anticipated from these changes will not begin until 1984–85.

The implementation delay has resulted in additional General Fund costs of $16.7 million.

Property Transfers. The Central California U.S. District Court found the state may not penalize the transfers of property when the property was exempt from consideration for purposes of Medi-Cal eligibility determinations at the time of the transfer. The most common situation addressed by this case was one in which an individual entering long-term care transferred ownership of his/her home or other real property in order to become eligible for Medi-Cal. The major part of this case was resolved prior to July 1, 1983, and was included in the 1983 Budget Act. On July 29, 1983, however, the court ruled that retroactive damages would be paid to individuals who were denied Medi-Cal benefits or assessed a share of cost for these benefits due to the property transfer rules applied prior to July 1, 1981. General Fund costs of $2.7 million for these retroactive payments were not reflected in the 1983 Budget Act. The department estimates this case will result in General Fund costs of $21 million during the budget year.

Social Security Payment Increases. On October 21, 1983, the U.S. District Court in San Francisco ordered the Department of Health Services to send notices to all members of a class of persons affected by the "Pickle Amendment" to the federal Social Security Act. The Pickle Amendment provides that individuals who are discontinued from SSI/SSP due to increased income directly or indirectly related to increases in social security payments must remain eligible for Medi-Cal health care services with no share of cost. Additional costs of $1.0 million and $1.2 million are anticipated in 1983–84 and 1984–85, respectively, related to (1) identifying potential class members and sending notices and (2) increases in the number of Medi-Cal beneficiaries.

Disability Determinations. In *Lopez v. Heckler,* the federal district court in Fresno ruled in June 1983 and the United States Supreme Court affirmed in September 1983 that the federal Department of Health and Human Services may not discontinue persons already receiving SSI/SSP payments due solely to a change in federal disability criteria. Because this ruling results in continued Medi-Cal eligibility for some SSI/SSP recipients who otherwise would have been ineligible, the department anticipates increased Medi-Cal costs of $717,000 and $4.3 million in 1983–84 and 1984–85, respectively.

AFDC Income Deductions. The San Francisco Federal District Court's decision in the *Turner v. Woods* case requires the state to exclude mandatory payroll deductions in calculating income for purposes of determining AFDC grants. This decison results in annual General Fund Medi-Cal costs of $6.2 million due to (1) an increase in the number of AFDC recipients and, therefore, an increase in the number of categorically eligible Medi-Cal beneficiaries and (2) application of the revised income deduction rules to the medically needy program.

Other Cases. Estimated current-year expenditures also include $550,000 for the cost of court rulings and settlements in 12 minor lawsuits. The budget proposes $608,000 for three specific minor cases and for other unspecified minor settlements and orders in 1984–85.

Abortion Restrictions Proposed

The 1984 Budget Bill proposes to restrict funding for abortions for categorically needy and medically needy Medi-Cal beneficiaries to virtually the same circumstances allowed under the 1983 Budget Act. In addi-

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tion, the Budget Bill proposes to allow Medi-Cal expenditures for abortions only from a special abortions budget item. Specifically, the budget limits Medi-Cal funding for abortions provided after August 15, 1984, to situations where (1) the woman's life is endangered, (2) the pregnancy results from rape, statutory rape, or incest, or (3) prenatal studies determine that the woman will give birth to a child with severe genetic or congenital abnormalities.

Differences from 1983–84 Legislative Actions. There are several differences between the budget proposal and the provisions included by the Legislature in the 1983 Budget Act.

- ***Budget Bill May Not Restrict Abortions for Medically Indigent.*** Language in the 1984 Budget Bill, as proposed, restricts abortion funding for categorically needy and medically needy Medi-Cal recipients. The restrictions do not appear to apply to medically indigent children (0 to 21 years of age) or pregnant women who remain eligible for Medi-Cal as medically indigent adults. It is unclear whether the exclusion of medically indigent beneficiaries from the abortion restrictions would result in (1) unlimited Medi-Cal funding for abortions provided to this group or (2) no Medi-Cal support for *any* abortions provided to these beneficiaries. The $14 million proposed for abortion funding in the special abortions item assumes that Medi-Cal will pay for abortions for medically indigent beneficiaries on a restricted basis. The $14 million is not sufficient to pay for unrestricted abortions for medically indigent beneficiaries and restricted abortions for other Medi-Cal beneficiaries.
- ***Federal Fund Item Not Included.*** The 1983 Budget Act appropriated $252,000 in federal funds for abortions. The Department of Finance advises that because the necessary documentation for claiming these federal funds has not been developed, no federal support is anticipated for Medi-Cal abortions during 1984–85.
- ***Special Fund Proposed.*** The companion bill to the 1984 Budget Bill (AB 2314 and SB 1379) establishes, without regard to fiscal year, a special financing fund to be the sole source of funds for Medi-Cal abortions. The 1983 Budget Act established a special financing account in the General Fund to be the sole source of funds for Medi-Cal abortions. Thus, the companion bill would make this special financing account permanent. We are unaware of any technical differences between the use of a special account in the General Fund and a special financing fund.
- ***Further Restricts Abortions for Genetic Defects.*** The 1984 Budget Bill specifies that abortions may be paid for by Medi-Cal in cases of genetic or congenital abnormalities only if the abortion occurs not later than the second trimester. The gestational age of the fetus was not specified in the 1983 Budget Act.

Restrictions Projected to Save $15.7 Million. The budget proposes $13.7 million from the General Fund for abortions and $2 million for health care services required for pregnancies carried to full-term due to restrictions on abortion payments. This is $15.7 million less than the $31.4 million estimated cost of 99,000 abortions that would be supported by Medi-Cal without restrictions.

The $13.7 million proposed for abortions includes (1) $2.4 million for 6,360 abortions meeting the conditions required for funding in 1984–85,

(2) $3.9 million for 12,310 abortions performed in 1984–85 prior to implementation of the restrictions, and (3) $7.4 million for 23,400 abortions performed in 1983–84 but not billed until 1984–85.

Savings Unlikely. The conditions under which funding for abortions would be allowed and the mechanism for funding abortion payments included in the Budget Bill are virtually identical to those rejected by the San Francisco Appeals Court in the current year. Moreover, these conditions are similar to those specified in the 1981 and 1982 Budget Acts and subsequently overturned by the courts. Given the courts' refusal to allow the Legislature to restrict state-funded abortions in this manner, it is doubtful that any savings will be realized if this policy is adopted for 1984–85. If the restrictions are not allowed by the courts, Medi-Cal expenditures for 99,000 abortions in 1984–85 would total $31.4 million, all from the General Fund. Therefore, the proposed budget may be underfunded by $15.7 million.

Budget Proposes a 2 Percent Beneficiary Cost-of-Living Adjustment

Income standards for categorically needy Medi-Cal beneficiaries and maintenance need levels for medically needy and medically indigent beneficiaries are based on cash grant payment levels under the Aid to Families with Dependent Children (AFDC) and Supplemental Security Income/State Supplementary Payment (SSI/SSP) programs. Thus increases in cash grant payments affect Medi-Cal costs.

The budget contains $10,792,000 ($5,396,000 General Fund) for a 2 percent increase to income standards and maintenance need levels for Medi-Cal beneficiaries. This is consistent with the administration's proposal that AFDC payments increase by 2 percent on July 1, 1984, and that SSI/SSP grants increase by 2 percent on January 1, 1985.

Under current law, both grants will increase by 5.5 percent during the budget year. This is the projected percentage change in the California Necessities Index during the 12-month period ending January 1, 1984. The budget assumes that legislation will be enacted allowing the Legislature to determine in the Budget Act the size of any increase in cash assistance payments. The cost of providing the full 5.5 percent increase to Medi-Cal maintenance need levels would be $28.1 million ($14 million General Fund), or $17.3 million ($8.6 million General Fund) more than what is included in the budget.

The difference between a 2 percent increase and a 5.5 percent increase for Medi-Cal beneficiaries is a difference in the amount of income they may retain for their monthly living expenses. For example, in 1983–84, a three-person medically needy family may retain $709 each month for food, housing, and other costs. Any excess income must be spent for health care in order for the family to be eligible to receive Medi-Cal benefits. A 2 percent increase in the maintenance need level would increase the amount this family could retain by $8, to a total of $717. The statutorily required 5.5 percent increase would result in allowable monthly income of $742 for this family, or $33 more than in 1983–84.

Provider Rate Increases

The budget proposes $63.3 million ($31.4 million General Fund) for Medi-Cal provider rate increases in 1984–85, consisting of (1) a 7.4 percent increase in the price of prescription drug ingredients, (2) a 10 percent increase in the cost of hospital care not covered by negotiated contracts, and (3) a 2 percent increase for most other providers.

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The budget does not contain funds to support increases in the cost of contracted hospital care. The California Medical Assistance Commission advises that many hospital contracts will be renegotiated during 1984–85. Any rate increases resulting from these renegotiations, however, may be offset by elimination of high-cost contracts or rate reductions in other contracts.

For many providers, the proposed payment levels are less than the rates they received for providing the same services during 1981–82. This is due to the rate reductions imposed by the 1982 Medi-Cal reforms. The department estimates that restoration of these 1982–83 rate reductions would require additional expenditures of $70 million ($34 million General Fund) in 1984–85.

Table 37

Medi-Cal Provider Reimbursement Rate Changes
1982–83 through 1984–85

			1984–85		Cost of 1984–85 Rate Increases (in thousands)	
	1982–83[a]	1983–84	Proposed	Statutory	All Funds	General Fund
Physicians	−10.0%	—[b]	2.0%	—	$5,965	$2,950
Dental	−10.0[c]	—[b]	2.0	—	2,170	1,102
Drug dispensing	—[d]	—[b]	2.0	—	1,362	660
Drug ingredient	8.4	8.0	7.4	7.4	6,866	3,216
Hospital inpatient						
Contract services	13.9	—	—	—	—	—
Noncontract services	13.9	8.2	10.0	10.0	18,027[e]	9,086[e]
Hospital outpatient	−10.0	—[b]	2.0	—	2,236	1,121
Prepaid health plans	9.6	6.9	2.0	—[f]	2,548	1,302
Redwood Health Foundation	9.6	6.9	2.0	—[f]	476	238
Skilled nursing facilities	7.9	2.9	2.0	—[f]	10,338	5,234
Intermediate care facilities	7.9	1.1	2.0	—[f]	1,238	624
Laboratory and pathology	−25.0	—[b]	2.0	—	—[g]	—[g]
Psychological, acupuncture, portable X-ray, chiropractic	−10.0	—[b]	2.0	—	—[g]	—[g]
Other providers	—	—[b]	2.0	—	12,030	5,884
Totals					$63,256	$31,417

[a] Reimbursement rates for several provider groups were reduced by Ch 328/82 and Ch 329/82, the 1982 Medi-Cal reform measures.

[b] The Governor vetoed a 3 percent provider rate increase adopted by the Legislature.

[c] The 1982 Medi-Cal reforms reduced the appropriation for dental services by 10 percent. Actual 1982–83 General Fund expenditures for this contract, however, exceeded the amount appropriated by $9 million.

[d] A 9.6 percent reduction in drug dispensing fees has not been implemented due to federal rejection of a $1 beneficiary copayment for prescription drugs.

[e] Includes $10,080,000 ($5,133,000 General Fund) for hospital services provided by prepaid health plans and the Redwood Health Foundation.

[f] Current statute requires annual cost-of-living adjustments based on actuarial rate studies. These studies have not yet been completed.

[g] Costs of rate increases to these providers are included in other categories.

Our analysis indicates that inflation in health care costs between 1982–83 and 1984–85 will exceed 2 percent. Thus, in real terms, the rate increases proposed by the administration for many Medi-Cal providers actually represents a decrease in rates, relative to (1) rates paid by other purchasers of health care and (2) the cost of providing health care. The size of this difference between Medi-Cal payments and those made by other payors, however, will be less in 1983–84 and 1984–85 than it was in 1982–83, due to cost containment measures (1) instituted under the Medicare program and (2) made available to private health insurers by the 1982 Medi-Cal reforms. The ability and willingness of providers to continue providing health care services to Medi-Cal recipients when the state's reimbursement rates are reduced in "real" terms varies. We are not able to assess the extent to which providers may choose not to provide services to Medi-Cal patients if the state's reimbursement rates continue to decline in real terms.

Table 37 summarizes the changes in reimbursement rates for various Medi-Cal providers, from 1982–83 through 1984–85.

Prudent Purchasing Project Stalled

We recommend the department advise the Legislature during budget hearings regarding its plans for implementing the prudent purchasing contracts for drugs and other health care products authorized by the 1982 Medi-Cal reforms.

Under the provisions of Ch 328/82 (AB 799) and Ch 329/82 (SB 2012), the department may contract with various vendors for the purpose of obtaining drugs and other health care products at the most favorable prices to the state. The budget anticipates savings of $16.3 million ($8.1 million General Fund) from prudent purchasing programs for drug products, laboratory services, and eye appliances. The budget assumes that implementation will begin in 1983–84.

Implementation Schedule. The first program scheduled for implementation beginning January 1, 1984, is a drug rebate program. Under this program the department will contract with drug manufacturers or labelers to provide monetary rebates to the state in exchange for becoming the exclusive supplier to the Medi-Cal program of specific drug products. The budget anticipates the Medi-Cal program will realize savings of $8.5 million ($4.2 million General Fund) in 1984–85 from this program, due to (1) lower payments to pharmacists for drug ingredients and (2) rebates to the state from drug manfacturers and labelers. The budget projects that implementation of similar programs for laboratory services and eye appliances, beginning in March 1984, will save $7.8 million ($3.9 million General Fund) during 1984–85.

Drug Project Implementation Postponed. In a December 1983 report to the Legislature, the department stated that contracts with 16 manufacturers and labelers for provision of 50 separate drug products were prepared and ready for execution on January 1, 1984. This report, required by the 1982 reforms, demonstrates the cost-effectiveness of the prudent purchasing of drugs project. During December 1983, two separate courts rejected challenges to the planned implementation of this project.

On December 29, 1983, however, the department announced that this project was being postponed indefinitely while the department studied (1) the economic impacts of the project on various parties and (2) the relationship of this project to the proposed expansion of capitated payments under the Medi-Cal program.

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Savings Uncertain. Because execution of the contracts with drug manufacturers and labelers has been postponed, the prospect for budget-year savings from these contracts is uncertain, at best. In addition, it does not appear likely that volume purchasing agreements for laboratory services and eye appliances will be implemented by March 1984, as scheduled. The department has not provided a revised implementation schedule for this program. Therefore, the budgeted savings of $16.3 million ($8.1 million General Fund) may not occur. To ensure that the Legislature (1) is well-informed regarding the status of this project and (2) is able to properly budget for Medi-Cal expenditures anticipated in 1984–85, we recommend that the department advise the Legislature during budget hearings regarding the administration's plans for implementing prudent purchase contracts.

Savings Budgeted for Copayments Is Questionable

The budget reflects savings of $12.8 million ($6.4 million General Fund) due to the imposition of mandatory copayments for certain services, beginning January 1985. The budget assumes that legislation will be enacted to (1) reduce reimbursements to Medi-Cal providers by the amount of the copayments, (2) require providers to charge copayments, and (3) increase copayments for certain services and authorize new copayments for others. Table 38 compares proposed mandatory copayments with copayments allowed under current law.

Table 38
Medi-Cal Program
Comparison of Current and Proposed Copayments

	Current Optional Copayments	*Proposed Mandatory Copayments*	*Unit*
1. Use of emergency room services for nonemergency situations	$5	$10	per visit
2. Drug prescriptions under $10	$1	$1	per prescription
3. Drug prescriptions $10 or more	$1	$2	per prescription
4. Outpatient services	$1	$2	per visit
5. Dental services	$1	—	per visit
6. Medical transportation	—	$2	per trip
7. Home health	—	$2	per visit
8. Durable medical equipment	—	$2	per item
9. Hearing aids and eyeglasses	—	$2	per item

The budget trailer bill (AB 2314 and SB 1379) does not propose the necessary statutory amendments to existing law needed to implement the copayment proposal. The administration advises that the amendments will be proposed at a later date. If the statutory changes are not approved by July 1984, or if Federal waivers are not secured by November 1984, it is unlikely that the full amount of the budgeted savings will be realized during 1984–85. If the proposal is implemented, however, actual savings probably will be greater than the amount estimated because the copayment is likely to deter some beneficiaries seeking health care.

Emergency Room Copayment Conflicts with Federal Law. The department estimates that savings of $2,138,000 ($1,069,000 General Fund) will be generated from copayments on nonemergency use of emergency room services. The proposed $10 copayment for the nonemergency use of emergency room services exceeds the maximum $6 copayment allowed

under federal law. If copayments greater than the amounts allowed by federal law are imposed by the state, the federal government could withdraw its financial support for the affected Medi-Cal claims.

Hospital Contracts Implemented

The 1982 Medi-Cal reform measures require hospitals wishing to participate in the Medi-Cal program to contract with the state. These measures established a special negotiator in the Governor's office to negotiate hospital contracts. The negotiator was replaced on July 1, 1984, by the California Medical Assistance Commission.

Charitable research hospitals, children's hospitals, hospitals operated by health maintenance organizations, and state hospitals are exempt from the contract requirements. The exemption for charitable research hospitals and children's hospitals expires June 30, 1984.

A nonexempt hospital may continue to provide a full range of Medi-Cal services until the commission has signed enough contracts to assure needed bed capacity for Medi-Cal patients in the hospital's geographic area. When sufficient contracts have been signed in an area, the acts require the commission to notify all noncontracting hospitals that they will no longer be reimbursed for serving Medi-Cal patients unless (1) they provide emergency services needed to prevent loss of life or permanent impairment, (2) the beneficiary is covered by the federal Medicare program, or (3) the beneficiary resides farther than established community travel time standards from a contract hospital.

