MAJOR ISSUES

General Government

✔ Year 2000 Computer Problem Poses Challenge to State

- State government has embarked on a major effort to ensure its computer systems accommodate the year 2000 (Y2K) change. The Department of Information Technology (DOIT) estimates that it will cost the state at least $240 million over several years to address the problem, but we believe that this estimate is understated.
- We have identified a number of issues with the state's Y2K efforts, including optimistic time lines, lack of contingency planning, and insufficient oversight resources.
- We recommend that the Legislature require departments to report at budget hearings on the status of their Y2K efforts, delay funding for new projects in departments which have not completed Y2K modifications, approve DOIT's budget to provide additional resources for oversight and assistance to departments, and establish a reserve fund for yet-to-be identified Y2K efforts by departments (see page G-11 to G-21).

✔ Implementation of Enhanced Smog Check Program Is Problematic

- The Department of Consumer Affairs is unclear on how it plans to implement various aspects of the Smog Check program.
- We recommend the Legislature not approve funding for these programs until the Department of Consumer Affairs reports to the Legislature on how these programs will be implemented (see page G-23).

✔ Health and Welfare Agency Data Center Should Identify Tools it Needs

- In 1995, the administration transferred three of the nation's largest information technology projects to the Health and Welfare Agency Data Center (HWDC)—projects to automate welfare, child support, and child welfare services. The projects were all experiencing difficulty at the time. Since then one project has been cancelled after the state spent $100 million, and others have had significant cost increases and delays.
- Currently, the data center is responsible for a total of ten projects, with total costs exceeding $1.2 billion.
- The additional responsibility given to HWDC occurred without any review of whether it had the appropriate tools for developing and deploying information technology projects of this magnitude.
- Given the major tasks it faces in managing these projects, we recommend that HWDC report to the Legislature during budget hearings on its suggested strategies for developing the additional tools and resources it needs to successfully deploy the projects (see page G-76 to G-93).

✔ Trade and Commerce Agency Augmentations for Economic Development

- The Trade and Commerce Agency has requested a $7.8 million augmentation for a series of activities for economic development.
- The agency's budget has increase by over 150 percent since it was created in 1992 even though when it was created the expectation was that there would be economies and overall savings in the operations of this agency.
- We recommend that the agency reevaluate the need for these increases by setting priorities within existing resources and identify the specific expected outcomes from spending any additional funds (see page G-120).

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OVERVIEW

General Government

Funding for general government is proposed to decrease in the budget year. The General Fund portion of the budget is proposed to decrease substantially, while the special fund portion is proposed to increase slightly. The decrease in support from the General Fund is primarily a result of the large ($1.2 billion) one-time payment made to the Public Employees' Retirement System fund in the current year.

The General Government section of the budget contains a variety of programs and departments with a wide range of responsibilities and functions. These programs and departments provide financial assistance to local governments, protect consumers, promote business development, provide services to state agencies, ensure fair employment practices, and collect revenue to fund state operations. The *1998-99 Governor's Budget* proposes $10.2 billion to fund these functions, not including federal funds. The proposed budget year funding is $414 million less than estimated 1997-98 expenditures.

SPENDING BY MAJOR PROGRAM

There are seven major program areas within general government:

- Shared revenues—state-collected revenues distributed to local governments.
- Tax relief.
- Local government financing.
- Regulatory programs.
- Tax collection programs.
- State administrative functions.
- State retirement and employment.

We describe these program areas below and Figure 1 shows the estimated 1997-98 and proposed 1998-99 budget expenditures by program area.

Figure 1

General Government Spending By Program Area

1997-98 and 1998-99 (In Millions)

Agency/Program	1997-98	1998-99	Difference
Shared revenue	$3,598.7	$3,749.1	$150.4
Tax relief	461.3	465.4	4.1
Local government financing	165.9	112.7	-53.2
Regulatory programs	1,088.3	1,289.4	201.1
Tax collections programs	562.2	573.3	11.1
State administration programs	993.3	967.3	-26.0
Retirement and employment	3,703.0	3,001.6	-701.4
Totals	**$10,572.7**	**$10,158.8**	**-$413.9**

Shared Revenues

The largest general government program is the shared revenues program, which distributes state-collected revenue (primarily from vehicle license fees and gas taxes) to local government agencies. The budget includes $3.8 billion for shared revenues, an increase of $150 million, or 4.2 percent, above the current-year amount. The increase in spending primarily results from an increase in the Motor Vehicle License Fund apportionments to local governments as a result of growth in the fee revenues collected.

Tax Relief

The state provides local property tax relief, both as subventions to local governments and as direct payments to eligible taxpayers, through seven different programs. The two largest are the Homeowners' Property Tax Relief (homeowners' exemption) and the Renters' Tax Relief (renters' credit) programs. The Governor's budget proposes an expenditure of $395 million on the homeowners' exemption program in 1998-99, which comprises most of the $465 million budgeted for tax relief.

The renters' credit provides a refundable tax credit to Californians who rent their principal place of residence. The renters' credit program was suspended from 1993 through 1997 as one of many spending reductions enacted to address the state's budgetary problems. The Governor's budget proposes eliminating this program in 1998. The estimated cost of this program in 1998-99, if it were not altered or discontinued, would be approximately $540 million.

Local Government Financing

The Governor's budget proposes to subvene $112 million (General Fund) to cities and counties. Almost all of this amount ($100 million) would go for continuation of the Citizen's Option for Public Safety (COPs) program created in 1996-97. This program provides $75 million to cities and counties for police and sheriffs' patrol services and $25 million to counties for prosecution and jail services.

Regulatory Activities

A total of 20 agencies are responsible for providing regulatory oversight of various consumer and business issues. Most of these departments are funded from special funds that receive revenue from those subject to regulation. Included in this total are the Departments of Consumer Affairs, Industrial Relations, Food and Agriculture, Financial Institutions and Corporations, and the Public Utilities Commission.

Total proposed expenditures for all regulatory activities in the budget year are $1.3 billion. This includes approximately $1 billion from various special funds and $247 million from the General Fund. Total expenditures in this category are $201 million, or 19 percent, more than the estimated current-year expenditures. The four largest agencies in terms of overall proposed budget expenditures are the Department of Consumer Affairs, $331 million ($1.7 million General Fund); the Energy Commission, $226 million (all special funds); the Department of Industrial Relations, $190 million ($147 million General Fund); and the Department of Food and Agriculture, $181 million ($67.1 million General Fund).

These regulatory agencies protect the consumer and promote business development while regulating various aspects of licensee, business, and employment practices. The groups regulated range from individual licensees to large corporations.

Tax Collection Programs

Expenditures. The Franchise Tax Board and the Board of Equalization are the largest revenue collection agencies in the state. Together, both boards collect the state's personal and business income taxes, sales tax, and special use taxes. The budget proposes $573 million for these tax programs in 1998-99. This is an increase of $11 million from estimated current-year expenditures.

Revenues. The estimated combined General Fund collections by both boards is projected to be almost $55 billion in 1998-99. This is an increase of nearly $3 billion over estimated current-year revenues. Slightly more than half of all General Fund revenues ($28 billion) comes from personal income taxes.

State Administrative Functions

There are more than 30 departments and agencies that provide a wide range of administrative services. These services range from oversight and support of other departments (such as the Department of General Services, the Department of Information Technology, and the Office of Administrative Law), to economic development (such as the Trade and Commerce Agency), to various specialized services provided to individuals and communities (such as the Office of Emergency Services (OES), the Military Department, and the Department of Veterans Affairs).

The budget proposes a total of $967 million to support these functions in 1998-99. This is a decrease of $26 million, or 2.6 percent, from current-year expenditures. The most significant budget-year decrease is in the OES and is a result of reductions in estimated amounts budgeted for disaster assistance.

State Retirement Programs

Retirement-related expenditures account for a significant part of state spending for the budget year. In 1998-99, state expenditures for various costs associated with public employee retirement (excluding University of California costs and nongovernmental cost funds) will total over $3 billion, including $2.4 billion from the General Fund. As summarized in Figure 2, the General Fund provides for employer contributions and / or various other payments to four retirement systems. In addition, the state (1) makes Social Security and Medicare contributions for most state employees and (2) contributes to the payment of premiums for health and dental benefit plans for retired state employees.

Public Employees' Retirement System. The Public Employees' Retirement System (PERS) is the retirement system for most state employees. The budget projects General Fund expenditures of $982 million for PERS in 1998-99. Under the provisions of Chapter 71, Statutes of 1993 (SB 240, Committee on Budget and Fiscal Review), General Fund contributions were made two fiscal years in arrears until the current year. As a result of a lawsuit filed by the PERS, the Superior Court in Sacramento County ordered the state to pay all deferred payments plus interest and to resume sending state funds to the PERS on a current, rather than a deferred, basis. The state paid the $1.2 billion in deferred contributions in the current year. The budget proposes to make the related interest payment of $310 million in 1998-99 (this amount is included in the amount shown in Figure 2).

Figure 2

General Fund Costs For Retirement Programs[a]

1998-99
(In Millions)

Program	1998-99
Public Employees' Retirement	$982
State Teachers' Retirement	731
Judges' Retirement	88
Legislators' Retirement	1
Social Security and Medicare[b]	300
Health and Dental Benefits for Annuitants	302
Total	**$2,404**

[a] Excludes costs for University of California employees.
[b] Legislative Analyst's Office estimate based on 1997 costs.

State Teachers' Retirement System. The State Teachers' Retirement System (STRS) is the retirement system for teachers in public K-12 schools and community colleges. The STRS receives contributions from teachers and their employers. These contributions, however, are insufficient to provide for the cost of basic retirement benefits, the protection of retirees' purchasing power, and to cover past unfunded liabilities. These shortfalls are covered by annual transfers from the General Fund. In the budget year, the shortfalls are expected to total nearly $1.1 billion—about $100 million higher than the current year. The increase is due to an expected increase in teacher payrolls resulting from a combination of more teachers under class size reduction as well as salary increases. In the budget year, the General Fund transfer for these shortfalls will only be $731 million. This is because under Chapter 939, Statutes of 1997 (SB 1026, Schiff), the funds the state will receive from the sale of the Elk Hills Naval Petroleum Reserve in Kern County (under the provisions of a settlement with the federal government) is to be used to offset the required General Fund transfers in the budget year. The Elk Hills property has been sold and the state's share of the sale proceeds is $320 million. This is a one-time reduction in General Fund costs.

Health and Dental Premiums. The budget also includes $302 million from the General Fund to pay the state share of health and dental insurance premiums for retired state employees and their qualifying beneficiaries. This is $23.6 million more than estimated current-year expenditures, which reflects an increase in the number of retirees. The PERS is currently negotiating the health and dental premiums rates for the second half of the budget year. These negotiations may result in a change in the estimated General Fund cost for the budget year. There also may be an adjustment because the number of annuitants covered under this program may be overstated.

Employee Compensation

The collective bargaining memoranda of understanding that govern pay, benefits, and other working conditions for over 150,000 rank-and-file state employees (other than higher education) expired June 30, 1995. At this time, only one bargaining unit—the California Correctional Peace Officers Association—has reached a tentative agreement, but that agreement has not been approved by the Legislature. Moreover, under the terms of the proposed agreement it would expire on June 30, 1998.

The budget includes $279 million as an augmentation for employee compensation. This amount is equivalent to a 3 percent salary increase for state employees other than those in higher education (salary increases for these employees are provided in the budgets for the segments of higher education). The Governor's budget indicates that the amount ultimately needed for this purpose is dependent on reaching agreement with the employee bargaining units through the collective bargaining process.

CROSSCUTTING ISSUES

General Government

THE YEAR 2000 ("Y2K") COMPUTER PROBLEM

Most governmental agencies will need to make changes to their computer systems to accommodate the year 2000 change. California has embarked on a major effort to fix its computers, headed by the Department of Information Technology (DOIT). The DOIT estimates that it will cost the state at least $240 million over several years to fix the problem, but we believe that this estimate is understated. We have identified a number of problems with the state's effort, including optimistic time lines, lack of contingency planning, and insufficient oversight.

We recommend that the Legislature (1) require departments to provide, during budget hearings, a status of their efforts to modify computers to accommodate the year 2000, (2) delay funding for new projects in those departments which have not modified their computers for year 2000, (3) approve DOIT's budget to provide additional oversight and assistance to departments, and (4) establish a reserve fund from which departments can request monies for yet-to-be identified efforts to address the problems related to the year 2000 conversion.

The budget proposes augmentations totaling $19.6 million by state agencies to fund efforts to modify computers to accommodate the year 2000 (Y2K). This does not include hundreds of millions of dollars in redirections within departments' budgets to address these efforts. In this analysis, we outline the nature of the problem, what the state is doing about it, the potential costs and risks, and how the Legislature can ensure that the problem is addressed adequately.

WHAT IS THE Y2K PROBLEM?

In the 1960s and 1970s when mainframe computer capacity was expensive, programmers established a standard for identification of dates in order to reduce the amount of space needed. By using the last two digits to represent the year (for example, 1973 was designated as 73), computing costs were reduced. With the new millennium approaching, these computer systems must now distinguish between dates in the 1900s and the 2000s. Computers, both in the public and private sectors, are unable to distinguish between these dates and must be modified to accommodate the change to the year 2000.

Failure to make the Y2K change will for some systems simply produce undetectable erroneous calculations, but some systems will completely fail. The "failure date," as it is known, is not necessarily January 1, 2000. For some systems in California, it has been as early as 1995, because these systems were required to provide dates into the future (for example, licenses that were granted in the mid- to late 1990s that will expire after the year 2000).

The potential risk for the state if computer systems are not converted is significant. For example, the Department of Motor Vehicles reports that the failure to convert its computer systems could result in $3 billion in lost revenue annually. The Department of Consumer Affairs reports a potential annual revenue loss of $241 million.

The DOIT identified almost 3,000 state computer systems; of these 1,100 are either fixed already or do not need to be fixed. Of the remaining 1,900 systems, 650 are mission critical, meaning that they enable the department to carry out its primary responsibilities such as issuing drivers' licenses, collecting taxes, et cetera. The remaining 1,250 systems were identified as essential but not mission critical and will also need to be fixed.

HOW CAN THE PROBLEM BE FIXED?

In an effort to correct the problem, hundreds of millions of dollars are being spent on replacing, retiring, or modifying computer systems in state government. Each department must decide whether it is going to eliminate the system if it is no longer necessary to meet the department's business needs, replace a system which is essential but not currently meeting the business needs, or modify an existing system to become Y2K compliant. These efforts are collectively known as "remediation."

Several Methods of Y2K Remediation Available

In addition to simply replacing an existing system, a department can fix an existing system through several different methods. First, the department must determine how to identify within all of its lines of codes the dates that need to be changed. In some cases, an automated tool can read the lines of code and determine where the dates are and change them with the department's chosen new date standard. Other cases will require all the work to be done manually, taking much longer. Many systems will require a combination of the two approaches.

Once identified, there are several ways to fix the code. The code can be changed to accept dates with the entire year included (1973 rather than 73, 1910 or 2010 rather than 10). An alternative method is referred to as "windowing" in which the system is told that any date between 00-10 should be considered in the 2000s and any date from 11 through 99 should be considered in the 1900s. A department can choose one of these or many other solutions, depending upon what type of code it has and how much the existing code has been customized over the years. The more customized the code, the more manual intervention will be necessary.

Some of the methods of remediation, such as windowing, should be considered short-term fixes because dates will once again become a problem as the calendar nears the end of the window. Those departments that use a short-term fix may find that they still have to replace an entire system in the near future.

THE STATE'S Y2K PROGRAM

Shortly after DOIT was established in 1995, it began to make other departments and agencies aware of the impact the year 2000 would have on computer systems. Departments received a "white paper" on the issue in October 1996. One month later, DOIT distributed to departments its official Y2K Program Guide.

The DOIT's Y2K Program Guide lists the steps a department should go through to establish a plan for modifying the affected systems. It requires departments to create an inventory of existing systems; identify those systems that are critical to the overall mission of the department (referred to as "mission critical systems"); assess the impact the century change will have on these systems; and develop a plan to fix the systems. Departments had to identify the impact its computer systems have on the department, outside entities with whom it exchanges information, and the public. In addition, DOIT required departments to report this information as well as budget and Y2K conversion schedule in June 1997 with quarterly updates thereafter. Executive Order W-163-97, issued in October 1997, requires all state departments to complete their Y2K remediation efforts by December 31, 1998.

WHAT WILL IT COST?

In January 1998, DOIT estimated that remediation of the mission critical computer systems in state government will cost at least $240 million over several years. As we discuss below, we believe this estimate understates the total costs to the state because it does not include a number of project components and costs.

Current-Year Funding. The *1997-98 Budget Act* (Item 9899) appropriated $55 million for Y2K conversion costs. This included $25 million from the General Fund, $25 million from special funds, and $5 million from non-governmental cost funds. As of early January 1998, 14 departments have requested and received about $44 million.

Budget-Year Funding. The Governor's budget does not propose to include funding for Y2K efforts in Item 9899 for 1998-99, but rather includes funding for Y2K projects in individual departmental budgets. The budget proposes total augmentations of $19.6 million in 12 departments for 1998-99. This amount does not include funds in the baseline budgets. The Department of Finance has not been able to provide information on how much departments have in their baseline budgets for Y2K efforts.

ANALYST'S ASSESSMENT OF THE ADMINISTRATION'S PROGRAM

As we have indicated previously, DOIT has made the Y2K Program a top priority and has taken a number of positive steps to address the issue. It started work on the problem early, developed the Y2K Program Guide, conducted education and training seminars, and provided information and assistance to state departments. However, we have identified a number of shortfalls and missing elements in the program.

Essential, But Nonmission Critical, Systems Need to Be Fixed, Too

In addition to performing tasks on mission critical computer systems, each department will need to review its essential, but nonmission critical computer systems. To date, the focus has been on the mission critical systems so that departments can continue to provide programmatic services such as issuing business licenses, registering vehicles, and collecting taxes. Such a focus on mission critical systems is appropriate, however, there are many essential computer systems which the departments will need to fix in order to administer the department. Systems such as human resources, accounting, inventory, and others are not currently included in many department's plans to become Y2K compliant, yet will need to be fixed. Such efforts will add to the state's current cost estimate for remediation.

Embedded-Chip Technology. Nontraditional information technology, known as "embedded chip" technology, also needs to be fixed to accommodate Y2K. This includes elevators, voice mail systems, security systems, heating and air conditioning systems, as well as many other aspects of state government's daily functions. At this time, few vendors have indicated an ability or willingness to perform remediation efforts on the nontraditional systems. Although DOIT's program requires departments to indicate whether they have created plans and embarked on these efforts, the program does not require this to be included in the department's cost estimate, and DOIT does not review these plans. Thus, the state's planning and budgeting for these efforts is in the preliminary stages.

Costs Are Underestimated

As we indicated earlier, the DOIT estimates that the total costs of Y2K remediation will be $240 million over several years. However, this estimate does not include a number of direct and indirect costs to the state, including:

- ***Embedded chip*** remediation efforts are not included, as mentioned above.
- ***Costs to departments and agencies that do not report to DOIT***, including the Judiciary, the Legislature, the University of California, California State University, and the Community Colleges.
- ***Legal Expenses***. Recent estimates from well-regarded information technology consultants estimate that Y2K remediation efforts should recognize that an additional 40 percent of the project costs might be needed for legal expenses. These legal expenses may arise due to the need to review contracts to determine liability and to participate in litigation, whether as a plaintiff or a defendant.
- ***Implementation of contingency plans***, if needed because projects do not work as planned or are not completed before a prescribed failure date.

- ***Redirected resources*** within state departments. Given that most departments have had to undertake remediation efforts without additional resources, DOIT estimates that about $500 million in staff time is being redirected to Y2K efforts.

Who Pays?—Contracts Need to Be Reviewed

State departments have entered into thousands of contracts over the years to purchase hardware, software, and services. It was not until recently that these contracts contained language that required the vendor to provide hardware and software that was year 2000 compliant. Thus, in addition to fixing mission critical systems, departments must review existing contracts to determine whether the vendor or the state is responsible for paying for these remediation efforts. In most cases, this review is not currently being done. Some contracts require the vendor to ensure the system is maintained and "bug" free. Other contracts may require the state to accept this fiscal responsibility.

Additionally, each contract needs to be reviewed to determine responsibility for liability for noncompliance. If a major system is not remediated in time, the state runs the risk of being sued by someone who alleges harm as a result of the system's failure. As we indicated above, industry experts predict that legal expenses could *add* 40 percent to projects costs. Forty percent of the existing $240 million estimate is approximately $100 million for state government. Determining which failures pose the greatest risk to the state should help to prioritize remediation efforts throughout the state and thus reduce potential liability. Review of existing contracts by qualified legal counsel is an important component to the total effort. The DOIT proposes in its 1998-99 budget to provide these services for all state departments that request it.

Contingency Plans Lacking

Although DOIT required departments to provide contingency plans in their initial reports, our review indicates that few departments have such plans. For departments whose systems have already failed (because they did not meet their conversion date), it is unclear what has been done to enable the department to continue to provide its core business services.

Time Lines Are Too Optimistic

As we indicated above, the executive order provides that all departments complete remediation efforts by December 31, 1998. This is probably an optimistic time line for three reasons.

Testing. The time lines outlined by the departments and reported by DOIT do not provide sufficient time for testing. After the computer code is fixed, the system must be tested. It is generally accepted in the information technology industry that 40 percent of total project time and cost should be devoted to testing. Testing is a critical component of a project because it is at this phase that problems are identified. If adequate time is not set aside for testing, and significant problems are identified when the system is tested, the project may not be completed on time. Once testing has proven successful, the system is put into "production." This is the process in which the system is actually implemented and workers are trained to use it.

Contingency Planning. The time lines do not incorporate time to activate or invoke contingency plans in the event a remediation effort fails to meet project milestones.

Entities With Whom the State Exchanges Data. The state exchanges data with many entities including the federal government, welfare offices, car dealerships, hospitals, schools, and emergency response services. The time lines do not always include enough time for the state department to develop a "bridge" with these partners in the event the partner is unable to modify its systems in time. Without a bridge, even if the state modifies its system on time, it will be unable to exchange data with the confidence that the data are accurate.

WHAT SHOULD THE LEGISLATURE DO?

The Need for Oversight

The consequences can be significant if a state department does not make the Y2K conversion on time. Departments which rely on computer systems to carry out their business, whether it be to collect revenues, ensure public safety, or regulate an industry, need close legislative and executive branch scrutiny. We are concerned that DOIT is currently unable to provide the necessary level of oversight with its limited staff (we discuss this issue below and in our analysis of DOIT contained in this chapter).

As a result of the lack of adequate oversight, the Legislature will not be apprised of the full extent of the problem, efforts being undertaken to fix it, the budget required to complete these efforts, and the fiscal effects if systems are not fixed on time. Since this is the largest information technology project the state has ever undertaken and it has significant ramifications to all citizens, closer monitoring by both the administration and Legislature is warranted.

Require Departments to Report on Progress During Budget Hearings

We recommend that the budget subcommittees require departments to provide a status report on efforts to become Year 2000 compliant during hearings on the 1998-99 budget.

During budget hearings, the budget subcommittees should require each department to provide a status report on its progress in making its systems Y2K compliant. Some departments which submitted plans to DOIT did not indicate how they were going to fix embedded chip problems; what the impact to the General Fund and special funds would be if its systems failed; potential legal exposure; or what they intended to do should their plans fail. The DOIT does not know whether these departments have a backup plan if initial efforts to fix the computer systems are unsuccessful. If a large computer system which issues billings or tracks collections is not remediated before its failure date, the state could stand to lose hundreds of millions of dollars. Likewise, should a computer system which keeps records for law enforcement not be expected to be remediated on time, the Legislature should know of the potential problems beforehand.

According to DOIT's Y2K project time line, all departments should now be done with developing Y2K solutions and should be in the testing phase. If departments are not in the testing phase, it may be a sign that the state will be at risk of not meeting the deadline. Many department's plans contain a minimum number of days between the time at which the first failure date occurs and the time at which the system will be fixed, known as the "cushion" time. This is a key factor in determining risk. A cushion is needed to allow for resolving unanticipated problems due to the complexity of the Y2K modifications. The less cushion time, the higher the risk to achieving success.

Here are some of the questions that the budget subcommittees should ask of departments during budget hearings:

- Does the department's Y2K plan call for having all of its mission critical systems remediated before the failure dates?
- Is the department on schedule with each of its plans? If not, what are the fiscal and policy ramifications of failure?
- How much money is in the department's baseline budget for Y2K efforts?
- Does the department have a detailed contingency plan for each mission critical project?

- What is the status of the department's plans to fix essential, but not mission critical, systems?

We recommend that the Legislature require every department, during budget hearings, to provide an update on the status of its efforts to complete remediation efforts. This would allow the Legislature to direct the departments to improve their efforts, develop contingency plans, or take other steps to ensure that the negative impacts of failure to remediate systems are minimized.

Deny Funding for New Information Technology Projects Until a Department Has Completed Y2K Projects

We recommend that the Legislature deny the budget request for a new information technology project in any department that has not completed its year 2000 projects.

In order to encourage departments to focus their resources on Y2K remediation efforts, the Governor issued an executive order (W-163-97), which requires the deferral of new computer systems unless the proposed new system is legislatively mandated or is necessary to help the department become Y2K compliant. A preliminary review of approval letters indicates 28 new projects (totaling over $200 million) were approved in the three months since issuance of the executive order. Of those, only 11 could be identified as being mandated to meet a department's business needs or necessary for a department to become Y2K compliant.

Some of these nonmandated projects are being requested by departments which will not have their systems compliant before they fail or before the Governor's deadline of December 31, 1998.

Due to the nature of the impact of the century change on nearly every aspect of an organization's mission and the immovable deadline, any new project will likely deflect resources from Y2K efforts. For this reason, we recommend that the Legislature deny funding new projects until the department has its mission critical systems working correctly or the system is mandated by law. In addition to mission critical systems, departments still need to make their essential but nonmission critical systems Y2K compliant. The Legislature may consider requiring a department to have *all* of its systems substantially compliant before approving funding requests for new systems. Failure of the systems that are essential, but not mission critical, may nonetheless significantly affect the ability of an entity to do business effectively.

Approve the DOIT's Y2K Program Funding Request for 1998-99

We recommend that the Legislature approve the Department of Information Technology's request for additional resources for its Year 2000 office.

In our analysis of the DOIT budget (later in this chapter), we recommend approval of the department's request for additional resources for its Y2K office. Currently, DOIT is unable to review many department's plans for, and monitor progress toward, remediation. We believe that close monitoring of departmental Y2K efforts by the state's information technology office is necessary, and recommend that they be provided with the tools to do so. We believe that the funding request is the minimum necessary to accomplish the task.

Establish a Reserve Fund

We recommend that the Legislature consider setting aside a reserve fund in the* 1998-99 Budget Bill *for additional Year 2000 projects.

The state is involved in a multiyear effort to be Y2K compliant. As we indicated earlier, the state's estimate of Y2K remediation costs is probably understated. This is because not all of the plans filed with DOIT include remediation of all systems (especially essential, but not mission critical systems, and embedded chip), implementation of contingency plans, and legal expenses. We believe that the Legislature is likely to receive additional funding requests for these efforts in addition to what is in the Governor's proposed budget.

Departments are refining their cost estimates as they further define the scope of their Y2K remediation efforts. Departments will need to perform the same remediation efforts for nonmission critical systems, potentially invoke contingency plans, review existing contract terms, and defend themselves in court. Many of these expenses have not been identified yet and are not accounted for in the proposed budget.

The Department of Finance is only tracking the augmentation requests made by departments. It is not tracking how much departments are actually spending on Y2K efforts. Nor does it plan to track the Y2K efforts in a way to be able to plan for revenue shortfalls in the General Fund or special funds should these systems not be fixed on time. This will be problematic if a computer system at a department that is charged with collecting revenue does not function properly.