Status of Hospital Contracts. As of January 1984, contracts between the state and 246 hospitals, including three psychiatric hospitals, had been implemented. Each of the contracts pays a fixed amount per day for hospitalization and specifies the services that the hospital must provide or arrange for. In addition, individual contracts contain terms unique to each hospital.

The 246 hospitals are located in 65 of the state's 137 health facility planning areas. Eighty-nine percent of all Medi-Cal expenditures for hospital inpatient services occur in these 65 areas. The commission has elected not to pursue contracts in the remaining health facility planning areas, primarily because most of the areas contain very few hospitals. In these areas, hospital contracting is not expected to generate significant cost savings.

Services Available Under Contract. In the areas where contracts have been implemented, 68 percent of all acute care beds and 67 percent of all operating rooms are in hospitals that have Medi-Cal contracts or are exempt from contracting. Table 39 compares the number of hospital beds and operating rooms available to Medi-Cal recipients with the total number of these facilities in the areas covered by contract.

Renegotiations Will Begin in 1984. Under the terms of these contracts, either the state or the hospital may request renegotiation of the contract with 120 days' advance notice (30 days' notice, with cause). The commission anticipates renegotiating most contracts at the anniversary of the contract's effective date. The effective dates of hospital contracts currently in effect range from February 1 to August 1, 1983. The commission's January 1984 report to the Legislature identifies several objectives for contract renegotiation. These objectives involve (1) changes to contract terms, such as range of service provided to patients, (2) refinement of the number of hospital beds necessary for the Medi-Cal population in

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Table 39

Selected Hospital Beds and Operating Rooms Available Under Contracts to Medi-Cal In Health Facility Planning Areas Covered By Contracts

	Total All Hospitals	*Exempt and Contracting Hospitals*	*Percent in Exempt and Contracting Hospitals*
1. General acute care beds			
Medical/surgical	54,361	36,530	67%
Perinatal	4,217	2,885	68
Pediatric	3,727	2,748	74
Intensive care (ICU)	3,863	2,698	70
Coronary care (CCU)	1,479	915	62
Respiratory acute	137	115	84
Burn care	149	108	72
Neonatal intensive care (NICU)	896	723	81
Rehabilitation	1,715	1,438	84
Totals	70,544	48,160	68%
2. Operating rooms	2,081	1,392	67%

Source: California Medical Assistance Commission.

each area, (3) reconsideration of the availability of special care, such as neonatal intensive care, (4) review of hospital performance, and (5) development of new price strategies and savings targets. As of January 20, 1984, no renegotiations had been conducted.

Hospital Contracts Expected to Save the State $118 Million During 1984–85. The budget anticipates that hospital contracts will result in savings of $235 million ($118 million General Fund) in 1984–85. These savings are calculated based on the cost of providing hospital care without these contracts. This projected savings exceeds the estimated current-year savings by $56 million ($28 million General Fund). This 31 percent increase is due primarily to anticipated increases in the cost of hospital care if contract rates were not in existence.

The projection of savings from Medi-Cal contracts is based on several critical assumptions about the percentage of hospital days remaining in noncontract hospitals and the cost of hospital care without contracts. If the departments, assumptions are incorrect, hospital contract savings may be greater or less than projected.

In addition, actual savings will depend upon the results of contract renegotiations. The budget does not contain any funds for rate increases for contract hospitals. If, in the aggregate, higher rates allowed under renegotiated contracts are not offset by savings in other contracts, the savings projected in the budget may turn out to be too high.

Hospitals Agree to Peer Group Rates

We recommend a reduction of $47,343,000 ($24,311,000 General Fund) to reflect savings anticipated from implementation of peer group rates for hospital reimbursement.

The 1982 Medi-Cal reforms required the department to develop a back-up method for reimbursing noncontracting hospitals, based on costs in-

curred by similar hospitals. These rates would be paid in areas where contracts have not been executed, for emergency services provided by noncontract hospitals, and to hospitals exempt from hospital contracting. The "peer group" reimbursement system developed by the department and approved by the federal government was delayed by a court-imposed temporary restraining order issued on January 25, 1983. Because of this order, the budget does not reflect any savings related to peer group reimbursement.

The restraining order was lifted November 9, 1983, allowing the implementation of peer group rates for all but one of the 117 plaintiff hospitals. The remaining hospital has chosen to resist peer grouping through litigation, and a trial hearing is scheduled for March 20, 1984. The outcome of this hearing may affect implementation of peer group rates for all hospitals.

Initial Peer Group System. Under the peer group system, the department assigns hospitals to groups with certain common characteristics. For example, university teaching hospitals are clustered together and rural hospitals form a separate group. Hospitals with average costs per discharge above the median for their peer group would have their reimbursement reduced to the median level for their peer group. Hospitals with disproportionately large numbers of Medi-Cal patients would be allowed higher reimbursement rates, based on the percentage of such patients. In addition to these peer group rates, the department has established separate controls on hospitals' labor costs.

Results of Settlement. The plaintiff hospitals challenged (1) the methodology used to assign hospitals to particular peer groups, (2) use of the median (50th percentile) cost of each group as a reimbursement standard, rather than some higher percentile such as the 60th percentile, (3) the reasonableness of peer group costs as a basis for maximum reimbursement rates, given regional cost variations and case-mix differences, (4) separate treatment of labor costs, and (5) the procedures followed by the department in establishing the new rates.

The settlement agreed to by the state and all but one of the plaintiffs (1) requires use of the 60th percentile rather than the median, (2) abandons separate labor cost controls, and (3) grants hospitals the right to appeal both interim monthly payments and year-end settlements, based on special circumstances resulting in costs higher than the 60th percentile. The settlement allows implementation beginning March 1, 1984, for hospital services provided from December 1, 1982, forward.

Savings Not Budgeted. The department estimates that implementation of peer group rates pursuant to this settlement will result in total savings of $40,402,000 ($20,986,000 General Fund) in the current year and $47,343,000 ($24,311,000 General Fund) in 1984–85, in addition to the savings included in the budget for hospital contracts. The department advises that these savings were not included in the budget because the court had not ruled on the merits of the case regarding the remaining plaintiff hospital. Based on (1) the willingness of most hospitals to accept peer group rates, (2) the fact that federal approval was granted for this system prior to the initial challenge, and (3) the existence of similar peer group reimbursement systems in other states, we believe it is likely that these savings will materialize during 1984–85.

Moreover, the department issued emergency regulations on January 13, 1984, to implement this new reimbursement system. In order to reflect these savings, we recommend a reduction of $47,343,000 ($24,311,000 General Fund).

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Savings From New Claims Processing Contract Not Budgeted

We recommend a reduction of $2,850,000 ($1,425,000 General Fund) to reflect savings anticipated from two improvements in Medi-Cal claims processing.

Medi-Cal claims will be processed under the terms of a new contract with the Computer Sciences Corporation beginning July 5, 1984. In order for this contract to be fully operational on July 5, the Department of Finance has authorized early start-up of certain claims processing improvements during the current year. Two of these improvements are already operational, and are expected to result in health care services expenditure reductions of $2,850,000 ($1,425,000 General Fund) in 1984–85.

These two improvements:

- Identify costs of certain hospital services that should be billed to the Medicare program but have been paid by Medi-Cal. The department estimates that ongoing annual savings from this change is $2,500,000 ($1,250,000 General Fund). In addition, the department advises that in the current year it will submit retroactive claims for services paid during 1980–81 and 1981–82, for one-time recoveries of up to $5,000,000 ($2,500,000 General Fund). Due to processing delays, it is likely that a portion of these payments for past years will be received during 1984–85.
- Update the provider master file to exclude providers who have been disqualified from receiving Medi-Cal reimbursements. The department estimates this improvement will reduce Medi-Cal expenditures by $350,000 ($175,000 General Fund) in 1984–85.

The reductions in the cost of health care services expected from these improvements in Medi-Cal claims processing are not reflected in the budget. Therefore, we recommend a reduction of $2,850,000 ($1,425,000 General Fund) to reflect savings anticipated from these improvements.

Dental Contract Reprocurement Begins

The budget proposes $108,158,000 ($54,079,000 General Fund) for dental services and administrative costs pursuant to the state's contract with California Dental Services (CDS). The CDS contract will expire on June 30, 1984. The budget proposes to procure a new dental services contract during 1984–85, through a competitive process. In order to provide services until the implementation date of any new contract, the budget proposes to extend the current contract through June 1985.

Background. Since January 1974, CDS has processed dental claims and paid dentists for services provided to Medi-Cal beneficiaries. The initial contract was scheduled to expire on December 31, 1977. Legislation in 1977 (Ch 1036/77) and 1981 (Ch 1059/81) permitted the department to extend the contract until a new contract is procured. This is the seventh year that the state has operated under an extension of the original contract.

Advantages to the State from Reprocurement. The state will realize several advantages by reprocuring this contract through a competitive process.

- ***Cost Savings.*** Procurement of a new contract could result in sub-

stantially lower costs to the state for claims processing services. The current contract was negotiated with no competition from other prospective bidders. Therefore, the current contractor has never had a fiscal incentive to offer lower rates.

The potential magnitude of the savings to the state from reprocurement of the dental contract is illustrated by the state's experience in the recent reprocurement of the Medi-Cal fee-for-service claims processing contract. In this procurement, the department received bids that ranged from $73 million to $89 million, a difference of $16 million. This disparity in bids suggests that a competitive process for the dental contract could generate savings for the state. Moreover, the department estimates that future savings over the life of the fee-for-service claims processing contract will be $47 million ($11 million General Fund), when compared to the cost of extending the prior contract into the future.

- ***Federal Funding for Administrative Costs Will Resume.*** The federal Department of Health and Human Services has withheld from the state $500,000 in federal funds for the administrative costs associated with the CDS contract. This funding has been withheld because of delays in the dental reprocurement. It is unknown whether the state will recover these funds. A competitive reprocurement is necessary to avoid additional federal funding reductions.

New Contract Will Differ from Current Contract. Based on the draft request for proposals, the current contract will differ from the new contract in several respects.

- ***Liquidated Damages.*** Under the new contract, the department will be able to assess damages if the contractor fails to fulfill the terms of the contract. Under the current contract, there is no provision for assessing damages.
- ***Liability for Overpayments.*** Under the current contract, the contractor is not liable for any overpayments or unrecovered payments. Under the new contract, the department will select a sample of claims and prior authorizations, and the contractor will be responsible for any overpayments and unrecovered errors found in the sample.
- ***Allocation of Gains.*** Gains occur when the cost of providing services to beneficiaries is lower than the state anticipates. Under the current contract, the state receives any gains that exceed 5 percent of the total payments made by the state. The contractor receives all gains up to 5 percent. Under the new contract, the state will receive 40 percent of any gains up to 5 percent, 75 percent of any gains between 6 and 10 percent, and 100 percent of any gains in excess of 10 percent.
- ***Compensation for Administrative Costs.*** Under the current contract, CDS receives monthly payments for administration, based upon the number of claims per month. These rates are negotiated annually. Under the new contract, administrative costs will be determined on the basis of bids submitted and will not be adjusted.
- ***Claims Lines Adjudication.*** Under the current contract, entire claims are either paid or denied. A claim may contain a number of claim lines for a number of services provided during a visit. Paying on a claim line basis under the new contract will permit the vendor to pay for some services while others are being reviewed.
- ***Provider Enrollment.*** Under the current contract, the contractor is responsible for enrolling providers. Under the new contract, the

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department and the contractor will have joint responsibilities for provider enrollment.

- ***State Will Own System.*** The state will own any computer software, systems, and manuals required to operate the dental claims processing system. Currently, the contractor owns the system.

Project Schedule Delayed

We recommend that prior to budget hearings, the department report to the Legislature on the schedule for and status of the dental contract reprocurement.

In our *Analysis of the 1983 Budget Bill,* we stated that according to the department's timetable, the dental contract would be effective January 15, 1984, with assumption of claims processing and payment occurring in February 1985.

The department now advises that the request for proposals (RFP) for this contract will be released in mid-March 1984 and that the contract will be fully implemented by mid-July 1985. The department further advises, however, that this schedule may be revised.

Table 40 outlines past and current timetables for reprocurement of the dental contract.

Table 40

Medi-Cal Dental Procurement Project
Proposed Timelines

Milestones	*Timeline Proposed as of*		
	12/82	*3/2/83*	*1/21/84*
RFP released	7/1/83	9/16/83	mid-March 1984
Technical proposals due	9/1/83	11/16/83	mid-May 1984
Technical proposal evaluation	11/14/83	2/5/84	mid-August 1984
Invitation for bid issued	11/15/83	2/6/84	mid-August 1984
Bids opened	12/1/83	2/20/84	mid-September 1984
Contract signed and approved	12/16/83	3/8/84	early October 1984
Transition begins	2/1/84	4/20/84	mid-November 1984
Full implementation	12/1/84	2/1/85	mid-July 1985

According to the department, delays in reprocurement have resulted from (1) a dispute between the department and the Department of Corporations regarding Knox-Keene licensure of the contractor, (2) the department's decision to postpone the procurement of this contract until after the new fee-for-service claims processing contract was negotiated, and (3) language included in the 1983 Budget Act requiring the Auditor General to review any request for proposal prior to its release.

These three sources of delay have all been removed. The Auditor General submitted his report in September 1983. The new Medi-Cal claims processing contract has been reprocured. Finally, the department advises that agreement has been reached with the Department of Corporations on the applicability of the Knox-Keene Act to the dental services contract.

Knox-Keene Issue Settled. The Knox-Keene Act requires health care service plans to be licensed by the Department of Corporations. Each plan is required to have specified financial reserves and maintain agreements with providers to continue health care services if the plan ceases to transact business. Additionally, each plan is required to establish a beneficiary grievance process.

The Department of Corporations has contended that any successful bidder for the Medi-Cal dental services contract must have a Knox-Keene license. Because the current contractor, CDS, is the only dental provider with a Knox-Keene license, this requirement would have prevented a competitive bid process.

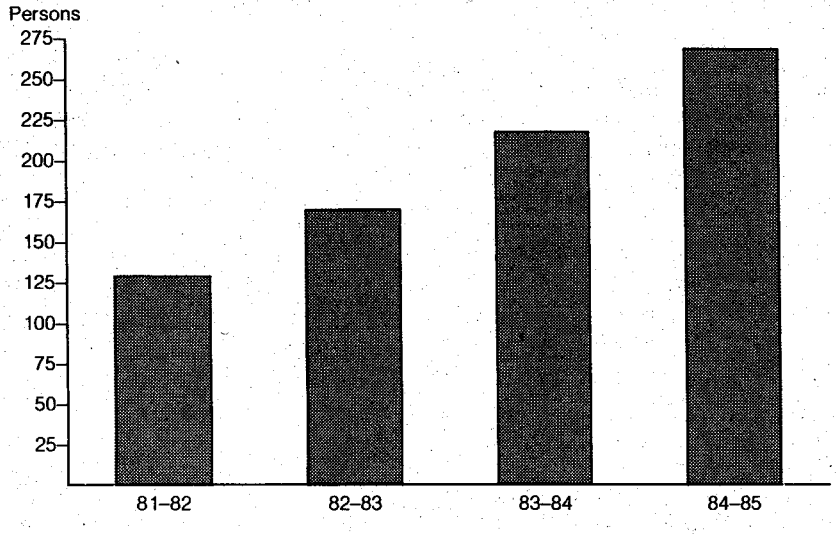
In January 1984, the Departments of Corporations and Health Services reached a compromise on the Knox-Keene provisions. The successful bidder will be exempt from Knox-Keene requirements for nine months, beginning with the effective date of the contract. After this period, the dental contractor must obtain a license under the Knox-Keene Act.

Recommendation. Delays in the reprocuring the dental service contract are costing the state money, since (1) our analysis indicates that the new contract is likely to be less expensive than the current contract and (2) the federal government is withholding funds because the reprocurement has not proceeded. For these reasons, and because the department advises that the schedule for the reprocurement project is likely to change, we recommend that prior to budget hearings, the department advise the Legislature on the schedule for and status of the dental contract reprocurement.

Enrollment in Prepaid Health Plans Increases

The budget proposes $212,168,000 ($106,084,000 General Fund) for prepaid health plans (PHPs) in 1984–85. This is $38,791,000 ($19,395,500 General Fund), or 22 percent, more than estimated current-year expenditures for this purpose.

Chart 8
Medi-Cal Prepaid Health Plans
Average Monthly Enrollments
1981–82 through 1984–85
(in thousands)



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The primary reason for the increased cost is an estimated 24 percent increase expected in the average number of persons enrolled in PHPs. PHP enrollment has increased 109 percent since 1981–82. The department attributes the growth in enrollment to (1) more effective dual-choice presentations by county eligibility workers and (2) more effective marketing of health plans. Chart 8 illustrates the growth in PHP enrollment.

Enrollments in existing PHPs are lower than the maximum enrollments allowed under the contracts. The department projects that an additional 61,000 Medi-Cal beneficiaries could enroll in the 14 existing prepaid health plans with Medi-Cal contracts during 1984–85. Actual enrollment in PHPs has grown from 48 percent of contract capacity in 1981–82 to 82 percent in 1984–85. Table 41 compares actual enrollment with maximum contracted capacity from 1981–82 to 1984–85.

Table 41
Prepaid Health Plans
Average Monthly Enrollment and
Maximum Contracted Capacity
1981–82 through 1984–85

Year	*Average Monthly Enrollment*	*Maximum Contracted Capacity*	*Actual Enrollment as a Percent of Maximum Contracted Capacity*
1981–82	129,000	266,000	48%
1982–83	170,000	283,000	60
1983–84	218,000	330,000	66
1984–85	269,000	330,000	82

PHP Rates Have Not Been Determined for Current Year

We recommend that:

1. ***Prior to budget hearings, the department submit (a) the 1983–84 PHP rates, (b) the comparable fee-for-service costs, (c) the methods for determining these rates, and (d) a schedule for developing 1984–85 rates.***

2. ***During budget hearings, the department report the reasons for the delay in establishing PHP rates in the current year.***

To prepare this analysis, we requested information regarding rates paid to prepaid health plans (PHPs) during the current year. We have not received this information because, as of January 25, 1984, the department had not established the 1983–84 rates. The department advises that the delay has been caused by a disagreement within the administration over the computation of comparable fee-for-service costs.