Since departments will not be able to wait until the *1999-00 Budget Act* for appropriations to resolve these yet-to-be identified efforts, and shortfalls in revenue collected poses a potential problem to the General Fund, the Legislature should consider setting aside funds to resolve these problems. Although some level of redirection of resources by departments is appropriate, we believe that additional resources will be necessary. In the *1997-98 Budget Act*, the Legislature appropriated $55 million (all funds) for Y2K remediation efforts. We believe that a reserve fund of at least that magnitude is warranted for 1998-99 above the amounts proposed for the individual departmental budgets.

DEPARTMENTAL ISSUES

General Government

CONSUMER AFFAIRS
(1110-1600)

The Department of Consumer Affairs is responsible for promoting consumer protection while supporting a fair and competitive marketplace. The department includes 28 semiautonomous regulatory boards and nine bureaus and programs that regulate various professions. The nine bureaus and programs are statutorily under the direct control of the department. The 28 regulatory boards are administered by appointed consumer and industry representatives.

Expenditures for the support of the department and its constituent boards are expected to total $359 million in 1998-99, a 16.5 percent increase from the current year, which is primarily a result of the transfer of approximately $65 million in special fee revenue to fund the Smog Check program. Included in the total are $1.7 million in expenditures from the General Fund, a 115 percent increase. The increase in funding from the General Fund is the result of the department's request for a $900,000 augmentation for the call center—a toll-free inquiry/complaint system which handles telephone inquires/complaints from consumers and licensees.

SMOG CHECK PROGRAM

We recommend that the Legislature not approve funds requested for the Smog Check program until the department provides a complete report to the Legislature, detailing the current status of all of its components

(including the implementation strategy for the low-income repair assistance and high-polluting vehicle purchase programs and implementation of remote sensing technology). We withhold recommendation on the requested $68 million to implement legislation adopted in 1997, pending receipt and review of the requested report.

Current Smog Check Program

The Legislature adopted legislation establishing the first Smog Check program in 1982. The original framework for a statewide biennial inspection program was implemented in 1984 by the department's Bureau of Automotive Repair. Under this program, both smog (emission) testing and needed vehicle repairs were permitted at any privately owned smog test-and-repair station.

The 1990 federal Clean Air Act amendments required a somewhat different smog check program in states with the most polluted urban areas, including California. As a result, California was directed in 1992 to adopt a program that would have required vehicles to be tested and repaired at different stations. In response to this directive, the state, after negotiating with the federal government, adopted a "hybrid" program in 1994. The new program is designed to meet the federal clean air requirements by focusing on the highest-polluting vehicles and the smoggiest areas. The program is funded through a variety of fees, and the annual budget totals approximately $89 million.

Several bills adopted during 1996 and 1997 amended the Smog Check program. The new laws:

- Exempt from the biennial smog check, vehicles up to four model years old, 1973 model year and older vehicles, and all vehicles 30 years old and older beginning in 2003.
- Repeal the annual testing requirement for vehicles classified as "gross polluters."
- Provide financial assistance to low-income motorists for repairs to their vehicles.
- Provide the department greater flexibility in establishing and administering the test-only and test and repair station networks.

Budget Proposal. The budget contains two proposals, detailed in Figure 3, to implement the recent changes to the Smog Check program. Essentially, the department has grouped the program changes into two different categories based on the funding source. We discuss below the funding and implementation problems associated with these two components.

Figure 3

Department of Consumer Affairs
Smog Check Proposals

(Dollars in Thousands)

DCA Division/ Program	Repair Assistance and Purchase: Proposed Augmentation	Repair Assistance and Purchase: Proposed Positions	Enhanced Smog Check: Proposed Augmentation	Enhanced Smog Check: Proposed Positions
Enforcement	$2,253	25.0	$2,627	25.0
Operations/Engineering	4,366	24.4	1,081	4.0
Office of Information Services	—	—	424	3.0
Administration	442	6.0	1,064	10.8
Consumer Education and Awareness	684	1.0	—	—
Department of Motor Vehicles	—	—	100	—
Repair Assistance and Vehicle Purchase	55,000	—	—	—
Call Center	1,510	32.7	3,402	53.0
Totals	**$64,255**	**89.1**	**$8,698**[a]	**95.8**

[a] Includes $4.5 million redirected from existing ufnds appropriated for remote sensing.

Vehicle Repair Assistance and Purchase Programs

This request is for $64.3 million in funding from the High Polluter Repair or Removal Account to implement (1) a repair assistance program for low-income motorists and (2) a vehicle purchase program for motorists who own high polluting vehicles. (We address $62.8 million of the total proposal in this discussion and the remaining $1.5 million in the next section on the request for augmentations to the department's call center.)

Low-Income Repair Assistance. The department is authorized to offer qualifying motorists a low-income repair assistance program beginning March 1, 1998. Qualifying motorists are those automobile owners (1) whose income is at or below 175 percent of the federal poverty level and (2) who make a co-payment equal to the repair cost limit (set by the department at either $250 or not more than $200, depending on the level of participation in the program). The program is to be funded by smog impact fee revenue (a $300 fee collected when an out-of-state vehicle is registered in California for the first time).

According to the department, a method to verify the income level for potential participants has not been developed and there is no date certain when the method would be developed. Consequently, it is uncertain as to when this program will be operating or how the funds will be used in the budget year. In view of this situation, we recommend the Legislature withhold action until the department is able to provide information on the method to be used for income verification and an implementation plan for this proposal.

High Polluting Vehicle Purchase Program. The department is also authorized to establish a program to purchase high polluting vehicles at a price equal to the market value of the vehicle, not to exceed $800. Based on information from the department, it is clear that the department is not ready to implement this program. For example, the department is still in the process of determining how the purchased vehicles will be disposed of and what costs may be associated with vehicle disposal. According to the department, there could be a relatively high cost associated with disposal of the vehicles. If this is the case, then the state will not be able to purchase as many vehicles. Additionally, the department is still developing guidelines for determining which vehicles should be targeted for purchase and at what price.

Enhanced Smog Check

This request totals $8.7 million from the Vehicle Inspection and Repair Fund (VIRF). This amount includes $4.5 million redirected from existing appropriations that were provided for the remote sensing element of Smog Check and a $4.2 million augmentation from the VIRF. This request is to address those 1996 and 1997 program changes and associated workload that are funded solely from the VIRF. For purposes of our discussion, we will refer to this proposal as the Enhanced Smog Check. (We address $5.3 million of the total proposal in this discussion, and the remaining $3.4 million in the next section on the request for augmentations to the department's call center.)

Previous Redirections From Remote Sensing. It is our understanding that the department has previously redirected funding from the remote sensing component to other areas within the Smog Check program. During the 1997-98 budget hearings, the administration asked the Legislature to provide an augmentation to the referee services component of the Smog Check program. At that time the department indicated funds could no longer be redirected from the remote sensing component because the redirection of funds "....has reduced the ability of the....State to meet mandates established by the Federal Clean Air Act...." The proposed budget-year redirection of $4.5 million is inconsistent with the department's position last spring. Without the proposed redirection, the remote sensing budget for 1998-99 would total $14.5 million.

Additionally, the department's justification for the proposed redirection is that the remote sensing technology is not yet accurate enough to warrant full implementation. It is not clear what level of accuracy is necessary, how the department will determine this accuracy level or when the technology will provide this accuracy. Given these issues, the department needs to provide the Legislature information regarding the desired accuracy level that remote sensing needs in order to be fully implemented and a time frame of when that accuracy level will be achieved.

Consequently, we recommend that the department provide the Legislature an update on the status of the remote sensing component of Smog Check, including the needed funding, before the Legislature considers redirecting any funds from this element of the program.

Current-Year Expenditure Controls

The department has mandated a hiring freeze and other expenditure controls during the current year to generate savings within the VIRF to implement various legislative mandates. The department's stated goal is to obtain $4 million in "savings" from authorized VIRF expenditures to fund the new mandates. Included in this $4 million "savings" is a $2 million redirection from remote sensing.

We recommend the department provide a detailed report to the Legislature prior to budget hearings addressing the current-year expenditure controls and hiring freeze. The report should include, at a minimum, a listing of which positions have been held vacant; which expenditures, by program area, have been curtailed or postponed; and which remote sensing activities have been curtailed or postponed.

Department of Motor Vehicle Fee Collections

Under Chapter 802, Statutes of 1997 (AB 208, Migden), owners of vehicles that are four model years old or newer must pay a $4 annual smog abatement fee but are not required to have their vehicle smog checked until the vehicle is more than four years old.

The smog abatement fee is to be collected at the time the vehicle owner registers (initial registration and each renewal) the vehicle with the Department of Motor Vehicles (DMV). The DMV is to deposit these fees daily in the VIRF. The proceeds from this fee are estimated to total $12 million per year.

It is our understanding that because the DMV has not made the necessary changes to its computer systems, it is unable to collect the fee. Furthermore, under a Governor's Executive Order, the DMV will not make the needed modifications until it has successfully completed changes to its computer systems to meet year 2000 requirements. According to DMV, this work will not be complete until late 1998 and fee revenue will not begin to be collected until January 1, 1999. Therefore, only about $6 million would be collected in the budget year. The Governor's budget for the Smog Check program, however, anticipates receiving a combined total of $18 million in the current year and budget year. Thus, the department will not receive most of the anticipated fee revenue.

At the time this *Analysis* was prepared, the department—along with the Department of Finance and the DMV—was attempting to secure alternative funds to replace the smog abatement fees that will not be collected. The departments were also investigating the feasibility of collecting the first year of smog abatement fee revenue in arrears. Prior to budget hearings, the department should provide the Legislature an update on the status of the smog abatement fee collections and any impact lost collections will have on the overall Smog Check program.

Call Center Augmentations Not Justified

We recommend the Legislature delete the proposed augmentations totaling $6.1 million and 109.7 positions for the department's call center because the department has not justified the need at this time for these augmentations. (Reduce various items by a total of $6.1 million and 109.7 positions.)

The department has requested a total $6.1 million augmentation and 109.7 positions for the call center. The augmentations are spread across three different programs (as detailed in Figure 4) and essentially triple the size of the call center.

The department operates a toll-free inquiry/complaint (800 number) telephone line to handle telephone inquiries and complaints from consumers and department licensees. The department established the combination automated and live operator call center in 1994 and has since expanded the center to respond to inquiries received via the Internet. The call center currently has a staff of 50 permanent positions and is entirely supported by special fund revenue.

Figure 4

Department of Consumer Affairs
Proposed Augmentation for Call Center

(Dollars in Thousands)

Program	Proposed Funding	Fund Source	Proposed Positions
Smog Check	$4,912	Various	85.7
Barber and Cosmetologists	292	Special funds	5.0
Nonjurisdictional workload	900	General Fund	19.0
Totals	**$6,104**		**109.7**

General Fund Call Center Augmentation

The budget proposes a General Fund augmentation of $900,000, on the basis that it is needed to offset costs associated with answering calls and inquiries concerning matters not under the department's jurisdiction. These include landlord/tenant issues, vehicle registration and driver's license renewals, and collection agency practices. The department indicates that approximately one-third of telephone calls and one-half of Internet inquires concern matters not under the department's jurisdiction.

According to the department, because call center operators are tied-up with nonjurisdictional calls, department licensees and consumers of business activities regulated by the department experience service delays. Available information, however, does not indicate that callers are experiencing extraordinary delays in service. In fact, the department's December 1997 year-end report on its participation in the performance-based budgeting pilot indicates that in 1996-97 the call center:

- Decreased wait time for consumers by 50 percent.
- Decreased busy signals received by callers by 67 percent.
- Increased the number of calls answered by 17 percent.

Thus, it appears that the department is able to not only handle the center workload, but is also consistently improving customer service.

Furthermore, we believe that several options exist for the department to reduce operator workload associated with handling nonjurisdictional calls. For example, the call center currently offers recorded landlord/tenant information. The department should consider expanding recorded information programs for other frequently asked nonjurisdictional questions. In addition, the department should explore (as called for in its own report) further automation of the call center so that overall operator workload is reduced.

Given the department's report of customer satisfaction and improved service along with the options that exist for reducing costs associated with answering nonjurisdictional calls, we believe an augmentation to the call center is not justified. Accordingly, we recommend that the Legislature delete $900,000 under Item 1111-001-0001.

Barbering and Cosmetology Workload

When the Barbering and Cosmetology program was structured as a board, the board and the department entered into a memorandum of understanding (MOU) for the call center to handle the program's workload. The MOU was initiated at the beginning of 1995-96. It provides for three dedicated positions in the call center and requires the Barbering and Cosmetology program to reimburse the department for work performed, based on call volume. In addition, when the Barbering and Cosmetology program was organized as a board, it operated its own call center, which was funded out of $80,000 budgeted for communications expenses. At that time, the board responded to over 250,000 calls annually.

The current workload identified by the department is only 120,000 calls annually. Thus, the current budget for Barbering and Cosmetology activities should be sufficient to handle the call center workload. We therefore, recommend that the Legislature not approve any additional funds for the Barbering and Cosmetology call center workload, as it is unclear that the current funding is insufficient for the program needs. (Reduce Item 1111-001-0069 by $292,000 and five positions.)

Smog Check Augmentation

The proposed call center augmentation includes $4.9 million and 85.7 positions to handle *projected* Smog Check program workload growth resulting from the implementation of various pieces of legislation adopted in 1996 and 1997. This request is directly related to the Smog Check program changes (repair assistance, vehicle purchase, and Enhanced Smog Check) discussed earlier. As we mentioned in the previous section, the department has not finalized implementation plans for these changes.

Thus, the requested increase in call center staff to handle to smog check workload is highly speculative. Given this uncertainty, the department cannot at this time, be assured there will be any new workload in 1998-99, let alone an increase which would nearly triple the workload of the call center. Thus, we believe that it is premature to authorize this level of expansion. Should the department experience a significant increase in workload at the call center, the flexibility exists within the department under performance-based budgeting to shift personnel and funds to accommodate such a need. (Reduce Item 1111-001-0421 by $3.4 million and Item 1111-001-0582 by $1.5 million.)

OTHER ISSUES

Barbering and Cosmetology Augmentations Unnecessary

We recommend the deletion of proposed augmentations for the Barbering and Cosmetology program because these costs should be accommodated within current resources using the flexibilities given to the department under performance based budgeting. (Reduce Item 1111-001-0069 by $737,000 and 18.3 positions.)

The budget proposes the following augmentations totaling $737,000 and 18.3 positions for the board:

- Workload adjustment for citation appeals ($372,000 and seven positions).
- Workload adjustment for examination administration ($236,000 and 11.3 positions).
- Distribution of board health and safety rules ($129,000).

In past years, the Legislature has provided these augmentations on a one-time, limited-term basis. This action was taken as a result of the uncertainty surrounding the board's transition into the department as a bureau.

Board Was Restructured as a Bureau. The Board of Barbering and Cosmetology sunsetted on June 30, 1997. The program functions of the board were restructured as a bureau within the department, effective July 1, 1997. Consequently, the activities and functions in this regulatory area should be evaluated by the department for inclusion in existing departmental administrative structures, such as the case management branch and the office of examination resources. We believe it is inappropriate for the department to continue to evaluate the needs of the Barbering and Cosmetology program as if it were a stand alone board. Also, because this is now a bureau under the department's performance-based budgeting approach, the department (1) has greater flexibility to accommodate any new expenditures from existing resources and (2) the ability to realize savings associated with the elimination of the board structure. These economies would certainly not be realized under the budget proposal, which would result in expenditures in this program area increasing from the $7.8 million in 1996-97 (the last year as a board) to the $9 million proposed for the budget year. Thus, we recommend that the Legislature delete $737,000 and 18.3 positions from Item 1111-010-0702.

State Funding for Bureau of Home Furnishings and Thermal Insulation Laboratory Upgrades Inappropriate

We recommend the Legislature delete a $221,000 augmentation to fund a rent increase ($86,000) and structural upgrades ($194,500) for the Bureau of Home Furnishings and Thermal Insulation Laboratory because improvements to a privately owned building should not be funded with state dollars. (Reduce Item 1111-001-0752 by $221,000.)

The Governor's budget contains $281,000 from special funds for improvements to the testing laboratory operated by the Bureau of Home Furnishings and Thermal Insulation. The laboratory is located in North Highlands in a rented building, and the current lease expires in 1998. The proposed augmentation would provide for a rent increase (however, the new lease agreement has not been finalized), electrical wiring, plumbing, and other structural upgrades. Since the laboratory is located in a rented building, we believe providing permanent improvements to a private building is an inappropriate use of state funding. Instead, these improvements should be the responsibility of the owner. Any improvements that are needed specifically for the state program should be amortized through the state's lease payment. Thus, we recommend the Legislature delete the $221,000 related to this work.

Of the amount requested, $60,000 is for the purchase and installation of ventilation hoods for health and safety purposes. These hoods are movable and would be state property. This portion of the request is appropriate, and we recommend the Legislature approve the related $60,000.

Implementation Plan for Chapter 401, Statutes of 1997 Not Complete

We recommend deletion of the proposed $326,000 increase in reimbursement authority for the implementation of Chapter 401, Statutes of 1997 (SB 780, Kelley) since the department is to provide an estimate of ongoing costs at a later date. (Reduce reimbursements under Item 1111-010-0702 by $326,000.)

Chapter 401 amended the Private Investigators Act and the Private Security Services Act relating to: (1) fee structures; (2) new, technologically advanced licensee identification cards; and (3) synchronization of licensee firearm and license renewal cycles. The department indicates that the new licensee identification cards and synchronization of the license renewals will result in one-time and ongoing costs and has requested a one-time increase in reimbursement authority totaling $326,000. The department, however, has also indicated that the ongoing costs, as yet unidentified, will be included in a proposal to be submitted at an unspecified future date. Consequently, we recommend the Legislature not approve this request. When the department develops the necessary budget information to implement Chapter 401, a revised proposal would warrant legislative consideration. (Reduce Item 1111-010-0702 by $326,000.)

Private Postsecondary and Vocational Education Program

We withhold recommendation on the $6.6 million proposed for the department to assume the responsibilities of the Council for Private Postsecondary and Vocational Education pursuant to Chapter 78, Statutes of 1997 (AB 71, Wright), pending receipt of an implementation plan.

Chapter 78 transferred the regulatory responsibilities of the Council for Private Postsecondary and Vocational Education (hereafter referred to as program) to the department effective January 1, 1998. In addition, Chapter 78 makes structural changes to the program. The department is requesting $6.6 million and 79.5 positions to implement Chapter 78. This is the same funding level previously authorized for this program when the authority for operation was within the council.

The department just recently assumed responsibility for the program and has not yet identified the workload involved with administering the changes mandated by Chapter 78, nor has the department identified the savings, if any, that should occur as a result of the transfer. The department is proposing to adjust the budget, if necessary, in the 1999-00 budget proposal.

We withhold recommendation on this proposal and the department should provide an implementation plan to the Legislature before the budget hearings begin. The plan should include, at a minimum, what the department plans to accomplish in the first 18 months of program operation; a time-line of implementation; and a revised first-year cost estimate reflecting initial savings from the transfer.

Department Should Report on Status of Year 2000 Modifications

The department should, prior to budget hearings, submit a report to the Legislature on the status of modifying critical information technology systems to accommodate the year 2000 change.

The Consumer Affairs System (CAS) is the primary computer system operated by the department. The CAS issues, tracks, and maintains business and individual occupational licenses (initial and renewals); and records and tracks complaints, investigations, and administrative, civil, and criminal sanctions against licensees. Additionally, the CAS operations collect approximately $241 million in revenue annually.

The department has identified the CAS as being "mission critical" for the department's operation. This designation—mission critical—means that operation of the CAS supports the department's main function, which is licensing and enforcement. According to the department, if the CAS is not modified on time to be year 2000 compliant, the department will: (1) experience a delay in issuing licenses; (2) be unable to collect licensing revenue, conduct enforcement actions or determine the validity of existing licenses; and (3) pass on erroneous information to other state systems with which the CAS shares information.

The department has indicated that (1) the CAS failure date (the date when the department can no longer be completely confident the system is functioning properly) was January 1, 1998, and (2) the system will not be completely reliable until December 31, 1998. The department also has indicated that a "work around" or temporary fix has been implemented to keep the CAS functioning until December 31, 1998. Based on the available information, it is unclear as to the extent of the work around and whether the work around is sufficient to keep the CAS functioning.

Given the importance of the CAS and the uncertainty of the reliability of the "work around," the department should, prior to budget hearings, submit a report to the Legislature on the status of modifying all information technology systems to be year 2000 compliant. The report should address the current operations of the department, including licensing, enforcement, and cashiering; and identify if any of these operations are compromised or limited as a result of year 2000 operational problems with the CAS.

FAIR EMPLOYMENT AND HOUSING (1700)

The Department of Fair Employment and Housing (DFEH) enforces laws that promote equal opportunity in housing, employment and public accommodations, and that protect citizens from hate violence. Specifically, DFEH has responsibility for enforcing the state's main equal opportunity law, the Fair Employment and Housing Act, and resolving complaints in a timely manner. The budget proposes expenditures of $19.2 million ($15.2 million from the General Fund and $4 million federal funds) for support of DFEH in 1998-99. This represents a General Fund increase of $1.7 million (13 percent) over its estimated current-year expenditures.

Management Improvements Required Before Consideration of Further Staffing Increases

We recommend the Legislature not approve the department's request for a $1,250,000 augmentation and 21 new positions because of the need for management improvements. Further, we recommend the Legislature adopt supplemental report language directing the department to submit to the Legislature by November 1, 1998, a report on its progress in implementing management changes, the specific performance improvements realized from each change, and other changes/improvements to be implemented. (Reduce Item 1700-001-0001 by $1,250,000.)

The Governor's budget proposes $1.25 million from the General Fund for the department to add 21 additional positions to investigate employment discrimination complaints. This is the same proposal that was denied by the Legislature in 1997-98. The current proposal would bring the department's staffing level to 295 personnel-years, an increase of 56 percent since 1993-94. The issues associated with this proposal are the same as were addressed by the Legislature last year.

Background. In the *1995-96 Budget Act*, the Legislature augmented the department's budget by $2.5 million and 41 positions for a similar purpose—investigation of employment discrimination complaints. This augmentation was based on the premise that additional staff could reduce the backlog in employment discrimination cases within the statutorily required one-year period to move a case to prosecution. At that time we expressed concerns that the department had not justified the augmentation, that the number of cases at risk of missing the one-year deadline was already declining without the additional positions and that, according to the department, about one-half of the backlogged cases were probably not meritorious. The augmentation, however, was approved.

In the *1996-97 Budget Act*, the Legislature deleted funding for 11 of the 41 positions added in 1995-96 and converted the remaining 30 positions to two-year limited-term positions to work off the backlog. In response to concerns about the department's management procedures, the Legislature adopted language in the *1996-97 Budget Act* requiring the Bureau of State Audits (BSA) to conduct a comprehensive fiscal and performance audit of the department.

In the *1997-98 Budget Act*, the Legislature converted the remaining 30 limited-term positions to permanent status. At the same time, because of continued concern over workload management, the Legislature denied one-half of the department's new augmentation request for $2.5 million and 42 positions. Thus, the Legislature again increased the department's resources—this time by $1.25 million and 21 positions.

Management Improvements Needed. A continuing theme in the Legislature's review of this department's budget is its management of workload. This was a concern last year when the Legislature reduced the department's augmentation request. The department has not provided any information to substantiate the need to overturn the Legislature's action last year. Given the funding and management history of this department, we recommend that instead of again increasing the department's budget and staff, the department should fully use existing positions and concentrate their efforts on improving the management of workload.

The BSA report called for in the *1996-97 Budget Act* was completed in January 1997. The report identified 15 areas in which the department's performance was deficient, and made recommendations for specific improvements. The department has indicated that it intends to make management improvements in response to the BSA report. As these changes are implemented, the department should be able to identify the specific improvements that result. After all necessary management improvements are in place and the department has gained sufficient experience under these improvements, the need for additional staff may warrant the Legislature's consideration. Until changes are made and performance improvements clearly demonstrated, however, the Legislature should not provide additional staff.

Recommendation. Based on the issues discussed above, we recommend the Legislature delete the request for $1.25 million and 21 positions. Further, we recommend the Legislature adopt supplemental report language directing the department to submit to the Legislature by November 1, 1998, a report on its progress in implementation of management changes, the specific performance improvements realized from each change, and other changes/improvements to be implemented. Such a report will permit the Legislature to then evaluate any ensuing budget increase requests in light of management's performance improvement. After its ability to effectively manage its staff and workload has been demonstrated, a need for additional staff can be more accurately assessed.

ALCOHOLIC BEVERAGE CONTROL (2100)

The Department of Alcoholic Beverage Control (ABC), established by constitutional amendment in 1954, administers the Alcoholic Beverage Control Act (Act). Under the Act, the ABC has the exclusive authority to (1) license and regulate the manufacture, sale, purchase, possession, and transportation of alcoholic beverages in California; (2) collect licensing fees; and (3) deny, suspend, and revoke licenses.

The Governor's budget proposes $34.5 million for support of the ABC in 1998-99 from the Alcohol Beverage Control Fund ($33.6 million) and reimbursements ($869,000). This represents a 3.3 percent increase from the previous year. Included in this amount is $1.5 million for local assistance, which is the same as the current year.

Alcoholic Beverage Control Fund Condition— Longer Term Solution Warranted

We recommend the Legislature enact trailer bill legislation allowing the Alcoholic Beverage Control (ABC) to increase license fees in an amount higher than proposed by the Governor in order to generate revenues adequate to sustain the ABC's current enforcement efforts.

As mentioned above, the ABC is funded from the Alcohol Beverage Control Fund. The majority of revenues to this fund are received from issuing 61 different types of manufacturer, importer, retail, and wholesale liquor licenses. The ABC currently monitors over 70,000 licensees. Estimated net revenues to the fund in 1997-98 are $29.4 million. Net revenues are projected to increase in the budget year to $33.1 million, as a result of a fee increase proposed by the Governor.

Proposed Fee Increase. Based on current- and budget-year expenditures, the ABC will face a fund deficit at the end of the budget year. To address this problem, the Governor is proposing to increase enforcement fees (through trailer bill legislation) to raise an additional $5.2 million in annual revenues. The higher fees would range from $60 to $80 and would be assessed on 31 license categories that require the greatest amount of enforcement activities by the ABC. The proposed fee increase is based on the assumption that ABC's expenditures will remain at the 1997-98 level through fiscal year 1999-00. Spending, however, is likely to grow—if only to account for the effects of inflation. For comparison purposes, the department's expenditures over the past four years have increased an average of 3.5 percent. If ABC's expenditures continue to increase at the same rate, our analysis indicates that the department would incur a $1 million deficit in four years (2001-02). Consequently, at its current program level, the proposed fee increase would provide only a very short-term solution.

Assuming expenditures increase at the recent rates, our analysis indicates that the ABC would need to generate at least an additional $7.8 million annually, rather than the $5.2 million proposed by the Governor. We believe that this is a more appropriate level of authorized resources in order to sustain the level of current enforcement efforts. Consequently, we recommend that the Legislature enact trailer bill legislation allowing the ABC to increase license fees to generate additional revenues of at least $7.8 million annually. To provide a degree of flexibility, the legislation should not limit the ABC to a specific fee amount, but rather give the ABC authority to increase fees *up to* a maximum amount.

Request for Nondocumented Alien Workload Premature

We recommend that the Legislature delete $928,000 and 21.5 positions proposed for the projected increased workload resulting from the Alcoholic Beverage Control (ABC) undertaking efforts to verify citizenship of all licensees, because the ABC has not yet developed an implementation strategy and plan for this verification. (Reduce Item 2100-001-0081 by $928,000.)

Based on a provision of the 1996 federal Personal Responsibility and Work Opportunity Reconciliation Act (which denies professional and commercial licensure to certain immigrants), the ABC has determined that all current licensees and license applicants must be screened to determine if they are ineligible for licensure. The Governor's budget contains $928,000 and 21.5 positions to perform this verification. The bulk of the total augmentation would be limited to two years ($736,366 and 17.5 positions), with the remaining $191,634 and 4 positions ongoing.

The ABC indicates that the administration is currently developing the policy, procedures, and processes necessary to perform the verification of licensee citizenship status. The ABC also anticipates that there could be substantial costs associated with this workload. However, the ABC has not yet completely identified these costs. Given the lack of a plan to undertake this verification and the uncertainty of the resource level needed, we recommend the Legislature delete the request. When the ABC develops an implementation plan with associated costs and staffing, a proposal would warrant legislative consideration.

DEPARTMENT OF INDUSTRIAL RELATIONS (8350)

The mission of the Department of Industrial Relations (DIR) is to protect the workforce of California, improve working conditions, and advance opportunities for profitable employment. These responsibilities are carried out through three major programs: the adjudication of workers' compensation disputes; the prevention of industrial injuries and deaths; and the enforcement of laws relating to wages, hours, and working conditions. In addition, the department regulates self-insured workers' compensation insurance plans, provides workers' compensation payments to injured workers of uninsured employers and other special categories of employees, offers conciliation services in labor disputes, and conducts and disseminates labor force research.

The budget proposes expenditures totaling $229 million for the department in 1998-99, which is 4.6 percent more than the estimated expenditures for the current year. The request includes $147 million from the General Fund, a 6 percent increase over 1997-98.

The Targeted Industries Partnership Program Should Not Be Funded From General Fund

We recommend that the Legislature delete the proposed $2.4 million General Fund augmentation for the Targeted Industries Partnership Program to (1) replace funds currently received from the Employment Development Department and (2) expand the program to the restaurant industry because this would not be a cost-effective expenditure of General Fund money. (Reduce Item 8350-001-0001 by $2,407,000.)

Background. Since November 1992 the DIR has teamed with the Employment Development Department (EDD) and the U.S. Department of Labor to coordinate the enforcement of federal and state labor laws in the garment and agricultural industries because of widespread violations of workplace safety, wage, and hour laws. This effort, the Targeted Inspection Partnership Program (TIPP), was initially funded as a two-year pilot program. Until 1996-97, state funding for these programs had been from the Industrial Relations Unpaid Wage Fund (UWF). In 1996-97 EDD agreed to provide additional funding for TIPP through 1998-99 from the Benefit Audit Fund (BAF) which is funded by collection of fraudulent unemployment insurance overpayments. In July 1997, however, EDD notified DIR that because of reductions in unemployment claims and fraudulent claims collections, the BAF was anticipated to have a deficit of $3.3 million in 1999 and EDD would not fund TIPP in 1998-99 and thereafter.

In the current year, the budget for TIPP is for 39 positions funded by $1.7 million from BAF and $0.9 million from the UWF. The proposal for the budget year includes $1.8 million from the General Fund to replace BAF funding and an additional $0.6 million and 9.5 personnel-years (PYs) to expand the program to the restaurant and other industries believed to operate in the underground economy.

Benefit of Replacing EDD Funds With General Funds Is Unclear. Based on DIR data, TIPP inspections have resulted in a significant level of assessments against employers in the garment and agricultural industries, but only a small amount of the assessments have been collected. Over the four-year period 1993 through 1996, TIPP assessed a total of $20.5 million in penalties and collected only $3.3 million. The data, however, also indicate that there appears to have been improvements in some aspects of working conditions in the targeted industries. For example, comparing the 1996 data to 1994 data, the percent of firms inspected and cited for violations in several areas, such as minimum wage requirements and for not having workers' compensation insurance, has declined.

On the other hand, the percent of firms found to not be registered with the state has increased significantly as has those cited for serious Occupational and Safety Health Administration (CAL OSHA) violations. Furthermore, even though there have been declines in the percentage of inspected firms cited for violations, there are still many firms receiving citations. In 1996, 43 percent of the firms inspected were cited for minimum wage violations and 72 percent were cited for serious CAL OSHA violations. These data certainly indicate that the state needs to continue inspections in these industries. What is not clear is what results the Legislature could expect by providing $1.8 million from the General Fund to replace EDD funds.

In 1996-97 the Legislature augmented TIPP by $ 1.7 million and increased the staffing level from 15 to 39. The source of funds for this increase was reimbursements from EDD. At that time, the DIR justified the expansion using EDD funds on the basis that the increased effort would result in $1.8 million in collections from assessments for various employment and tax law violations. On this basis the increased effort would have essentially paid for itself. This apparently has not been the case. As mentioned above, EDD has notified the DIR that it will not fund TIPP in the budget year and thereafter. The withdrawal of funding was apparently based on EDD's conclusion that TIPP spending was not a cost-effective expenditure of funds. If true, its not clear why the state would want to substitute General Fund money for this purpose. Consequently, we recommend the Legislature delete the requested $1.8 million and 39 positions. This would leave the TIPP program funded at the pre-EDD level of about $1 million from the UWF and 15 staff.

Expansion of TIPP. In addition to requesting $1.8 million from the General Fund to replace EDD money, the department requests an additional $0.6 million and 9.5 PYs to expand the program to the restaurant industry and other industries believed to be heavily represented in the underground economy. We recommend the Legislature not fund this expansion because the department has not provided information that would justify additional staff for this purpose. If the DIR believes inspections are necessary in the restaurant or other industries, it could schedule these inspections on a priority basis using existing resources. Once the DIR has gained experience and knowledge of problems and workload for such an effort, along with how effective these inspection are, a proposal for additional staff may warrant legislative consideration. At this time, however, we recommend that the Legislature delete the $610,000 and 9.5 PYs.

Joint Enforcement Strike Force Should Also Not Be Funded by General Fund

We recommend the Legislature reject the department's request for a $1.2 million augmentation from the General Fund to continue the Joint Enforcement Strike Force because it has not proven to be a cost-effective mechanism for enforcing payroll tax laws. (Reduce Item 8350-001-0001 by $1,173,000.)

The Joint Enforcement Strike Force (JESF) was statutorily established in 1994 as the successor to a federally funded program to increase tax collections in the underground economy. The participants in the strike force include EDD, DIR, and the Department of Consumer Affairs. The DIR's participation in JESF has been reimbursed by EDD ($1.2 million in 1997-98), but on a year-to-year basis. In July 1997, EDD notified the DIR that, as with the TIPP program, money from BAF would not be available for JESF after 1997-98. An important purpose of JESF is collection of unpaid taxes that are avoided by cash payments in the underground economy. However, JESF has demonstrated that it can not do this cost-effectively. For example, in 1996, the cost of DIR's participation in the JESF program was $1.2 million, but only $450,000 was collected. Since JESF is not cost effective, the General Fund should not be used to backfill EDD funding. The DIR can continue to enforce the wage and hour laws for which it is responsible using its existing resources. Accordingly, we recommend the Legislature not approve the proposed augmentation.

Eliminate Managed Care Unit

We recommend the Legislature delete $222,000 and 3.3 personnel-years for the Managed Care Unit within the Division of Workers' Compensation because there is little workload and insufficient fee revenue to support the program. (Reduce Item 8350-001-0001 by $222,000, delete Item 8350-001-0132, and transfer the balance in the Workers' Compensation Managed Care Fund to the General Fund.)

Background. In 1993-94 the Managed Care Program (MCP) was established as part of workers' compensation reform legislation adopted in 1993. Under this program private and not-for-profit health care providers apply to the state for eligibility to become a health care organization (HCO) that, upon certification, may contract with employers to provide managed care for employees with injuries covered by workers' compensation claims. The applicant is assessed an application fee and, if certified, is charged an annual fee based on enrollment. The MCP was intended to be self-funding. In 1994-95 the Workers' Compensation Managed Care Fund received a loan of $1.7 million to provide cash for MCP's initial operations.

Lack of Workload. In 1994-95, the Managed Care Unit (MCU) was funded based on an estimate there would be about 50 HCO applicants in that year. In fact, only 18 organizations have applied for HCO certification in the four years the program has been operating, and only three of those applications have been received since 1995. Moreover, there are only ten organizations currently certified. The primary purpose of the MCU is to evaluate and certify HCO applicants, yet it is apparent that there is virtually no workload to justify maintaining this organization. The premise upon which this program was founded—that the managed care approach could be translated to the workers' compensation field—has not proven out. It makes little sense, then, to continue to budget for this unit.

In addition, only $52,000 of certification fees were received in 1996-97. The Governor's budget estimates only $68,000 will be collected in 1997-98 and shows no money in the fund by June 30, 1998. This historical revenue stream makes it unlikely that $222,000 in fee revenues will be realized in 1998-99 as estimated in the Governor's budget.

Given this situation, we recommend funding for the MCU be deleted from the department's support budget, the program be terminated, and any unexpended balance remaining in the Workers' Compensation Managed Care Fund be transferred to the General Fund in partial repayment of the loan that was provided to fund the MCP's start up costs. Any workload involved in winding up the program can be handled by the department's other staff and budget.

Reduce Requested Increase for Rent

We recommend the Legislature delete the $4,110,000 augmentation for building rent costs because the budget overestimates the rental costs the department will incur when it moves into new state office buildings in San Bernardino, Los Angeles, Oakland, and San Francisco. (Reduce Item 8350-001-0001 by $4,111,000.)

The department proposes an augmentation of over $4.1 million for increased rent when it moves into new state office buildings in San Bernardino, Los Angeles, Oakland, and San Francisco. It includes one-time moving costs of $1 million, and increased rent in 1998-99 of $0.6 million each at San Bernardino, Oakland, and Los Angeles, and $1.3 million in San Francisco.

The new buildings will be managed by the Department of General Services (DGS) which will charge the department rent based on the amount of lease-payment bond costs due on the respective buildings plus the cost of operation and maintenance. The amount in the budget is based on the full cost of annual lease-payment bond costs. The Governor's budget, however, indicates that the lease-payment bonds for San Francisco and Los Angeles will not be sold in the budget year. In these buildings, therefore, the department will be paying only the operation and maintenance cost in 1998-99. In addition, in Oakland and San Bernardino, the department based its estimates on higher rental rates than DGS is actually proposing to charge. The result is that the department will actually have a $1 million reduction in building rental costs in 1998-99. Thus, there is no need for an augmentation and the DIR can absorb the moving costs of $1 million from the total reduction in rental costs. Consequently, we recommend the Legislature delete the requested $4,110,000 augmentation.

Wage Law Enforcement on Public Works Contracts

We recommend the Legislature delete $191,000 and 2.5 positions requested for enforcement of prevailing wages because under recent legislation the department's workload should decrease rather than increase. (Reduce Item 8350-001-0001 by $191,000.)

The DIR is charged with enforcement of statutes requiring the payment of prevailing wages on public works contracts. Recently enacted legislation has changed the responsibilities of prime and subcontractors in complying with these laws, and has extended the statute of limitations for filing suits in cases of dispute. The budget includes an increase of $191,000 and 2.5 two-year limited-term positions because of a workload increase it anticipates as a result of this new legislation.

Background. Effective the first of this year, several statutes in the Labor Code were amended by Chapter 757, Statutes of 1997 (SB 1328, Brulte). The act requires a prime contractor to include in its contract with a subcontractor, language requiring that prevailing wages be paid. It also requires the prime contractor to obtain an affidavit from subcontractors affirming that prevailing wages were, in fact, paid. It further requires the subcontractor to keep accurate payroll records of wages paid to workers at its principal office and to produce certified copies when requested. If a prime contractor is aware of a wage law violation and fails to take timely corrective action to halt or rectify the subcontractor's violation, the prime contractor will be liable for penalties imposed by DIR. The legislation further provides that the prime and subcontractor are jointly liable for any violations of the public works law and extends from 90 to 180 days the period after completion of the project or acceptance of the work within which the DIR may initiate a suit against the prime and subcontractor.

Workload Should Not Increase. In effect, this law (1) provides additional legal imperatives for both the prime contractor and subcontractors to comply with wage laws, (2) shifts wage law enforcement burden on to the prime contractor (with penalties for failure to do so), and (3) provides additional time for DIR to complete its investigative work when its intervention is required. As a result of this shift of responsibilities and increased liability for both the prime and subcontractor, we do not see DIR's workload increasing (in fact, some workload may decrease). Further, the additional time for investigative work should result in a more effective use of existing staff. Consequently, we recommend the Legislature not approve this request for $191,000 and 2.5 additional staff positions.

DEPARTMENT OF FOOD AND AGRICULTURE (8570)

The California Department of Food and Agriculture (department) promotes and protects the state's agriculture industry through marketing and industry inspections; develops California's agricultural policies; assures accurate weights and measures in commerce; and provides financial oversight to county, district, and citrus fairs.

The *1998-99 Governor's Budget* includes $198 million for the department, a 2 percent increase from estimated current-year expenditures. The budget total includes General Fund expenditures of $67 million, an increase of more than 5 percent from the current year.

Food Safety Program Not Defined

We recommend deletion of the requested $991,000 from the General Fund and eight positions for various food safety program augmentations until the department can present a comprehensive food safety plan to the Legislature for review. (Reduce Item 8570-001-0001 by $991,000.)

The budget proposes $991,000 from the General Fund (and eight positions) to support various activities related to food safety, as described below.

Cheese Surveillance Program ($389,000 and Four Positions). Currently, the department is responsible for ensuring the safety of all milk and dairy foods from farm origin to the point of final consumption. The department and the Department of Health Services (DHS) work cooperatively to respond to disease outbreaks related to dairy foods. This proposal would augment the current inspection and monitoring program to target imported and illegally manufactured cheeses.

Field Sanitation ($332,000 and Two Positions). The department currently conducts quality assurance inspections of fresh fruits and vegetables. This funding would support the review of field sanitation practices and procedures for fresh fruits and vegetables. Currently, the department is developing, in conjunction with private industry, preventive and remedial sanitation measures to reduce the risk of produce contamination.

Agricultural Waste ($106,000 and One Position). This augmentation is requested to address the potential of food contamination from agricultural waste.

Education and Training ($164,000 and One Position). This augmentation would provide resources to work with the private sector to establish a public-private partnership for food safety education, develop support materials, educate professional and high-risk groups, continue a long range planning process, and establish regular training and informational seminars.

Program Lacks Comprehensive Plan. The above augmentations are components of what the department refers to as the "Food Safety Program." An initial augmentation of $418,000 and four positions to enhance food safety measures relating to the production of animal products was approved by the Legislature in the *1997-98 Budget Act*. The budget proposal would significantly expand the department's current food safety activities. We are concerned that the department is requesting the Legislature to incrementally increase activities in this area without having the benefit of a comprehensive plan that identifies the goals and objectives of the program. Such a plan would also include an anticipated implementation schedule, staffing and budget requirements, and expected results of the program.

Based on available information, the department currently has no such plan for either the current-year or budget-year components of the food safety program. Until the Legislature has this type of program information, it cannot assess the appropriateness of the requested amount or what to expect as a result of providing the requested funds.

The department has apparently recognized the need to develop a comprehensive plan. In the department's strategic plan (published July 1, 1997), the department has *begun* some degree of planning for the food safety program. The department identifies eight objectives relating to food safety. Four of these objectives appear to directly relate to the department developing a comprehensive food safety program:

- Define jurisdiction and authority of department food safety activities in relation to other government agencies by June 1998.
- Develop a food safety management system by June 1999.
- Design a system to provide enhanced food safety programs.
- Enhance crop safety for consumer protection.

Coordination of Statewide Food Safety Responsibilities. It is especially important that the department delineate its program goals because it is not the primary state agency responsible for food safety. The DHS has jurisdiction for inspection of all food products. The DHS maintains oversight of the processed food industry through a fee-based inspection program, conducts epidemiologic investigations of disease outbreaks, assists county investigators when disease outbreaks occur, consults with members of the various health professions, and operates a regulatory food safety section.

The two departments have, in the past, cooperatively responded to disease outbreaks that can be linked to raw agricultural products. This activity has included joint investigations of suspected contamination at the farm level and coordinated inspections of the raw and minimally processed food product industries. Given the department's responsibility for and knowledge of the agricultural industry in California, this type of coordination is appropriate. Expanding the food safety program within Food and Agriculture without first clearly defining the program goals and objectives and coordinating this effort with the DHS, however, could lead to a program that duplicates and / or conflicts with the role of the DHS as the lead state agency responsible for food safety issues.

The program planning effort discussed above is important in order for the Legislature and the administration to assure that any increase in the food safety area is effective and cost efficient. The department should, in coordination with the DHS, expedite the development of this information. Pending completion of this effort and submittal of the results to the Legislature, we recommend the Legislature not approve the additional $991,000 and eight positions requested.

Domestic Parcels Inspection Program

We withhold recommendation on the $1,874,000 from the General Fund and 26.3 personnel-years requested for continuation and augmentation of the Domestic Parcels Inspection Program until the pilot program report, due March 1, 1998, has been submitted and reviewed.

The budget includes $1,874,000 from the General Fund and 26.3 personnel-years (PYs) for continuation and augmentation of the Domestic Parcels Inspection Program. This proposal would essentially double the size of the current pilot program.

The inspection program was initiated in the *1996-97 Budget Act* when the Legislature approved $895,000 from the General Fund and 14.6 PYs for a two-year pilot program. The program was initiated to provide inspection of domestic parcels for agricultural pests. The program currently includes eight dog teams—each team consists of one handler/biologist, one seasonal assistant, and one dog—that are deployed in the Los Angeles basin and the San Jose metropolitan area.

The teams inspect 44 private parcel facilities, considered high risk based on historical interceptions. Dog teams visit each facility a minimum of once per week to search packages for agricultural products. The department estimates that this level of coverage provides inspection of 15 percent to 17 percent of the parcels entering the state through the 44 facilities.

The department is due to submit a report to the Legislature on March 1, 1998, evaluating the effectiveness of the domestic parcels inspection pilot program. Pending review of the report, we withhold recommendation on the $1,874,000 request.

Agricultural Export Program Augmentation Not Necessary

We recommend that the Legislature delete a $464,000 augmentation from the General Fund for the Agricultural Export Program and a one-time equipment purchase for the department's chemical laboratory. The export program activities should be undertaken within current department resources and the equipment purchase should be funded through laboratory service fees. Reduce Item 8570-001-0001 by $464,000.

The budget proposes $464,000 from the General Fund for two positions and one-time equipment costs for the department to expand its efforts to relax international trade restrictions on the state's agricultural exports (specifically relating to chemical residues) by participating in meetings conducted by a subsidiary of the United Nations. This augmentation to the Agricultural Export Program would provide two additional staff to work with California agricultural exporters and participate in international meetings on establishing food product chemical residue limits. Included in the proposal is $180,000 for purchase of a mass spectrometer for the department chemistry lab.

The Agricultural Export Program, established in 1985, provides technical assistance and support to California agricultural exporters by coordinating trade missions, participating in trade shows; maintaining a comprehensive database, which includes market reports and trade statistics; and providing information to aid California exporters in gaining access to foreign markets.

The export program currently participates in many international events. Should the department determine that participation in the United

Nations subsidiary meetings is a priority, the department can allocate existing personnel and funding. However, the workload presented by the department does not warrant an augmentation.

Therefore, we recommend that the department fund these activities from its existing resources. We also recommend that the laboratory equipment purchase be made from fee revenue generated by laboratory services provided to the agricultural industry.

Marketing Campaign Not Necessary

We recommend that the Legislature delete a request for $82,000 from the General Fund for a new marketing campaign because this should be the responsibility of the agricultural industry and not the General Fund. (Reduce Item 8570-001-0001 by $82,000.)

The department is requesting $82,000 a year for a two-year period to develop a California Food and Agricultural Campaign. The marketing campaign would consist of a "California Grown" logo and associated advertising to distinguish California agricultural products from others in the marketplace. The department would establish a fee to be paid by program participants to provide funding after the two-year start up period.

Currently, there are 46 marketing programs that represent 40 different agricultural commodities produced in California. Approximately 62 percent of the agricultural economy in California is represented by these marketing programs. These programs are entirely self-supporting and function at no cost to the state. According to the department, research and promotion are the major functions of marketing programs—including promotions in both domestic and global markets. If the agricultural industry believes a "California Grown" marketing program would be beneficial to selling its products, the industry could develop the program independent of the state. In addition, if the industry believes the state should participate, the industry should pay the state the costs of developing and managing a marketing program for agricultural products. In either case, this should not be a General Fund expense. Consequently, we recommend the deletion of the requested $82,000.

Laboratory Contract Cost Increase

We recommend that the Legislature delete a $1,110,000 General Fund augmentation for the department's contract for services from the California Veterinary Diagnostic Laboratory System because the department has not justified the higher contract costs. Reduce Item 8570-001-0001 by $1,110,000.

The budget contains a $1,110,000 General Fund augmentation to the department budget to increase the contract costs for services provided by the California Veterinary Diagnostic Laboratory System. The laboratory was established in 1918 and was operated as a program within the department until 1987-88 when the University of California (UC) at Davis took over responsibility for management of the laboratory. The laboratory employees are UC employees and are covered by UC personnel policies, including salary adjustments. The department contracts with the laboratory to provide diagnostic services for its animal disease control program.

In the 1997-98 budget the department requested a $509,000 augmentation to fund salary increases granted to employees at the laboratory by the UC. The Legislature denied this augmentation. Additionally, the Legislature adopted supplemental report language directing the department not to approve an increase in the annual contract costs for operation of the laboratory without prior legislative approval and to forward a copy of the annual contract costs to the Legislature by December 31 of each year.

Budget Proposal. Instead of identifying the proposed $1.1 million augmentation as a change to the department's budget, the administration simply made a "baseline adjustment." Therefore, although the department's budget is increased by $1.1 million, the Governor's budget does not identify or explain this change.

Legislature Needs Workload and Cost Increase Detail. The department has provided limited information that identified two main reasons for the requested augmentation: cost increases generated by the UC and increasing workload. However, the department has not provided workload detail or the basis for the cost increase. Lacking any information substantiating the need for an additional $1.1 million, we recommend that the Legislature not approve this request. If the department provides adequate justification for the requested increase, a proposal to increase the contract cost may warrant review by the Legislature.

FAIR POLITICAL PRACTICES COMMISSION (8620)

The Fair Political Practices Commission (FPPC) was established in 1974 to implement and administer the Political Reform Act (PRA), an omnibus measure designed to improve the elections process in California for candidates for state and local office. The act (1) established rules for the disclosure of money received and spent by candidates seeking political office, (2) required state ballot pamphlets to have useful and understandable information, (3) established lobbyist activity disclosure regulations, and (4) required the disclosure of assets of public officeholders and barred conflicts of interest with their official decision making. The California Political Reform Act of 1996 (CPRA), established by Proposition 208, among other provisions established specific limits on the amount and source of campaign contributions and established voluntary campaign spending limits for candidates.

The provisions of the PRA and CPRA are carried out by four state agencies, including the FPPC (the other agencies are the Secretary of State, Department of Justice, and the Franchise Tax Board). The FPPC adopts regulations, establishes procedures to monitor compliance, and provides advice to officeholders regarding the requirements of the PRA and CPRA. The FPPC also investigates alleged violations of the laws and imposes sanctions on violators.

The PRA provided a $1 million annual appropriation to the FPPC. The CPRA provided an additional $500,000 annual appropriation to the commission. By law, the amounts are to be adjusted each year for changes in the cost of living. The PRA further provides that the Legislature shall provide such additional amounts as may be necessary to the FPPC and other state agencies to carry out the political reform laws.

The budget proposes total expenditures of $6 million for the FPPC in 1998-99. This is almost exactly the same amount the commission is estimated to spend in the current year.

Court Ruling on Proposition 208 Brings Spending Plan into Question

Because a federal court recently ordered the Fair Political Practices Commission (FPPC) to halt enforcement of the California Political Reform Act of 1996 (CPRA), we withhold recommendation on $1.2 million and 22 personnel-years for the support of commission activities to carry out the law. We recommend that the FPPC report at budget hearings on the status of that and other pending legal cases related to the CPRA and, if necessary, submit a revised budget request.

In November 1996, California voters approved Proposition 208, the initiative ballot measure enacting the CPRA. The *1997-98 Budget Act* included $1.2 million and about 22 personnel-years for the FPPC's legal, enforcement, technical assistance, and administrative divisions to implement the CPRA. The budget limited the terms of the new positions and the related funding until December 31, 1998, because of the uncertainty as to whether the CPRA would withstand pending legal challenges to its constitutionality. The proposed 1998-99 budget for the FPPC includes a request for $790,000 to continue the 22 personnel-years for CPRA-related activity for the duration of the budget year.

Court Invalidated New Law. About the time the proposed FPPC budget was submitted to the Legislature, however, a federal district court ruled that the campaign contribution limits in the measure were unconstitutional. The court indicated that some other provisions of the law may be legal. Accordingly, the court enjoined the FPPC from enforcing any part of the CPRA for now and ordered the FPPC to file a petition before the California Supreme Court to determine whether some portions of the law could be legally separated and allowed to take legal effect at a later date. The FPPC is appealing the federal court decision.

As a result, it is highly uncertain at this time what staffing and funding the FPPC will need, and for what purposes, to carry out the CPRA in the budget year. If the FPPC were to prevail in its appeal and succeeded in overturning the recent court ruling, it may be appropriate for the Legislature to approve the 1998-99 budget request as submitted. If the court injunction were to stand, or if new rulings affecting enforcement of the law were to be issued as a result of four other pending legal challenges to the CPRA, the request should be modified.

Some Staffing and Funds Needed. The FPPC has indicated that, even if the recent court injunction were to stay in effect during the entire budget year, it will need some level of staffing and funding to challenge the federal court decision and to simultaneously carry out the federal court's mandate to pursue related legal issues before the California Supreme Court.

Analyst's Recommendation. Under these circumstances, we believe the Legislature should wait until later in the budget process to determine the 1998-99 budget appropriation for the FPPC. Thus, we withhold recommendation at this time on the $1.2 million and 22 personnel-years provided in the FPPC's budget proposal for CPRA-related activity. We further propose that the FPPC report to the Legislature at budget hearings regarding the status of ongoing litigation over the CPRA and, given the standing of the legal matter at that time, submit a revised request as necessary for funding and staffing in the budget year

BOARD OF EQUALIZATION (0860)

The Board of Equalization (BOE) is one of California's major tax collection agencies. The BOE collects state and local sales and use taxes and a variety of business and excise taxes and fees, including those levied on gasoline, diesel fuel, cigarettes, and hazardous wastes. The BOE is responsible for allocating tax proceeds to the appropriate local jurisdiction(s). The BOE also oversees the administration of the property tax by county assessors and assesses property owned by public utilities. The BOE is also the final administrative appellate body for personal income and bank and corporate taxes, as well as for the taxes it administers.

The *1998-99 Governor's Budget* proposes approximately $300 million in support of the board's operations, $184.6 million of this total is from the General Fund. The total proposed budget is less than a 2 percent increase from the current year and includes a $1.6 million ($1.2 million from the General Fund) augmentation for merit salary adjustments. Again, this year the BOE is one of three departments that receives an augmentation for merit salary adjustments. The others are the Franchise Tax Board and the Department of Corrections.

Request for Funding to Implement Legislation Is Premature

We recommend the Legislature delete the proposed increase in reimbursement authority for the Board of Equalization (BOE) to implement Chapter 702, Statutes of 1997 (SB 110, Dills) because the BOE has not approved an implementation plan for this legislation. (Reduce Item 0860-501-0995 by $4,177,000.)

The budget proposes $4.2 million in increased reimbursement authority and 85.5 positions to implement Chapter 702. Chapter 702 contains two major provisions, the first requires the BOE to issue a "use tax direct payment permit" that will allow the purchasing taxpayer to self-assess and pay state and local use tax directly to the BOE rather than relying on the information provided by the selling taxpayer. The second provision, and the most significant in terms of potential workload, requires the BOE to allocate use tax revenue separate from sales tax revenue. Currently, use tax and sales tax revenue are pooled for allocation. Under Chapter 702, use tax revenues would have to be separated from sales tax revenue (not currently done by the BOE) and then allocated to the appropriate jurisdiction.

We recommend that the Legislature delete the proposed augmentation. The BOE has not determined how to implement Chapter 702. In fact, at a recent meeting the BOE disapproved a similar proposal in the current year. It is our understanding that the BOE is reconsidering how to implement Chapter 702 and what additional workload and associated costs, if any, may be required. Consequently, at this time, it is not clear either when the BOE will begin implementing Chapter 702 or what additional costs and staffing levels, if any, will be required. Until this information is available to the Legislature, it is premature to authorize the expenditure of nearly $4.2 million and the hiring of 85.5 positions. Once the BOE has established an implementation plan, a proposal for the necessary funds and staff would warrant legislative consideration.