The issue under discussion is whether savings generated from hospital contracts should be subtracted from fee-for-service costs prior to comparing these costs with PHP rates. This would have the effect of reducing allowable rates for some prepaid health plans because current law requires that PHP rates be less than fee-for-service costs for comparable services. If comparable service costs used in the PHP rate calculations do not reflect hospital contract savings, some PHP rates could be higher than

actual costs of comparable services provided on a fee-for-service basis.

Because most of the data needed to determine the rates for 1983–84 were available prior to April 1983, we see no reason for the delay in establishing current-year rates. This delay, however, suggests that rate determinations for 1984–85 may also be delayed. Current law requires that (1) new rates for PHPs shall be effective no later than September 1 of the fiscal year to which they apply and (2) these rates shall not exceed the cost of comparable services provided on a fee-for-service basis. Because the department has not met the deadline for establishing rates and has been unable or unwilling to provide the Legislature with the 1983–84 rates, we are unable to assess whether PHP rates are below the cost of comparable services provided on a fee-for-service basis, as required by current law. Therefore, we recommend that:

1. Prior to budget hearings, the department submit (a) the 1983–84 PHP rates, (b) the comparable fee-for-service costs, (c) the methods for determining these rates, and (d) a schedule for developing 1984–85 rates.
2. During budget hearings, the department explain the reasons for the delays in establishing PHP rates for the current year.

Legislative Notification of Changes in Rules or Regulations

We recommend the adoption of Budget Bill language requiring the department to notify the Legislature of any rule change expected to cost $1 million or more.

The 1984 Budget Bill does not include language that was placed in the 1983 Budget Act by the Legislature as a means of assuring legislative oversight of proposed expenditure changes. The 1983 Budget Act requires the Department of Finance to notify the Joint Legislative Budget Committee of any change in Medi-Cal rules or regulations that is expected to result in annual General Fund costs or savings of $100,000 or more.

We believe the Legislature should receive notification of regulations or rule changes expected to result in significant increases or decreases in Medi-Cal expenditures, in order to (1) assure continued provision of legislatively authorized program services and (2) monitor General Fund costs. We recommend, however, that the requirements be modified to require notification of changes that result in annual General Fund costs of $1 million, rather than $100,000. We recommend this change because our analysis indicates that any significant changes in Medi-Cal rules and regulations will result in costs of at least $1 million. Because the Legislature should be informed of significant rule changes that affect General Fund expenditures, we recommend that language be added to the 1984 Budget Bill. Specifically, we recommend adoption of the following language:

"Provided, that when a date for public hearing has been established for a change in any program, rule, or regulation, or the Department of Finance has approved any communication revising any department program, the two fiscal committees and the Joint Legislative Budget Committee shall be notified if the annual General Fund cost of the proposed change is $1 million or more."

Limitation on Expenditures

We recommend that the Legislature adopt Budget Bill language included in the 1983 Budget Act (1) forbidding expenditures in excess of 3 percent of the amount appropriated in any expenditure category and (2) requiring legislative notification of augmentations to any service category.

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The 1984 Budget Bill appropriates funds for all Medi-Cal local assistance categories in a single budget item. As a result, funds can be transferred among the amounts appropriated for (1) health care benefits, (2) county administration, and (3) claims processing, so long as total expenditures do not exceed the total local assistance appropriation. Since the 1982 Budget Act, when the local assistance amounts were first combined into one item, the Legislature has added language to the Budget Bill as a means of ensuring that the Legislature is notified of all augmentations to any of the three local assistance categories and that these augmentations do not exceed 3 percent of the amount appropriated by the Legislature for that category.

Without this limitation, the Legislature would not have an accurate indication of the costs of particular services, because the department would have the authority to make unlimited shifts of funds between Medi-Cal local assistance program categories. For example, the administration could transfer unlimited amounts from the legislative appropriation for Medi-Cal health care services to support funding increases for county administration or claims processing.

The 1984 Budget Bill does not contain the language added by the Legislature in earlier years. To ensure that unlimited transfers do not occur, we recommend that language be added to the 1984 Budget Bill prohibiting augmentations in excess of 3 percent and requiring that the Legislature be notified of other augmentations. Specifically, we recommend that the Legislature adopt the following language, which is identical to language contained in the 1983 Budget Act:

"The augmentation of amounts available for expenditure for any category shall not exceed 3 percent of the amount scheduled for that category, and any augmentation of amounts available for expenditure in any category shall be subject to Section 28.00 notification requirements."

B. MEDI-CAL COUNTY ADMINISTRATION

The budget proposes $119,815,000 ($56,371,000 General Fund) to support Medi-Cal eligibility determination activities in 1984–85. This is a decrease of $6 million, or 5 percent, below estimated current-year expenditures. Proposed General Fund expenditures for these activities are $1.7 million, or 3.2 percent, above estimated current-year expenditures.

Funds proposed in this item support eligibility determination and quality control costs related to medically needy and medically indigent Medi-Cal beneficiaries. The costs of eligibility determinations for categorically eligible Medi-Cal beneficiaries are supported through Item 5180 in the Department of Social Services.

The major factor responsible for the increase in General Fund expenditures is a proposal to remove limitations on state funding for past-year county employee salary and benefit increases. The reduction in total expenditures (all funds) reflects:

- Reductions in costs for hospital-based eligibility determinations.
- An assessment against Los Angeles County for violating reporting requirements.
- One-time federal fund expenditures in the current year that will not be repeated in the budget year.
- Lower-than-expected costs due to lawsuits.

- Savings resulting from various cost control measures.

Current estimates of 1983–84 expenditures indicate that General Fund costs for county eligibility determinations will be $2,538,000, or 4.4 percent, lower than the amount appropriated for those costs in the 1983 Budget Act. The surplus is due primarily to caseload reductions and cost reductions for Los Angeles County hospital intakes.

Table 42 displays estimated and proposed expenditures for county administration in 1983–84 and 1984–85.

Table 42
Medi-Cal County Administration
Proposed Budget Changes
(in thousands)

	General Fund	*All Funds*
A. 1983 Budget Act	$57,182	$120,695
B. Unanticipated current-year expenditure changes		
1. Major reestimates that increase 1983–84 costs		
a. Hospital-based eligibility determination—reduced savings	1,383	2,766
b. Los Angeles County status reporting sanction	805	1,559
c. Federal fund participation changes	358	11,690
d. Title II disregard	968	1,937
e. Court cases	1,320	2,641
f. MEDS, EPSDT, and CCS county administration	666	571
g. Prior-year refugee costs	1,198	1,198
h. AB 799 changes	696	1,392
2. Major reestimates that reduce 1983–84 costs		
a. Caseload reductions	−7,053	−14,064
b. Maintenance need increase	−111	−221
c. Los Angeles County hospital intakes	−1,246	−2,491
d. AFDC eligibility changes	−325	−650
e. MIA elimination	−1,366	−1,147
3. All other changes	169	313
C. 1983–84 expenditures (revised)	$54,644	$126,189
D. Projected current-year surplus/deficiency (−)	(2,538)	(−5,494)
E. Budget-year changes		
1. Full funding for prior-year county salary and benefit increases in excess of legislatively approved amounts	6,779	13,292
2. Title II disregard	−844	−1,687
3. Elimination of one-time 1983–84 costs	21	−12,340
4. Los Angeles County hospital intakes	469	938
5. Hospital-based eligibility determination	−1,443	−2,886
6. Court cases	−1,078	−2,157
7. AB 799 changes	40	471
8. Maintenance need intakes	−483	−241
9. Los Angeles County status reporting sanction	−1,047	−2,043
10. All other changes	−687	279
F. 1984–85 expenditures (proposed)	$56,371	$119,815
G. Change from 1983–84 (revised):		
Amount	$1,727	−$6,374
Percent	3.2%	−5.1%

Quality Control Reviews

Under current law, the federal and state governments conduct sample quality control reviews every six months to determine the amount of Medi-Cal expenditures that were made in error. Separate error rates are

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calculated for county eligibility determinations, claims processing, and third-party liability recoveries. Federal law defines (1) *the payment error rate* as payments made on behalf of an ineligible person or in excess of amounts to which eligible persons are entitled as a percentage of all medical assistance payments and (2) *the case error rate* as cases in error as a percentage of total cases.

Three Percent Federal Error Rate Standard

The federal Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) requires the Secretary of the federal Department of Health and Human Services (DHHS) to withhold state Medicaid payments based on quality control reviews of eligibility determinations. The TEFRA established a performance standard of 3 percent. Therefore, any state with a payment error rate exceeding 3 percent may have its Medicaid payments reduced by the amount of erroneous payments above 3 percent.

During the period July through September 1983, the DHHS withheld $210,600 in federal funds from the state as a sanction for the 3.1 percent payment error rate during the period April 1981 through March 1982. During the period October to December 1983, the DHHS did not withhold any funds because federal regulations had lapsed. The regulations were renewed in January 1984. By January 1984, data from the October 1982 to March 1983 period had become available. In this period, California had a payment error rate of 1.1 percent. Due to this low error rate, it is unlikely that additional federal funds will be withheld through December 1984. Beginning in January 1985, however, federal funds may be withheld depending on payment error rates determined for the April to September 1983 review period. If the state's payment error rate is 4 percent, or 1 percentage point above the federal standard, the federal government could withhold up to $5 million during the third and fourth quarters of 1984–85.

Chapter 102, Statutes of 1981 (AB 251) Requires County-Specific Quality Control Reviews

In Chapter 102, Statutes of 1981 (AB 251), the Legislature required the department to (1) determine, on a one-time basis, statistically valid eligibility error rates for each county and (2) report its findings by May 1982.

Instead of submitting this report, the department proposed to (1) conduct quality control reviews in the 16 largest counties, (2) perform management and case reviews for the remaining 42 counties, and (3) present a preliminary report to the Legislature on February 1, 1983, and a final report on June 1, 1983. The Legislature approved the department's proposal and added language to the *Supplemental Report to the 1982 Budget Act* that additionally required the department to determine error rates for hospitals operated by Los Angeles County and report by April 15, 1983. The department administratively established 19 positions for county reviews during 1981–82 and received an additional 11 positions in the 1982 Budget Act to review Los Angeles County hospitals. All 30 of these positions were made permanent.

In February 1983, the department determined that due to staff shortages, it was unable to complete (1) management reviews of the 42 small counties and (2) reviews for more than two of the Los Angeles County hospitals. The department completed the quality control reviews in the 16 largest counties and two hospitals operated by Los Angeles County, and reported its findings to the Legislature in June 1983.

Sixteen-County Review Completed. In June 1983, the department completed the study of case and payment error rates in the 16 counties with the largest Medi-Cal caseloads. These counties include 78 percent of the statewide Medi-Cal cases. Quality control staff performed a desk review of 160 eligibility determinations in each county for the period September 1981 through August 1982. If the reviewers found errors in more than 7 percent of the cases reviewed, they examined 200 additional cases. The reviewers compared their findings with paid claims to determine payment error rates.

These county reviews were different from the federal review required to determine statewide dollar error rates because the federal review (1) requires beneficiary contact and third-party verification, as well as a desk review, and (2) cites errors caused by both the county and the beneficiary, not just the county. As a result, a review of the same sample in these 16 counties using the federal evaluation method would probably produce different findings.

County Error Rates Vary Widely. In its report, the department indicates that 3.4 percent of Medi-Cal expenditures and 7.1 percent of all eligibility determinations in these 16 counties were in error. Based on this 3.4 percent payment error rate, $25.3 million ($12.6 million General Fund) may have been expended in error in these 16 counties during this period.

County case error rates ranged from a low of 2.5 percent (Kern) to a high of 12 percent (Alameda). County payment error rates ranged from a low of 0.3 percent (Ventura) to a high of 26 percent (San Francisco). Table 43 presents the findings for each of the 16 counties.

Table 43
Medi-Cal Eligibility Determination
Percent of Payments and Cases in Error
Sixteen Largest Counties
September 1981 through August 1982

County	*Payments*	*Cases*
Alameda	2.3%	12.0%
Contra Costa	0.7	9.0
Fresno	2.2	4.3
Kern	0.8	2.5
Los Angeles	0.9	6.7
Orange	1.6	6.7
Riverside	5.3	7.0
Sacramento	7.3	11.0
San Bernardino	2.8	6.0
San Diego	1.0	7.2
San Francisco	26.3	11.0
San Joaquin	0.3	3.8
Santa Clara	0.7	6.3
Stanislaus	1.2	2.6
Tulare	1.0	8.0
Ventura	0.3	3.0
Average	3.4%	7.1%

The department reported that the major causes of county errors were:

- Failure to consider reported information, such as income, in eligibility determination (34 percent).
- Failure to investigate possible changes in income and household composition that may affect eligibility (22 percent).

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- Use of incorrect policies (19 percent).
- Incorrect application of policies (9 percent).
- Other errors, including failure to investigate incomplete or inconsistent information, failure to verify information, and incorrect arithmetic computation (16 percent).

Los Angeles County Hospitals Have High Error Rates. To study error rates at Los Angeles County hospitals, the department performed desk reviews of 298 cases at Los Angeles County-University of Southern California General Hospital and 366 cases at Martin Luther King Hospital, for the period January through June 1982.

The overall case error rate at these hospitals was 54 percent for County General and 70 percent for Martin Luther King. The payment error rate was 76 percent for County General and 61 percent for Martin Luther King. Table 44 displays the error rates for the two hospitals and the cost of the payment error rates.

Table 44
Medi-Cal Eligibility Determination
Los Angeles County-University of Southern California General
And Martin Luther King Hospitals
January through June 1982

	County General	*Martin Luther King*
Overall case error rate	54%	70%
Overall payment error rate	76%	61%
Total Medi-Cal dollars in sample	$592,000	$443,000
Total Medi-Cal dollars paid in error	$447,000	$262,000

The major cause of eligibility determination errors in these hospitals was failure to submit alien status verifications to the federal Immigration and Naturalization Service prior to certification of Medi-Cal eligibility. This error accounts for 64 percent of the payment errors at County General and 67 percent of the errors at Martin Luther King. Another major cause of errors was inability of county eligibility workers to locate sample case files. This caused 15 percent of the errors at Los Angeles County General and 23 percent of the errors at Martin Luther King.

No Corrective Action Plan in Place

We recommend that the department report to the fiscal subcommittees during budget hearings of the status of corrective action plans for counties and Los Angeles County hospitals that had high error rates in the department's study of county eligibility determination errors.

In addition to determining error rates, the department's June 1983 report to the Legislature includes several broad recommendations for reducing errors. For example, the report recommends that:

- Counties should examine existing case control systems to ensure that changes reported by recipients are acted upon in a timely manner.
- The department should mandate that counties establish formal internal quality assurance programs.
- The department should require a quarterly status report for recipients in long-term care facilities.

Our analysis indicates that these changes could reduce error rates. Based on the 3.4 percent payment error rate reported in the review of 16 counties for the period September 1981 through August 1982, payments in error in these counties amount to $25.3 million ($12.6 million General fund). If the statewide error rate during this period was as high as 3.4 percent, total Medi-Cal payments in error may have been as large as $32 million ($16 million General Fund).

The department advises that as of January 31, 1984, it has not instituted a corrective action plan to assure that the recommended changes are made. The department advises, however, that such a plan may be developed during the first few months of 1984. Without a detailed corrective action plan, it is uncertain that these recommendations would be implemented.

At a minimum, a corrective action plan should include:

- Identification of those specific actions that need to be taken at both the state and county levels.
- Concise statements of the factors causing errors in each of the counties.
- Guidelines that need to be followed in order to reduce these errors.
- Identification of the agencies and individuals responsible for implementing each change.
- Timetables that include goals and the activities to be accomplished by specific dates.
- A system of ongoing reviews to ensure that these goals are attained.

In order to assure that the corrective actions suggested by the department in its June 1983 report are taken, we recommend that the department report to the Legislature during budget hearings on the status of corrective action plans (1) at the state level and (2) for each of the counties and the two Los Angeles County hospitals reviewed in the department's evaluation of county-specific error rates.

Assembly Bill 799 Requires State Fiscal Sanctions Against Counties

We recommend that the department advise the Legislature by April 1, 1983, of its plans to (1) determine county-specific payment error rates and (2) utilize these rates to pass along federal error rate fiscal sanctions and assess state sanctions as required under current state law. We withhold recommendation on (1) $2,466,000 ($1,233,000 General Fund) proposed for quality control evaluations and (2) the proposed reduction of 6 positions and $158,000 ($79,000 General Fund), pending receipt of this plan.

In an attempt to avoid any cost to the state from federal sanctions caused by county errors, and to provide an incentive for the counties to reduce eligibility determination errors, the Legislature, in AB 799 (Ch 328/82), required the department to:

- Levy fiscal sanctions against counties for payment errors in Medi-Cal eligibility determinations that are in excess of a specified error rate standard. It required the department to report to the Legislature by July 1, 1983, specifying the error rate standard to be used during 1983–84.
- "Pass on" to counties the portion of any federal sanction levied against the state that results from an individual county's failure to apply Medi-Cal eligibility regulations.
- Seek payment from counties for additional administrative or program benefit costs that result from incorrect application of established policies and procedures.

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No Ongoing County-Specific Reviews. In its July 1983 report to the Legislature, the department established a 3 percent payment error rate standard for use in applying sanctions to the counties. At the time this analysis was prepared, however, the department had not established (1) a method for applying county sanctions based on this standard and (2) an ongoing county-specific quality control review program.