The BOE Audit Programs

The Legislature adopted language in the *Supplemental Report of the 1997-98 Budget Act* directing the BOE to report on its audit program. The purpose of the reporting requirement was to provide the Legislature with information to evaluate the effectiveness of the BOE's audit programs.

The reporting requirement was implemented as a result of issues we raised during 1997-98 budget hearings concerning the BOE's calculation of (1) its benefit-cost ratio on audit spending and (2) the impact on revenues of changes in nonaudit-related programs. The report has been submitted. We are in the process of reviewing it, and we will, if appropriate, make recommendations to the Legislature during budget hearings.

FRANCHISE TAX BOARD (1730)

The Franchise Tax Board (FTB) is one of the state's major tax collecting agencies. The FTB's primary responsibility is to administer California's Personal Income Tax and Bank and Corporation Tax laws. The FTB also administers the Homeowners' and Renters' Assistance Programs and the Political Reform Act audit program. In addition, the FTB administers several nontax programs including collection of child support and motor vehicle registration delinquencies, collection of court-ordered payments, and collection of student loan delinquencies. A three-member board—consisting of the Director of Finance, the Chair of the State Board of Equalization, and the State Controller—oversees the FTB. An executive officer is charged with administering the day-to-day operations of the FTB.

The *1998-99 Governor's Budget* proposes $384 million in support of the FTB, a 2.2 percent increase over the current year. The majority of FTB's operations are funded from the General Fund. The total proposed General Fund support is $358.2 million. Included in the budget is a $2.3 million merit salary adjustment. Again this year, the FTB is one of three departments to receive an augmentation for merit salary adjustments. The others are the Board of Equalization and the Department of Corrections.

Augmentation for Workload Growth Not Justified

We recommend the Legislature delete the proposed $3 million General Fund augmentation and 65.8 positions to address projected growth in tax return processing because the Franchise Tax Board has been unable to justify the need for these positions. (Reduce Item 1730-001-0001 by $2,992,000.)

The budget proposes a $3 million General Fund augmentation (65.8 positions) to the FTB for expected workload growth in income tax return processing. We have several concerns with this request. First, in the current year the FTB received a similar augmentation (totaling

$5.3 million and 96.1 two-year limited-term positions) to accommodate workload growth in return processing. Instead of using this augmentation for the purposes approved by the Legislature, however, the FTB is holding 51 of the limited-term positions vacant and using the funds associated with these positions to fund other, *permanent* positions. The FTB indicates that this action was taken in order to meet their salary savings requirement. The FTB budget, however, includes only a four percent salary savings requirement which is lower than most state agencies. Thus, it is not clear why the FTB would have to arbitrarily hold any positions open.

Additionally, the FTB did not experience the level of growth in personal income tax returns expected in the previous year. Thus, the augmentation received for the previous year should be sufficient to accommodate at least some of the board's processing needs in the budget year.

Given the many issues surrounding the agency's request, we recommend that at this time the Legislature delete the proposed augmentation.

Separate Preprinted Labels for Tax Returns

We recommend the Legislature delete the proposed $1.2 million General Fund augmentation to provide a separate preprinted label to taxpayers because taxpayers can provide the necessary information on their tax returns. (Reduce Item 1730-001-0001 by $1,231,000.)

The budget proposes $1.2 million from the General Fund and four positions to implement Chapter 685, Statutes of 1997 (SB 458, Peace). This legislation prohibits all state agencies from sending any outgoing United States mail to an individual that contains personal information (including social security numbers) unless that information is contained within sealed correspondence and cannot be viewed from the outside.

Currently, the FTB sends out personal income tax booklets and forms with a pre-printed address label that the taxpayer then places on their tax forms when submitting them to the FTB. These pre-printed address labels contain the taxpayer's social security number or their taxpayer identification number.

To modify the current practice to conform with Chapter 685, the FTB proposes to eliminate the social security or taxpayer identification number from the pre-printed address label and instead include a second preprinted label in an envelope attached to the outside of the tax booklet. Taxpayers would then remove the preprinted label from the envelope for use on their tax returns. The FTB indicates that to implement this change would require an additional $1.2 million from the General Fund and four positions in the budget year. Approximately $1 million dollars would be annual ongoing costs.

The FTB processes approximately 14 million personal income tax returns annually. Of those, approximately 40 percent are received without a preprinted label. There are no data to indicate that the FTB experiences a higher error rate on returns that are sent in without a preprinted label. In addition, the FTB currently has verification procedures in place to catch incorrectly entered numbers.

Given this, we recommend that the FTB simply not print the confidential numbers on the address label and rely on taxpayers to enter the numbers themselves. If this process results in the FTB receiving a significantly larger number of returns with incorrect or illegible social security numbers, the need for this proposal could be revisited. At this time, however, we recommend that the Legislature reduce Item 1730-001-0001 by $1,231,000.

Department Expects to Miss Critical Failure Date for Year 2000 Implementation

The department should report to the Legislature on the status of modifying critical information technology systems to accommodate the year 2000 change.

The FTB indicates that the Taxpayer Identification System and Return Validation System are "mission critical" information technology systems for the department's operation. This designation "mission critical" means that operation of the systems support the department's main function, which is collection of tax revenue. According to the FTB, if the systems are not modified on time to be year 2000 compliant, the FTB will experience a delay in processing returns, collecting revenues and issuing refunds. Additionally, the FTB indicates that because of the processing functions of the systems and the size of the system databases (the Taxpayer Identification data base stores approximately 14 million accounts) there is not a viable contingency plan if the systems become nonfunctional due to noncompliance with the year 2000 modifications.

The FTB indicates the first failure date for both systems is April 15, 1998 and that the systems won't be remediated until July 1998 (taxpayer identification) and September 1998 (return validation). The FTB has also indicated that failure of these systems would negatively affect other nontax functions (child support collections, Department of Motor Vehicles delinquent registration collection, and court-ordered debt collections) by providing incorrect data. Since the FTB shares information with other entities (Board of Equalization, Employment Development Department, and Department of Corrections) any errors or malfunctions in the computer systems at the FTB also may cause those systems to fail.

In view of this situation, the FTB should report to the Legislature on the status of modifying all information technology systems to be year 2000 compliant. The report should address the current operations of the FTB since its "mission critical" systems are not projected to be year 2000 compliant before the failure dates.

Franchise Tax Board Tax Audit Program

The Legislature adopted language in the *Supplemental Report of the 1997-98 Budget Act* directing the FTB to report on its audit program. The purpose of the reporting requirement was to provide the Legislature with information to evaluate the effectiveness of the department's audit programs.

The reporting requirement was implemented as a result of issues we raised during 1997-98 budget hearings concerning the FTB's calculation of (1) its benefit-cost ratio on audit spending and (2) the impact on revenues of changes in nonaudit-related programs. The report has been submitted. We are in the process of reviewing it, and we will, if appropriate, make recommendations to the Legislature during budget hearings.

DEPARTMENT OF INFORMATION TECHNOLOGY (0505)

The Department of Information Technology (DOIT) is responsible for planning and overseeing the state's use of information technology by ensuring that appropriate plans, policies, and procedures are in place to assure successful implementation of projects. The DOIT was created by Chapter 508, Statutes of 1995 (SB 1, Alquist), in response to the difficulties the state experienced in attempting to successfully deploy information technology projects.

The budget proposes $8.5 million ($7.7 million from the General Fund) for support of the department's operations in 1998-99, an increase of $1.5 million, or 21 percent, over estimated current-year expenditures. Current-year expenditures include $2 million transferred from Item 9899 of the *1997-98 Budget Act* for DOIT's work on the year 2000 computer conversion projects. The increase in the budget year is proposed to support 19 new positions, as well as additional external consulting services.

Department Still Needs to Develop Information Technology Policies

We recommend the adoption of budget bill language appropriating $437,000 for initiation and implementation of information technology projects once the Department of Information Technology develops a number of specific information technology policies.

Budget Proposal. The proposed budget includes establishment of two positions and $437,000 for consulting services to carry out information technology planning and project initiation. This request was initially approved by the Legislature in 1997-98, but was eliminated at the end of last year's budget process as part of the Public Employees' Retirement System loan repayment decision.

Background. Last year, we reported that the department indicated it was on the verge of completing a number of tasks which must be accomplished in order for it to fulfill its statutory oversight responsibilities. Among these tasks were development of policies regarding initiation and oversight of information technology projects, disaster recovery, information security, and improved reporting to the Legislature regarding information technology projects. Since last year, DOIT has not established formal policies for most of these issues, although the department has taken informal positions on some of these matters.

Specific Project Development Policies and Procedures Needed. Currently, departments submit project proposals to DOIT for review. After reviewing and approving a project, DOIT sends a letter of approval to the department indicating the conditions under which the project has been approved. Although DOIT supports the use of project initiation and deployment standards used in the private sector, it has yet to establish formal policies on:

- Use of independent oversight to ensure the proposed system does what the state wants it to do.
- Appropriate level of project management experience necessary.
- Whether a cost- or needs-based procurement should be conducted.
- Whether the vendor should provide a letter of credit or performance bond.
- How large a project should be.
- Whether the department should request the intellectual property rights from the vendor.
- Whether a department should use DOIT's risk assessment model.
- When development of a risk mitigation plan is necessary.

As a result of not having policies, the conditions required in the letters of approval come unexpectedly. Departments must then implement DOIT's recommendations after they have already begun planning for the project. Establishing these policies in advance of departments beginning their project planning could further improve the planning phase. Although DOIT generally supports these concepts (which are often referred to in the information technology industry as "best practices"), it has not developed and distributed a statewide policy on these and many other important issues as we discuss below.

Policy on Minimal Qualifications for Project Managers Still Critical. The *Supplemental Report of the 1997-98 Budget Act* required DOIT to report to the Legislature quarterly, beginning in September 1997, on its progress in providing training and certification of project managers. In response, the DOIT has entered into a partnership with the University of California, Davis to develop a project management training program which has since enrolled its first class of students. Because it is a two-year effort, projects are currently underway which are being managed by personnel not necessarily experienced or knowledgeable in project management skill sets. Additionally, since the training program is completely voluntary, it is unclear how many existing state project managers plan to complete it. Consequently, the impact of this training program is likely to be limited without a policy requiring such training.

It is also important that DOIT establish a policy that identifies minimum qualifications to be a project manager. Additionally, DOIT should review the qualifications of the project managers on all major information technology projects and decide whether their skills need to be augmented with public sector managers or private sector consultants who have the necessary project management experience.

Progress Still Needed on Procurement Policy Reform. In 1994, the Governor's Task Force on Government Technology Policy and Procurement identified the procurement process as one of the major obstacles to successful deployment of major information technology projects in California. Three years have elapsed since the report was issued and California uses the same policy to procure major projects today as it did then.

In the *1997-98 Budget Act*, the Legislature required DOIT, in cooperation with the Department of General Services (DGS), to develop recommendations for improving the current state contracting practices so that contract awards are needs-based, not cost-based. In vetoing the language, the Governor indicated that it was not necessary because DGS had already developed such recommendations in pending procurement reform legislation. However, DGS' reform efforts have yet to be adopted by the Legislature. More importantly though, Chapter 508, the measure that created DOIT, clearly requires DOIT to develop procurement policies for information technology. Therefore, DOIT should develop and implement procurement policies for information technology goods and services, while DGS develops procurement policy for commodities.

Department Should Adopt Policy to Make Funding Requests Understandable. The *1997-98 Budget Act* directed DOIT to develop a process to better coordinate between DOIT and the Department of Finance (DOF) the approval of departmental requests for information technology project funding. In response to the legislative directive, DOIT has adopted a new process that should result in more timely approval of proposed projects.

Although the process has been improved, the quality of the information contained in the documents has not. In general, state departments advise the Legislature about information technology projects through feasibility study reports (FSRs) for proposed new projects and special project reports (SPRs) when significant changes occur to existing projects.

In many cases, the documents provided to the Legislature are difficult to understand because they are poorly prepared and do not contain important summary information. To correct at least part of this problem, Chapter 508 required that these documents contain specific summary information at the front of the document. The DOIT has yet to require this summary information from departments. In the absence of this information, it is extremely difficult and sometimes impossible to evaluate the proposal. Consistent with its enabling statute, DOIT should create a form requesting summary information for departments to transmit to DOF, DOIT, and the Legislature with each FSR and SPR.

Policy to Advise Legislature of All Major Information Technology Projects Needed. Under current state policy, departments are required to notify the Legislature whenever they transmit an FSR or SPR to DOIT for review. Although this policy results in the Legislature being notified of some major information technology projects, many are not reported because state policy allows DOIT to delegate to departments the authority to approve their own projects. As a result, these departments are not required to report projects or funding amounts to the Legislature on these projects.

Given the unresolved problems with the state's information technology infrastructure, including telecommunications and networks, we believe that the Legislature should be notified of projects that would have to be reported had the department not received delegated authority. We recommend DOIT establish a policy on notifying the Legislature when funding is requested for these information technology projects. This would provide the Legislature with more complete information on projects and funding.

Analyst's Recommendation. In summary, we recommend that the Legislature adopt budget bill language directing DOIT to develop and distribute policies, per its enabling legislation, on the following:

- When a department should hire an independent oversight vendor.
- When a department should require a letter of credit or performance bond from the vendor.

- What is an appropriate size of a project.
- When acquiring intellectual property rights is appropriate.
- When a risk assessment model should be conducted on a project.
- When a risk mitigation plan needs to be developed.
- The level of experience project managers should have.
- How to determine whether a procurement should be cost- or needs-based.

In order to ensure the enactment of the policies, we recommend that the budget request for planning and project initiation be tied to completion of the policies. Specifically, we recommend the following budget bill language:

> In addition to the funds otherwise appropriated by this item, the sum of $437,000 is hereby appropriated from the General Fund for the support of the Department of Information Technology for the 1998-99 fiscal year. The appropriation made by this provision is not available unless and until the Department of Information Technology drafts or produces final policies establishing (1) when a department should hire an independent oversight vendor, (2) the level of experience project managers should have, (3) how to determine whether a procurement should be cost- or needs-based, (4) when a department should require a letter of credit or performance bond from the vendor, (5) what an appropriate size of a project is, (6) when acquiring intellectual property rights is appropriate, (7) when a risk assessment model should be conducted on a project, (8) when a risk mitigation plan needs to be developed, (9) summary information that should be contained in the front of funding documents, and (10) notification to the Legislature of information technology projects which are being conducted under delegated authority. Final policies shall be distributed to state departments prior to June 30, 1999.

Project Cost and Schedule Estimates Are Rarely Accurate

We recommend that the Legislature adopt supplemental report language directing the Department of Information Technology to require that feasibility study report transmittal letters and special project reports contain the administration's assessment of the sensitivity to change of the costs, benefits, and schedules contained in these documents.

Over the past several years, we have identified several major information technology projects where costs have increased significantly above the original or updated estimates. The problem of inaccurate project estimates is not new and is not unique to public sector projects. Nevertheless, the Legislature continues to be asked to approve budgets for information technology projects which are based on cost estimates which are likely to change, most often in an upward direction. Project implementation schedules are often optimistic as well.

Given this situation, we believe that FSR and SPR transmittal letters for information technology projects should address the probability that cost, benefit, and schedule estimates are likely to be accurate, including any qualifications regarding those estimates. To help improve the meaningfulness of budget requests based on estimates contained in information technology project-related documents, we recommend that the Legislature adopt the following supplemental report language:

> The Department of Information Technology shall require that feasibility study report transmittal letters and special project reports address the sensitivity to change of the cost, benefit, and schedule estimates contained in these reports.

The DOIT's Advocacy Role Conflicts With Oversight Responsibilities

We recommend that the Legislature approve the Department of Information Technology's funding request for additional resources to institute the new funding approval process, but require the resources requested for advocacy be redirected to responsibilities the department is required by statute to fulfill.

Budget Proposal. The *1997-98 Budget Act* required DOIT, in collaboration with DOF, to develop a new process for the initiation and approval of information technology projects. The DOIT published a report in December 1997 outlining the new process. The budget proposes six additional personnel-years and $288,000 in consulting services to implement the new process. As a component of the new process, DOIT indicates its intention to become an *advocate* for departments before the legislative budget hearings once an information technology project is approved.

Analyst's Recommendation. The enabling legislation which created DOIT required the department to establish policy in a number of significant areas. Since DOIT has yet to establish these policies as discussed above, it would appear as though the proposed resources devoted to advocacy in the funding request could be better used to meet the department's statutory requirements. Alternatively, as we indicate later in this analysis, DOIT has limited resources for year 2000 remediation activities and these resources could be used for such efforts.

Additionally, it would appear as though a department which is supposed to critically assess a project from initiation through its life cycle would have a conflict of interest as an advocate for the project. In fact, DOIT itself has stated that it believes an oversight body should be severed from the unit it is overseeing. In its 1996 Annual Report, the department wrote: "The most effective project oversight is applied in a condition of independence, i.e., the individuals performing project oversight must be detached from the organizational chain of command."

In view of the above, we recommend that the Legislature approve DOIT's augmentation, but require the resources proposed for advocacy be redirected to responsibilities DOIT is required by statute to perform.

State Civil Service Classifications Still Need Reforming

We recommend that the Department of Information Technology report to the Legislature, prior to budget hearings, on its progress and plans to change the civil service classification system to improve the state's access to information technology expertise.

In 1994, the Governor's Task Force on Government Technology Policy and Procurement identified the state's civil service classifications as too rigid and a barrier to hiring information technology expertise at higher than entry-level positions. The state's hiring policies require departments, as a general rule, to hire at the entry level. In some cases, this limits a department's ability to hire personnel with extensive experience. Additionally, the task force noted that the state is unable to match private sector salaries in this employment field.

To resolve this problem, DOIT indicated in its 1996 Annual Report that it is involved in reforming information technology civil service classifications. However, we are unaware of any steps taken in this regard. Consequently, we recommend that DOIT report to the Legislature, prior to budget hearings, on the progress that has been made in addressing the civil service classification issues identified in the Governor's task force report.

Department Continues to Be Leader On Year 2000 Conversion

In the last year, the Department of Information Technology has continued to provide leadership to state agencies in planning the conversion of their computer programs to accommodate the millennium change. We recommend that the Legislature approve the department's request for

additional resources in 1998-99 for oversight of the year 2000 conversion efforts. We also recommend that the Legislature direct the department to take a number of additional steps with regard to the conversion.

In the 1960s and 1970s when mainframe computer capacity was expensive, programmers established a standard for identification of dates in order to reduce the amount of space needed. By using the last two digits to represent the year (for example, 1973 was designated as 73), computing costs were reduced. With the new millennium approaching, these computer systems must now distinguish between dates in the 1900s and the 2000s. Computers, both in the public and private sectors, are unable to distinguish between these dates and must be modified to accommodate the change to the year 2000 (Y2K).

Failure to make the Y2K change will for some systems simply produce undetectable erroneous calculations, but some systems will completely fail. The "failure date," as it is known, is not necessarily January 1, 2000. For some systems in California, it has been as early as 1995, because these systems were required to provide dates into the future (for example, licenses that were granted in the mid- to late 1990s that will expire after the year 2000).

The Y2K conversion poses a significant problem because (1) California has never undertaken such a large statewide information technology project; (2) in most cases, it is probably too late to begin to deploy a replacement system, as opposed to modifying a system, thus limiting choices in how to respond to Y2K; and (3) as we approach the year 2000, resources are likely to become more scarce and prices will increase.

Budget Proposal. The budget proposes an augmentation of four limited-term positions and $302,000 for consulting services for DOIT's Y2K program. This would increase to seven the number of positions which currently staff the program. With this augmentation, DOIT proposes to use its Risk Assessment Model (RAM) on each project to determine risk and prioritize high risk projects for additional oversight.

The DOIT Started Early and Continues to Plan For Compliance. The administration initially focused attention on this problem when the Governor's Office of Information Technology (now DOIT) was established in late 1995. Significant effort to develop a strong program was made in 1996. In October 1996, DOIT published a "white paper" describing the Y2K problem. In November 1996, the DOIT issued the "California 2000 Program Guide" which identified the DOIT's approach to fixing the Y2K problem. Additionally, DOIT established a Y2K site on its home page which facilitates the exchange of information on policies and process.

The DOIT identified almost 3,000 state computer systems, of these 1,100 are either fixed already or do not need to be fixed. Of the remaining 1,900 systems, 650 are mission critical, meaning that they enable the department to carry out its primary responsibilities such as issuing drivers' licenses, collecting taxes, et cetera. The remaining 1,250 systems were identified as essential but not mission critical and will also need to be fixed. The DOIT's approach to addressing Y2K issues is contained in its program guide.

The California 2000 Program Guide. The program developed by DOIT requires departments to: (1) create an inventory of existing systems, (2) identify those that are critical to the overall mission of the department or program, (3) assess the impact the century change will have on these mission critical systems, and (4) develop a plan to fix them and submit this plan to DOIT along with its budget and schedule for Y2K conversion activities. Departments were required to identify the impact mission critical computer systems have on the department, outside entities with whom it exchanges information, and the public.

The DOIT Continues to Be Proactive. In addition to creating the program guide, DOIT has proactively:

- Begun to create a plan to upgrade embedded chip technologies, such as facsimiles, elevators, security systems, and more.
- Offered seminars on the impact of litigation and ways to minimize litigation.
- Sponsored a convention to create a forum to discuss the interdependence of state departments, local and federal government systems in the context of Y2K.
- Begun to develop a white paper and seminar on how to plan and execute testing of systems.
- Begun to develop a program to help departments identify and minimize liability and recover some of its Y2K costs from responsible vendors.
- Begun to develop information to help departments identify and resolve desktop Y2K related issues.

Although DOIT has taken a proactive role on Y2K issues, we have the following concerns with some of its efforts.

Value of Validation Statements, as Implemented, Appears Questionable. Last year, the Legislature required DOIT to review the plans for departments requesting an augmentation in funding for Y2K efforts and issue a Statement of Validation for each project. Once the statement was issued by DOIT, the DOF was to release the funds for the project. The required components of the Statement of Validation are shown in Figure 5.

Figure 5

Year 2000 Program (Y2K) Statements of Validation

Required Components
✔ Reasonableness of the state agency's strategy for addressing its Y2K problems.
✔ Comprehensive systems inventory, an assessment of year 2000-impacted systems and the scope of work to address Y2K problems.
✔ Extent to which the department's plan is aligned with the Department of Information Technology's (DOIT) Y2K methodology.
✔ Consistency of the department's proposal with information available to DOIT, including plans, schedules, and costs.
✔ Extent to which the department's systems are critical to its business with a prioritization of these systems and a consequence of failure.
✔ Identification of high risk activities.
✔ Assumptions and methods used to estimate the resources required.
✔ Redirection of resources within the department.
✔ Coordination of statewide and interdepartmental implementations of interdependent year 2000 affected systems.

Our review of the Statements of Validation has found that they are merely restatements of a department's plan. Although all of the information included is helpful, the statements do not (1) evaluate plans on the degree of reasonableness, (2) determine the accuracy of the estimation of resources, or (3) coordinate the projects with the statewide Y2K efforts. In fact, some Statements of Validation were issued for departments whose plans indicated the department would be a year behind schedule and contained no contingency plan.

The analysis on the degree of reasonableness of the plans is important because if realistic plans are not established then the chances for modifying the computer system on time decrease. Due to the large number of Y2K projects, we believe that it will be difficult for DOIT to complete such a thorough analysis even with the department's proposed budget augmentation.

Quarterly Reports Provide Few Details. The *Supplemental Report of 1997-98 Budget Act* required DOIT to report on October 15, 1997 and quarterly thereafter, on the status of the state's Year 2000 conversion efforts. In addition to other issues, DOIT was to identify any program which it believes is at risk of not completing necessary conversion in a timely manner. For those programs at risk, DOIT was to identify the factors which create the risk and what steps are being taken to mitigate the risk. Lastly, DOIT was to update the estimate of the costs to accomplish Y2K compliance.

The DOIT has submitted two quarterly reports thus far. Each report indicated DOIT's concern with the state's ability to fix all of its mission critical systems in a timely manner. However, the reports did not identify any projects at risk of failing, steps being taken to mitigate risk, or provide a revised total project cost estimate. The DOIT did decide to meet individually with each of the departments with high risk projects to review their plans. For high risk projects, DOIT will require monthly updates and take appropriate action including escalation and intervention.

Shortfalls in Oversight of Departmental Plans. Although the Y2K plans DOIT requires departments to complete contain important information, DOIT has limited staff resources to follow up on those that are deficient. This is a significant shortcoming because some departmental plans filed with DOIT indicate the department's efforts will not be completed until a year after the computer's failure date; that the department has no contingency plan; and that potentially hundreds of millions of dollars are at risk of not being collected as a result. The DOIT has not required departments in such situations to submit detailed contingency plans or to explain how they would continue to function without an operational system.

Some Y2K plans submitted by departments include timelines which are too optimistic, with many not allocating enough time to test the finished products. In fact, if departments followed DOIT's suggested time line, all departments should be concluding development and moving into the testing phase now. However, as of January 1998, few departments had reached the testing stage. Additionally, even for those departments whose plans project completion before the computer's failure date, there is not enough time to invoke a contingency plan, should one be needed. Thus, although DOIT required departments to submit Y2K plans, the plans do not necessarily protect the state's assets and DOIT does not appear to have the resources to review each plan in detail and require specific remediation steps.

Costs Continue to Rise. In our *Analysis of the 1996-97 Budget Bill*, we estimated that efforts to fix the state's systems could exceed $50 million. In April 1997, DOIT projected costs at $83 million. After departments had submitted the first planning report, DOIT revised the cost estimate to $187 million in July 1997. In January 1998, DOIT calculated that project costs will exceed $240 million, based on an ex-trapolation of costs presented in the last quarterly reports submitted by departments.

We believe the costs for Y2K conversion will be substantially higher than DOIT's most recent estimates. The $240 million estimate DOIT provided in January 1998 does not include (1) conversion of essential, but nonmission critical systems such as payroll and accounting; (2) efforts to remediate embedded chip technologies; (3) legal review of existing contracts to determine liability for expenses and failure to perform, currently projected to cost 40 percent of total remediation expenses (on that basis, approximately $100 million for California); (4) complete replacement of computer systems where necessary; (5) departments which do not report to DOIT (Judiciary, Legislature, University of California, California State University, Community Colleges, and others); and (6) the redirection of personnel-years which DOIT currently estimated are valued at over $500 million. If all of these costs were to be included, we estimate that efforts to fix the state's systems could easily cost $1 billion.

What Else Should DOIT Do? Figure 6 (see next page) outlines DOIT's current Y2K program, and what we believe should be added. As we outline in the Crosscutting Issues section of this chapter, although DOIT developed a program early that contains important components, we believe that there are several steps the state—through DOIT—can take to strengthen its Y2K Program.

Analyst's Recommendation. We recommend that the Legislature approve DOIT's proposed budget request in order to ensure DOIT can increase its oversight of Y2K activities. Additionally, we recommend that the Legislature direct DOIT to prioritize its statewide efforts based on the most critical Y2K conversions; require departments to create detailed contingency plans for each mission critical project; enhance project management on high risk projects; and plan to fix systems that are essential, but may not be mission critical.

Figure 6

Department of Information Technology's (DOIT) Year 2000 (Y2K) Program

DOIT Y2K Program required:

- Inventory of all computer systems.
- Prioritization of mission critical systems within the department.
- Development of a plan to remediate mission critical systems.
- Estimate of cost to remediate.
- Filing of quarterly progress reports.

To complement the Y2K Program, DOIT has also:

- Conducted a seminar to review legal issues related to system failure.
- Begun creation of a plan to fix all noninformation technology embedded chips (security badges, facsimile machines, building environment, elevators, et cetera.)
- Established Master Services Agreements to facilitate departments in hiring vendors to assist in remediation efforts.
- Crafted contract language to require all new information technology purchases to be Y2K compliant.
- Created a web site to serve as a clearinghouse for Y2K information.

What DOIT should also do:

- Require establishment of detailed contingency plans which include a date in which the plan is invoked if the proposed project has not met its goal.
- Prioritize projects statewide by revenue generated, public safety impact, impact on other departments' systems, impact to citizens, or other criteria it determines are most important.
- Concentrate resources on projects in these categories which are having difficulty meeting deadlines.
- Continue to deny requests for specified new information technology projects thereby concentrating resources on Y2K efforts.
- Take a more proactive role to keep projects on schedule, including intervening when necessary.

The DOIT Needs to Develop Data Center Configuration Policy

We recommend that the Legislature require the Department of Information Technology to develop a five-year strategic plan for configuration of the state's data centers.

In 1996, DOIT contracted for a study of feasibility of consolidating the state's data centers. In July 1997, DOIT released the report, which recommended consolidation and identified savings if the major data centers were consolidated.

In the budget year, the Health and Welfare Agency Data Center (HWDC) proposes to purchase one of the two buildings it occupies. The Stephen P. Teale Data Center is proposing a long-term lease purchase of a new facility.

Should the state decide to consolidate the two data centers, such a consolidation could affect the facility needs of each. Accordingly, we recommend that the DOIT provide the Legislature with a five-year strategic plan for configuration of the state's data centers before the state purchases or leases any new data center facilities. We note that the DOF plans to release a report later this year on the fiscal impacts of consolidation.

(For a more thorough discussion of the issue, please see our write up in the Capital Outlay chapter, as well as the analysis on the HWDC in the General Government chapter.)

HEALTH AND WELFARE AGENCY DATA CENTER (4130)

The Health and Welfare Agency Data Center (HWDC) provides information technology services, including computer and communications network services, to the various departments and other organizational components of the Health and Welfare Agency. The center also provides services to other state entities and various local jurisdictions. The cost of the center's operations is reimbursed fully by its clients.

The budget proposes $199 million for support of the data center's operations in 1998-99, which is a decrease of $43.5 million, or 18 percent, from estimated current-year expenditures. The decrease is a result primarily of the cancellation of the Statewide Automated Child Support System (SACSS) and a decrease in the Interim Statewide Automated Welfare System (ISAWS) budget. In addition to these decreases, the budget includes increases in requested appropriations for the Child Welfare Services / Case Management System (CWS / CMS), the Statewide Fingerprint Imaging System (SFIS), additional computer capacity, and year 2000 conversion activities.

DATA CENTER OPERATIONS

State Should Increase Expertise of State Staff

We recommend that the Health and Welfare Agency Data Center (HWDC) provide the Legislature, prior to budget hearings, with an estimate on how much it would cost to train state staff to perform services to support the HWDC Router Network that the budget proposes be supported by private consultants.

The data center budget requests $653,000 to hire four private sector consultants at $152 per hour, or $260,000 per consultant per year, to provide support for the HWDC Router Network. The network allows for electronic communication between computers. The data center indicates that these consultants will have special expertise, which they will pass on to data center staff over several years. (The budget documentation supporting the request, however, indicates that the consultants are needed due to workload, not expertise.)

If the need is for specialized expertise, it may be more advantageous to provide additional training to *existing* staff, who are more likely to remain at HWDC, rather than hire consultants to perform the services and transfer knowledge over several years. By doing so, the data center reaps the long-term benefit of having experts on staff.

Analyst's Recommendation. We recommend HWDC provide the Legislature, prior to budget hearings, with an estimate on how much it would cost to train existing state staff to perform the network-related services.

Acquisition of Data Center Building Premature

We recommend that the Legislature deny the data center's request to purchase a building it currently occupies and delete $445,000 in related maintenance and operating expenses. Instead, we recommend that the Legislature appropriate $455,000 to continue the existing lease of the facility.

The HWDC currently leases two buildings in Sacramento. The HWDC proposes to purchase one of the two buildings in the budget year. Chapter 1032, Statutes of 1996 (AB 3280, Cunneen) authorized the issuance of revenue bonds to purchase these facilities. However, the state is not using this bonding authority and instead the data center is requesting a General Fund loan.

The budget includes a capital outlay request for the state to purchase one of the buildings using a $5.2 million loan from the General Fund. The loan would be repaid from the data center's revolving fund. The HWDC's support budget proposes $445,000 for maintenance and operating costs for the building after it is purchased. (Currently, these services are provided by the landlord within the lease amount.) If the loan is not granted, HWDC will need $455,000 in the budget year to continue the existing lease.

Purchase Is Premature. In our analysis of the request to purchase the building (please see the Capital Outlay chapter in this *Analysis*), we conclude that the proposed purchase is premature and recommend that it be denied. We believe that the proposal is premature given that the administration has endorsed a 1997 report calling for consolidation of HWDC with the Teale Data Center. Such a consolidation could affect the facility needs of HWDC. Accordingly, we recommend that the Department of Information Technology (DOIT) provide the Legislature with a five-year strategic plan for configuration of the state's data centers before the state purchases or leases any new data center facilities.

Thus, we recommend that the proposal for $445,000 for maintenance and operating costs of the data center be denied, and that the Legislature instead appropriate $455,000 to continue to lease the facility in 1998-99.

Data Center Should Seek Review

We recommend that the Health and Welfare Agency Data Center, in cooperation with the Department of Information Technology, report to the Legislature during budget hearings on what additional tools and resources are needed to review project management methodologies and legal contracts.

In 1995, the Department of Social Services (DSS) transferred to HWDC responsibility for three of the largest information technology projects any state in the nation had undertaken. The projects, which were to automate welfare, child support, and child welfare services, were transferred due to the difficulties the DSS was experiencing in developing the projects.

Accepting responsibility for these projects posed a significant challenge to HWDC for several reasons:

- Each project was unusually large in size.
- Each project was experiencing significant development troubles.
- Contracts for two of the three projects were incomplete and did not specify work that the state wanted to have done.
- The projects were at a stage where going back and making substantial changes to the basic design would have been akin to starting over.
- Finding state or private sector project managers with experience deploying projects this large was difficult at best.

Taking over these projects, even for a well-run organization such as HWDC, posed a potentially overwhelming task for the data center. Not only were the projects in trouble, but the skills necessary to administer a data center are quite different from those necessary to conduct project management oversight, especially for major projects. In addition, while the data center was attempting to salvage these three major projects, it still had to administer its operations and meet the needs of its state department customers.

In 1997, the HWDC had to cancel one of the projects after spending $100 million because it would not work as planned. The other two projects, compared to recently revised estimates, continue to experience very significant cost increases (more than 70 percent) and delays (schedule slippages of up to two years). Although cost increases and delays are not uncommon on large projects, there are methods by which they can be minimized. For example, the Governor's Task Force on Government Technology Policy and Procurement recommended that a project not take more than two years to finish; that it be deployed in small, discrete components; and that project managers have experience commensurate with the size of the project.

In addition to the three major projects transferred in 1995, the center has since been given responsibility for seven more projects, bringing the total to ten. The cumulative cost of the ten projects exceeds $1.2 billion. Figure 7 shows the projects currently being managed by the center. As the figure shows, half of the projects are estimated to cost at least $100 million each and require a number of years to implement.

Outside Review Could Be Helpful. The data center was initially created to provide computer and communication services to its constituent departments. Only recently has the data center had thrust upon it the responsibility for developing and deploying major automation systems.

When the three projects were transferred from DSS, HWDC was given significant responsibility without any review of whether it had the appropriate tools for developing and deploying projects of this magnitude. We believe that a review of the center's major projects by an experienced consultant is warranted and will identify areas in which the data center can modify its resources and approach to increase the chances for successful deployment of the projects. With more than $1 billion of projects at stake, it is in the interest of the state to ensure that the data center has all the resources necessary to increase the opportunity for success.

Figure 7

Heath and Welfare Agency Data Center Projects Being Developed and Deployed

(Dollars in Millions)

Project	Purpose of System	Estimated Budget	Estimated Duration
Statewide Automated Welfare System (SAWS) Planning	Planning efforts to automate welfare benefit calculation and determination.	$18	4 years
SAWS Technical Architecture (SAWS-TA)	Enable multiple welfare systems to exchange data.	$45.3	10 years
Interim SAWS (ISAWS)	Automate 14 percent of statewide welfare caseload.	$285	10 years
Welfare Case Data System (WCDS)	Automate 41 percent of statewide welfare caseload.	$288	11 years
Los Angeles Eligibility, Automated Determination, Evaluation and Reporting System (LEADER)	Automate 33 percent of statewide welfare caseload.	$243	8 years
SAWS Consortium IV (C-IV)	Automate 12 percent of statewide welfare caseload.	To be determined	To be determined
Statewide Automated Child Support System (SACSS)	Automate collection and enforcement of child support.	$100 expended; future costs to be determined	Unknown
Child Welfare Services Case Management System (CWS/CMS)	Automate cases of children in child welfare services.	$206	9 years
Electronic Benefits Transfer (EBT)	Enable the electronic exchange of funds for food stamp recipients.	$1.5 (planning only)	—
Statewide Fingerprint Identification System (SFIS)	Fingerprint welfare recipients to identify duplicate aid cases.	$38	5 years
Total		**$1,224.8**	

Such a review would make recommendations on how the data center can mitigate risk on these issues:

- A single data center having to manage many of the largest projects in the nation.
- Different skill sets necessary between managing a data center and managing deployment of information technology projects.
- Circumstances that lead to canceling a project (such as SACSS after spending $100 million).
- Significant increases in project costs (such as the 73 percent increase for CWS / CMS).
- Delays in project deployment of several months to years.
- Size of the projects being much larger than information technology industry standards suggest they should.
- Project managers with limited experience, especially on major projects.
- Contracts needing specialized legal review.

Analyst's Recommendation. We believe that the tasks and responsibilities given to the data center would be daunting for any private or public sector entity, and that some additional assistance could be helpful to the center, the users of its systems, and the state as a whole. For this reason, we recommend that the center and DOIT report to the Legislature during budget hearings on their suggested strategy for addressing the issues raised above. Specifically, the center and DOIT should consider the need for additional tools and resources for the center, an outside review by an experienced consultant with expertise in project management to review the center's project management methodologies, and a review of legal contracts for major projects to ensure that the contract terms protect the state.

STATEWIDE AUTOMATED WELFARE SYSTEM (SAWS)

Background

The data center's budget includes $88 million to continue support for the Statewide Automated Welfare Systems (SAWS). The purpose of SAWS is to provide improved and uniform information technology capability to county welfare operations, through a state partnership with the counties, which have chosen to be in one of four consortia. The four consortia were authorized by the Legislature in the *1995-96 Budget Act* and are comprised of:

- Interim Statewide Automated Welfare System (ISAWS).
- Los Angeles Eligibility Automated Determination, Evaluation and Reporting System (LEADER).
- Welfare Case Data System (WCDS).
- Consortium IV (C-IV).

We describe the progress of the consortia in more detail below.

The budget proposes an increase of $4 million in the current-year and a decrease of $3 million in the budget year for SAWS planning efforts. The multiyear total estimated cost for SAWS planning is $18 million.

Impact of Welfare Reform on System Requirements. Of the four consortia authorized by the Legislature, two (ISAWS and LEADER) were close to finishing the development of systems based on requirements which were established prior to welfare reform legislation being enacted in 1997. These consortia will need to be modified to reflect the new policies resulting from welfare reform. The other two systems (WCDS and C-IV) are in the planning stages and will need to incorporate the new welfare policies into procurement documents.

The DOIT required HWDC to hire a consultant to conduct an assessment of the impact of welfare reform on each of the four projects and departments (all departments under the Health and Welfare Agency, as well as the Department of the Youth Authority, Office of Child Development and Education and the Department of Education). The assessment, due in March 1998, will include: (1) an assessment of how welfare reform policies will affect existing computer systems; (2) an analysis of the gaps between what the existing computer systems can do and what welfare reform policies need them to do; and (3) recommendations on how to close the gaps.

SAWS Technical Architecture Facilitates Exchange of Data. In addition to the four consortia, the HWDC is responsible for deployment of the SAWS Technical Architecture (SAWS-TA) which will enable the four consortia to exchange data. The SAWS-TA is also supposed to be able to identify recipients in order to reduce duplicate aid payments. The SAWS-TA will be run at the data center and serve as an information broker among each of the systems for all of the counties. The SAWS-TA was originally due to be deployed by October 1997, but has been delayed. The latest plan was to have it support LEADER by February 1998; however

LEADER is now delayed due to the effort to incorporate welfare reform. It is unclear when the SAWS-TA will be complete. Total estimated project cost is $45 million over the ten year life of the project.

The budget requests an increase in spending authority of $3.5 million for the current year and a decrease of $1.6 million in the budget year.

Requested Reports Not Received

We recommend that the Legislature withhold action on $88 million of Health and Welfare Agency Data Center's budget until the center submits a series of reports requested by the Legislature in the* 1997-98 Budget Act *and statute.

The *1997-98 Budget Act*, the *Supplemental Report of the 1997-98 Budget Act* and the Welfare and Institutions Code required the HWDC to provide a series of reports related to the SAWS project during the year. The purpose of the reports is to apprise the Legislature of progress in implementing SAWS, of potential problems with the projects and the fiscal impact of any such problems. None of the reports has been submitted. The reports include:

- A report on the progress of implementing the Statewide Automated Welfare System, Technical Architecture (SAWS-TA) project, which was due by January 1, 1998.
- Quarterly reports to the Legislature, beginning October 1997, on the status and progress of incorporating welfare program requirements into the SAWS systems. The reports are to include issues, time lines and cost estimates.
- An annual report to the Legislature on the progress of SAWS, as well as interim reports as necessary to raise significant time-critical issues.

Since the Legislature needs to be aware of the progress of the projects before appropriating funds for them, we recommend that the Legislature take no action on the $88 million proposed for SAWS until it receives the required reports.

Implementation Status of the SAWS Consortia

Interim Statewide Automated Welfare System (ISAWS) Is Almost Finished. The ISAWS project, being managed by HWDC, is currently operational in 20 counties. When fully deployed in July 1998, 35 primarily small counties representing 14 percent of the statewide caseload, will be using ISAWS. Since ISAWS is almost completely deployed, HWDC will need to retrofit the system with welfare reform policies in the future. A new budget and schedule to do so have not been released.

The HWDC budget for development of ISAWS proposes a decrease of $221,000 in the current year and $14 million in the budget year as the data center will no longer need these baseline expenses with the project coming to completion. Funding for maintenance and operation for this project will be approximately $21 million annually thereafter.

Los Angeles Eligibility Automated Determination, Evaluation and Reporting System Delayed to Incorporate Welfare Changes. The LEADER is being implemented by Los Angeles County and is currently under development. Although testing was to begin late last year, further deployment has been suspended while policies reflecting welfare reform are incorporated into the system. A revised schedule and budget have not yet been released. This project will serve 33 percent of the statewide caseload, all in Los Angeles County, when complete.

The HWDC is requesting an increase of $2.7 million in the current year and $4.2 million in the budget year is DSS' local assistance budget to fund development and operational activities.

Welfare Case Data System in Procurement Phase. The WCDS will serve 18 counties representing 41 percent of the statewide caseload when completed. The consortium released its procurement document, the Invitation to Partner (ITP), in December 1997. The WCDS intends to conduct an alternative procurement, which is an iterative process allowing refinement of the conceived system as the vendors and consortium discuss the business problem that needs to be solved. Ultimately, it is up to the vendor to propose the solution. The information technology industry generally considers this a "best practice," thereby increasing the chances for success.

The estimate of total project costs is $288 million. The *1998-99 Governor's Budget* requests an augmentation of $6.2 million, bringing the baseline expenditures to $18 million for the project. We discuss the proposed ITP in more detail below.

Consortium IV in Planning Stage. The C-IV, which will serve four counties and 12 percent of the statewide caseload when finished, is in the beginning stages of planning its strategy and procurement. The HWDC's proposed budget does not include monies for C-IV as it is still in the planning stages, for which it received an augmentation of $2 million in current-year expenditures.

Welfare Case Data System Lacks Welfare Reform Policies and Oversight

We recommend that the Legislature appropriate the $18 million proposed for the Welfare Case Data System through budget bill language, making it available if (1) the Department of Information Technology certifies that the procurement document allows for expansion of the system and (2) the state's oversight role is increased.

As indicated above, WCDS is one of the four consortia that comprise SAWS. When completed, it will serve 18 counties and 41 percent of the state caseload. The *1998-99 Governor's Budget* requests $18 million to enter into a contract and begin development of the system. As currently envisioned, the state has a minor role in the deployment of the WCDS. Rather, the 18 counties which comprise the consortium are primarily responsible for development and deployment of this system.

The WCDS consortium finished developing its procurement document—now called the Invitation to Partner (ITP)—while the Legislature and Governor were enacting a new welfare program in response to federal welfare reform. We have two primary concerns regarding the ITP, which was developed by counties within the consortium.

Welfare Reform Changes Not Included. First, the ITP was developed before welfare reform legislation was enacted. Our review of the ITP indicates that the system is focused on determining welfare *eligibility*. Under welfare reform, however, county welfare departments are required to undertake tasks that go beyond eligibility determination. The changes require departments to exchange information electronically with many partners, including local school districts, the Immigration and Naturalization Service, substance abuse programs, child welfare services programs, and work programs, among others. More importantly, the changes suggest the need for comprehensive case management capability. These components do not appear to be included in the ITP and will likely add substantially to the cost and the effort to deploy the system.

To the extent that the vendor who is awarded the contract develops a flexible system (known as "open architecture"), the consortium could add welfare reform in modules in the future. However, it is not clear from the ITP whether the proposal will have this flexibility, or whether it will have a "closed architecture." If the latter is the case, then the consortium would need to revise the ITP to include welfare reform policies. Alternatively, the consortium could develop a plan in which the vendor goes back and incorporates welfare reform policies into the system after it is deployed. Trying to incorporate the policies into a system that does not allow for the degree of expansion that will be necessary significantly increases the risk of failure.

For this reason, we believe that it is critical to require that the system be created with an open architecture, which would allow "adding on" of welfare policy components, or that the procurement document be revised to include welfare reform policies.

Insufficient State Oversight. Our second concern with the proposal is that it envisions very little state oversight. This is because the administration proposes to have the counties sign the contracts with the vendors and, although the state and federal government will be responsible for 95 percent of the costs, the state will not be able to amend, suspend, or terminate the contract.

Although the counties and state will be working in cooperation, there will be times when the counties and state disagree on a direction, as was evidenced in 1995 on CWS/CMS and more recently on SACSS. The HWDC's willingness to allow the counties to have such an exclusive role raises a larger concern of what responsibility and authority HWDC is going to have over the deployment of the project. Although HWDC indicates it will have *oversight* responsibility, the *1995-96 Budget Act* which authorized the four consortia, required HWDC to be *ultimately responsible* for each of the four projects—a much more significant role than simply providing oversight. If HWDC does not have the authority to require specific changes to the contract, then no state agency can be held accountable, despite the large investment of state money.

Approval of the $18 million being requested will essentially demonstrate the Legislature's approval of the project as conceived, which is preliminarily estimated to cost $288 million.

Analyst's Recommendation. We recommend that the Legislature appropriate the $18 million proposed for the Welfare Case Data System through Budget Bill language, making it available if (1) DOIT certifies that the procurement document allows for expansion in order to more easily accommodate welfare reform policies and (2) the contract with vendors is signed by DOIT and HWDC so that state oversight can be preserved. We recommend the adoption of the following budget bill language:

> In augmentation of the funds appropriated by this item, an additional sum up to $18 million is hereby appropriated for development and implementation of the Welfare Case Data System (WCDS), subject to the review and approval of the Department of Information Technology (DOIT) of the Invitation to Partner (ITP) proposed by the WCDS Consortium. The DOIT shall certify that the ITP requires the vendor to provide an open architecture to allow the system to expand as needed. Additionally, both DOIT and

the Health and Welfare Agency Data Center shall sign contracts with vendors which obligate state funds to create and deploy this project. The Department of Finance shall notify the Joint Legislative Budget Committee and the Legislature's fiscal committees at least 30 days before authorization of expenditure of any funds.

STATEWIDE AUTOMATED CHILD SUPPORT SYSTEM (SACSS)

Child Support Project Canceled; New Project Offers Opportunities, Challenges

After spending $100 million on the Statewide Automated Child Support System project, the state canceled the contract in November 1997. An audit of the project from the Bureau of State Audits should be available for the Legislature to review during budget hearings.

The budget indicates that the administration plans to come forward in the spring with a plan for automation of child support. We recommend that the Legislature require that the new automation system be purchased using a method in which the state outlines for vendors its desired outcomes, rather than specifying a particular technology. In addition, we recommend that Health and Welfare Agency Data Center report at budget hearings on the status of the level of federal funding for the new project.

The SACSS is a federal and state-mandated computer-based system to provide an automated statewide child support enforcement tracking and monitoring capability through the offices of county district attorneys. In 1995, the administration transferred the responsibility to manage this project from the DSS to HWDC in order to resolve serious implementation problems. In November 1997, after two years of difficulty implementing the project, HWDC canceled the contract and project. The state had spent $100 million on the project.

The Governor's budget has set aside $20 million from the General Fund (in a non-Budget Act item in the Health and Welfare Agency) in anticipation of a Finance letter for planning and development of a new project. The HWDC indicates it anticipates having a plan for future automation efforts completed by March 1998.

There are some counties currently using the working components of SACSS. The vendor was retained to maintain and operate the system for these counties for six months, beginning in November 1997, and will transfer knowledge of the system to state staff so that they can maintain the system. The vendor will be paid $11 million for these services.

Audit of Project Due. Last year, the Legislature directed the Bureau of State Audits (BSA) to conduct an audit of the management of the SACSS contract and project. This audit is due to be released in late February and, thus, should be available for the Legislature to review during hearings on HWDC's budget. The *1997-98 Budget Act* requires HWDC to respond with a plan for implementing the audit's recommendations or take other actions that will improve performance in order to better protect the state's interests and ensure success of the SACSS project.

New Project Offers Opportunity to Follow "Best Practices." Although it is important to deploy a statewide system for child support enforcement as soon as possible, the cancellation of the SACSS project gives the state an opportunity to "start from scratch" to procure a system in such a way as to increase the chance of successful deployment.

In 1994, the Governor's Task Force on Government Technology Policy and Procurement recommended that the state revise its procurement process such that it lays out the business problem that needs solving, rather than specifying the technology it wants to purchase. This process, known in state government as an alternative procurement, is considered a "best practice" by the information technology industry. This new procurement process was successfully employed for a major project at the Franchise Tax Board.

Although it may seem as though starting over on SACSS will take longer than transferring an existing technology to California, such a conclusion is not necessarily accurate. Even though the state started with an existing technology on the SACSS project (it was transferred from another state), it could not be made to work in California, even after years of significant effort, a substantial investment of state monies, and a major change in project management. Procuring a new child support system using a process in which the state outlines its business needs should increase the state's chances of deploying a successful project.

In addition to the procurement method, there are other industry best practices that should be considered for this and future automation projects to better protect the state and increase the chances for success. For example, vendors should be willing to share in any potential financial loss to a greater degree than they have in the past. Vendors can share in the risk by providing a letter of credit, receiving payment only upon acceptance of deliverables, and including liquidated and consequential damages in the contract. In order to protect the taxpayers' investment, the state needs to procure major information technology systems using industry best practices such as these.

We recommend that the Legislature require that the new project be based on this alternative procurement process model which details the outcome desired, rather than specifying a technical solution in the procurement documents. Additionally, we recommend that DOIT require other appropriate best practices be incorporated into the contract and project management methodology.

Future Federal Financial Participation Unclear. When California began deploying SACSS, the federal government agreed to pay 90 percent of development costs. It is unclear whether the federal government intends to share in any of the cost of creating another system in California. If not, then HWDC may need to ask the Legislature for several hundred million dollars from the General Fund to support future child support automation efforts.

In addition, when first planning automation for child support, the DSS believed the federal regulations required that each state deploy a single system statewide in order to receive 90 percent enhanced federal funding. A letter from the federal agency responsible for this program indicates that it has the authority to grant a waiver to allow states to deploy multiple systems, as long as counties can exchange information amongst themselves. Due to California's size, it may have more success by deploying multiple systems that can exchange data, rather than one system, statewide. It remains unclear, however, whether the federal government will share in the expense of deploying multiple systems if they agree to fund any future automation efforts in California. If the state decides to deploy multiple systems which can exchange information for child support automation, it needs to understand the level of federal financial participation.

We recommend that the HWDC report at budget hearings on the status of federal financial participation for the new child support automation efforts in California.

County Child Support Systems Need Upgrading for Year 2000

We recommend that Health and Welfare Agency Data Center and Department of Social Services report during budget hearings on the progress of the counties in modifying existing child support systems to accommodate the year 2000.

The counties have been planning to use SACSS since 1995. As a consequence, many counties did not devote resources to modify county-based child support enforcement computers to be able to accommodate the year

2000 change. (For a full discussion of the impact of the year 2000 on computers, see the Crosscutting issues section earlier in this chapter.)

With the cancellation of SACSS in late 1997, counties are now faced with having to modify their computers to accommodate the year 2000. This effort will be expensive and time consuming. Failure to modify existing systems can lead to serious problems ranging from miscalculations of child support orders to complete failure of systems. It is unclear whether counties are receiving any assistance from the state to complete these modifications and whether they will all be able to complete them in time. The state should help ensure that these systems will be able to function without failing until a statewide system is deployed.

Analyst's Recommendation. We recommend that the HWDC and DSS report during budget hearings on the progress of the counties in modifying existing child support systems to accommodate the year 2000.

CHILD WELFARE SERVICES CASE MANAGEMENT SYSTEM (CWS/CMS)

Contract Increases Not Justified

We recommend the Legislature delete the proposed $15.1 million augmentation for the Child Welfare Services Case Management System because the costs should be incurred by the vendor, not the state. (Reduce Item 4130-001-0632 by $15.1 million.)

The budget proposes $48 million to continue support for the CWS/CMS in 1998-99. This includes an augmentation of $15.1 million to increase the vendor's contract. This is the first installment of a total contract increase over several years of $58 million.

Background. Chapter 1294, Statutes of 1989 (SB 370, Presley), required the implementation of the CWS/CMS. The primary goal of this system is to provide a statewide database, case management tools, and reporting system for the Child Welfare Services program. The DSS began the project in 1990.

In April 1995, the administration transferred responsibility for project management from the DSS to HWDC in an effort to improve the project's prospects for success. When HWDC was given responsibility for this project, the project was at a critical stage, with the counties no longer supporting the project and the state close to canceling the contract. The HWDC spent several months renegotiating the contract with the vendor. When the negotiations were completed, HWDC advised the Legislature that the vendor guaranteed that the project would be fully deployed by fall 1997, for $119 million, and that if there were delays the vendor would pay penalties up to $5,000 per day depending on the missed milestone; share in the loss of federal funding; and guarantee maintenance for 15 months after every county received the system.

The project is now estimated to cost approximately $206 million and is not projected to be fully deployed until June 1998. If the proposed increase of $58 million spread over several years is approved, the vendor's contract will be increased 60 percent above the amount negotiated in 1995. We have the following concerns with the proposed increase in funding for the vendor.

State Paying Twice. The proposed increase in funding is to pay the vendor for a variety of activities. These include additional help troubleshooting problems at the county level, changing the fundamental operating system, resolving problems experienced in Los Angeles and Fresno Counties, completing additional testing of data, extending the vendor's contract to maintain the system, and continuing independent validation and verification (IV&V) services. Each of the services proposed for funding is necessary due to project delays and the system not working as planned. In our view, the contract requires the vendor to deploy a working system, therefore the state should not pay for fixing what is not working. Of the proposed increases noted above, two in particular are worrisome.

Software and Hardware Upgrades Should Not Be Necessary at This Time. A portion of the increase is being requested to upgrade the system infrastructure—both software and hardware—which HWDC advises is necessary for the continued performance and viability of CWS/CMS. However, HWDC's quality assurance vendor estimates that major software and hardware changes such as those being proposed should occur only every two to two-and-a-half years. Yet, the system has been operating for only a year in most counties. Accordingly, we do not believe that there is operational need to make the changes now.