Ongoing county-specific reviews of payment errors are necessary if the state is to assess sanctions against individual counties. The department advises, however, that it does not plan to conduct these statutorily required reviews during 1984–85 because:

- It does not have enough staff to obtain a statistically valid sample of cases in each county. This is most surprising. The Legislature authorized 30 positions in the 1982 Budget Act for county-specific reviews. The department subsequently eliminated 7 of these positions on the basis that they were not needed to determine county-specific error rates. (Funds appropriated by the 1982 Budget Act for these 7 positions were used by the department to partially restore legislative reductions to the department's travel budget.) In addition, the department proposes to eliminate 6 more positions in the 1984–85 budget. No specific rationale for this reduction has been provided to the Legislature. Yet, the department advises that it is understaffed and cannot develop statistically valid county-specific payment error rates. This makes no sense.
- It is now considering the use of case error rates, rather than payment error rates, as the basis for applying sanctions. Although case errors may accurately reflect the number of mistakes made by county eligibility workers, it is the *cost* of those mistakes that is the primary concern of the state. Case error rates may not capture the cost of eligibility determination errors, because the health care costs of Medi-Cal beneficiaries vary widely. Moreover, (1) AB 799 requires the department to base sanctions on a payment error rate and (2) if federal sanctions are to be passed on to the counties, county error rates should be based upon the same standards used by the federal government to sanction the state—that is, payment error rates, not a case error rate.

During 1983–84, a federal sanction of $210,600 was not passed on to those counties with high error rates because the department had failed to develop a method for determining error rates on a county-specific basis. Thus, state taxpayers were forced to absorb the cost of errors made by county employees. In the event that additional sanctions are imposed on the state, it will have to absorb these costs as well, because it will not be able to pass them along to the counties with high error rates. In addition, the wide variation in error rates among the counties shown in Table 43 indicates some action, perhaps fiscal sanctions, is necessary, regardless of whether sanctions are imposed on the state by the federal government.

In short, it does not appear that the Legislature's goals are being achieved because of the department's refusal to comply with current statutory requirements. We recommend that the department advise the Legislature by April 1, 1984, of plans, if any, to (1) determine county-specific payment error rates and (2) utilize these rates to pass along federal error rate fiscal sanctions and assess state sanctions. We withhold

recommendation on (1) $2,466,000 ($1,233,000 General Fund) proposed for quality control evaluations and (2) the proposed reduction of six positions and $158,000 ($79,000 General Fund), pending receipt of this plan.

Salary and Benefit Increase Proposal Flawed

We recommend that:

1. ***$10,133,000 ($5,165,000 General Fund) be transferred from the main Medi-Cal benefits item (4260-101) to the rate increase item (4260-106) to fund a 1984–85 cost-of-living adjustment for county administration, in lieu of past-year county salary and benefit increases that exceed what the state agreed to fund.***

2. ***The Legislature adopt Budget Bill language limiting the extent to which the state will share in the cost of salary and benefit increases granted by the counties.***

3. ***The Legislature establish 1984–85 cost-of-living adjustments for county employees based on the final 1984 Budget Act increase for state employee compensation.***

The budget contains $13,300,000 ($6,779,000 General Fund) to fund a proposal to remove existing limitations on the state share of costs for salary and benefit increases granted by counties in prior years. These limitations were imposed in prior years in order to cap the percentage increase in county welfare department salaries that the state would fund at the percentage increase granted to state employees. This amount exceeds the amount actually required for this purpose by $3,167,000 ($1,614,000 General Fund), due to a technical budgeting error. The actual amount needed to fund the proposal is $10,133,000 ($5,165,000 General Fund).

The budget does not contain any funds for county salary or benefit increases that may be granted in 1984–85.

The Legislature has sought to limit the state's share of county-granted cost-of-living adjustments (COLAs). Under current law, the state reimburses counties for 100 percent of the costs associated with Medi-Cal eligibility determination. Fifty percent of these costs are supported from the General Fund; the balance comes from federal funds. Since 1981–82, however, the state has placed limits on the costs that it will reimburse. Specifically, it has limited the size of any salary and benefit increases granted by the counties that it will fund.

The 1981 Budget Act contained sufficient funds to pay the state's share of salary and benefit increases for county eligibility staff up to 6 percent. In addition, the 1981 Budget Act stated that counties would be responsible for paying the state's share of any increases granted in excess of 6 percent, unless the excess COLA could be funded by permanent productivity increases. The purpose of this limitation was twofold. First, it sought to avoid cost overruns for county administration, such as occurred in 1980–81 when the counties granted increases of 10.1 percent, or approximately one percentage point more than the 9 percent provided in the 1980 Budget Act. Partially as a result of these higher-than-anticipated salary and benefit increases, Medi-Cal county administration expenditures in 1980–81 exceeded the amount included in the 1980 Budget Act by nearly $6 million or 6 percent. Second, the Legislature sought to avoid funding larger salary increases for county workers than what it provided to state employees.

The 1982 Budget Act did not contain any funds for a COLA. It continued the COLA limits established in 1981–82. In the 1983 Budget Act, the Legislature provided a 3 percent COLA for county employees, and allowed

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counties that granted salary and benefit increases less than 3 percent to apply the difference to COLA costs not funded in the previous two years. The Governor vetoed the COLA authorized by the Legislature. Table 45 summarizes budget controls on county salary and benefit increases from 1980–81 through 1984–85.

Table 45
Budget Act Controls on the State's Share of Costs Resulting from County-Granted COLAs for Welfare Department Employee Salaries and Benefits 1980–81 through 1984–85

Budget Act	*Budget Increase*	*Budget Act Language*	*Effect*
1980	9%	None.	State shared in the cost of actual salary and benefit increases averaging 10.1 percent. Expenditures exceeded appropriations by $6 million, or 6 percent, in part due to higher-than-anticipated county salary and benefit increases.
1981	6%	The state shall not share in the cost of salary and benefit increases that exceed the percentage increase authorized by the Legislature unless the excesses are funded by permanent productivity increases.	Counties granted an average 8.6 percent COLA. This was 2.6 percent above the level supported by state funds.
1982	0%	Same as above.	Counties granted an average COLA of 4.6 percent.
1983	0% [a]	Same as above, except counties may use COLA funds for the current year to fund prior-year increases, provided that the increase does not exceed the current-year allocation.	The department estimates that counties will grant average salary and benefit increases of 4.6 percent to their employees.
1984	0%	Proposes $13,300,000 ($6,779,000 General Fund) to restore the 50 percent share of actual county salary and benefit levels.	$13,300,000 ($6,779,000 General Fund) added cost.

[a] The Governor vetoed a 3 percent COLA provided by the Legislature.

Counties Granted Increases of 19 Percent. Table 46 compares the salary and benefit increases granted to county workers with limitations on such increases adopted by the Legislature, the increases granted state employees, and other measures. The table shows that during the period that state funds for county salary and benefit increases were limited to 6 percent, the counties actually granted increases that averaged 19 percent. During this same period, the state granted increases of 10 percent to its own employees and 16 percent to Aid to Families with Dependent Children grant recipients. Only the county salary and benefit increases exceeded the changes in the California Consumer Price Index during this period.

Table 46
Comparison of State-Supported Salary and Benefit Increases With Actual Increases and Other Related Measures [a] 1980–81 through 1983–84

	State-Funded County Salary Benefit Increases	*Average for County Welfare Staff*	*Range of Increases Provided by Individual Counties*	*Salary Increase for State Civil Service*	*Change in California CPI*	*Increase in AFDC Grants*
1980–81	10.4%	10.4%	3.6%–14.2%	10.0%	11.3%	12.9%
1981–82	6.0	8.6	0–15.0	6.5	10.8	9.3
1982–83	—	4.6	–4.4–14.7	—	1.8	—
1983–84	—[b]	4.6 (est)	N/A[c]	3.0	4.6	4.0
Cumulative 1981–82 through 1983–84	6.0%	18.8%	1.5%–25.6%[d]	9.7%	18.0%	15.9%

[a] All increases represent average annual increases.
[b] The Governor vetoed a 3 percent increase provided by the Legislature.
[c] Actual 1983–84 increases are not yet available.
[d] Includes increases only as of 1982–83.

San Francisco County Granted 26 Percent COLAs. Table 47 compares the *budgeted* salary and benefit increases in the period July 1981 through June 1983 with the actual increases granted by the 12 largest counties. The table shows that the average salary and benefit increase reported by counties during this period was 14 percent, or more than double the 6 percent increase in which the state would share. Of the 12 largest counties, Riverside provided the lowest increase, 9 percent. San Francisco County granted increases totaling 26 percent, the highest among the 12 largest counties. The estimated statewide cost of salary increases granted by counties between 1981–82 and 1983–84 in excess of 6 percent is $10,133,000.

Table 47
Comparison of Budgeted and Actual Salary and Benefit Increases Granted by 12 Largest Counties July 1981 through June 1983

Counties	*Budgeted Increases*	*Actual Increases*	*Difference*	*Unfunded Cost of Salary Increases*
Alameda	6%	23.3%	17.3%	$577,000
Contra Costa	6	18.9	12.9	250,000
Fresno	6	9.9	3.9	153,000
Los Angeles	6	19.2	13.2	3,925,000
Orange	6	21.6	15.6	560,000
Riverside	6	8.8	2.8	78,000
Sacramento	6	9.1	3.1	97,000
San Bernardino	6	17.4	11.4	403,000
San Diego	6	12.2	6.2	301,000
San Francisco	6	25.6	19.6	537,000
Santa Clara	6	18.0	12.0	667,000
San Joaquin	6	15.2	9.2	182,000
Statewide total	6	13.6[a]	7.6[a]	$10,133,000

[a] Based on increases reported by counties.

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Governor's Proposal Flawed. The budget proposes to remove limitations on state funding for county-granted salary and benefit increases during the period 1981–82 to 1983–84. For example, during this period the state shared in the cost of increases up to a total of 6 percent over the 1980–81 salary and benefit levels. If a county actually granted an 8 percent increase in salaries and benefits, the budget proposal would increase the county's allocation to make up the 2 percent deficit, which is currently supported by county rather than state funds. On the other hand, if the county granted increases of 5 percent during that period, the county would receive no additional funds under the Governor's proposal.

We identified several major problems with the budget proposal:

- ***Proposal Rewards High-Cost Counties.*** Funding prior-year increases in the manner proposed is inequitable to counties that attempted, in good faith, to follow the state's lead in keeping their salaries within the ranges for which state funds were available. Counties that postponed salary and benefit increases in anticipation of larger state increases in 1984–85 or later years would not receive one cent under the Governor's proposal. Instead, the proposal rewards the counties that have not controlled salary and benefit costs. Actual county increases in the period July 1981 to June 1983 ranged from 1.5 percent to 26 percent. The Governor's proposal would provide no additional funds for the county that chose to forego salary and benefit increases and would fully fund the 26 percent increase in the other county for a period during which state employee salaries and benefits were increased by 10 percent. Moreover, funding excess past salary and benefit increases without any provision for 1984–85 increases may create an expectation among counties that the state will participate in the future in the cost of any salary and benefit increase granted during 1984–85.
- ***Budget Proposal is Based on a Faulty Premise.*** The budget asserts that (1) counties have funded higher salary and benefit increases than supported by the state through staff reductions and (2) these staff reductions may lead to high error rates. Our analysis indicates that this premise is incorrect.

  First, counties that granted high salary and benefit increases have *not* funded these increases through staff reductions. In fact, our analysis indicates that the counties most likely to have increased the cases per worker during the time salary increases were limited were those counties with low salary adjustments! We compared productivity per worker for each of 30 counties to the average productivity in the county's size group. The 10 counties with the largest salary increases (19 percent to 26 percent) between July 1981 and June 1983 showed *no increase* in worker productivity, and remain at 98 percent of the average productivity level for counties in their respective size groups.

  In comparison, productivity *has* improved in the 10 counties with the smallest salary increases (1.5 percent to 7.5 percent) since state funding for salary increases has been limited. Prior to salary limitations, these counties' productivity was 5 percent above the average productivity for counties in their size group. By 1982–83, productivity was 11 percent above productivity for counties of similar size. Table 48 displays the results of this analysis.

  Second, no evidence has been provided to show that error rates are increasing. It is possible that the number of cases per worker could

increase to a point where the accuracy of eligibility determinations is jeopardized. It does not appear, however, that this point has been reached in the Medi-Cal program. In fact, statewide, Medi-Cal error rates during the period in which the Legislature maintains salary increase limits actually declined (6.1 percent and 1.1 percent for the last two review periods). In fact, if there is a problem due to increases in the number of cases per worker, the budget proposal does not address it, since the funds generally would *not* go to counties that have increased cases per worker.

Table 48

Employee Productivity as a Percent of Average for County Group Size [a] For 30 Counties With Small, Medium, and Large COLAs July 1981 through June 1983

	1980–81	*1981–82*	*1982–83*
Counties with small COLAs (1.5 percent to 7.5 percent)	105%	105%	111%
Counties with medium COLAs (7.6 percent to 19 percent)	102%	108%	108%
Counties with large COLAs (19 percent to 26 percent)	98%	98%	98%

[a] Includes applications, continuing cases, and various administrative tasks.

Analyst's Recommendation. We believe the Governor's proposal to abandon legislative policy established for the purpose of limiting state spending for county salary and benefit increases is inequitable to counties who *have* attempted to control the growth in salary and benefit costs as the Legislature directed. Moreover, the budget's failure to provide for any salary increase in 1984–85 is shortsighted. This failure, in combination with the precedent set by funding all prior-year increases, may result in substantial state costs in 1985–86 and subsequent years.

Therefore, we recommend rejection of the budget proposal. Instead we recommend:

1. Transfer of funds proposed for this past-year cost increase, $10,133,000 ($5,165,000 General Fund), from the main Medi-Cal item to the rate increase item to provide salary increases up to the amount set by the Legislature. This total is sufficient to provide up to an 8.9 percent salary increase for county employers. Each 1 percent increase for this purpose would require $1,160,000 ($580,000 General Fund).
2. The Legislature adopt Budget Bill language that specifies (a) the state will not pay for 1984–85 salary increases in excess of the percent allowed by the Budget Act and (b) counties may fund past-year increases within the amount made available to them based upon the percentage increase specified in the Budget Act. This is the same language the Legislature included in the 1983 Budget Act.
3. The Legislature fix the maximum COLA for which the state will provide funding at a level comparable to the percentage salary increases granted to state employees.

This course of action would offer several improvements over what the budget proposes.

1. ***It Allows All Counties Additional Funding for Salary and Benefit Increases.*** Those counties that exceeded past caps could receive state support for all or a portion of the excess. Counties that stayed within past caps can increase salaries and benefits in 1984–85 if they choose and receive state participation in the increases.

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2. ***State Participation in Salaries Will Increase Uniformly Throughout the State.*** The budget proposal would result in the state allowing significantly different increases in different counties. The mechanism we recommend to increase allowable salaries would limit state participation to equal increases in all counties, up to a specified limit (except in those counties granting salary increases that are less than that allowed by the salary caps from 1981–82 to 1984–85).

3. ***It Prevents the Legislature from Being Criticized for Funding Salary and Benefit Increases Paid to County Employees that are Larger Than Increases that it Provides to State Employees.*** Since 1980–81, salary and benefit levels in the state civil service have increased by 10 percent. This includes 6.5 percent in 1981–82 and a 6 percent increase provided for half of 1983–84. County administration COLAs have been limited to 6 percent. Under our proposal, the state could limit the COLA for which counties would receive state funding to that provided state employees.

Our recommended Budget Act language is identical to the language contained in the 1983 Budget Act. Following is the suggested language:

"Notwithstanding any other provision of law, the funds appropriated by this item shall be used to provide cost-of-living adjustments to county welfare departments for personal and nonpersonal services, or to fund the amount of cost-of-living increases granted by counties which exceeded the levels specified in the state Budget Acts for the 1981–82, 1982–83 and 1983–84 fiscal years, not to exceed the percentage increase authorized by the Legislature for all counties in this item for the 1984–85 fiscal year.

"The 1984–85 county administration cost control plan shall contain a provision which specifies that any county cost-of-living increase for personal and nonpersonal services which exceeds the percentage increase authorized by the Legislature shall be the sole fiscal responsibility of the county unless the excess costs are funded by permanent productivity increases, or in subsequent years the cost-of-living adjustments granted by counties are less than the percentage increase authorized by the Legislature.

"The department shall not allocate, reallocate, or transfer unused portions of county cost-of-living funds between counties nor shall the department use any funds to fund cost-of-living adjustments in excess of the percentage increase authorized by the Legislature in this item."

Technical Error in Past Salary Increase Calculation

We recommend a reduction of $3,167,000 ($1,614,000 General Fund) to correct a technical budgeting error made in calculating the cost of providing state support for past county employee salary and benefit increases.

The budget proposes $13,300,000 ($6,779,000 General Fund) to provide state support for past county salary and benefit increases.

The department overestimated the cost of these increases by including the cost of operating expenses and equipment in the cost of clerical and administrative support staff salaries. These costs were *not* limited by the Budget Act language controlling salary increases.

In 1983–84, operating expenses and equipment account for 23 percent of county eligibility determination costs for the seven largest counties. Based on this percentage, we estimate that the amount proposed for past

salary increases is overbudgeted by $3,167,000 ($1,614,000 General Fund). To correct this technical budgeting error, we recommend a reduction of $3,167,000 ($1,614,000 General Fund).

C. MEDI-CAL CLAIMS PROCESSING

The Department of Health Services does not directly pay doctors, pharmacists, hospitals, nursing homes, and other providers for the services they render. Instead, the department contracts with fiscal intermediaries for Medi-Cal fee-for-service claims processing. Currently, the department has contracts with the Computer Sciences Corporation (CSC) and two other vendors. In addition, the department reimburses the State Controller's Office for writing and mailing payments to Medi-Cal fee-for-service providers and the State Treasurer's Office for redeeming Medi-Cal warrants. Payments to organized health systems and for mental health services provided under the Short-Doyle Act are processed directly by the department or by the health system itself in the case of the Redwood Health Foundation and the California Dental Service.

The budget anticipates that General Fund expenditures for claims processing in the *current year* will be $735,000, or 7.7 percent, higher than the amount included in the 1983 Budget Act. Total current-year expenditures for claims processing, including federal funds ($28,205,000) and reimbursements from the County Medical Services program ($397,000), will be $2,278,000, or 6.2 percent, higher than budgeted. The $735,000 increase in current-year General Fund costs is due to start-up costs for a new claims processing contract ($243,000), reductions in federal funding ($318,000), and various workload and cost changes ($174,000). The budget proposes to fund the claims processing deficit and a shortfall in funds budgeted for Medi-Cal health care services by redirecting surplus funds from county administration and using unanticipated federal funds.

The budget proposes $28,774,000 ($7,190,000 General Fund) for fee-for-service claims processing in 1984–85. This is a reduction of $10.1 million ($3.1 million General Fund), or 26 percent (30 percent General Fund), below estimated current-year expenditures for this function. The primary causes of this reduction are procurement of a new lower-cost claims processing contract, adjustments for one-time 1983–84 costs, and reestimates of federal funding ratios.

Table 49 summarizes estimated and proposed expenditures for Medi-Cal claims processing in 1983–84 and 1984–85.

Current-Year Costs Will Exceed 1983 Budget Act

The estimated $735,000 increase in current-year General Fund claims processing costs reflects the following costs and savings:

- An increase of $124,000 in the costs of the previous (1978 to 1984) claims processing contract with the Computer Sciences Corporation. This increase is due to (1) recalculation of the number of claims that will be processed under an extension of the old contract and thereby subject to higher-than-usual reimbursement rates and (2) repricing of some change orders.
- Start-up costs of $243,000 and transition costs of $33,000 associated with the procurement of a new claims processing contract with the Computer Sciences Corporation.
- Payment of $201,000 to the federal government for inappropriately claimed funds in past years.

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Table 49
Medi-Cal Claims Processing
Proposed Budget Changes
(in thousands)

	General Fund	*All Funds*
A. 1983 Budget Act	$9,553	$36,612
B. Unanticipated current-year expenditure changes		
1. Computer Sciences Corporation contract		
a. Workload, sales tax, and operating costs	66	189
b. Change orders	58	532
c. Turnover to new contract	33	131
d. Costs of new contract	243	905
2. Increased cost for warrant redemption by State Treasurer	37	144
3. State Controller's Office	2	10
4. Changes in federal funding		
a. Reduced federal sharing ratio	117	—
b. Net refugee reimbursements	−22	166
c. Return of overdrawn federal funds	201	201
C. 1983–84 expenditures (revised)	$10,288	$38,890
D. Projected current-year deficit	($735)	($2,278)
E. Budget-year changes		
1. CSC contract		
a. Reduction in workload, sales tax, and operating costs	−1,857	−6,730
b. New contract enhancements	321	1,274
c. Reduction in required change orders	−869	−4,104
d. Deletion of one-time contract turnover costs	−33	−131
e. Reduction in costs for County Medical Services program claims	—	−140
2. Fully reimbursable contracts		
a. Crossover claims contracts—increased volume	20	82
b. State Controller's Office—enhanced federal funding	−3	—
3. Adjustments for one-time 1983–84 costs	−367	−367
4. Reestimate of federal matching reduction	−189	—
5. Refund of withheld federal funds	−135	—
6. Reduction in refugee reimbursements	14	—
F. 1984–85 expenditures (proposed)	$7,190	$28,774
G. Change from 1983–84 (revised):		
Amount	−$3,098	−$10,116
Percent	−30%	−26%

- Higher-than-anticipated net General Fund costs ($117,000) due to the federal matching reductions established by the Omnibus Budget Reconciliation Act of 1981.
- Increases of $39,000 in costs for warrant redemption by the State Treasurer and check mailing by the State Controller.
- Change in reimbursements for refugee claims processing, for a net savings of $22,000.

Budget Reduction Due to New Contract

The budget proposes $28.8 million ($7.2 million General Fund) for Medi-Cal claims processing activities in 1984–85. The General Fund request is $3.1 million, or 30 percent, less than estimated 1983–84 expenditures. The major reasons for this decrease are as follows:

- A reduction in operating costs of $1,857,000, attributable primarily to the change from a rate based on claim volume to a flat annual rate under the new claims processing contract.

- A reduction of $869,000 in the cost of change orders due to the new contract.
- Additional costs of $321,000 for support of a systems development group and implementation of claims processing enhancements under the new contract.
- Reductions of $400,000 to adjust for one-time 1983–84 expenditures.
- Net reductions of $313,000 due to federal funding changes and a reduction in anticipated reimbursements for refugee claims processing.
- Additional costs of $20,000, due to projected volume increases in Medi-Cal/Medicare crossover patient claims.

Table 50
Fiscal Intermediary Expenditures
1983–84 and 1984–85
(in thousands)

	Estimated 1983–84		*Proposed 1984–85*	
	General Fund	*All Funds*	*General Fund*	*All Funds*
A. Computer Sciences Corporation (CSC)				
1. Old contract				
a. Operations, reimbursable items, and sales tax	$4,381	$16,238	—	—
b. Change orders				
(1) Diagnosis coding	338	1,330	—	—
(2) Systems enhancements	100	996	—	—
(3) Hospital contracting	150	589	—	—
(4) Other	104	417	—	—
c. County Medical Services program	—	260	—	—
Subtotals	$5,073	$19,830	—	—
2. Extension of old contract				
a. Operations, reimbursable items, and sales tax	$3,513	$13,049	$1,019	$3,820
b. Turnover to new contract	33	131	—	—
c. Change orders	240	1,022	—	—
d. County Medical Services program	—	137	—	11
Subtotals	$3,786	$14,339	$1,019	$3,831
3. New contract				
a. Operations, reimbursable items, and sales tax	$68	$217	$5,086	$18,954
b. Enhancements and change orders	50	198	147	584
c. Systems development group	45	177	398	1,574
d. Turnover costs	80	313	14	55
e. County Medical Services program	—	—	—	246
Subtotals	$243	$905	$5,645	$21,413
Subtotals, CSC	$9,102	$35,074	$6,664	$25,244
B. Medicare crossover claims contracts	$303	$1,210	$323	$1,292
C. State Controller and Treasurer	569	2,239	566	2,239
D. One-time costs	367	367	—	—
E. Federal sharing ratio reductions	739	—	550	—
F. Return of past federal sharing ratio reductions	−604	—	−739	—
G. Reimbursements for refugee claims	−188	—	−174	—
Totals	$10,288	$38,890	$7,190	$28,775

The CSC contracts account for 93 percent ($6.7 million) of proposed General Fund expenditures and 88 percent ($25.2 million) of expenditures from all funds for claims processing in 1984–85. During 1984–85, costs for CSC claims processing will be incurred under the terms of two separate contractual arrangements, due to the transition from one contract to the next. Of the $25 million total, $21 million is proposed for expenditure

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under the new contract and $4 million is proposed under an extension of the old contract. Claims processing under the new contract begins on July 5, 1984. Claims received in June 1984 and during the first five days of July 1984 will be processed under the extension of the old contract, at higher rates.

The remaining 7 percent ($526,000) of General Fund expenditures budgeted for claims processing consists of expenditures for (1) contracts with three firms to process claims for persons who are eligible for both Medicare and Medi-Cal ($323,000); (2) reimbursements to the State Controller and State Treasurer for writing, mailing, and redeeming Medi-Cal warrants ($566,000); and (3) replacement of federal funds withheld due to reduced federal sharing ratios ($550,000), offset by reimbursements and additional federal funds ($913,000). Table 50 shows the amounts proposed for each of these claims processing activities during 1983–84 and 1984–85.

New Contract Could Save $11 Million

The CSC will begin processing claims for all fee-for-service Medi-Cal provider categories under the terms of a new contract beginning on July 5, 1984. This contract expires March 31, 1988, unless extended for up to one year by the state. The total contract price through March 31, 1989 (assuming a one-year extension), is $72,950,000, based on the CSC bid. Actual costs of this contract probably will exceed this amount, however, due to (1) payments for cost-reimbursable items not included in the bid price, (2) additional costs for potential major change orders, although most processing changes should not require change orders under the new contract, and (3) possible additional payments in the event that claims volumes exceed the projected volumes covered by a flat price per year under the new contract.

The department estimates this contract may result in *total savings of $41 million* ($11 million General Fund) over the next five years. In addition, the department advises that several system improvements will result in Medi-Cal health care services costs and savings. Actual costs or savings due to the new contract will depend on Medi-Cal claims volume, the number of change orders, and the cost of fully reimbursable items.

The major features of the new contract are as follows:

- ***Fixed Price.*** The major portion of contract costs, payments for actual operations, is based on a fixed price per year, provided that claim volume does not fall above or below specified limits for each year. If claims volume is outside the specified range for a given year, the price per claim line will be renegotiated. Under the previous contract, CSC was paid for each claim line processed, based on different fees for each major claim type.
- ***Systems Development Group.*** Most changes to the claims processing system will be handled on a routine basis by a group of up to 45 professional staff employed by CSC and funded within the contract price. Under the previous contract, any modifications were subject to cost-based pricing, and many change orders were delayed due to lengthy negotiations between the department and CSC. In order to assure that various enhancements are fully operational as soon as possible, the administration authorized early hiring of 5 staff in December 1983 and 10 additional staff in March 1984.
- ***Enhancements.*** The new contract requires CSC to install by July

5, 1984, a number of enhancements to the previous contract, including a capability to accept provider claims on magnetic tape. Several of these enhancements were initially proposed as change orders under the old contract but were withdrawn prior to release of the invitation for bids for the new contract. Under the new contract, change orders will be required only for major processing changes.

- ***Regional Provider Relations Centers.*** The contractor will employ 3–5 staff in each of five separate locations throughout the state to respond to provider problems and conduct claims preparation training. Actual claims adjudication, however, will continue to be handled at the main CSC processing facility in Sacramento. Under the old contract, most provider relations activities were conducted by telephone from Sacramento.

Procurement on Schedule But Delays Are Possible. All major milestones in the procurement of a new claims processing contract were met by the staff of the Medi-Cal Procurement project. After the opening of bids and notification of intent to award the new contract to CSC, however, one of the unsuccessful bidders filed a protest with the Department of General Services. The McAuto Systems Group, Incorporated, alleged that CSC had inappropriately reduced its estimate of staff costs in order to reduce its bid price. The Department of General Services ruled against McAuto and the contract with CSC was executed. Subsequently, McAuto filed suit in the San Francisco Superior Court against the Department of General Services. This case will be heard in late January 1984. Depending on the court's ruling, it is possible that a delay in the implementation of the new contract may result. Table 51 summarizes the major events in the new contract procurement and implementation process, from the release of the final request for proposals to the expiration of the new contract.

Table 51

Chronology of Transition to New Claims Processing Contract

Event	*Date*
Final request for proposal released	March 1983
Invitation for bid sent to qualified vendors	August 1, 1983
Bids opened	August 24, 1983
Notification of intent to award contract	August 29, 1983
New contract executed	October 19, 1983
CSC systems testing and enhancements	October 1, 1983 to January 31, 1984
Drug and long-term care claims shifted to extension price	October 1983
State acceptance testing of new system	February 1 to June 1, 1984
Final date for official extension of old contract	January 29, 1984
Hospital and professional services claims shift to extension price	February 29, 1984
All claims types except residual claims types processed under the extension contract shift to new contract	July 5, 1984
Residual claim types not processed under the extension contract shift to new contract prices	October 1, 1984
Extension of old contract expires	February 28, 1985
New contract expires	March 31, 1988
Optional extension of new contract expires	March 31, 1989

Budget Proposes Extension of Old Contract. The budget indicates that the previous contract with CSC will be extended to cover processing

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between the expiration of that contract and the beginning of processing under the new contract on July 5, 1984. The previous CSC claims processing contract expired October 1983 for drug and long-term care claims and is due to expire February 29, 1984, for the remaining claim types. The 1983 Budget Act requires the Department of Finance to notify the Legislature 30 days prior to extending the old contract. On January 30, 1984, the Department of Finance notified the Legislature that the contract would be extended.

The Department of Health Services projects that a total of 11.7 million claim lines will be processed in 1984–85 under the terms of the contract extension, at a cost of $3.8 million ($1 million General Fund). All claims received by CSC after July 5, 1984, will be processed under the new contract at the fixed price per year. The Department of Finance advises the extension contract will require that the claim lines received in the contract extension period be completely adjudicated by October 1, 1984, and that the price per claim line will be based on the old contract rates adjusted by changes in the California Consumer Price Index.

Auditor General Continues Monitoring. The 1982 and 1983 Budget Acts required the Auditor General to monitor the procurement and implementation of the new claims processing contract. In his September 1983 report, the Auditor General stated that the evaluation of bids was consistent with the process outlined in the request for proposal and cited no problems in the review and award process. Staff of the Auditor General advise that an additional report addressing the progress of system testing by CSC and resolution of the McAuto protest on the award of the contract to CSC will be released by February 1984.

Job Well Done. Our analysis indicates that the department and the staff of the Medi-Cal Procurement project have nearly completed the extremely difficult task of procuring a new Medi-Cal claims processing contract. Throughout this effort, the administration has been open and responsive to potential bidders, the staff of the Auditor General, and other legislative staff. In addition, the staff of the Auditor General provided numerous productive suggestions to the department. We believe the Legislature has good reason to congratulate both the department and the Auditor General for a job well done.

Cost Reimbursements Overbudgeted

We recommend a reduction of $796,000 ($201,000 General Fund) to reflect anticipated decreases in cost-based reimbursements to the CSC.

The budget proposes $5,300,000 ($1,341,000 General Fund) for payments to CSC for items and services not included in the overall contract bid price. These cost-reimbursable items consist primarily of (1) printing and mailing of various forms, provider manuals, and training materials and (2) rental and maintenance of a network of remote terminals for state access to payment records. Under the new contract, total cost-based reimbursements will be reduced due to inclusion in the bid price of costs for printing and mailing treatment authorization requests and claim inquiry forms. The department estimates that removing the costs of these two commonly used forms from the list of cost-reimbursable items will reduce cost-based payments by 15 percent annually.

In calculating the budget request for cost-based reimbursements, the department reduced by 15 percent the maximum amount allowed under

the old contract for this purpose ($6 million). Actual cost-based payments were $4.9 million in 1981–82 and $5.1 million in 1982–83. Because the department used planned, rather than actual, costs in its calculation of this portion of claims processing costs, the budget is overstated by $796,000 ($201,000 General Fund), including $750,000 for cost reimbursements and $46,000 for sales tax. In order to more accurately reflect the cost of claims processing in 1984–85, we recommend a reduction of $796,000 ($201,000 General Fund).

Controller Audits are Medi-Cal Function

We recommend an increase of $371,000 ($185,000 General Fund) for support of the ongoing checkwrite audit performed by the State Controller's office, because this is a Medi-Cal administration function and funding it from the Medi-Cal items will permit a $186,000 savings to the General Fund.

Since 1979, the State Controller's office has audited Medi-Cal claims tapes prior to mailing warrants to providers. These audits have identified and prevented payment of exceptions totaling $19 million. The Controller's budget proposes $371,000 *from the General Fund* to support this function.

Because the audit activity is a legitimate part of state administration of the Medi-Cal program, we believe the $371,000 should be partially supported by federal funds. Therefore, we recommend an increase of $371,000 ($185,000 General Fund) in this item. In our analysis of the proposed budget for the State Controller, Item 0840, we recommend a reduction in the General Fund appropriation and an increase in reimbursements consistent with this recommendation. The net effect of the change to the two budget items will be a General Fund savings of $186,000.

D. MEDI-CAL STATE ADMINISTRATION

The budget proposes $106.8 million ($39.4 million General Fund) for state administration of the Medi-Cal program in 1984–85. This is a reduction of $1.6 million, or 1.5 percent, in total funds and a reduction of $800,000, or 2 percent, in General Fund support. Of the total amounts proposed for Medi-Cal state administration, $97.4 million ($35.8 million General Fund) is proposed for the support of the Department of Health Services. This is $1.7 million ($900,000 General Fund) less than estimated 1983–84 expenditures for this purpose. The remaining $9.4 million ($3.6 million General Fund) is proposed for support of other agencies.

The $1.7 million reduction in Medi-Cal costs for support of the department is due primarily to the termination of state-funded health care services for medically indigent adults on January 1, 1983. Table 52 displays Medi-Cal state administration expenditures in 1983–84 and 1984–85.

Medi-Cal Program Positions

The budget proposes 1,789.5 positions for administration of the Medi-Cal program in the department. This is 113.1 positions, or 5.9 percent, less than the number of authorized positions in the 1983–84 base budget. Of the 1,789.5 positions, 1,009.6 are located in various Medi-Cal program units, 450.5 are in the Audits and Investigations Division, and 329.4 are located in various administrative units throughout the department.

Table 53 shows the changes in Medi-Cal related positions proposed for the budget year.

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Table 52
Medi-Cal State Administration Expenditures
1983–84 and 1984–85
(in thousands)

	Estimated 1983–84		Proposed 1984–85		Percent Change in
	General Fund	All Funds	General Fund	All Funds	General Fund
Department of Health Services	$36,643	$99,143 [a]	$35,764	$97,394 [a]	−2.4%
Department of Social Services	2,700	7,715 [a]	2,700	7,715 [a]	—
California Medical Assistance Commission	851	1,630 [a]	889	1,703 [a]	4.5
Totals	$40,194	$108,488	$39,353	$106,812	−2.0%

[a] Table 52 shows where funds are actually proposed to be spent, not where they are appropriated. All federal funds spent in the Department of Social Services and California Medical Assistance Commission are apppropriated in the Department of Health Services items.