Maintenance Costs Agreed to in 1995 Negotiated Away. The budget includes $8 million for the contractor to maintain and operate the system through June 1999. The HWDC informed the Legislature when it renegotiated the contract in 1995 that it secured a firm 15 months of maintenance and operation from the time the system worked *in all counties.* Now the center indicates that due to the delay in completion, the contract was amended to allow maintenance to end earlier in exchange for other services. It appears, however, that these are services the vendor should perform without additional charge to make the system work.

Analyst's Recommendation. We believe that the contract requires the vendor to deploy a working system. Since these appear to be expenses the vendor is already under contract to produce, we recommend denying the requested $15.1 million augmentation and prohibit HWDC from amending the vendor's contract for these expenses.

OTHER ISSUES

Statewide Fingerprint Imaging System (SFIS) Expansion Not Justified

We withhold recommendation on $8.9 million requested for Statewide Fingerprint Imaging System, pending receipt and review of the justification for the request.

The *1995-96 Budget Act* assigned responsibility for implementing the Statewide Fingerprint Imaging System (SFIS) to the HWDC. The system, modeled after one implemented in Los Angeles County in 1994, is intended to reduce the cost of fraud associated with state welfare programs. The contract for this project was to be awarded in June 1997 with full system operation in July 1998. However, award of the contract has been delayed.

The proposed budget includes an augmentation of $8.9 million in 1998-99 to implement the SFIS. The total amount proposed for the budget year is $10 million.

At the time this analysis was prepared, we had not received budget documentation to justify this request. Thus, we withhold recommendation, pending receipt and review of the documentation.

Electronic Benefits Transfer (EBT) System Delayed

We recommend that Health and Welfare Agency Data Center report during budget hearings on its progress in implementing this project.

Electronic Benefits Transfer (EBT) allows for the electronic transmission of funds to a food stamp recipient. The system uses debit card technology and retailer terminals to automate benefit authorization, delivery, redemption and financial settlement thereby eliminating the need for food stamp coupons. Federal Food Stamp regulations, implemented as a result of the federal Personal Responsibility and Work Opportunity Reconciliation Act of 1996, require that all states implement an EBT system by October 2002. Chapter 270, Statutes of 1997 (AB 1542, Ducheny) authorized EBT and established an EBT committee, which will advise HWDC on the planning, development and implementation of the statewide EBT.

The HWDC is required to certify one or more EBT processors as eligible to contract with counties to implement EBT systems. A county or group of counties will contract with the certified processors directly and will have principal responsibility to manage operation of the EBT system implemented by the county or group of counties. At the time this analysis was prepared, HWDC indicates that the project has been delayed.

The proposed budget requests $194,000 and two positions to complete planning efforts to implement an EBT program.

We recommend that HWDC report to the Legislature during budget hearings on the progress of certifying processors.

Automated Tape Library Not Yet Justified

We withhold recommendation on $671,000 requested for the Automated Tape Library, pending receipt and review of the justification for the request.

The budget proposes an augmentation of $671,000 for an Automated Tape Library (ATL). The ATL will enable an automated system to access data on computer cartridge tapes, thereby increasing accuracy and productivity. Total project costs are estimated to be $7.2 million over the life of the five year project.

At the time this analysis was prepared, we had not received documentation to justify this request. Thus, we withhold recommendation, pending receipt and review of the documentation.

Year 2000 Funding Request Not Yet Justified

We withhold recommendation on $3.6 million requested for Health and Welfare Agency Data Center's Year 2000 project pending receipt and review of the justification for the request.

The budget proposes an augmentation of $3.6 million to continue the data center's activities to enable all computer systems to accommodate the year 2000. The data center's proposal is to purchase hardware for increased capacity, consulting services for testing, and general overhead expenses.

At the time this analysis was prepared, we had not received documentation to justify this request. Thus, we withhold recommendation, pending receipt and review of the documentation.

OFFICE OF EMERGENCY SERVICES (0690)

The Office of Emergency Services (OES) coordinates emergency activities necessary to save lives and reduce losses from disasters. The OES further acts as the state's conduit for federal assistance related to recovery from disasters and hazard mitigation.

The budget proposes $356 million in total expenditures in 1998-99. This is a decrease of $220 million, or 38 percent, below estimated current-year expenditures. The decline in the budget is due to reductions in the estimated amounts budgeted for disaster assistance. The budget does not include funds to pay for any potential state expenses and local assistance that might arise as a consequence of El Niño storms or other potential disasters.

Support Budget. Of the OES' total $356 million budget, $48.9 million is for direct support of the office. This includes $25.4 million from the General Fund, $18.1 million from federal funds, and the remainder ($5.4 million) from various other funds and reimbursements. The amount proposed for support is $14.7 million, or 23 percent, less than estimated current-year expenditures.

Local Assistance Budget. In addition to support costs, the budget includes $307 million for local assistance to pay claims from previous disasters. This is $205 million, or 40 percent, less than estimated current-year expenditures for local assistance. The proposed local assistance expenditures for the budget year include $255 million from federal funds, $43 million from the General Fund, $7 million from the Disaster Relief Fund, and $1.9 million from the Nuclear Planning Assessment Special Account.

The OES Should Retain Law Enforcement Coordination Responsibilities

We recommend that the Office of Emergency Services retain responsibility for coordinating law enforcement mutual aid and other law enforcement activities during disasters. We also recommend approval of two proposed law enforcement coordinator positions to ensure that all mutual aid regions are adequately served.

The *Supplemental Report of the 1997 Budget Act* directed the Legislative Analyst's Office to review the responsibilities of OES' law enforcement branch and report whether their responsibilities are best performed by the OES or whether they can be performed as effectively, or better, through transfer to another state agency. Our review is outlined below.

Background. California has over 800 local law enforcement agencies—sheriffs; city police; university, college, school district police departments; the California Highway Patrol (CHP); state park rangers; and fish and game wardens—each responsible for law enforcement within their respective jurisdictions. Generally, there is limited overlap in jurisdictions, except at times of emergency or disaster. In 1950, recognizing that the resources of the various law enforcement jurisdictions could be overwhelmed under certain circumstances, a mutual aid system for local law enforcement agencies was established through the California Master Mutual Aid Agreement. In 1970, the agreement, and the state's role, was established in statute in the California Emergency Services Act.

The mutual aid system allows local law enforcement agencies to mutually support adjacent or regional jurisdictions at any time a single agency's own resources are insufficient. The mutual aid plan outlines the procedures for alerting, coordinating, dispatching, and utilizing law enforcement personnel and equipment resources. For example, mutual aid agreements have been invoked when a city must deal with a large protest demonstration, civil disobedience or disturbance, or natural disaster. The mutual aid system provides the framework for local law enforcement agencies to deal with most unusual occurrences or emergencies.

The state has seven mutual aid regions, each under the direction of one of the region's sheriffs, who acts for the region as an operational area coordinator. Mutual aid is used when local law enforcement agencies determine that a situation is, or may become, beyond the agency's resources to manage. In those circumstances, the local law enforcement agency requests resources from the operational coordinator. Resources are then pooled from other agencies in support of the requesting agency. Depending on the event that triggers the mutual aid request, the operational area coordinator can direct the use of both local and state resources.

State-Level Mutual Aid Coordination. Most mutual aid requests are handled within the seven regions. The state has a limited role in coordination of these mutual aid events, except in providing state resources that are deployed locally (CHP officers, for example). However, in the event of natural disaster or major civil disturbance, a region may need resources from outside its area, including federal assistance. In those instances when the region has depleted its own law enforcement resources, the OES law enforcement branch assumes coordination responsibilities and ensures that appropriate local, regional, state, and federal resources are transferred to the afflicted area. In addition, the law enforcement branch has responsibility for law enforcement coordination in the event of any declared disaster or calamity. The branch will either assume responsibility for coordination at these times or will act to aid regional operational area coordinators.

The law enforcement branch currently has seven staff and a budget of about $1 million. There are five regional coordinators for the seven mutual aid regions. The regional coordinators and supervisors are sworn law enforcement officers.

Who Should Be Responsible for Coordinating Law Enforcement? As indicated above, the 1997-98 Supplemental Report directed our office to review the responsibilities of the law enforcement branch and report whether these responsibilities should be transferred to another state agency. We have reviewed the statutory and regulatory basis for branch activities, met with branch staff, contacted and received input from the California State Sheriff's Association and from various sheriffs acting as mutual aid operational area coordinators. In addition, we have reviewed how the state uses law enforcement resources during special occurrences and emergencies. Based on this review, we conclude that the OES is the proper place for disaster-related law enforcement coordination.

While there are other state-level agencies that have law enforcement and disaster experience (for example, the CHP), we found that these agencies could have competing priorities which might result in a conflict of interest if they were to become responsible for the allocation of resources in emergencies. For instance, during a disaster, the CHP may be assigned to provide transportation related resources, while in other instances the CHP may be called upon to provide logistical support or emergency communications. These tasks are separate from law enforcement tasks. Requiring the CHP to allocate its own resources and those of local agencies may lead to instances where there is an appearance of a conflict of interest when determining how resources are to be provided and allocated. When an OES law enforcement coordinator, because he or she is not associated with any of the agencies providing resources, makes allocation decisions there is less chance of competing priorities. Furthermore, the OES' current system cost is small, considering the scope of its responsibilities. It is not clear whether another state agency would be able to provide similar services with the same level of resources.

New Coordinator Positions. As part of its budget request, the OES is requesting $129,000 from the General Fund and two new law enforcement coordinator positions. These positions will allow OES to assign one coordinator to *each* of the state's seven mutual aid regions. Currently, the coordinator for Los Angeles and Orange counties (Region I) also serves the region encompassing Ventura, Santa Barbara, and San Luis Obispo counties (Region IA). In addition, the coordinator for the 13-county region of northeastern California (Region III) also serves the 11 county Sierra foothill region (Region IV). The number of mutual aid events and disasters in the regions where the OES proposes to place the new coordinators has increased. We believe that the addition of full-time coordinators for these regions is justified on a workload basis.

Analyst's Recommendation. We conclude that the OES is the proper place for disaster-related law enforcement coordination, and recommend that the Legislature take no action to move these responsibilities to another state agency. Furthermore, we recommend approval of $129,000 and two new law enforcement coordinator positions to allow for a dedicated coordinator for each of the state's seven mutual aid regions.

Disaster Claims Processing to Stay at OES

The Office of Emergency Services reviewed the feasibility of transferring its disaster claims processing to another state agency, as was required by recent legislation, and determined that it would be more costly and less efficient to transfer these responsibilities.

The Legislature enacted Chapter 338, Statutes of 1997 (SB 959, Kopp) as part of last year's budget. Chapter 338 required the OES to develop a plan to limit its role in disaster claims processing to the absolute minimum number of staff necessary to work with the Federal Emergency Management Agency (FEMA) on issues related to state disasters. It also stated that it was the intent of the Legislature that the OES rely on interagency agreements with other state agencies to process disaster claims. Chapter 338 specifically stated that the OES plan not include contracting with private contractors. This legislation was the result of deficiencies cited in two Bureau of State Audit (BSA) audits of the OES claims processing system.

The OES completed its plan and submitted it to the Legislature in early January 1998. The OES concluded that it would not be cost effective to transfer its processing responsibilities to another state agency. The OES staff reviewed the processing systems of the Board of Control, Department of General Services, and State Controller's Office, compared its processing system to the systems of these agencies, and determined that whatever marginal efficiency might accrue from a transfer would be lost in the need for interagency coordination and in developing expertise with the federal FEMA regulations. As a consequence, the administration plans to have OES keep the claims processing function and not transfer it to another agency.

It should be noted that the OES processing system has undergone significant changes and improvements in the past two years. The OES has implemented the major recommendations of the BSA and appears to have made its system more efficient. In addition, 323 limited-term positions will be terminated at the end of the current year as claims from prior years are completed, while other positions are planned for elimination due to other efficiencies. As a consequence, total OES claims processing staff will decline to 232 in the budget year, from a high of 563 in the current year. Furthermore, during our review of OES claims processing, we saw evidence of the cooperation between OES staff and FEMA claims processing staff that appears to bolster OES' argument that it, rather than another state agency, has specialized expertise that helps in the expeditious processing of California disaster claims.

STATE CONTROLLER
(0840)

The State Controller is responsible for (1) the receipt and disbursement of public funds, (2) reporting on the financial condition of the state and local governments, (3) administering certain tax laws and collecting amounts due the state, and (4) enforcing unclaimed property laws. The Controller is also a member of various boards and commissions, including the Board of Equalization, the Franchise Tax Board, the Board of Control, the Commission on State Mandates, the State Land Commission, the Pooled Money Investment Board, and assorted bond finance committees.

The Governor's budget proposes expenditures of $98.4 million ($61 million from the General Fund) to support the activities of the State Controller in 1998-99. This amount is $656,000, or less than 1 percent, more than estimated current-year expenditures.

Statewide Travel Reimbursement Project Not Mission Critical

We recommend a reduction of $689,000 in reimbursements requested for the development of an automated statewide travel reimbursement project because the proposed system is not mission critical and is premature until the Controller's Office converts its computers to accommodate the year 2000 changes. (Reduce Item 0840-001-0001 by $689,000.)

The proposed budget requests $689,000 in reimbursements to begin a new information technology project, known as the Automated Statewide Travel Expense Reimbursement Process Project. The total cost of the project, which would be completed over several years, is estimated to be $7.7 million. The State Controller's Office (SCO) indicates that development and maintenance costs for the proposed system will be funded on a reimbursable basis by departments that intend to use the system.

Many state agencies, including the SCO, are working to make their computer systems accommodate the year 2000 change. In order to focus the state's information technology resources on this problem, we have recommended that the Legislature deny funding requests for new nonyear 2000 information technology projects unless the request is for a project that is mission critical to the state, or is specifically mandated by state or federal law. Because this proposed project is neither mission critical nor mandated, we recommend, without prejudice to the merits of the project, that the Legislature deny funding for this request. (For more information on the year 2000 problem, please see our analysis in the Crosscutting Issues section earlier in this chapter.)

Additional Information Needed for Local Government Reporting System

We withhold recommendation on $724,000 requested to replace the current Local Government Reporting Systems pending receipt of additional information from the State Controller's Office on the critical failure dates for their current systems and a plan to include users of the proposed system in the development process.

The budget requests $724,000 from the General Fund in one-time costs to replace the current Local Government Reporting Systems (LGRS) with a new, single automated system. Using this system, the SCO currently collects data from local governments and produces nine mandated publications, including the annual reports of financial transactions for counties and cities. The financial information published in these reports includes revenue and expenditure statements and long-term debt schedules.

Budget Proposes System Replacement. The SCO reports that the current LGRS has not been converted to handle the year 2000 change at the end of the century. The cost for system improvements to accommodate the century change is estimated to be $332,000. The SCO indicates that investing in a new, single automated system would streamline the reporting and data collection process. Therefore, the SCO is requesting funds to replace rather than modify the current systems. The SCO expects that software needed for the new system already exists and can be purchased and modified to meet the reporting requirements. The SCO intends to develop a request for proposals in the current year by redirecting funds.

Critical Failure Dates Not Identified. The SCO's most recent quarterly update to the Department of Information Technology for the year 2000 project plan identifies the various systems of the LGRS. However, the SCO has not identified the dates by when these systems must be modified (known as the "critical failure dates"). In order to consider the priority and the merit of this request, it will be important to obtain the critical failure dates for these systems, including information on the impact that the year 2000 will have on the operations of the current systems.

Users Not Consulted. The users of the information from the LGRS systems include, the Legislature, local governments and associations, municipal finance analysts, and academics. Over the years, concerns have been raised by many of the users of the LGRS information. The concerns involved (1) the timeliness of the information, (2) the availability of data over the Internet, (3) the appropriateness of the categories of information currently available, and (4) the compatibility of data within each local government category. The current plans of the SCO do not include obtaining input from these groups in the development of the new system prior to the request for proposals. In order to ensure that the new system addresses the concerns of its "customers," we believe that the users should be included in the process that determines how the new system is designed.

Analyst's Recommendation. Based on the above findings, we withhold recommendation on the $724,000 requested to replace the current LGRS, pending receipt of additional information from the SCO regarding the critical failure dates for the current systems and a plan to include users of the information in the development of the new system.

SECRETARY OF STATE (0890)

The Secretary of State, a constitutionally established office, has statutory responsibility for examining and filing financial statements and corporate-related documents for the public record. The Secretary, as the chief elections officer, also administers and enforces election law and campaign disclosure requirements. In addition, the Secretary of State appoints notaries public, registers auctioneers, and manages the state's archival function.

The budget proposes total expenditures of $70.3 million for the Secretary of State in 1998-99. This is $8.4 million, or 11 percent, less than the current-year expenditures. Expenditures from the General Fund total about $33.9 million, a decrease of $14.5 million, or almost 30 percent, compared to current-year expenditures.

The reduction in General Fund expenditures is primarily due to the use of $10 million in surplus bond funds to offset on a one-time basis the cost of certain programs which otherwise would be supported with General Fund monies. Also, General Fund expenditures would decline in 1998-99 because less money is needed than in 1997-98 to pay for programs the state mandates upon local government, particularly those establishing rules for the conduct of elections.

Expenditures from the Secretary of State Business Fees Fund are projected to be $19 million, a decrease of $4.2 million, or 18 percent, from current-year expenditures. The decrease is related primarily to the completion of information technology projects and streamlining in the Secretary of State's business programs division responsible for the filing of various corporate documents through new procedures.

Slowdown in Computer Project May Delay Repayment of State Loan

A new statewide computer information system to track voter registration will not be deployed in all California counties, as originally scheduled, in time for the 1998 primary and general elections. As a result, we recommend the adoption of legislation that would delay for 18 months the date upon which the Secretary of State must repay $3.5 million borrowed to build the system.

Chapter 913, Statutes of 1995 (AB 1701, McPherson) directed the Secretary of State to establish a statewide computer system comprised of voter registration data that would facilitate the removal of duplicate or prior registration of voters. The computer system is to be designed to result in the removal of large numbers of out-of-date registrations from the county voter rolls. Purging the rolls, for example, could eventually save the state and the counties millions of dollars annually because election officials would no longer print and mail election materials to persons who are listed on obsolete county voter registration lists but who have actually moved and possibly re-registered to vote in another county.

Chapter 913 provided a $3.5 million loan from the General Fund to the Secretary of State to develop the voter registration tracking system and specified that the loan be repaid out of the savings in printing and mailing costs made possible through the new system. The loan is repayable with interest by June 30, 1999.

Projected Completion Date Not Met. The Feasibility Study Report outlining the project specified that the new computer system was to have been deployed in all California counties as of November 1997, in time to achieve the maximum possible savings in printing and mailing costs for both the June and November 1998 elections. However, a Special Project Report issued recently by the Secretary of State indicates that deployment of the system will commence in 14 counties this spring but will not be completed in all counties until July 1998 at the earliest. The Secretary of State has indicated that the delay is necessary in order to accommodate county election officials, who must play a significant role in implementing the new computer system while simultaneously making preparations for the 1998 elections.

The delay in the full deployment of the voter registration computer system means it is unlikely that the Secretary of State will achieve the full $3.5 million in savings needed to repay the loan as required by the end of the budget year. However, our review of the status of the project indicates that the project is likely to generate the additional state savings needed to repay the loan during the June and November 2000 elections. We would note that the 1998-99 expenditure plan does not assume the $3.5 million repayment.

Analyst's Recommendation. Although we believe the voter registration project remains a worthwhile state investment that will ultimately prove to be successful, the delay in its implementation means it is unlikely that $3.5 million in total state savings will be achieved in time to meet the present loan repayment deadline. Therefore, we recommend the adoption of legislation that would postpone the due date for the loan until December 31, 2000. We believe this time extension is reasonable given the progress made to date on the project and the likelihood that it will result in major additional state savings during the year 2000 election cycle.

Legal Ruling on Proposition 208 May Invalidate Funding Request

Because a federal court recently ordered a halt to enforcement of the California Political Reform Act of 1996 (CPRA), we withhold recommendation on $286,000 and 2.8 personnel-years requested to implement the measure. We recommend that the Secretary of State report at budget hearings on the status of the CPRA case and, if necessary, submit a revised funding request that takes into account the outcome of continued litigation over the matter.

In November 1996, California voters approved Proposition 208, the initiative ballot measure enacting the CPRA. In our analysis of the budget of the Fair Political Practices Commission (FPPC) (see Item 8620), we discuss in detail the ongoing litigation in federal court that has resulted in an injunction against state enforcement of the CPRA on the grounds that the measure's limits on campaign contributions are unconstitutional.

The Secretary of State, along with the FPPC, was to play a significant role in the implementation of the CPRA. The Secretary of State's 1998-99 budget includes a request for $286,000 from the General Fund and 2.8 personnel-years for the Political Reform Division to ensure that campaign finance disclosure statements filed by candidates are in compliance with the requirements of the CPRA. Because of the orders issued by the federal court and the subsequent decision of the FPPC to appeal that ruling, however, it is now uncertain what resources, if any, the Secretary of State will need during the budget year to implement the CPRA.

Analyst's Recommendation. Because of uncertainty as to the final outcome of this court case, we believe the Legislature should wait until later in the budget process to take action on the CPRA-related budget request. Thus, we withhold recommendation on the funding and staffing sought for this purpose at this time. We further propose that the Secretary of State report to the Legislature at budget hearings regarding the status of the CPRA case and, if warranted, submit a revised budget request by then in regard to implementation of the political reform law.

DEPARTMENT OF GENERAL SERVICES (1760)

The Department of General Services (DGS) is responsible for providing a broad range of support services to state departments and performing management and oversight activities related to these services. It provides these services through three programs: statewide support, building regulation, and real estate services.

The Governor's budget proposes total expenditures of $567 million from various funds (including $12.3 million from the General Fund) to support the activities of the DGS in 1998-99. This is $3.4 million, or about 1 percent, above estimated current-year expenditures.

Statewide Support Services. Expenditures for statewide support services are $340 million in the budget year, representing an increase of $6.6 million, or 2 percent, over estimated current-year expenditures. The augmentation is primarily for local assistance to continue efforts to upgrade the 9-1-1 telephone system to handle the increased volume of calls due to expanding cellular phone usage.

Building Regulation Services and Real Estate Services. Proposed budget-year expenditures for these services are $220 million—$2.9 million less than current-year levels. Major changes include (1) a decrease of $18 million for one-time expenditures in the local public buildings portion of the 1990 earthquake safety program, (2) an increase of $7 million for debt-service payments on the new state office building in Oakland, (3) an increase of $3.1 million to operate and maintain the new state office complex in San Francisco, (4) an increase of $0.9 million for repairs to state office buildings, and (5) an increase of $4.1 million (from currently authorized general obligation bonds for prisons) to remove and/or replace single-walled, underground storage tanks owned by the Department of Corrections. Federal regulations require removal of these underground tanks by December 1998.

STATEWIDE SUPPORT SERVICES

Efforts on Surplus Property Warehouses Fall Short of Legislature's Direction

We recommend that the department report at budget hearings on how it intends to phase out the surplus property warehouses, as directed in the* Supplemental Report of the 1997-98 Budget Act*.

The Legislature adopted supplemental report language last year requiring the department to develop a plan to phase out operations of the two state surplus property warehouses, which comprise the Property Reutilization Program. The Legislature's action stemmed from its concerns with excessive cost and little return on investment of the surplus property warehouses. The department was required to submit the plan to the Legislature by December 1, 1997.

On January 14, 1998 the department submitted a plan on how it was going to survey interested parties to determine *whether* to phase out the surplus property warehouses. The department indicated that it would provide its report to the Legislature in March 1998. The plan indicated that DGS may not phase out these warehouses.

In our view, the department's actions are inconsistent with the legislative direction given in the of 1997-98 supplemental report. The Property Reutilization Program was established to save tax dollars by reusing state-owned materials. However, the program lost $400,000 in 1996-97 and is projected to lose $500,000 in both 1997-98 and 1998-99. We recommend that the department report at budget hearings on how it intends to comply with the supplemental report language.

Update on CALNET Procurement

We recommend that the Department of General Services report during budget hearings on the status of the procurement of telecommunications services for state departments.

In 1996, the DGS began the divestiture of the state's telecommunications operations, known as CALNET, and the procurement of telecommunications services from another firm. CALNET, which was developed in the early 1990s, was never fully accepted by state departments as DGS had planned. As a result, it never generated the revenues anticipated and has lost, and is projected to lose, approximately $2 million in each of the last four years since 1994-95. The DGS attributes the annual financial losses to the fact that departments used other telephone services. If they had been required to use CALNET, DGS maintains that the service would have been profitable. Departments cite better service and lower rates as the reason for not using CALNET. As it is, the state still owes approximately $20 million on equipment it purchased.

Because CALNET has been losing money, the state decided to sell off its hardware (switches, routers, etc.) and procure these services from a vendor without owning any equipment. In January 1997, the department released its strategic plan for providing statewide telecommunications services, known as the *California Integrated Information Network*. The plan included moving to a privately owned and operated network, which would involve a contract with a vendor which could be valued at $500 million over five years.

Last year, we expressed concern that DGS would not be able to complete its procurement for the telecommunications services by January 1, 1998, as planned. As a result, the Legislature adopted budget bill language requiring DGS to provide the Legislature with a copy of the Feasibility Study Report and Request for Proposals and to report to the Legislature by February 1, 1998 on its progress. Because the procurement process was still underway at the time this analysis was prepared, these documents had not yet been provided to the Legislature.

Because of the impact of this procurement on state government, we recommend that DGS report to the Legislature during budget hearings on its progress in awarding this contract.

Department Unnecessarily Expanding Pilot

We recommend a reduction of $710,000 from the State Emergency Telephone Number Account, requested to implement a pilot project because the department's request is not consistent with the project's authorizing legislation. (Reduce Item 1760-101-0022 by $710,000.)

Background. Chapter 887, Statutes of 1997 (AB 1198, Hertzberg) requires DGS to develop two pilot projects to test different ways of reducing the number of nonemergency telephone calls that are made to the emergency telephone system, known as 9-1-1. The bill appropriated $200,000 from the State Emergency Telephone Number Account (known as the 9-1-1 Account) for the pilots. One pilot is to implement a new technology using a telephone number, 3-1-1, for the public to reach public safety agencies for nonemergency assistance. The other pilot requires the establishment of an educational campaign in a locale different from the first pilot on the appropriate use of 9-1-1 and how to find the appropriate seven-digit nonemergency telephone number. Chapter 887 directed the department to compare the results of each pilot project, including measuring the decrease in nonemergency calls to the 9-1-1 system in each of the two areas, and to report its findings to the Legislature.

Department Should Not Expand Pilot Project. The budget requests $985,000 from the 9-1-1 Account to fully fund the two pilot projects required by Chapter 887, plus fund a third pilot. The third pilot will test an alternative technology to implement the 3-1-1 telephone number. The department discussed the pilot projects for a special telephone number with three vendors and chose two to participate. These two vendors will provide specific technologies to switch calls to a 3-1-1 telephone system from the local 9-1-1 system.

We have two concerns with the department's proposal. First, it is unclear why the department is testing different technologies when Chapter 887 established the pilot projects to compare the merits of an educational campaign versus the creation of a special telephone number. If creation of a separate telephone number proves to be more successful than an educational campaign, the department ought to solicit bids from vendors at that time and choose the proposal, and its associated technology, which meets the needs of the state. Otherwise, the department may end up acquiring a technology that is outdated once the pilot projects are finished and the department begins implementation. Second, if the department decides to implement one of these technologies to establish a 3-1-1 telephone system statewide, it is essentially selecting a vendor which has exclusive ownership and thus effectively eliminating competition.

Analyst's Recommendation. The department indicates that to meet the minimum requirements of Chapter 887 (that is, two pilots), it needs an additional $275,000. We concur and recommend approval of that amount. As regards the third pilot, we believe that it is premature and would lead to an award of a contract without competitive procurement. Rather, the department should first determine whether an educational campaign or a 3-1-1 number is most likely to significantly reduce nonemergency calls to the 9-1-1 system. If it determines that a separate 3-1-1 number is most effective, it should then solicit bids from vendors to implement this solution. Thus, we recommend a reduction of $710,000.