Table 53
Department of Health Services
Medi-Cal Program Proposed Position Changes
1984–85

	Existing Positions	Workload Adjustments	Total Medi-Cal Positions	Percent Change
Eligibility	77.2	−16.5	60.7	−21.3%
Benefits	41.5	—	41.5	—
Rate development	38.1	−4.0	34.1	−10.5
Field services	463.7	−20.0	443.7	−4.3
Organized health systems	81.3	−9.0	72.3	−11.0
Recoveries	241.8	—	241.8	—
Fiscal intermediary	129.4	−36.0	93.4	−27.8
Program management	24.1	−2.0	22.1	−8.3
Audits and investigations	470.5	−20.0	450.5	−4.2
Administration	335.0	−5.6	329.4	−1.7
"Three percent" reductions	—	(−9.0)	—	(−0.5)
Totals	1,902.6	−113.1	1,789.5	−5.9%

The reduction of 113.1 Medi-Cal positions is due to:

- A reduction of 16.5 positions in the Eligibility Branch as a result of automating beneficiary share-of-cost processing under the new fiscal intermediary contract.
- Termination of 4 limited-term rate development positions.
- A reduction of 16 prior authorization review positions in the Field Services Branch, due to greater-than-anticipated workload reductions from the transfer of medically indigent adults to the counties.
- Deletion of 6 positions from quality assurance monitoring of prepaid health plans in the Organized Health Systems Division. It is uncertain whether this monitoring will be conducted by other staff or if this project will be discontinued.
- Reduction of 25 positions due to termination of the Medi-Cal fiscal intermediary procurement project.

- Decrease of 17 positions in audits and investigations due to redistribution of workload.
- Elimination of 19.6 positions due to the consolidation of certain functions (mostly clerical) in various units.
- Reduction of 9 positions resulting from the Governor's "3 percent" reduction.

Fewer Treatment Authorization Request (TAR) Review Staff Needed

We recommend a reduction of 21 positions that are no longer needed, due to reductions in the number of treatment authorization requests (TARs), for a savings of $745,000 ($221,000 General Fund).

The budget proposes 430 positions and $15,263,000 ($4,533,000 General Fund) in the Field Services Branch to review treatment authorization requests (TARs) and support these reviews. TARs are submitted by Medi-Cal health care providers seeking authorization for elective hospital admissions and certain other services. Except for emergencies, TARs must be approved before the service can be provided. Because these authorizations often result in denial of unnecessary services, the TAR review process is a cost-effective utilization control.

The budget proposal reflects a reduction of 16 positions and $512,000 ($152,000 General Fund) from the 1983–84 TAR review staffing level, due to a projected 12 percent reduction in TAR volume. This workload reduction is due primarily to the termination of Medi-Cal eligibility for medically indigent adults and other eligibility-related changes made by the 1982 Medi-Cal reform legislation.

Staff Reduction Underestimated. Our analysis indicates that the proposed 16-position reduction does not reflect the actual workload decreases resulting from the 1982 Medi-Cal reform measures. Specifically, the proposed staff reduction:

- ***Is based on low estimates of the actual workload reduction.*** The 12 percent reduction in TARs received is based on a comparison of adjusted volumes during January to August 1982 and the same eight-month period in 1983. Using only eight months of data may not capture the full effect of the workload changes due to the 1982 reform legislation. By comparing average monthly TARs received during 1981–82 (104,825) and during the 10-month period from January to November 1983 (89,826), we determined that the workload reduction has been 14 percent, somewhat higher than that projected by the budget. Moreover, budget documents state that TAR workload is expected to increase after August 1983 due to greater understanding by providers of the new rules. In the three months after August 1983, however, TAR workload *declined* by 3.5 percent from the previous quarter.
- ***Uses outdated workload standards.*** The proposed staff reduction is based on workload standards developed in 1976, which do not accurately reflect either (1) the work required for TAR processing in 1984–85 or (2) the budgeted staff levels for any year since 1979–80. To develop its budget proposal, the department applied the workload standards to the projected reduction in each of 12 separate TAR categories to arrive at the total position reduction. Our analysis indicates that the workload standards used in this calculation understate the staff reduction allowed by the reduced TAR volume. For example, if these workload standards had been applied to projected *total* workload, instead of the projected *reduction* in workload, the total staff required for TAR review and various support functions would be 315,

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rather than the 430 proposed by the budget. It does not appear reasonable to reduce staff for this function by 115 positions based on these outdated workload standards. Because these workload standards have not been used in calculating total staff, it is equally inappropriate to use them to calculate the reduction in staff.

Additional Reduction of 21 Positions is Warranted. Our analysis indicates that the appropriate staffing level for TAR reviews is 409, or 21 positions less than proposed for 1984–85. Our calculation of necessary staff is based on the ratio of actual TARs received per budgeted position during 1981–82 and the actual workload during January to November 1983, rather than on outdated workload standards. Specifically, our estimate of staff requirements is based on:

- Actual TARs received per budgeted position during 1981–82. This 12-month period represents the most recent full year of data prior to implementation of the Medi-Cal reform measures. During this year, the branch received 236 TARs monthly for every budgeted position.
- Actual average monthly TARs received during January to November 1983. During January to November 1983, an average of 89,826 TARs were received each month. We project that this baseline level of TARs will continue in 1984–85. This is a decrease of 15,000, or 14 percent, below the number of TARs received per month during 1981–82, the last full year prior to implementation of the 1982 Medi-Cal reforms.
- Adjustments due to new workload. Dividing the average monthly TARs (89,826) by average monthly TARs received per budgeted position (236) results in the need for 381 positions. This total should be adjusted, however, to reflect (1) 21 additional positions for TAR reviews for Los Angeles County hospitals, (2) 10 additional positions for new TARs required by the 1982 Medi-Cal reforms, and (3) 3 fewer positions due to reduced workload associated with the establishment of county health initiatives in Santa Barbara and Monterey Counties.

Analyst's Recommendation. After making these adjustments, our analysis indicates that a total of 409 staff, or 21 fewer than budgeted, are necessary for TAR reviews and associated functions in 1984–85. Based on the average cost per position of the Field Services Branch in 1984–85 ($35,496), savings from the deletion of the 21 unnecessary positions would be $745,000 ($221,000 General Fund). Consequently, to fully reflect the workload reductions resulting from the termination of medically indigent adults and other eligibility changes made by the 1982 Medi-Cal reform measures, we recommend a reduction of 21 positions and $745,000 ($221,000 General Fund).

Field Services Has 15 Percent Vacancy Rate

We recommend the department advise the fiscal committees during budget hearings regarding (1) the administration's plans for filling vacant positions in the Field Services Branch and (2) the effects of high vacancy rates on the state's review of treatment authorization requests.

Our review of staffing levels for review of treatment authorization requests (TARs) indicates that the Field Services Branch has experienced a high vacancy rate during the past three fiscal years. During the first four months of 1983–84, 15 percent of the positions in this branch were vacant.

Table 54 compares budgeted positions with filled positions for this branch from 1981–82 to October 1983.

Table 54
Vacancies in the Field Services Branch
1981–82 through October 1983

	Budgeted Positions	*Filled Positions*	*Percent Vacant*
1981–82	443	384	13.3%
1982–83	432	384	11.1
July—October 1983	437	370	15.3

We are unable to determine the effect these high vacancies have on the department's ability to effectively review TARs. During this period, no significant changes have occurred in the percentages of requests denied or approved. Moreover, the review time for most request categories has remained relatively stable or actually declined since 1980–81. For example, the turnaround time for hospital extension requests declined from 9 days in 1980–81 to an average of 6 days during the first four months of 1983–84.

Our analysis of the staffing needs of this branch indicates that 409 positions, rather than the 430 proposed by the budget, are sufficient for TAR reviews. The approval of 409 positions, however, would still leave 39 vacant positions in the branch, or 6 percent of the total. If these positions are necessary to complete the review of TARs, they should be filled. If the positions are not necessary, we see no reason for them to remain in the budget. Because a high vacancy rate has existed in this branch since 1981–82, we recommend the department advise the fiscal committees during budget hearings regarding (1) the administration's plans for filling vacant positions in the Field Services Branch and (2) the effects of high vacancy rates on the state's review of TARs.

E. REVIEW OF MEDI-CAL RECOVERY PROGRAM PERFORMANCE

The Medi-Cal recovery program (a) identifies and collects funds due the Medi-Cal program from beneficiaries, service providers, insurance carriers, and other third-party payors, and (b) administers the Medicare Part B Buy-In program and other cost-avoidance activities. The objective of these post-payment and cost-avoidance activities is to reduce public expenditures for Medi-Cal health care services by shifting a portion of these costs to other payors, where appropriate.

Recovery program will reduce 1984–85 General Fund costs by $430 million. The budget projects net General Fund savings of $429.7 million from the Medi-Cal recovery program. These savings are the net effect of (1) post-payment recoveries of $27.1 million, (2) cost avoidance estimated at $472.4 million, and (3) costs of $69.8 million for Medicare Part B premiums and administration. Table 55 summarizes 1983–84 and 1984–85 savings and costs resulting from the recovery program.

As shown by Table 55, the state is expected to pay 41 percent of the administrative cost of collecting post-payment recoveries but will be credited with 50 percent of the estimated post-payment collections. Consequently, each General Fund dollar spent on post-payment recoveries yields $8 in benefits, while each federal dollar yields only $5 in benefits.

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Table 55

Medi-Cal Recoveries Program
Savings and Costs
1983–84 and 1984–85
(in millions)

	Estimated 1983–84			*Proposed 1984–85*		
	General Fund	*All Funds*	*Percent General Fund*	*General Fund*	*All Funds*	*Percent General Fund*
Post-payment						
Administrative costs	$3.4	$8.2	40.0%	$3.4	$8.3	40.6%
Medi-Cal recoveries	−20.4	−40.8	50.0	−27.1	−54.2	50.0
Net savings	−$17.0	−$32.6	51.4%	−$23.7	−$45.9	51.7%
Cost avoidance						
Administrative costs	$0.3	$1.1	27.8%	$0.4	$1.1	36.3%
Buy in premiums	55.8	91.2	61.0	66.0	107.3	61.6
Medi-Cal savings	−424.1	−458.1	92.6	−472.4	−514.4	91.8
Net savings	−$368.0	−$365.8	100.0%	−$406.0	−$406.0	100.0%
Total						
Costs	$59.5	$100.5	59.2%	$69.8	$116.7	59.8%
Savings	−444.5	−498.9	89.0	−499.5	−568.6	87.8
Net savings	−$385.0	−$398.4	96.6%	−$429.7	−$451.9	95.0%

Post-Payment Recoveries

The major objective of California's post-payment recovery program is to assure collection of funds due the state for past Medi-Cal health care services expenditures. Post-payment recoveries include collections from:

- Private health insurance carriers for health care provided to Medi-Cal beneficiaries who hold health insurance policies.
- Liable third parties for casualty and work-related injury cases involving Medi-Cal beneficiaries.
- Referrals from other state, county, and federal agencies. For example, the recovery program serves as a general collections agency for assuring that amounts identified in provider audits are paid.

Our analysis indicates California's post-payment recovery program is performing well, based on (1) growth in total collections, (2) collections compared to administrative costs, and (3) recoveries as a percentage of total Medi-Cal health care services expenditures.

Post-payment recoveries expected to increase by $13.4 million. One measure of program performance is total post-payment collections. Projected 1984–85 recoveries are $13.4 million, or 33 percent, more than the levels estimated for 1983–84. This increase is expected due to implementation of a provision contained in the 1982 Medi-Cal reform legislation that requires liens on some real property held by Medi-Cal beneficiaries. Chart 9 shows recoveries, by category, from 1981–82 to 1984–85. As shown by Chart 9, the majority of post-payment recoveries result from casualty and workers' compensation cases. Total recoveries have increased $27.4 million, or 102 percent, since 1981–82.

Chart 9
Post-Payment Medi-Cal Recoveries—All Funds
By Recovery Category
1981–82 through 1984–85 (in millions)

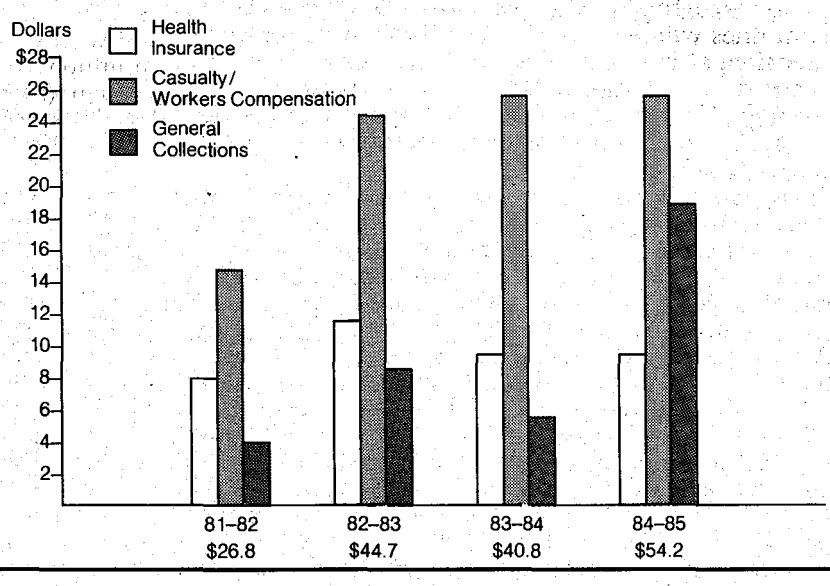

Table 56
Recoveries and Administrative Costs
by Recovery Category
1982–83 through 1984–85
General Fund
(in thousands)

	Recoveries	*Administrative Costs*	*Net Recoveries*	*Recoveries Per $1 Spent for Administrative Costs*
1982–83				
Health insurance	$6,364	$817	$5,547	$7.79
Casualty/workers' compensation	13,475	1,677	11,798	8.04
General collections	4,747	572	4,175	8.30
Totals	$24,586	$3,066	$21,520	$8.02
1983–84 (estimated)				
Health insurance	$4,750	$920	$3,830	$5.16
Casualty/workers' compensation	12,850	1,888	10,962	6.81
General collections	2,800	598	2,202	4.68
Totals	$20,400	$3,406	$16,994	$5.99
1984–85 (proposed)				
Health insurance	$4,750	$860	$3,890	$5.52
Casualty/workers' compensation	12,850	1,950	10,900	6.59
General collections	9,450	640	8,810	14.77
Totals	$27,050	$3,450	$23,600	$7.84

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Eight dollars are recovered for every General Fund dollar spent. The Medi-Cal post-payment recovery program expects to generate $7.84 in recoveries for every General Fund dollar of administrative costs. This is an increase of nearly $2, or 40 percent, over the 1983–84 recovery-to-cost ratio. The largest increase in recoveries per administrative dollar spent is expected to result from collections of liens on real property. The lowest recovery to cost ratio in 1984–85 is anticipated from health insurance collections. Table 56 compares post-payment recoveries with administrative costs for each of the three major recovery categories, from 1982–83 through 1984–85.

Total potential recoveries are hard to identify. While growth in total recoveries and positive benefit to cost ratios are good indicators of program performance, these measures do not address the degree to which the recovery program collects *potentially* recoverable Medi-Cal payments. It is extremely difficult to identify total potential recoveries because (1) amounts termed "accounts receivable" by the department generally include large uncollectible amounts that are several years out of date and (2) Medi-Cal payments subject to recovery have not all been identified by the department. The federal Department of Health and Human Services estimates that 3 to 4 percent of Medicaid payments are subject to recovery. If this estimate is accurate, California collects about 25 to 33 percent of the amounts potentially recoverable each year.

1984–85 recoveries are projected to be 1.3 percent of total Medi-Cal expenditures. In the absence of an accurate measure of potential recoveries, a useful measure of the performance of a state's post-payment recovery program is the percentage of total Medi-Cal health services expenditures that are recouped. This measure may be misleading because it is sensitive to (1) increases or decreases in total Medi-Cal expenditures and (2) delays between actual expenditure for service and recovery of amounts owed the state.

The budget projects that this recoupment rate will be 1.3 percent in 1984–85, which is slightly higher than that experienced over the last several years. Table 57 displays post payment recoveries as a percentage of Medi-Cal health care services expenditures during the period 1979–80 through 1984–85.

Table 57
Post-Payment Medi-Cal Recoveries as a Percent of Medi-Cal Health Care Services Expenditures 1979–80 through 1984–85 All Funds (in millions)

	Post-Payment Recoveries	*Medi-Cal Health Care Services Expenditures*	*Recoupment Rate (percent)*
1979–80	$21.6	$3,172	0.7%
1980–81	21.6	3,294	0.7
1981–82	26.8	4,460	0.6
1982–83	44.7	4,598	1.0
1983–84 (estimated)	40.8	3,984	1.0
1984–85 (proposed)	54.1	4,019	1.3

California's recoupment rate is third among largest states. California recouped 0.4 percent of federal expenditures in the state during federal fiscal year 1982 (FFY 82). This performance was third among the 10 largest

states, behind New York and Michigan, and exceeded the average recoupment rate for these 10 states. Table 58 compares the federal recoupment rates for the 10 largest states during FFY 82.

Table 58

Federal Fund Recoupment Rates
10 Largest States
Federal Fiscal Year 1982[a]

New York	.9%
Michigan	.8
California	.4
Illinois	.2
Massachusetts	.1
New Jersey	.1
Ohio	.1
Wisconsin	.1
Pennsylvania	.09
Texas	.01
Average for 10 largest states	.3

[a] Source: Department of Health and Human Services.