REAL ESTATE SERVICES

Surplus Property Assessments

We recommend a reduction of $925,000 because several proposed consultants studies should not be undertaken in 1998-99. We also withhold recommendation on $250,000 for a master plan for the Lanterman Developmental Center pending completion and review of consulting work funded in the current year. (Reduce Item 1760-015-0002 by $925,000.)

The budget includes $2.4 million to pay consultants for various studies related to potential selling or leasing of 12 specific state properties. This total is about $1 million above the amount provided in the current year for similar property studies. The amounts proposed for each property are listed under Item 1760-015-0002. The amounts range from $50,000 for a study related to the Long Beach state office building to $1 million for further studies related to Agnews Developmental Center property.

Under Chapter 193, Statutes of 1996 (SB 1770, Johnston), the Director of General Services was given authority to sell or lease most of these properties, which were previously identified as part of the state's Surplus Property Inventory. Disposition of the state office buildings in Long Beach and San Diego was authorized in other legislation. The sale and leasing of state-owned property is the responsibility of the Asset Planning and Enhancement Branch of the department's Real Estate Services Division.

Proposal. The purpose of the consultant studies is to obtain information about the characteristics of the properties so that the state can maximize its return through selling or leasing. The studies can include environmental assessments; engineering investigation of soils, toxic materials, and site infrastructure; planning; and zoning reviews.

We recommend reductions totaling $925,000 related to the department's proposals for the following sites:

- ***State Hospital Property.*** The budget includes a total of $400,000 to prepare land use master plans for each of the state hospitals (Atascadero, Metropolitan, Napa, and Patton). According to the DGS, the intent of these studies is to identify structures at the hospitals that will be needed for continued use, potential areas for expansion, and areas that are surplus to program needs. As discussed in our analysis of the Department of Mental Health's (DMH's) capital outlay program, the state needs to develop a plan for housing an increasing number of judicially committed / penal code patients. In particular, a study is currently underway to examine options for accommodating the patients committed under the Sexually Violent Predator program. Given the significant programmatic decisions facing the DMH regarding these matters, we do not believe that land use planning for the hospitals by the DGS is warranted at this time.

- ***Chino Prison.*** The budget includes $250,000 for a land use master plan for the California Institution for Men (CIM) in Chino. A land use analysis of this 2,500-acre property was completed in fall 1997. This report identifies the potential opportunities and the constraints on state and private sector development at various sections of this large site. The report indicates that "If and when the state decides to proceed with substantial land use conversions of the CIM site for public or private use, a Strategic Facilities Master Plan will be needed . . ." This statement is correct. Major policy decisions regarding the future use of this site, such as for expansion of correctional facilities, should first be considered prior to commencing of a master plan for disposition and/or development of the property.

- ***San Diego Office Building.*** The budget includes $100,000 for a property assessment of the San Diego Office building and parking garage. The DGS indicates that disposition of this site is on hold pending an updated assessment of state facilities needs for the downtown San Diego area. In addition, $50,000 was provided for studies related to this property in the current year. Given the status of this sale, we see no reason to provide additional funding for this property in 1998-99.

- ***Unspecified Sites.*** The budget includes $100,000 to identify unspecified state properties for potential sale or leasing. This preliminary work should be accomplished by existing DGS staff. After specific properties have been identified, it would be appropriate for DGS to request funding for further study of specific properties.

- ***Vacant Property in Sacramento.*** The budget includes $75,000 for marketing strategies for selling a portion of the former California Highway Patrol Academy in Sacramento. The DGS indicates that it is currently negotiating for the sale of this property to the City of Sacramento. Funding for marketing of the property should therefore not be needed.

In addition to the above reductions, we withhold recommendation on $250,000 proposed to prepare a master plan for the Lanterman Developmental Center in Pomona. The DGS, with funding for consultants provided in 1997-98, is performing an initial survey of the buildings and land at the center. Based on the results of survey, the DGS and the Department of Developmental Services will determine what portions of the property might be surplus to program needs. We will review the conclusions of this initial survey, which should be completed by the spring, and evaluate whether the budget proposal for master planning is consistent with those conclusions. We therefore withhold recommendation on the $250,000 proposed for master planning this site.

HOUSING AND COMMUNITY DEVELOPMENT (2240)

The mission of the Department of Housing and Community Development (HCD) is to help promote and expand housing opportunities for all Californians. As part of this mission, the department is responsible for implementing and enforcing building standards. The department also administers a variety of housing finance, economic development, and rehabilitation programs. In addition, the department provides policy advice and statewide guidance on housing issues.

The budget proposes expenditures of $164 million for 1998-99. This is a 1.4 percent decrease from the estimated current-year expenditures. The proposed General Fund appropriation of $14.9 million accounts for 9.1 percent of the department's funding. Federal funds account for $103.9 million, primarily for the Community Development Block Grant and Home Investment Partnership Act programs. A number of state special funds provide the remainder of the department's funding. The department has a proposed staffing level of 438 personnel-years.

Below, we review HCD's Emergency Housing Assistance Program (EHAP) and the department's proposal to verify the alien and citizenship status of program clients.

High Costs to Administer Homeless Grants

We recommend that the Legislature enact legislation simplifying the administration of the Emergency Housing Assistance Program in order to maximize the dollars going for direct homeless assistance.

As has been the case for the past several years, the budget proposes $2 million from the Housing Trust Fund to fund the EHAP. The EHAP is a grant program that provides funds to local governments and nonprofit organizations to support shelters and services for the homeless. The funds can be used for a wide variety of purposes, including rehabilitation, lease payments, general operations, housing vouchers, rental assistance, and administrative costs. Each county receives an allocation of EHAP funds, which are then distributed to various local agencies. In 1996-97, 114 grants totaling $1.9 million were distributed.

Program Has Improved Management and Service. Chapter 1022, Statutes of 1993 (SB 388, Rosenthal), created EHAP to replace the Emergency Shelter Program, a similar program but one that suffered from various inefficiencies and service problems. The new program included a number of innovations, such as the creation of Designated Local Boards (DLBs) to help administer the grants. Local communities can choose to create a DLB to replace HCD as the entity that ranks the applications in order of funding priority. In addition, the department has instituted a number of streamlining measures to simplify and speed up the distribution of grant funds.

Program Design Necessitates High Administration Costs. The program currently requires that each county receive an allocation of at least $10,000 in grant funds, and that rural counties receive at least 20 percent of total program funds. The remaining funds are added to county allocations based on local levels of poverty and unemployment. Funds are then distributed within each county to various government and nonprofit agencies that provide services for the homeless. In 1996-97, the average grant size was $16,650.

The department enters into a legal contract with each grant recipient. Over the course of the grant, the department monitors the recipient to ensure compliance with the requirements of the grant. While the contract and monitoring requirements help ensure funds are used appropriately, it is costly—the department spent an average of $4,600 to administer each grant in 1996-97. This level of administrative costs does not include the significant amounts of time and money that grant recipients spend applying for and receiving the funds. Figure 8 shows that the budget proposes to spend 22 percent of EHAP expenditures on administrative costs. While

Figure 8

EHAP Administrative Costs

1996-97 Through 1998-99
(Dollars in Thousands)

	1996-97	1997-98	1998-99
Administrative costs	$523	$611	$562
Local assistance	1,898	3,020	2,000
Administrative costs as a percent of total expenditures	22%	17%	22%

the program could distribute larger grant denominations without increasing administrative costs, the relatively small grant amounts under the current program design result in excessively high administrative costs.

Source of Administrative Funding Will Be Depleted in 1998-99. For the recent annual allocations of EHAP funds, the department has paid its administrative costs from an on-going reserve in the Emergency Housing Assistance Fund. This reserve, funded by interest earnings and unused previous year allocations, has allowed the department to distribute the entire annual EHAP appropriation to counties for direct homeless assistance. While the department proposes to use the same approach for funding administrative costs in 1998-99, the fund's reserve will be virtually exhausted in the proposed budget year. Therefore, to pay the current level of administrative costs in 1999-00 the Legislature would face the following choice:

- Pay administrative costs from the annual $2 million appropriation—reducing the funds that flow to local service providers.
- Augment the program from the General Fund by about $500,000.

Recommend Restructuring Program to Maximize Dollars for Actual Assistance. The current dollars that are annually spent on administering the EHAP program could be better spent directly providing services for the homeless. Consequently, we recommend that the Legislature enact legislation restructuring the program to eliminate its costly contract and monitoring components. Instead, the state should simply make the current county allocations available to those county governments that request it—with the requirement that the monies be spent on homeless services.

The 17 counties that currently use DLBs to distribute the grant funds should be encouraged to continue the use of this procedure. These boards base their decisions on an existing homeless strategy plan and could continue to do so. Since these DLB counties receive almost 60 percent of the EHAP funds, the majority of funds would continue to be allocated under current procedures. Other counties could integrate the allocation of EHAP funds within their existing administrative and budgeting processes.

Although the state would lose some of its ability to ensure that the funds are spent according to state priorities, local governments and service providers would likely take great strides on their own to ensure that the EHAP funds were put to good use. If needed for oversight purposes, the state could require a short report from counties listing grant recipients, amounts distributed, and the purpose for which the funds were used.

Alien Verification Fee Plan Lacks Necessary Federal Guidance

Given the lack of federal guidance on its new verification requirement, we recommend that the Legislature delete the authority for $258,000 in reimbursements and 3.8 positions for the purpose of verifying that benefit recipients are citizens or qualified aliens. (Reduce Item 2240-001-0001 by $258,000.)

The 1996 federal welfare reform legislation, known as the Personal Responsibility and Work Opportunity Reconciliation Act, requires that recipients of state and local government benefits be either U.S. citizens or qualified aliens. In terms of the state's housing programs, a public benefit pertains to "public or assisted housing" and professional licenses provided by the department. The department proposed regulations in September 1997 that would govern its verification procedures, including charging a fee of an estimated $15 for each verification performed. The regulations have gone through a public comment process and are currently being revised by the department.

The budget proposes $258,000 in fee reimbursement authority and 3.8 positions to implement these procedures in 1998-99. Of the total augmentation, $79,000 and 1 position would be ongoing.

Department Lacks Sufficient Federal Guidance to Implement Procedures. The department has attempted to move forward in the implementation of the federal verification requirement. However, the federal government has thus far failed to provide sufficient guidance. The United States Attorney General has issued initial guidelines for *federal agencies* to implement the requirement, but regulations for *state and local governments* have not yet been issued. Moreover, expected regulations from the federal Department of Housing and Urban Development (HUD) on housing-related benefits also have not yet been issued. These HUD guidelines would govern the state's components of federal housing programs, as well as provide clarifications for HCD's non-federal housing programs.

Without these federal guidelines, major legal questions regarding the verifications will not be clarified. For instance, the definition of which "public and assisted housing" programs would be subject to verification is unclear. In addition, the federal legislation exempted nonprofit organizations from performing verifications, but whether the state is responsible for verifications in these cases is unresolved.

Current Proposal Would Also Encounter Implementation Problems. The initial HCD approach proposes using an Immigration and Naturalization Services (INS) automated phone service to perform verifications.

However, the U.S. Attorney General has since informed states that this system will be unavailable for routine verifications. Instead, the department would be required to send document copies to INS local offices for verification. This process would likely take a minimum of 30 days and potentially much longer if the local offices are inundated with requests. Lengthy periods for verification could delay the provision of needed housing services to applicants.

Recommend Denying Approval Pending Federal Guidelines. For the reasons noted above, we recommend that the department's budget request for a verification and fee system be denied until federal guidelines are provided. At that time, the department will be in a better position to develop a proposal to submit to the Legislature.

TRADE AND COMMERCE (2920)

The Trade and Commerce Agency—created in 1992—is the state's primary economic development entity for promoting the establishment, retention, and expansion of business, employment, and international trade in California. It promotes tourism and foreign investment as well. The agency also has been designated as the entity leading the state's efforts in defense conversion.

The budget proposes expenditures of $133 million from various funds, including $103 million from the General Fund, for the agency in 1998-99. The total budget is $43.2 million, or 48 percent, more than estimated current-year expenditures. The budget-year increase is mainly due to a $50 million General Fund appropriation to the Infrastructure and Economic Development Bank for loans, loan guarantees, and other types of financing. The agency's budget has increased by over 230 percent since it was created in 1992. (Excluding the Infrastructure Bank augmentation, the agency's budget has increased over 150 percent.)

Other General Fund increases include $5.2 million for small business assistance programs and the establishment of four new trade offices. These increases are partially offset by reduced expenditures in a variety of areas—primarily in local assistance for removal of underground storage tanks and reduction in various special funds for one-time costs for local economic development projects.

New and Expanded Foreign Offices

We recommend that the Legislature delete $1,053,000 requested for four new foreign offices and expansion of other foreign offices because (1) establishing foreign offices should be considered as a policy issue through legislation other than the Budget Bill and (2) additional funds are not needed to sustain the current level of activity in existing offices. (Reduce Item 2920-012-0001 by $1,053,000)

The budget includes $1,053,000 from the General Fund to augment the level of expenditures on the state's foreign offices. This amount includes $750,000 to establish four new foreign offices—Singapore; Shanghai, China; Seoul, South Korea; and Sao Paulo, Brazil. The agency indicates that rather than develop "full-scale" offices, these would be staffed through a consultant contract at each location and funded with augmentations to the current foreign offices in Hong Kong, Japan, and Mexico, respectively. The augmentations would provide $150,000 for Shanghai and $200,000 for each of the other offices. The agency also has included $80,000 in the request for the Hong Kong office to continue a contract established in 1996 for a consultant to maintain a presence in Jakarta, Indonesia. These proposals are similar to the agency's request in 1997-98 that was denied by the Legislature.

Also included is $123,000 to increase the London office by one position and $100,000 for the Mexico office for a consultant under an interagency agreement with the California Department of Food and Agriculture.

The requested $1,053,000 would bring the total budget for these offices to $5.5 million, a 23 percent increase compared to estimated current-year expenditures.

Background. The state currently operates foreign offices in Tokyo, London, Mexico City, Frankfurt, Hong Kong, Taipei, and Johannesburg. There is also a representative office in Jerusalem, operating as the California-Israel Exchange, and a consultant contract for representation in Jakarta. According to the agency, the purpose of the foreign offices is to build additional business for the state that would not otherwise have been brought to California. In assessing the need for new offices, the agency considers:

- *Economic factors*, such as economic strength of a country, macroeconomic stability, market potential, infrastructure development, level of international trade and investment, and the existing economic relationship with California.
- *Strategic factors*, such as the role of the region in which the country is located; need for specific on-site assistance to California companies and international programs; need for assistance in overcoming language, business, and cultural barriers; and ability of the office to serve as a hub for the region.
- *Input from businesses* (considered decisive in considering the demand for a new location).

In addition to the foreign offices, the agency operates international trade and investment programs through the Office of Foreign Investments, Office of Export Development, Export Finance Office, Environmental Export Program, Office of Trade Policy and Research, and the Office of California-Mexico Affairs. California companies also have available the U.S. Department of Commerce, U.S. Department of Agriculture, and the U.S. Agency for International Development located around the world in embassies and consulates of the United States. In addition, the American Chamber of Commerce network helps support United States companies, and the World Trade Center in New York operates as a franchise-driven membership association. Thus, California companies have wide-ranging and extensive resources available for assistance in the foreign market.

Foreign Office Need and Location Are a Legislative Policy Decision. We believe that the establishment of foreign offices is a legislative policy decision that should be considered in policy legislation rather than through the budget. Specifically, the appropriate policy and fiscal committee in each house should consider policy issues such as (1) the extent that state government should be involved in foreign investments and trade; (2) criteria for determining when and where to open foreign offices; (3) methods for quantifying the benefits to the state that are a direct, and indirect, result from each existing and proposed location; and (4) the funding for these efforts (for example, since business is a major benefactor from these offices, should there be a sharing in the cost?). These decisions also need to be made in the context of other state and federal government activities in foreign investment and trade. These and other issues should be considered through legislation other than the Budget Bill. After specific policies are adopted by the Legislature, the cost of operating the foreign offices established under these policies would appropriately be considered in the annual Budget Bill. Consequently, we recommend that the Legislature delete the $830,000 requested for the new foreign offices and for extension of the Jakarta contract (that is currently funded from existing resources).

Expansion of Existing Foreign Office Not Justified. As mentioned above, the agency has also requested $123,000 for an additional position at the London office and $100,000 for a consultant (under an interagency agreement with the Department of Food and Agriculture) at the Mexico office. The agency has provided no justification for these requests, other than to cite the economies of both countries and to indicate that the augmentations would provide more resources to the foreign offices. There is no indication of what the Legislature could expect as a result of the expenditure of an additional $230,000. Consequently, we recommend the Legislature delete the $230,000 associated with these requests.

Agency Should Set Priorities Within Existing Resources

We withhold recommendation on $7.8 million in various augmentation requests (1) until the agency reassesses the need for these increases by setting priorities within current resources and (2) pending the agency's submission of information identifying the specific expected outcomes from the augmentations and how these outcomes will be measured.

The budget includes $7.8 million for various augmentations related to the agency's programs in economic development, international trade, and administration. As mentioned above, the agency's budget has increased by over 150 percent since it was created in 1992. During this time the authorized positions for the agency have increased from 197 to 333 (proposed in the budget), a 69 percent increase. These increases have occurred despite the expectation at the time the agency was created that there would be economies and savings as a result of consolidating several state departments into the new agency. Given the expectations when the agency was created and the dramatic increase in the agency's budget and staffing levels since that time, we believe the agency should reassess all augmentation requests and set priorities within existing resources instead of continuing to increase its budget and staff for each desired incremental change in activity.

In addition, based on our review of the justifications for the proposed augmentations, the agency needs to provide the Legislature details on what outcomes are expected and how these outcomes would be measured for each of the proposals. For example:

- The $3 million request to augment the Small Business Expansion Fund is primarily based on the increasing operating costs of the Financial Development Corporations and the annual default of about $2 million in loans. It is not clear why the corporation's operating costs are increasing or what benefit the state is receiving from guaranteeing loans that default at the cost of $2 million per year.

- It is not clear what the state benefit will be from spending $245,000 to permanently establish an Office of Military Base Retention. According to the agency, with the base closure rounds complete the "Defense Department is again free to shift workload as it sees fit." The agency indicates that the office staff would study the strengths and weaknesses of military bases from a military perspective and advise local communities on how to keep a base from being closed or downsized. The agency has not identified which bases are a concern or what expertise the staff has to advise the

Defense Department on military matters. Thus, it is not clear what the Legislature could expect from the expenditure of the $245,000.

As discussed above, the agency's budget has increased dramatically since 1992 and it is not clear what outcomes the Legislature could expect from the expenditure of an additional $7.8 million. In view of these factors, we withhold recommendation on the $7.8 million (1) until the agency reassesses the need for these increases by setting priorities within current resources to fund some, or all, of the requested augmentations within existing resources, and (2) pending the agency submitting information identifying the specific expected outcomes of spending additional funds and how the outcomes will be measured

DEPARTMENT OF FINANCE (8860)

The Department of Finance (DOF) advises the Governor on the fiscal condition of the state; assists in developing the Governor's budget and legislative programs; evaluates the operation of the state's programs; and provides economic, financial, and demographic information. In addition, the department oversees the operation of the state's accounting and reporting systems. Within the DOF is the Technology Investment Review Unit, which is responsible for evaluating the return on investment of proposed technology projects.

The Governor's budget proposes expenditures of $29.6 million to support the activities of the DOF in 1998-99. This is an increase of $609,000, or about 2 percent, above estimated current-year expenditures.

Highlighting Information Technology Expenditures in the Budget

We recommend that the Legislature adopt supplemental report language directing the Department of Finance to identify in the* 1999-00 Governor's Budget *each department's total information technology expenditures and all information technology project expenditures of $1 million or more, by project title.

Lack of Expenditure Information. Currently, no standard for reporting information technology expenditures throughout state government exists. Financial data on major information technology projects often provide no clear understanding of important facts about the projects. As a consequence, it is often difficult for the Legislature to ascertain how much money is or has been allocated for a particular project. With over $2 billion appropriated for information technology each year, we believe that it is important that the Legislature have information that clearly shows how much money is being appropriated for the many information technology projects underway.

Ideally, the state should have an automated accounting and budgeting system that makes information technology projects and expenditures easily discernable when queried. Such a change would probably take substantial time and effort, however.

Last year, the Legislature adopted supplemental report language directing the DOF to identify in the Governor's budget the total proposed expenditures for information technology, as well as project expenditures of $1 million or more, by project title. The DOF did not include this information in the *1998-99 Governor's Budget*, but indicates that it will present a separate report to the Legislature with the information.

Analyst's Recommendation. We recommend that the Legislature direct the DOF to identify for 1999-00 each department's total information technology expenditures and all information technology project expenditures of $1 million or more, by project title.

Specifically, we recommend the following supplemental report language:

> The Department of Finance shall display for each organizational budget contained in the *1999-00 Governor's Budget*, the total proposed expenditures for information technology, as well as any information technology project expenditure of $1 million or more, by project title, in any of the three fiscal years covered in the budget.

Audit of Data Centers Due to Be Published Soon

We recommend that the Department of Finance report to the Legislature during budget hearings on the Health and Welfare Agency Data Center and the Stephen P. Teale Data Center on the findings of its recent financial audit of the two centers.

The *1996-97 Budget Act* provided $800,000 to the DOF to perform a financial audit of the state's two major data centers, the Health and Welfare Agency Data Center (HWDC) and the Stephen P. Teale Data Center (TDC), to determine the financial feasibility of consolidating them. The audit is due to be published in early 1998.

We recommend that the DOF report its findings to the Legislature during budget hearings on HWDC and TDC.

OFFICE OF ADMINISTRATIVE LAW (8910)

The Office of Administrative Law (OAL) was created in 1979 and is charged with reviewing regulations promulgated by state agencies to ensure the regulations are in compliance with the Administrative Procedures Act. Thirty days after the regulations have been adopted by OAL, they become law. The office is charged with publishing and continuously updating the official copies of adopted regulations, known as the California Code of Regulations.

The Governor's budget proposes expenditures of $2.2 million to support the activities of OAL in 1998-99. This is virtually the same level as estimated current-year expenditures.

No Funding Proposed to Meet Statutory Requirement

The Office of Administrative Law's budget for the current and budget years contains no appropriation or redirection of existing resources to publish the regulations on the Internet, as required by a 1996 statute.

Chapter 501, Statutes of 1996 (SB 1910, Johannessen) requires OAL to publish state regulations on the Internet by July 1, 1998. Currently, a private firm publishes the California Code of Regulations under a contract with the state. Under the current contract, governmental entities (including the Legislature) and the public must purchase the published regulations solely from the publisher. The contract expires on April 1, 1998, at which time the Code of Regulations must be returned to OAL in an electronic form.

Our review indicates that the OAL's current-year budget and proposed budget for 1998-99 does not contain funding—either a new appropriation or a proposed redirection of funding—to publish the regulations on the Internet as required by Chapter 501. When we inquired, the OAL indicated it had no plans to implement the measure at this time.

DEPARTMENT OF VETERANS AFFAIRS AND VETERANS' HOMES OF CALIFORNIA (8955-8965)

The Department of Veterans Affairs (DVA) provides services to California veterans and their dependents, and to eligible members of the California National Guard. The principal activities of DVA include: (1) providing home and farm loans to qualifying veterans, using proceeds from the sale of general obligation and revenue bonds; (2) assisting eligible veterans and their dependents in obtaining federal and state benefits by providing claims representation, subventions to county veterans service officers, and direct educational assistance to qualifying dependents; and (3) operating veterans' homes in Yountville and Barstow with several levels of medical care, rehabilitation services, and residential services.

The budget proposes total expenditures of $360 million for DVA in 1998-99. This is $7.5 million, or 2 percent, less than the estimated current-year expenditures. Total expenditures from the General Fund during the budget year would be $46 million, which is $7.1 million, or 18 percent, more than the estimated current-year level.

The decrease in the overall budget reflects significant decreases in the Cal-Vet Farm and Home Loan Program (known as the Cal-Vet loan program) that are partly offset by staffing increases and a major information technology project at the Yountville facility that are largely supported by the General Fund.

Time to Rethink State Approach to Veterans' Assistance

We recommend the adoption of budget bill language initiating a review of the potential timing, availability, and priority use of surplus funds in the Cal-Vet home loan program to meet the unmet growing needs of California veterans. We also recommend the adoption of supplemental report language outlining the Legislature's intent to phase out new lend-

ing activity by the program by 2007 and to seek voter approval in June 2000 to transfer surplus funds for use for specific, identified programs that would benefit California veterans.

The Cal-Vet loan program has provided more than 400,000 California veterans of various wars the opportunity to buy a farm or home through state assistance. However, participation by veterans in the program has been declining sharply and the program has suffered significant financial and operational difficulties.

In our January 1998 report, *Rethinking the Cal-Vet Loan Program,* we outlined to our proposal to phase out additional Cal-Vet lending activity by 2007 and to direct surplus Cal-Vet funds to programs that will benefit both aging war veterans and state taxpayers. We noted that far fewer veterans than in the past need home loans, but that these veterans have a growing need for medical care, nursing home care, Alzheimer's treatment, and other types of state assistance. We concluded that it was time to rethink the state's approach to veterans' assistance given the changes which have occurred in recent times. We proposed in the report that use of surplus funds be submitted to California voters for approval, and that the transfer of such funds be accomplished carefully by means that ensure that all obligations of the state to bondholders are met and that adequate reserves are retained to meet the needs of the program.

Preliminary Steps Necessary. Before the Legislature acts on our proposal to phase out program lending activity and to ask voter permission to shift surplus Cal-Vet funds, we believe several preliminary steps are necessary:

- The DVA should conduct an analysis of the Cal-Vet operating fund to determine the size and the timing of the availability of the surplus.
- The DVA and the Veterans Finance Committee of 1943, a panel with authority over the interest rates set for the program, should analyze existing contracts related to the issuance of Cal-Vet bonds, as well as any relevant sections of the federal tax code, to ensure that they would not be violated by a future redirection of surplus funds.
- The California Veterans Board, which provides oversight of Cal-Vet and other veterans programs, should conduct public hearings to solicit the testimony of veterans and the general public and report to the Legislature regarding the best use of the available surplus.

Analyst's Recommendation. We recommend that the Legislature approve budget bill language directing that these preliminary activities occur during the 1998-99 budget year in order that it may take further legislative action to implement these changes in the program during the 1999 legislative session. Specifically, we recommend adoption of the following budget bill language:

> (a) The Department of Veterans Affairs (DVA) shall conduct an analysis of the Cal-Vet operating fund to determine the size and the timing of the availability of surplus funds that could be transferred into other programs that would benefit California veterans and state taxpayers. The DVA may at its discretion employ cash-flow and debt-management consultants to assist in this analysis, which shall detail how much of the cash and investment assets in the Cal-Vet operating fund are needed for prudent reserves to (1) ensure the repayment of outstanding Cal-Vet program debt, and (2) to provide all funding necessary for loan and related insurance program operations. The analysis shall be based upon the assumption that the issuance of new Cal-Vet loans would cease by the year 2007 in accordance with federal restrictions on general obligation bonds. The analysis shall detail, year by year for the remaining duration of the program until all outstanding program debt and loans are retired, the projected amount of surplus funds that could be available for transfer for other purposes in each year. The DVA shall provide the analysis to the Legislature by January 1, 1999.
>
> (b) The DVA and the Veterans Finance Committee of 1943 shall analyze existing Cal-Vet program agreements with bondholders, bond insurers, and bond rating agencies, as well as any relevant sections of the federal tax code, to ensure that they would not be violated by a future redirection of surplus Cal-Vet funds. If DVA or the Committee shall determine the existence of a conflict, they shall report to the Legislature regarding the nature of the conflict, the projected time period during which such a conflict would exist, and the steps that could be taken to resolve the conflict. The DVA and the Committee shall report its findings and determinations to the Legislature by January 1, 1999.
>
> (c) The California Veterans Board shall conduct public hearings to solicit the testimony of veterans and the general public and report to the Legislature regarding the best use of the available surplus in the Cal-Vet operating fund. The Board shall commence its hearings no sooner than January 1, 1999, and shall provide its completed report to the Legislature by May 1, 1999.
>
> (d) All reports to the Legislature specified in this Provision shall be provided to the Joint Legislative Budget Committee, the fiscal committees of the Assembly and of the Senate, and the policy or select committees of the Assembly and of the Senate relating to veterans affairs issues.