Recovery Program Changes Have Not Produced Intended Results

Assembly Bill 251 (Ch 102/81) and AB 799 (Ch 328/82), as amended by SB 2012 (Ch 1594/82), established nine new programs to recover Medi-Cal expenditures from liable third parties. At the time these programs were under consideration by the Legislature, the department estimated that recoveries from the program would total $69.2 million in 1983–84. Current estimates of 1983–84 recoveries as a result of these measures, however, are 89 percent less than the department's initial estimates. Seven of the nine new programs are expected to generate fewer collections than anticipated. Legislative changes and court-ordered implementation delays to the SB 2012 provisions regarding real property account for over one-half of the reduction in anticipated recoveries.

Table 59 compares recoveries initially anticipated in 1983–84 with revised 1983–84 recoveries estimates and identifies the reasons for changes from the initial estimate.

Health Insurance Recoveries—Direct County Input

We recommend a reduction of $2,300,000 ($1,220,000 General Fund) in Medi-Cal health expenditures to reflect full-year savings from county participation in health insurance data collection.

Assembly Bill 251 required county welfare offices to collect detailed health insurance data from Medi-Cal applicants. The department estimated that recoveries due to this program would increase from $2,700,000 ($1,430,000 General Fund) in 1982–83 to $5,000,000 ($2,650,000 General Fund) in 1983–84. The department advises that actual recoveries are one year behind original estimates, due to state and county implementation delays. Although the department advises that this program will be in effect throughout 1984–85, the budget does not reflect full-year recoveries of $5,000,000. Accordingly, we recommend a reduction of $2,300,000 ($1,220,000 General Fund) to reflect full-year savings from county participation in health insurance data collections.

DEPARTMENT OF HEALTH SERVICES—Continued

Table 59

Summary of Recovery Legislation
Original and Revised 1983–84 Estimates
All Funds
(in millions)

	Original 1983–84 Estimate[a]	*Revised 1983–84 Estimate*[b]	*Percent Change*	*Proposed 1984–85*[b]	*Reason for Change*
Assembly Bill 251 (Ch 102/81)					
Health insurance recoveries—direct county input	$7.5	$2.7	−64%	$2.7	Implementation delay
Health insurance recoveries—child support	0.8	0.2	−75	0.2	Counties not participating
Estates recoveries	5.4	3.0	−44	3.0	Reduced staff levels
Workers' compensation recoveries	1.5	1.7	13	1.7	Higher collections per case
Beneficiary overpayment—county contracts	2.2	—	−100	—	Counties not participating
Privately contracted recoveries	12.0[c]	0.1	−99	0.1	Information delays
Earnings clearance system	1.3	—	−100	—	Not implemented
Subtotals	$30.7	$7.7	−75%	$7.7	
Assembly Bill 799 (Ch 328/82					
Private insurance match	no estimate	no estimate	—	—	Pilot underway
Senate Bill 2012 (Ch 1594/82)					
Other real property	$38.5	$0.0	−100%	$13.3	Legislative changes (Ch 323/83) and court delays
Totals	$69.2	$7.7	−89%	$21.0	

[a] Original estimates from 1982–83 budget change proposals.
[b] Department of Health Services estimates, December 1983. The 1984–85 figures for AB 251 are based on continuation of estimated 1983–84 savings and may not reflect the actual savings due to these provisions.
[c] Amount included in AB 251 intent language.

Health Insurance Recoveries—Child Support Referrals

We recommend augmentations of (1) $50,000 ($25,000 General Fund) for department support and (2) $150,000 ($75,000 General Fund) to county administration so that the department and counties can process additional child support referrals. We further recommend a reduction of $1,200,000 ($600,000 General Fund) to reflect anticipated 1984–85 Medi-Cal savings associated with these augmentations.

Assembly Bill 251 authorizes the department to recover Medi-Cal payments made on behalf of children that are identified by district attorneys during child support enforcement proceedings as having health insurance coverage. Because only 18 out of 58 counties are participating in this recovery program, recoveries due to increased identification of health insurance coverage in 1983–84 are 75 percent less than initially estimated.

County staff advise that counties are not processing health insurance forms as required by AB 251 because no funds have been made available to cover their administrative costs. In addition, because counties have no share in Medi-Cal recoveries, there is no financial incentive for them to participate in this program.

If all counties complied with AB 251, the department estimates annual county costs would be $150,000 ($75,000 General Fund) and state costs would be $100,000 ($50,000 General Fund) for training county staff and printing forms. Assuming 18 participating counties, the 1984–85 budget proposes approximately $50,000 ($25,000 General Fund) for state processing. The budget, however, does not include any funds to cover county costs.

The department indicates that full funding of state and county processing costs would allow full county implementation by January 1, 1985. The department estimates that full county implementation would yield annual cost-avoidance savings of $2.4 million ($1.2 million General Fund). Based on a three-month delay for county training and an additional three-month payment lag, we estimate full implementation will result in 1984–85 savings of $1.2 million ($600,000 General Fund).

The department estimates full-year recovery and cost-avoidance savings of $4,750,000 ($2,375,000 General Fund) starting in 1985–86. Therefore, each additional General Fund dollar spent would save the General Fund $19 in Medi-Cal health care expenditures. In order to achieve this anticipated savings, we recommend augmentations of (1) $50,000 ($25,000 General Fund) to the department's support budget and (2) $150,000 ($75,000 General Fund) to the county administration budget. We further recommend a reduction of $1,200,000 ($600,000 General Fund) from the Medi-Cal benefits item to reflect anticipated 1984–85 savings associated with this augmentation.

Estate Recoveries

Assembly Bill 251 permits the Department of Health Services to file claims against estates of certain deceased Medi-Cal beneficiaries. The department estimated in 1981 that annual probate recoveries would increase by $5.4 million ($2.7 million General Fund) by 1984–85 if 10 new positions were approved. The Legislature approved six positions in 1982–83 to process these claims. In 1983–84, the Recovery Branch directed two additional staff from other areas to meet the increasing workload in this area. It is unclear whether additional staff will result in increased estate recoveries.

Workers' Compensation Recoveries

Assembly Bill 251 required the Workers' Compensation Appeals Board to provide data to the department that it can use to recover payments made by Medi-Cal on behalf of persons covered by workers' compensation carriers. In 1984–85, recoveries are expected to exceed $1.7 million ($850,000 General Fund), surpassing the annual goal of $1.5 million ($750,000 General Fund) due to a higher-than-expected average collection per case.

DEPARTMENT OF HEALTH SERVICES—Continued

Beneficiary Overpayment Recoveries—County Contracts

Assembly Bill 251 permits the department to contract with counties to recover the cost of any Medi-Cal benefits improperly received by beneficiaries. Currently, no counties are participating in this program. Department data indicate that beneficiary overpayment collections produce smaller savings than many other recovery activities. Counties advise that a 10 percent incentive fee in addition to county administrative costs is not adequate to enlist their participation. It is possible that an increase in the incentive amounts may encourage some county participation. State staff initially authorized for this activity have been redirected to other recovery activities.

Privately Contracted Recoveries

We recommend that the Legislature adopt supplemental report language directing the Department of Health Services to (1) extend for one year the pilot project contract with Lien Services of Northern California and (2) report to the Legislature by March 1, 1985, on the results of this project.

Assembly Bill 251 authorized the department to contract for up to three years with collection agencies in Northern and Southern California for recovery of amounts owed by third parties for Medi-Cal health services. The Legislature stated its intent that the department recover $12 million ($6 million General Fund) annually as a result of the private contracts. The department, however, initially estimated that it could recover approximately $1 million ($545,000 General Fund), less a 20 percent commission, in the 12 months following establishment of a contract.

The department awarded a two-year contract to Lien Services of Northern California (LSNC) to recover amounts owed by third parties, for the period July 1982 to June 1984. Under the terms of this contract, the contractor receives payment based on the actual amounts collected. The department reduced its estimate of annual recovery estimates from this activity to $100,000, due primarily to delays in data retrieval from the payment records of the Medi-Cal fiscal intermediaries.

The department currently is implementing a program to reduce delays in obtaining access to payment records by the contractor. In December 1983, the contractor received much of the claims payment information necessary to determine recovery amounts. Actual collections, however, will not be received until 1984–85.

Our analysis indicates there has not been adequate time to evaluate this project due to delays in actual start-up. AB 251 authorizes the department to continue this project for up to three years. Therefore, we recommend that the Legislature adopt supplemental report language directing the department to extend for one year the pilot project contract with Lien Services of Northern California. In order for the Legislature to have an opportunity to review the results of this project, as part of its review of the 1985 Budget Bill, we further recommend that it adopt supplemental report language to direct the department to report to the Legislature by March 1, 1985, on the results of the pilot project. The recommended language is as follows:

"The Department of Health Services shall (1) extend for one year the pilot project contract with Lien Services of Northern California, and (2)

report to the Legislature by March 1, 1985, on the results of this project. This report shall address at least the following items (1) amount recovered to date, (2) value of outstanding liens, (3) payments to the contractor, and (4) explanations of any delays in project operations for the period January 1984 to December 1984."

Earnings Clearance System

We recommend that the department submit to the Legislature by April 1, 1984, its plans for implementing the earnings clearance system required by AB 251 and information on the costs and potential recoveries of such a system.

Assembly Bill 251 required the department to develop a system to match income information reported by Medi-Cal beneficiaries and applicants with data reported to the Employment Development Department (EDD) by employers who pay unemployment and disability insurance taxes. In 1982, the department estimated that this system could increase recoveries of Medi-Cal costs by approximately $3.2 million ($1.6 million General Fund) through increased identification of beneficiaries with health insurance. As of January 1984, the department had indicated that the proposal is still under study and has no new estimates of anticipated recoveries.

The department has not indicated whether and when it intends to implement this program. We recommend that the department submit to the Legislature by April 1, 1984, its plans for implementing the earnings clearance system required in AB 251 and information on the costs and potential recoveries from this system.

Information From Insurance Companies

We recommend that the Legislature adopt supplemental report language directing the Department of Health Services to report by January 1, 1985, on (1) estimated costs and expenditure reductions resulting from pilot contracts with insurance companies and (2) projected costs and recoveries that would result from expanding the program to other high-volume carriers.

Assembly Bill 799 requires the department to contract with insurance companies to provide information on health insurance coverage of Medi-Cal applicants. The measure allows reimbursement to these companies at the same rates insurance companies pay the Department of Motor Vehicles for information. The measure also required the department to implement the information exchange with insurance companies and report to the Legislature by January 1, 1983. The report, which was submitted in July 1983, estimated one-time pilot program costs of up to $401,000 ($100,000 General Fund) beginning in October 1983 and up to $7,250,000 ($3,625,000 General Fund) in cost avoidance and recoveries.

The department advises that the initial match with three insurance carriers will be completed early in 1984, and that revised estimates of recoveries and cost avoidance will be available in September 1984.

The implementation and expansion of this system may result in significant health care savings to the state. Therefore, we recommend that the Legislature adopt supplemental report language directing the department to report by January 1, 1985, on (1) estimated costs and expenditure reductions resulting from pilot contracts with insurance companies, and (2) projected costs and recoveries that would result from expanding the program to other high-volume carriers.

DEPARTMENT OF HEALTH SERVICES—Continued

Our recommended language is as follows:

"The Department of Health Services shall report to the Legislature by January 1, 1985, on (1) the estimated costs, recoveries, and cost avoidance resulting from the pilot program contracts with insurance companies and (2) projected costs, recoveries, and cost avoidance from expansion of the program to other high volume carriers."

Real Property

We recommend that during budget hearings the department advise the Legislature on how it will staff increased recovery program workload due to the implementation of liens on real property.

Asembly Bill 799, as amended by SB 2012, (1) reduced from $25,000 to $6,000 the equity a Medi-Cal beneficiary may have in real property and (2) allowed persons whose homes are not exempt from being considered real property (primarily nursing home residents) to continue receiving Medi-Cal benefits prior to selling the home only if the home is listed for sale and a lien is placed against the property for the cost of benefits.

Annual post-payment recoveries from this lien requirement initially were estimated at $38 million ($19 million General Fund). Due primarily to court-ordered delays, the department currently estimates that no recoveries will be received in 1983–84. It estimates that recoveries from liens on real property will generate $13.3 million ($6.6 million General Fund) in 1984–85. The reduction in anticipated annual savings is due to (1) exemptions from the lien provisions granted by Ch 323/83 (AB 223, the companion bill to the 1983 Budget Act) and (2) reduced estimates of the number of persons owning real property. The department estimates the General Fund cost of the one-year court delay in implementation of this provision is $16.7 million.

The department advises that increased recovery workload due to additional lien collections on real property will require three to nine positions in 1984–85 and three to six positions thereafter. The budget, however, does not propose staff to handle the expected increase in workload. We are unable to determine how the department intends to implement this significant new recovery program. If staff are not available to collect and process lien recoveries, state savings will be reduced. Therefore, we recommend that the department report during budget hearings on (1) how the recovery program will handle increased workload associated with real property lien collection and (2) the additional resources, if any, the department plans to redirect to the activity in 1984–85.

Federal Funding and Technical Issues

The federal share of post-payment recoveries and administrative costs may vary from year to year. The federal share of *administrative costs* for qualified components of California's Medi-Cal recovery program ranges from 50 percent for workers' compensation activities to 75 percent for some health insurance activities that are certified by the federal government as part of the state's Medicaid Management Information System (MMIS). Federally supported administrative costs have increased as new recovery programs qualify for higher levels of federal funding.

The federal share of *recoveries* is 50 percent for federally eligible cases. The federal government does not receive any portion of recoveries from cases on which no federal health care services payments were made. The

federal share of recoveries has increased over the last three years due to (1) a decrease in 100 percent General Fund recoveries, reflecting the elimination of the medically indigent adult category and (2) a large dollar increase in recoveries in categories with a 50 percent state and federal split.

Budget Underestimates State Share of Recoveries

We recommend a General Fund reduction of $2 million from the amount proposed for health care expenditures and a corresponding increase in federal funds in order to more accurately budget savings from the recovery program.

The department estimates that the state's share of post-payment recoveries will drop from 55 percent in 1982–83 to 50 percent of total recoveries in 1983–84 and 1984–85. Our analysis indicates, however, that (1) the state share of recoveries in 1982–83 was 72 percent, not 55 percent, and will be 61 percent in 1983–84, not 50 percent, and (2) the state share of recoveries in 1984–85 will be 54 percent based on (a) a 50 percent state share for new recoveries due to real property liens, consistent with the department's estimate, and (b) a 55 percent state share for other recoveries.

Analyst's Estimate of State Share of 1982–83 and 1983–84 Recoveries. For the past three years, the department has underestimated the state share of recoveries in preparing its budget estimates because it has not utilized actual accounting data in preparing the estimates. While the margin of this underestimation is lower in 1983–84, even a 1 percent error could understate General Fund savings by $540,000. Table 60 compares the proposed state share of recoveries with actual state recoveries during the last three years. The table also shows our estimates of the state share of recoveries.

Table 60
General Fund Share of Recoveries
1981–82 through 1983–84
(in millions)

	Budget Proposal		Actual and Analyst's Estimate		
	Amount	*Percent*	*Amount*	*Percent*	*Difference*
1981–82	$16.2	61.7%	$16.8[a]	63.8%	$0.6
1982–83	17.8	55.4	32.0[a]	71.6	14.2
1983–84 (estimated)	20.4	50.0	24.8[b]	60.7	4.4
1984–85 (proposed)	27.1	50.0	29.1[c]	53.8	2.0
New recoveries due to real property liens	(6.7)	(50.0)	(6.7)	(50.0)	(—)
Other recoveries	(20.4)	(50.0)	(22.4)	(55.0)	(2.0)

[a] Source: Department of Health Services, Medi-Cal Accounting.
[b] Analyst's estimate, based on first quarter 1983–84.
[c] Analyst's estimate, based on accounting records.

State Share for Other Recoveries in 1984–85. Our analysis indicates that the state recovery sharing ratio for other recoveries will continue to decrease in 1984–85, due primarily to termination of the medically indigent adult (MIA) program. For state and federal sharing of recoveries to be equal, however, there could be *no* recoveries on behalf of non federally eligible cases. This is not likely to happen. Recoveries for payments made on behalf of MIAs will continue to be received in 1984–85, due to delays

DEPARTMENT OF HEALTH SERVICES—Continued

between the time of payment and collection of amounts owed the state. In addition, ongoing recoveries from other state-funded eligibility categories will continue in 1984–85.

Our analysis indicates that recoveries for nonfederally eligible cases may decline by as much as half, but will not disappear entirely. If nonfederal recoveries decline by half, the state's share of the $41 million in other recoveries will decline from 61 percent in 1983–84 to 55 percent in 1984–85. Thus, the state share of other recoveries would be $22.4 million. The state share of *all* recoveries in 1984–85, including increased real property collections, would be $29.1 million, or 54 percent. Therefore, we recommend that recoveries be budgeted at 54 percent General Fund, for a General Fund reduction of $2 million and an increase of the same amount in federal funds.

"Uncleared" Recoveries Not Cleared

We recommend the budget reflect historical Medi-Cal savings from "uncleared recoveries," for a reduction of $1,300,000 ($689,000 General Fund).

The department has consistently underestimated recoveries by not including "uncleared" recoveries in its estimates. Uncleared recovery monies are funds that have been collected but have not been assigned to a specific recovery account. These uncleared recoveries average $1,300,000 annually. Because these funds will be available to offset state and federal Medi-Cal expenditures in 1984–85, we recommend a reduction of $1,300,000 ($689,000 General Fund) in the amount budgeted.

Cost Avoidance

The second major purpose of the recovery program is to avoid costs by requiring health providers to bill other third-party payors before Medi-Cal payments are made. The department estimates that cost-avoidance activities will reduce General Fund costs by $406 million in 1984–85. This amount consists of (1) $364 million from the Medicare Buy-In program, (2) $39 million from health insurance, and (3) $3 million from general collections.

Medicare Part B Buy-In Program

The largest cost-avoidance program is the Medicare Buy-In program. Under this program, the state uses Medi-Cal funds to pay the monthly Medicare Part B insurance premiums for qualified Medi-Cal beneficiaries. The state General Fund benefits because the Medicare program pays a large portion of the costs of Part B services (primarily physician and outpatient clinic services) provided to eligible beneficiaries. The Medi-Cal program pays (1) any deductibles required by Medicare and (2) the difference between Medicare's reimbursement amounts (80 percent of the Medicare-determined rate) and Medi-Cal rates, up to 20 percent of the Medicare-determined rate.

Currently, the Medi-Cal program annually pays the federal government approximately $107 million ($66 million General Fund) in premiums for 560,000 enrolled Medi-Cal beneficiaries. The department estimates that the cost transfer from Medi-Cal to Medicare will be $364 million in 1984–85. Table 61 shows estimated Medicare Part B state and federal expenditures and net savings in 1984–85.

Table 61
Medicare Part B Buy-In Program
Federal and State Expenditures
1984–85
(in millions)

	General Fund	*Federal Funds*	*All Funds*
A. Medi-Cal			
Health care savings	−$528.8	−$528.8	−$1,057.6
Deductible	21.0	21.0	42.0
Medi-Cal payments for Medicare beneficiaries due to differences in payment amounts	77.6	77.6	155.2
Part B premiums	66.0	41.3	107.3
B. Medicare			
Health care costs	—	860.4	860.4
Part B premiums	—	−107.3	−107.3
Subtotals	−$364.2	$364.2	$0.0
C. Administrative costs	.2	.6	.8
Totals	−$364.0	$364.8	$.8

CHAMPUS Savings Not Budgeted

We recommend a reduction of $2,590,000 ($1,329,000 General Fund) in Medi-Cal health care expenditures to reflect savings from a recent match of Medi-Cal eligibility files with records for the CHAMPUS program.

The budget does not include savings from a 1982 computer match of Medi-Cal eligibility files with those of the Civilian Health and Medical Program of Uniformed Services (CHAMPUS). This match identified approximately 22,000 dual beneficiaries. A minimum of 10,000 beneficiaries will still be Medi-Cal eligible in 1984–85. Future health care claims from these dual beneficiaries will be suspended from Medi-Cal claims processing and referred to CHAMPUS for payment.

The department recovers an average of $113 for each beneficiary with other health coverage. Based on 10,000 eligibles, we estimate that 1984–85 recoveries from CHAMPUS for services provided in earlier years will be $1,130,000 ($599,000 General Fund).

Medi-Cal health care expenditures will also be reduced an average of $146 for each identified beneficiary due to CHAMPUS payments for 1984–85 health care services that would otherwise be paid by Medi-Cal. Therefore, we estimate cost avoidance of $1,460,000 ($730,000 General Fund) in 1984–85.

Accordingly, we recommend a reduction of $2,590,000 ($1,329,000 General Fund) to reflect this anticipated expenditure reduction.

DEPARTMENT OF HEALTH SERVICES—CAPITAL OUTLAY

Item 4260-301 from the General Fund, Special Account for Capital Outlay — Budget p. HW 88

Requested 1984–85	$1,735,000
Recommended approval	1,338,000
Recommended reduction	151,000
Recommendation pending	246,000

SUMMARY OF MAJOR ISSUES AND RECOMMENDATIONS

ANALYSIS AND RECOMMENDATIONS

The budget proposes $1,735,000 from the General Fund, Special Account for Capital Outlay, for capital outlay projects to be undertaken by the Department of Health Services in 1984–85. The funds will be used for the fourth and fifth phases of the six phase autoclave replacement program, and for various minor projects at Department of Health Services facilities around the state.

Transfer to General Fund

We recommend that the savings resulting from our recommendations on Item 4260-301-036 —$151,000—be transferred from the Special Account for Capital Outlay to the General Fund in order to increase the Legislature's flexibility in meeting high-priority needs statewide.

We recommend reductions amounting to $151,000 in the Department of Health Services capital outlay proposal from tideland oil funds. Approval of these reductions, which are discussed individually below, would leave an unappropriated balance of tidelands oil revenues in the Special Account for Capital Outlay which would be available only to finance programs and projects of a specific nature.

Leaving unappropriated funds in special purpose accounts limits the Legislature's options in allocating funds to meet high-priority needs. So that the Legislature may have additional flexibility in meeting these needs, we recommend that any savings resulting from approval of our recommendations be transferred to the General Fund.

Minor Capital Outlay

We recommend deletion of three projects for a savings of $151,000. Further, we withhold recommendation on two projects ($246,000).

The budget proposes $1,026,000 under Item 4260-301-036(1) for 24 minor capital outlay projects. They include (1) four projects at the Acton Street Laboratory in Berkeley, (2) 16 projects at the Berkeley Way Laboratory, (3) two projects at the Fairfield Animal Facility and (4) two projects at the Los Angeles laboratory. The projects range in cost from $14,000 to $149,000 and provide renovation of various laboratories and services, fire/life safety improvements and installation of alarm systems. We recommend approval except as discussed below.

Fire Sprinklers—Acton Street. The budget includes $100,000 to install fire sprinklers and make other safety modifications at the Acton Street Lab. This project initially was funded by the Legislature for $85,000 in 1981. The Department of Finance indicates that bids received for this project were higher than anticipated and that the appropriated funds are no longer available. Thus, the department is seeking a new appropriation for this project.

The department, however, has provided no information to the Legislature describing either why the amount appropriated in 1981 was not sufficient, or the difference between the amount appropriated and the lowest bid received on the project. Furthermore, it is our understanding that this project was put out to bid only recently. The department should explain why the project was delayed for over two years and provide documentation that the 1981 appropriation is no longer available. The State Controller does not yet show this appropriation as having reverted.

Accordingly, we withhold recommendation on this project, pending receipt of clarifying information on these issues from the department.

Emergency Electrical Generators. One minor project under Item 4260-301-036(1) provides for the installation of an emergency electrical generator. Specifically, the budget proposes $93,000 to install a 200 kw diesel-powered generator at the Fairfield Animal Facility. According to the department, the existing emergency generator requires extensive maintenance and is inadequate to meet the baseline electrical needs of the facility which is 78 kw. The electrical generator the department proposes to install, however, is 122 kw, or 156 percent, more than the total electrical requirements of the lab. The department has not explained why the existing generator capacity is insufficient or why excess electrical capacity is needed. If the existing generators need to be repaired or replaced with generators of equal size, then this is a maintenance problem and the department should undertake the work in priority with other maintenance needs from funds in the support/operations budget. Consequently, we recommend that the $93,000 included for this item be deleted.

Fire Alarm System. A total of $17,000 is included to install a fire alarm system at the Fairfield Animal Facility. In a letter from the State Fire Marshal to the Department of Health Services, dated March 28, 1980, the Fire Marshal provided a list of 11 separate modifications that the department was *required* to make at the Fairfield Lab in order to achieve compliance with existing fire safety regulations. The department has completed the majority of the required modifications. The fire alarm system proposed by the department was listed by the Fire Marshal as a non-regulation recommendation and not required by fire safety regulations. In view of the remote location of this facility, we believe the benefit of installing a fire alarm system would be marginal at best. For this reason,

DEPARTMENT OF HEALTH SERVICES—CAPITAL OUTLAY—Continued

and given that the fire alarm system is not required by either the State Fire Marshal or by existing fire safety regulations, we recommend that the $17,000 included for this item be deleted.

Compressed Air Vacuum System. The budget proposes $41,000 to install a new Compressed Air/Vacuum System in the boiler room at the Berkeley Lab. The department contends that installation of this new system will result in a more energy-efficient operation. The department, however, has identified no cost-savings to be realized by the project, and on this basis we recommend that the funds be deleted.

Fire and Life Safety Modifications—Los Angeles Lab Facility. The budget includes $146,000 to correct fire and life safety deficiencies in the Los Angeles laboratory facility. The department identifies this as the first of two phases to bring the building into compliance with the California Administrative Code. The first phase of the work includes electrical modifications and installation of a fire alarm and fire sprinkler system. The second phase would include modifications to improve handicapped accessibility and fire/life safety modifications to the exterior stairway and interior corridors. The department estimates that the work on first and second phases will cost $146,000 and $81,000, respectively. This estimate, however, was prepared in June 1982, and has not been adjusted to reflect 1984–85 price levels.

This project was included in the department's 1983–84 minor capital outlay request. In our analysis of the project (see 1983–84 *Analysis,* p. 912), we indicated that with a combined cost in excess of $230,000, this project was a major capital outlay project, and should not be budgeted within the minor category. This remains the case. Further, the department still has not provided any information to explain why this project is divided into two phases. Generally, savings can be achieved by including related work in a single project.

Prior to hearings on the Budget Bill, the department should provide updated cost information which compares the cost of proceeding with this project under two phases with the cost of funding the entire project in one year. Pending receipt of this information from the department, we withhold recommendation on this project.

Autoclave Replacement—Phases IV and V

We recommend approval of Item 4260-301-036(2) to replace autoclaves.

The budget proposes an appropriation of $709,000 under Item 4260-301-036(2) for Phase IV and Phase V of a six-phase project to replace autoclaves (steam sterilizers). The autoclaves are used to sterilize (1) equipment and reagents which are used in tests to determine the presence of infectious disease, and (2) material used in the testing process prior to disposal of the material.

A total of $710,000 has been appropriated by the Legislature in the past to replace 11 autoclaves. Funds were included in last year's budget for Phase IV, but were deferred by the Department of Finance. The department is requesting funding for Phase IV and V in the 1984–85 budget in order to put the project back on its original schedule.

The department proposes to replace four autoclaves under Phase IV and three autoclaves under Phase V. The present equipment is nineteen years old and is becoming unserviceable because replacement parts are difficult to obtain. Our analysis indicates that the proposed project is

necessary to ensure continued operation of the laboratories and accordingly, we recommend that it be approved.

Supplemental Report Language

For purposes of project definition and control, we recommend that supplemental report language be adopted by the fiscal subcommittees which describes the scope of each of the capital outlay projects approved under this item.

Projects by Descriptive Category

To aid the Legislature in establishing and funding its priorities, we have divided those capital outlay projects which our analysis indicates warrant funding into the following seven descriptive categories:

1. Reduce the state's legal liability—includes projects to correct life threatening security/code deficiencies and to meet contractual obligations.
2. Maintain the current level of service—includes projects which if not undertaken will lead to reductions in revenue and/or services.
3. Improve state programs by eliminating program deficiencies.
4. Increase the level of service provided by state programs.
5. Increase the cost efficiency of state operations—includes energy conservation projects and projects to replace lease space which have a payback period of less than five years.
6. Increase the cost efficiency of state operations—includes energy conservation projects and projects to replace lease space which have a payback period of greater than five years.
7. Other projects—include noncritical but desirable projects which fit none of the other categories, such as projects to improve buildings to meet current code requirements (other than those addressing life-threatening conditions), utility/site development improvements and general improvement of physical facilities.

Individual projects have been assigned to categories based on the intent and scope of each project. These assignments do not reflect the priority that individual projects should be given by the Legislature. Phases IV and V of the autoclave project fall under category two and the 19 minor projects fall under category seven.

DEPARTMENT OF HEALTH SERVICES—REAPPROPRIATION

Item 4260-490 from the General Fund and various other funds Budget p. HW 37

ANALYSIS AND RECOMMENDATIONS

We recommend that the Legislature reject the proposed reappropriation of unexpended state funds for Superfund remedial action contracts because reappropriating these funds would reduce legislative control of these expenditures. We recommend that the Legislature amend the proposed Budget Bill language authorizing the reappropriation of monies from the federal Superfund and responsible parties to clarify that only funds actually received in the current year are reappropriated.

The 1984 Budget Bill proposes to reappropriate the unexpended funds from the following appropriations for Superfund remedial action contracts in the 1983 Budget Act: (1) $6,422,465 in state funds from the Hazardous Substances Account (HSA), (2) $16,900,000 in receipts from the federal Superfund program, and (3) $21,200,000 in reimbursements from responsible parties. The reappropriated funds would be available for encumbrance until June 30, 1986. The department was unable to provide an estimate of the amounts from these appropriations that will be unexpended as of June 30, 1984.

State Funds. Our analysis indicates that reappropriation of state funds for cleanup projects is inappropriate because it eliminates the Legislature's review of specific expenditures supported by the reappropriation. Reappropriations are normally used to fund completion of specific projects when the project is delayed for some reason. In these circumstances, the Legislature does not need to review the expenditures during the latter years because the need for and costs of the project are well-established. In contrast, the state remedial action funds proposed for reappropriation in the budget are for a group of sites. The costs of each site cleanup and even the list of sites proposed for funding are subject to significant changes after the initial appropriation.

Consequently, we recommend that the Legislature reject the proposed reappropriation of state funds. We recommend instead that the department provide an estimate of the available unencumbered state funds and a proposal for expenditure of those funds in the budget year so that the Legislature can directly appropriate them in the 1984 Budget Bill. We discuss this issue in more detail in our discussion of the Superfund program that appears earlier in this analysis.

Federal and Responsible Party Funds. We recommend approval of the proposed reappropriation of federal and responsible party monies. We recommend, however, that the Legislature amend the proposed Budget Bill language to clarify that only funds that have actually been received from these sources are reappropriated. The proposed language allows for the total expenditure authority up to $38.1 million to be available regardless of the actual amounts received by the state. Additional legislative review of expenditures from these nonstate sources would not be productive because these monies can only be spent for the site and the purposes for which the monies were received from the federal government or responsible parties.

DEPARTMENT OF HEALTH SERVICES—REVERSION

Item 4260-495 to the General Fund Budget p. HW 37

ANALYSIS AND RECOMMENDATIONS

We recommend approval of eight reversions. We withhold recommendation on the proposed reversion of $150,000 for a study of the effect of ethylene-dibromide (EDB) on reproductive systems, pending a report from the department on whether it intends to perform the study.

The budget proposes reversion of the unencumbered balances of nine appropriations to the Department of Health Services. The funds would revert to the unappropriated surplus of the General Fund. The appropriations and our recommendations are set forth below:

1. Chapter 215, Statutes of 1977, appropriated $371,000 for a genetic counseling pilot program. Funding for this activity is now provided in the budget. As of December 31, 1983, a balance of $91,000 remained unexpended. We recommend approval of the proposed reversion.

2. Chapter 1134, Statutes of 1979, appropriated $2.1 million for a dental disease prevention program for children. Ongoing funding for this program has been included in subsequent Budget Acts. The 1984–85 budget proposes to include this program in the Public Health Enhancement program. As of December 31, 1983, a balance of $45,000 remained unexpended. We recommend approval of the proposed reversion.

3. Chapter 533, Statutes of 1980, provided a loan from the General Fund to the Genetic Disease Testing Fund to fund start-up costs of the newborn screening program. Adequate revenue is now being generated to support the program and repay the General Fund loan. The loan authority therefore is no longer needed and we recommend approval of the proposed reversion. As of December 31, 1983, $2,489,000 remained unexpended.

4. Chapter 911, Statutes of 1980, appropriated $500,000 to establish adult day health centers. Subsequent acts have appropriated additional funding. As of December 31, 1983, $7,000 remained unexpended from the original appropriation. We recommend approval of the proposed reversion.

5. Chapter 1161, Statutes of 1980, established a program to identify hazardous waste property and border zone property and to impose land use restrictions based on the contamination of the property. The act appropriated $105,000 from the General Fund to implement these provisions. Those funds have been expended and funding for this activity is provided in the budget from the Hazardous Waste Control Account. We therefore recommend approval of the proposed reversion.

6. Chapter 756, Statutes of 1981, established the state Superfund program to clean up uncontrolled hazardous waste sites. The act authorized a $2 million loan from the General Fund to the Hazardous Substances Account for program start-up costs. The loan was repaid in 1982–83 and is no longer needed. We therefore recommend approval of the proposed reversion.

7. Chapter 204, Statutes of 1982, appropriated $875,000 to establish a birth defects monitoring program ($450,000) and to conduct studies on the effect of (a) malathion on pregnant women ($275,000) and (b) ethylene-dibromide (EDB) on reproductive systems ($150,000). As of December 31, 1983, $307,000 remained unexpended, including $157,000 for the monitoring program and the malathion study and the entire $150,000 for the EDB study.

DEPARTMENT OF HEALTH SERVICES—REVERSION—Continued

The ongoing monitoring activities are now supported in the budget, and the department expects to encumber all of the funds for the malathion study in the current year. Consequently, we recommend approval of the proposed reversion of funds associated with these portions of the appropriation.

The department has not, however, implemented the EDB study and was unable to tell us if any of the $150,000 for the study would be encumbered by June 30, 1984, when the reversion would take effect.

We withhold recommendation on the proposed reversion of $150,000 for the EDB study and recommend that the department report at budget hearings on whether it intends to perform the study and its reasons for proposing to revert the funds.

8. Chapter 478, Statutes of 1982, appropriated $250,000 to establish adult day health centers. Those funds have been fully expended and we recommend approval of the proposed reversion.

9. Chapter 1461, Statutes of 1982, provided for the establishment of two Drug Utilization and Peer Review Committees to review standards of health practice under the Medi-Cal program. The act appropriated $14,000 for a two-year pilot program terminating January 1, 1985. As of December 31, 1983, the full amount of $14,000 remained unexpended. The Department of Finance advises that this program will be implemented and that the appropriation will be expended during 1983–84. We recommend approval of the proposed reversion.

Health and Welfare Agency

CALIFORNIA MEDICAL ASSISTANCE COMMISSION

Item 4270 from the General Fund — Budget p. HW 89

Requested 1984–85	$889,000
Estimated 1983–84	850,000
Actual 1982–83	505,000 [a]
Requested increase (excluding amount for salary increases) $39,000 (+4.6 percent)	
Total recommended reduction	34,000

[a] Includes Governor's Office of Special Health Care Negotiations.

SUMMARY OF MAJOR ISSUES AND RECOMMENDATIONS

$111,000 reduction withdrawn