In order to clarify the Legislature's intention to implement significant changes in the Cal-Vet program, we also recommend adoption of the following supplemental report language:

> It is the intent of the Legislature that:
>
> (a) The Cal-Vet home loan program shall cease making additional loans effective January 1, 2007;
>
> (b) The Department of Veterans Affairs (DVA) and the California Veterans Board shall continue loan-servicing, debt management, cash management, and other necessary operations of the program until all outstanding program debt and mortgages have been retired, except that the Department of General Services shall conduct a procurement for Cal-Vet loan services by January 1, 2006, in which DVA could compete with vendors on the basis of cost-effectiveness and service quality for the continued provision of those services;
>
> (c) The Legislature shall consider placing a ballot measure before the California voters in June 2000 or at another appropriate time seeking authorization to transfer surplus Cal-Vet funds for use for specific, identified programs of benefit to California veterans and state taxpayers.

Serious Deficiencies in Care Found at Yountville Home

We recommend that the Department of Veterans Affairs (DVA) and the Department of Health Services report at budget hearings regarding the action taken by the Yountville home to address substandard care for nursing home residents. The DVA should also report on the status of the federal regulatory actions to fine and withhold some federal support for the home and how the federal actions have affected the home's operation and budget.

Background. The Veterans' Home of California, which has been operating at Yountville in Napa County since 1884, provides five levels of medical and residential care for about 1,125 veterans. Specifically, it provides: (1) an acute care hospital for residents requiring significant medical services; (2) a skilled nursing facility (SNF) providing assistance in daily living, nursing, and therapy; (3) an intermediate care facility (ICF) providing both reduced living assistance and a minimal level of nursing care; (4) residential care in which minimal living assistance is provided; and (5) domiciliary care in which residents are fully self-sufficient.

The proposed 1998-99 budget for operation of the Yountville home is $60.9 million, an increase of $6.5 million, or 12 percent, over the current-year expenditure level. Of this sum, $31.5 million, or 52 percent, of support for the home would come from the General Fund. That is a significant increase from the current year, in which 46 percent of financial support for the home came from the General Fund. The balance of funds to support the facility consists primarily of Medicare and Medi-Cal reimbursements for medical and nursing services, aid and attendance allowances from the U.S. Department of Veterans Affairs, and fees paid by home residents.

State Inspection Led to Federal Penalties. In September 1997, the California Department of Health Services (DHS) completed a survey of the SNF and ICF nursing home beds and determined that the Yountville home was not in compliance with federal rules on the quality of care of patients. The U.S. Health Care Financing Administration (HCFA) concurred in the survey findings, concluded that they were "serious deficiencies," and determined that the conditions at the home "constitute substandard quality of care" for patients in nursing home wards.

These actions by federal authorities have significant potential consequences for the home's operations and finances. The HCFA imposed a $250 per day fine on the home, effective September 23, 1997, and indicated that those fines would continue until HCFA determined that the deficiencies had been remedied. More significantly, the HCFA prohibited federal Medi-Cal or Medicare reimbursements for any patients admitted to its SNF or ICF beds after November 11, 1997, until such time it determined that the deficiencies had been remedied.

The DVA has submitted a plan to correct the deficiencies noted by HCFA and the facility has since been reinspected. At the time this analysis was prepared, the suspension of federal payments and the daily fines of the facility still remained in effect but, according to DVA, were not anticipated to exceed an amount in the tens of thousands of dollars because of a slowing in admissions to the nursing beds. Federal authorities indicated that the findings of deficiencies may soon be resolved. In that event, the fines would cease and federal support for newly admitted patients would be reinstated.

However, it is likely that the nursing home wards would be subject to reinspection sometime within the next year to ensure that the problems found by the DHS are not continuing. A recurrence of the problems would put the home at risk of further fines, further suspensions of federal payments, and, if serious deficiencies were found, a federal order to close down the nursing home operation.

Analyst's Recommendations. Because of the significant potential ramifications of HCFA's actions for the home, we recommend that the DVA and the DHS report at budget hearings regarding the actions being taken by the home to address substandard quality of care for nursing home residents. The DVA should also report on the status of the federal regulatory actions to fine and withhold some federal support for the home and how the federal actions have affected the home operation and budget. The DVA should specifically report at budget hearings regarding: (1) the amount of fines assessed against the home, (2) the amount of funding lost due to HCFA's suspension of federal support, and (3) whether the fines levied against the home will be appealed.

Yountville Budget Includes Funds For Computers, More Hospital Beds

We recommend that the 1998-99 budget request for the Yountville veterans' home be reduced by about $2.4 million and 57 positions because of spending proposals that lack justification. We also recommend approval of $5.7 million in budget augmentations sought for the home, contingent upon the adoption of Budget Bill and supplemental report language and the receipt of additional information by the Legislature. We further recommend a study of the mix of nursing beds provided at the home. (Reduce Item 8960-011-0001 by $1,882,000, reduce federal funds by $255,000, and reduce reimbursements by $273,000.)

Augmentations Sought for Home. The 1998-99 budget proposal for the home includes the following augmentations requesting an additional $7.4 million and 41 positions:

- About $4.9 million on a one-time basis to implement a new computerized information system that can improve the tracking of medical costs and billings.
- About $1.7 million and 36 positions to begin phasing in 84 additional SNF and 58 additional ICF beds in Holderman Hospital Wings B and E upon completion of a seismic safety project. (The full cost of this proposal in 1999-2000 after all beds are activated would be $5.1 million and 131 positions.)
- $116,000 to add three staff members to drive home members to medical appointments.
- $193,000 for the one-time cost of dishes and other supplies to reopen the renovated kitchen and dining hall at the home, and an additional $291,000 on an ongoing basis to improve the quality of food served there.
- $250,000 for the one-time cost of purchasing a new heating, ventilation and air-conditioning (HVAC) system for the Lincoln Theater at the home. A nonprofit community organization has agreed to

provide matching funds to upgrade the system to a standard suitable for a theater facility and will assume the cost of maintaining the system.

- $38,000 for one position to reopen the cemetery at the home for the burial of the cremated remains of home residents and to improve cemetery landscaping.
- One position, and approval to redirect $30,000 in existing funds for a staff member to repair wheelchairs of home residents.

Analyst's Recommendations. We recommend that the 1998-99 budget request for the Yountville home be reduced by $2.4 million and 57 positions. We also recommend approval of $5.7 million in budget augmentations for the home with the Budget Bill and supplemental report language and other changes proposed below:

- ***Computer Project.*** We recommend approval of the $4.9 million requested for the computer system, because of its potential to greatly increase federal funding and other reimbursements for the support of the home. Approval should be contingent upon the adoption of the following budget bill language requiring that a similar computer system now being installed at the Barstow veterans' home has been implemented successfully:

  > Of the funds appropriated in this item, the sum of $4,898,000 shall be available for the installation of the Veterans Home Information System at the Veterans' Home of California at Yountville. These funds shall be expended subject to a determination by the Department of Veterans Affairs oversight contractor, the Department of Finance, and the Department of Information Technology that all modules installed at the Barstow veterans' home have been successfully implemented, except for the cost accounting module that is not scheduled to be installed until during 1998-99. Notification of that determination shall be transmitted to the Joint Legislative Budget Committee and the fiscal and relevant policy committees of the Assembly and Senate.

- ***Hospital Expansion.*** We recommend deletion of the funding and positions sought for the Holderman hospital expansion (in effect delaying the activation of additional beds for six months until 1999-00) for several reasons. First, the additional SNF and ICF beds are not needed to support the existing residential population of the home. Historically, the department has argued that the need for SNF and ICF beds is dependent upon size of the residential and domiciliary population. The DVA, however, has no plans to request funding for residential or domiciliary expansion until

1999-00. (In our view, adding more residential or domiciliary beds would not be advisable until the 100 vacant beds at the new 400-bed Barstow veterans' home have been filled.) Second, it would be premature to expand nursing home beds so soon after the home has been fined and federal support suspended for providing a substandard quality of care for patients. By waiting until next year after another reinspection of home has been completed, the Legislature can ensure that existing patients are cared for properly before additional patients are added. Third, the DVA has indicated that it intends to fill some of the new nursing home beds directly through new admissions. This is contrary to the longstanding policy of the home of only admitting persons to the home who are in good health. Lastly, waiting a year would provide time to conduct the study we recommend below of the appropriate mix of nursing beds provided at the home.

- ***Acuity Study.*** We recommend that funding be provided to reimburse the Bureau of State Audits (BSA) for the cost of conducting a study during 1998-99 that would ensure that the home has the proper mix of SNF and ICF nursing beds before additional beds are opened at Holderman hospital. The BSA, which has recommended that such a study be undertaken, should report at budget hearings on the amount of funding necessary to conduct a so-called clinical acuity study.

- ***Motor Pool.*** We recommend deletion of the $116,000 and three staff requested to drive home members to medical appointments because we believe this task could be accomplished at less cost through contracting with medical transportation providers. The home's budget request indicates that it did not evaluate this alternative before requesting staff for this new function. A nonprofit provider of nonemergency medical transportation in Napa County has indicated that it could meet the needs of home residents and is fully insured to accept that risk. We further recommend the adoption of supplemental report language directing the Department of General Services to review whether the existing motor pool, with staffing costs of more than $156,000, and additional expenditures for the maintenance and operations of vehicles, could be reduced through reliance on outside providers for the transportation needs of members. We propose the following language:

> The Department of General Services shall evaluate the motor pool at the Veterans' Home of California to determine whether expenditures for staffing and vehicles could be reduced by contracting with outside providers to meet the transportation needs of home

> members. The department shall report its findings to the Joint Legislative Budget Committee and the Legislature's fiscal and appropriate policy committees by December 1, 1998.

- ***Kitchen Remodeling.*** We recommend a net reduction of $285,000 and 18.5 dietary and food-service positions. At the time it requested $10 million to remodel the home's kitchen facilities, the home committed to making this personnel reduction and identified the specific positions that could be eliminated because the new operation would be more efficient. The personnel reduction from 114.5 personnel-years to 96 was a condition of legislative approval for the project adopted in supplemental report language in 1995-96. The DVA now is asking for additional funds for supplies to open the remodeled kitchen, but has failed to keep its commitment to reduce its funding and personnel. In documents supporting its request, the department cites personnel cuts to food services that were made *before* the remodeling project was approved by the Legislature and *before* DVA made its commitment to the personnel reductions. The reduction we have proposed reflects the activation of the new kitchen on January 1, 1999, halfway through the fiscal year. The full-year savings in 1999-00 would be $569,000.

- ***Lincoln Theater.*** We recommend approval of the full $250,000 requested for the Lincoln Theater HVAC system. However, we further recommend that the money be budgeted as a capital outlay item, rather than within the support budget of the home, in order to ensure that proper fiscal controls are in place for this work. We also recommend that the proposed Lincoln Theater funding be contingent upon the adoption of budget bill language requiring the commitment of the matching funds from the home's nonprofit partner to complete the work on the air-conditioning and heating system. We propose the following language:

  > The funds appropriated in this item for a new heating, ventilation, and air conditioning (HVAC) system for the Lincoln Theater are available for expenditure only if the Friends of Lincoln Theater, a nonprofit entity, provides the additional funds necessary to install a theater-quality HVAC system.

- ***Acute Care Hospital.*** We recommend DVA discuss at budget hearings the status of a report required by the Legislature regarding the potential for expanded use of the acute care hospital at the home. The report, which was due by January 1, 1998, but had not been received at the time this analysis was prepared, will provide guidance to the Legislature as to whether a $257,000 reduction in two physician positions at the hospital approved last year should be continued into 1998-99. Funding for the physicians was temporarily suspended in 1997-98 in order to allow for restoration of the positions in 1998-99 if the study indicated that expanded use of the acute care hospital was possible.

- ***Laundry Savings.*** We recommend that the DVA budget be reduced by $350,000 to reflect savings anticipated from a 1997-98 budget decision to contract out laundry services. The DVA, which has indicated that contracting out efforts are proceeding as planned, should report at budget hearings regarding the specific positions that should be removed from the DVA budget.

- ***Additional Reimbursements.*** We recommend that the DVA report at budget hearings regarding its estimate of the hundreds of thousands of dollars of additional funds that are likely to be available for reimbursement of certain pharmacy costs and for care of home residents during 1998-99, but that are not now included in the proposed 1998-99 budget for the home. We recommend that the additional federal funds and reimbursements be reflected in the 1998-99 budget for the home and that General Fund expenditures be reduced by a commensurate amount.

We recommend that the augmentation requests of the home for supplies for the new kitchen ($193,000), for improving the food quality ($291,000), for cemetery operations ($38,000), and establishing a wheelchair repair position be approved as budgeted.

Many Barstow Home Beds Still Vacant Two Years After Its Doors Have Opened

We withhold recommendation on the $16.9 million budgeted for the operation of the Barstow veterans' home because, two years after its opening, occupation of the facility is once again lagging behind schedule. We recommend that final legislative action on the Barstow home budget be postponed until the May Revision when it will be more clear whether 100 vacancies in the home will be filled and the potential availability of additional federal funds and collections from insurers to offset General Fund expenditures can be assessed.

The Veterans' Home of Southern California, located at Barstow in San Bernardino County, opened in February 1996 with 220 domiciliary care beds, a 120-bed SNF, and a 60-bed ICF. Since its opening, the DVA has had difficulty finding residents to occupy the facility and the scheduled date of full occupancy has slipped. The DVA initially advised the Legislature that the home would be filled by October 1996. The DVA later revised that date to December 1996, then to December 1997, and now projects that the home will reach full occupancy as of June 1999. The unanticipated number of vacancies has resulted in over-budgeting of the facility in each year of its existence. It has also meant that the cost-per-bed of operating the home is much higher than for the Yountville home.

Recent Population Trends. The population of the facility leveled off during the last three months of 1997, with about 100 beds remaining vacant. This is at odds with DVA's latest projection of continued growth in occupancy. The DVA has indicated that it intends to monitor the trend and will revise its budget at the time of the May Revision if it appears there will be another significant change in the number of veterans living at the Barstow home.

As we noted in our discussion of the Yountville veterans' home, tens of thousands of dollars in additional funds will likely be available for reimbursement of certain pharmacy costs and for care of Barstow home residents. These anticipated funds have not yet been included in the proposed 1998-99 budget for the Barstow home. The proposed budget also does not take into account collections from third-party insurers that DVA anticipates will be received during the budget year as a result of installation of its new computer system.

Analyst's Recommendation. For these reasons, we withhold recommendation on the Barstow home budget pending the receipt of updated population growth projections for the facility at the time of the May Revision. The budget should also be adjusted at that time to reflect the availability of federal funds and collections from insurers that could reduce the amount of General Fund resources budgeted for the home.

INTEREST PAYMENTS TO THE FEDERAL GOVERNMENT (9625)

This budget item provides for a "settle-up" of interest liabilities between California and the federal government. Federal funds flowing to the state often remain temporarily idle in state accounts prior to being paid out for program purposes, during which time the funds earn interest. Under the terms of the Cash Management Improvement Act of 1990 (CMIA), the federal government is entitled to the interest that federal funds generate when not dispersed by the state within a specified period. Conversely, when state receipt of federal funds for programs does not occur in a timely manner, and the state must temporarily use its own money to fund programs until the federal funds arrive, the state is entitled to interest on the amount of money it temporarily expended.

The interest liabilities owed by each level of government to the other are offset against each other to arrive at a net "settle-up" payment, which occurs during the subsequent fiscal year. During 1994-95 (the first year of this budget item) and 1995-96, the state owed a net liability to the federal government. Item 9625 provides the appropriation to make the interest payment. The Governor's budget assumes $4.9 million in General Fund interest expenses for both the current year and the budget year.

State's Interest Obligation Is in Dispute

We withhold recommendation on this item pending resolution of a dispute between the state and the federal government regarding the amount owed. Depending on the outcome of this dispute, the state could either save $9.8 million from the amount budgeted ($4.9 million each in 1997-98 and 1998-99) or owe an additional $21.2 million.

Figure 9 shows the history of this interest "settle-up" program. With regard to the current dispute, in 1996-97 the state incurred a net interest liability to the federal government totaling $11.2 million (based on 1995-96 obligations). However, before the state made this payment, the

Department of Finance (DOF) added an additional program to the settle-up calculation—the State Criminal Alien Assistance Program (SCAAP). Federal SCAAP funds for 1995-96 did not arrive until January 1997, 18 months following the beginning of the fiscal year. The DOF calculated that this delay created an *additional* federal interest liability of $15.1 million. This SCAAP-related federal interest liability not only offset the *entire* state interest obligation for 1996-97, but left $3.9 million to be carried over as a credit toward the amount owed for 1996-97 and payable in 1997-88.

Figure 9

General Fund Interest Payments To the Federal Government[a]

(In Millions)

	1996-97	1997-98	1998-99
Net interest fund liability	$11.2	$9.9	$9.9
Less SCAAP offset for:			
1995-96 ($15.1 million)	-11.2	-3.9	—
1996-97 ($11.0 million)	—	-6.0	-5.0
1997-98 (at least $4.9 million)	—	—	-4.9
Net amount owed by state	—	—	—
Amount in budget	—	$4.9	$4.9
Potential savings	**—**	**$4.9**	**$4.9**

[a] Assuming State Criminal Alien Assistance Program (SCAAP) interest liabilities are permitted. The SCAAP is a federal program which provides funds to states for incurred costs of incarcerating undocumented felons.

Additional Savings Possible. The state's delay in receiving SCAAP funds was not a one-time occurrence. In fact, the state is still awaiting reimbursement for the funds it expended for SCAAP purposes during 1996-97 (reimbursement is expected in February or March of 1998). The interest associated with this delay already is estimated to exceed $11 million. This new offset (which was only partially accounted for in the Governor's budget), combined with the $3.9 million residual from that of the prior year, would eliminate the entire state interest liability for 1997-98. Thus, the $4.9 million already appropriated for the current year would be saved.

In addition, some of the remaining $11 million federal interest owed for 1996-97 would carry over to the budget year. The combined effect of this carryover, in addition to yet *another* one related to delayed receipt of

SCAAP funds for 1997-98, would eliminate the need to appropriate funds for the budget year as well.

Thus, the combined cumulative impact of the three consecutive years of SCAAP federal interest liabilities would, based on DOF's interpretation, completely offset the state liabilities for both the current and budget years. This would provide the Legislature with the opportunity to save $9.8 million from amounts budgeted.

The Federal Government Disputes DOF's Action. The federal government currently is of the view that SCAAP should *not* be included in the interest calculations under CMIA. State and federal officials are currently working to resolve this dispute. If the department's approach of using SCAAP-related federal interest liabilities is disallowed, the General Fund would be liable for $21.2 million in interest obligations (for the three years involved) beyond the amounts included in the Governor's budget. At this time, we withhold recommendation on this item and will report to the Legislature on the status of this dispute at the time of the budget hearings.

CONTROL SECTION 24.10
PENALTY ASSESSMENT FUND

Budget Proposes to Modify Distribution of Penalty Assessments

The Governor's budget proposal to redirect penalty assessment revenues will result in a General Fund revenue loss of $12 million. The redirected funds will be used to pay for increased local peace officer training. The Legislature should consider that additional state and federal funds have been provided to local law enforcement before it decides to allocate additional penalty assessment revenues for the training. If it wishes to provide additional money for local peace officer training, it should weigh the needs of all training programs supported by penalty assessment revenues. Alternatively, the Legislature may wish to consider reducing penalty assessments or transferring funds to programs supported by the Motor Vehicle Account, which has experienced serious funding shortfalls.

The Governor's budget estimates that revenues from penalty assessments will be about $131 million in 1998-99. These revenues are deposited in the State Penalty Fund for distribution to eight other special funds, including the Driver Training Penalty Assessment Fund. The Governor's budget proposes to modify the distribution, increasing by $12 million the share allocated to the Peace Officers' Training Fund and reducing the Driver Training Penalty Assessment Fund by a like amount. This modification results in a General Fund loss of $12 million because Driver Training Penalty Assessment Fund balances have been transferred to the General Fund each year since 1992-93.

Background. Penalty assessments are imposed on persons who violate criminal and traffic laws. Funds are collected by the courts and transmitted to the State Treasurer. Penalty assessment revenues deposited in the Penalty Fund are divided among eight other special funds, based on a statutory formula, which support programs in seven different departments. Figure 10 shows the statutory distribution of the State Penalty Fund for 1998-99.

Figure 10

State Penalty Fund Distribution

1998-99
(Dollars in Thousands)

Fund	Percent[a]	Amount
Restitution	32.02%	$42,275
Driver Training Penalty Assessment	25.70	33,792
Peace Officers' Training	23.99	31,544
Victim/Witness Assistance	8.64	11,361
Corrections Training	7.88	10,361
Local Public Prosecutor's/Defender's Training	0.78	850
Fish and Game Preservation	0.66	650
Traumatic Brain Injury	0.33	500
Totals	**100.00%**	**$131,333**

[a] Statutorily required distribution.

In addition to the special fund programs, the State Controller's Office receives $933,000 to defray its administrative costs.

Proposed Redistribution Results in Loss of Revenue to General Fund. Since 1992, the Legislature and the Governor have appropriated only about $1 million annually from the Driver Training Penalty Assessment Fund. Rather, using Control Section 24.10 of the annual Budget Act, the Legislature has transferred a portion of the Driver Training Penalty Assessment Fund balance to the Victim / Witness Assistance Fund and Peace Officers' Training Fund, and transferred the remaining balances to the General Fund. In the current year, transfers from the Driver Training Penalty Assessment Fund pursuant to Control Section 24.10 included $5.1 million to the Victim / Witness Assistance Fund, $2 million to the Peace Officers' Training Fund, and $25.6 million to the General Fund.

The budget proposes to amend Control Section 24.10 to substantially increase the transfer of funds from the Driver Training Penalty Assessment Fund to the Peace Officers' Training Fund and reduce the transfer to the General Fund by a like amount. Specifically, the budget proposes to transfer $14 million to the Peace Officers' Training Fund (or $12 million more than the current-year amount), $5 million to the Victim / Witness Assistance Fund, and $13.8 million to the General Fund. Thus, the proposal will result in a General Fund revenue loss of $12 million in the budget year.

Additional Funds for Peace Officers' Training Fund. The Peace Officers' Training Fund provides assistance to local law enforcement agencies for the costs of training. The state pays a portion of the training costs; the bulk of the costs are paid by local governments. According to the Commission on Peace Officer Standards and Training (POST), which administers the training program, the augmentation will allow the commission to fully pay for workload growth. Specifically, the commission notes that there has been an 11 percent increase in the number of officers eligible for training reimbursement. Of the $12 million increase, the commission plans to use $10.5 million to defray training and related costs, and use an additional $1.5 million to develop new multimedia training programs to make training more efficient.

Local Law Enforcement Has Received Other Funds. Although we concur that state funding has not kept pace with growth in the program, we note that local law enforcement agencies have received substantial funds from other sources in recent years that can be used for training. For example, under the federal crime bill, in federal fiscal year 1997, county sheriffs and local police departments in 53 counties received a share of the state's total grant amount of more than $72 million. In addition, under the state's Citizen's Option for Public Safety (COPS) program, sheriffs and police received a total of $75 million from the state's General Fund each of the past two years, and the budget proposes to continue the same funding level in 1998-99. Finally, we estimate that local law enforcement agencies will receive a total of $27.5 million from Proposition 172 funds in the current and budget years above the amount assumed in the Governor's budget.

Legislature Should Weigh Peace Officers Training Needs. We believe that the Legislature should consider that additional state and federal money has been provided to local law enforcement before it decides to augment the Peace Officers' Training Fund as the budget proposes. In addition, the Legislature should consider the needs of all of the training programs funded from penalty assessments. In particular, the budget proposes to augment the Peace Officers' Training Fund budget but is silent on the needs of the Corrections Training Fund, which reimburses sheriffs, police departments, and probation departments for training provided to local corrections staff. Like the other program, the state pays a share of costs of the corrections training program, while local agencies are responsible for funding the bulk of the costs. This program, administered by the Board of Corrections, has also seen a significant increase in demand, a 54 percent increase in eligible staff since 1992, but its share of the State Penalty Fund has remained unchanged. To meet increased demand, the Corrections Training Fund would need approximately $6.5 million more than currently allocated.

If the Legislature is concerned about state support for the training needs of local peace officers, it should weigh the needs of both the Peace Officers' Training Fund and the Corrections Training Fund as it decides how to use the balance in the Training Penalty Assessment Fund.

Legislature Should Consider Other Options for Use of Penalty Assessments. In addition to the possible uses of the Driver Training Penalty Assessment Fund outlined above, we suggest that the Legislature consider two other options:

- ***Reduce Penalty Assessments.*** The bulk of revenues for this fund are from penalty assessments on traffic fines. With a supply of revenue in excess of program needs, the Legislature may wish to consider reducing the level of assessments, which would reduce the revenues to the fund.
- ***Transfer Funds to Programs Supported by the Motor Vehicle Account.*** The Legislature may also wish to consider using the money to support programs that would otherwise require funding from the Motor Vehicle Account (MVA), such as the California Highway Patrol. In recent years, the MVA has experienced significant shortfalls and faces potential funding shortfalls in the budget year and future years (we discuss this issue in the Crosscutting Issues section of the Transportation chapter). Because penalty assessments come primarily from driving violations, there is a strong connection to the MVA-supported programs. In addition, use of the penalty assessment revenues in this way could forestall driving fee increases or program reductions in the future.

HEALTH AND DENTAL BENEFITS FOR ANNUITANTS (9650)

This appropriation provides for the state's contribution toward health and dental insurance premiums for annuitants of the Judges', Legislators', District Agricultural Employees', and Public Employees' Retirement Systems, as well as specified annuitants of the State Teachers' Retirement System. The program provides annuitants the option of selecting from 17 state-approved health plans (depending on where an annuitant lives).

Budget-Year Costs Are Uncertain

We withhold recommendation on the $302.3 million General Fund request for annuitant benefits pending final determination of premium rates for calendar year 1999 and a possible adjustment for the number of annuitants in the program.

The budget proposes total expenditures of $302.3 million from the General Fund for health and dental benefits for annuitants in 1998-99. This is $23.6 million, or 8.5 percent, more than estimated expenditures for this purpose in the current year, reflecting an increase in the number of annuitants and no change in premium rates. Figure 11 (see next page) displays General Fund expenditures for annuitant health and dental benefits for the three fiscal years starting with 1996-97. Although these costs are initially paid from the General Fund, the state recovers a portion of these costs from special funds (about 33 percent) through pro rata charges.

The actual amounts needed in this item, however, are dependent on negotiations over health premiums currently underway between the state and providers. Hopefully, these negotiated premium rates will be available for review during legislative budget hearings. Pending receipt of these rates, we withhold recommendation on the amount requested under this item.

Figure 11

Health and Dental Benefits For Annuitants

(In Millions)

Program	1996-97 Actual	1997-98 Estimated	1998-99 Budgeted
Health	$235.8	$247.8	$269.2
Dental	30.0	30.9	33.1
Totals	**$265.8**	**$278.7**	**$302.3**

In addition, based on a review of past enrollment projections, the Governor's budget has consistently over estimated the number of enrollees in each budget year. Thus, when the negotiated premium rates are available, it may be appropriate to adjust the amount in the Budget Bill to account for fewer annuitants as well.

AUGMENTATION FOR EMPLOYEE COMPENSATION (9800)

A major portion of state government expenditures is for compensation of state employees. The Governor's budget projects $13 billion in salary and wage expenditures for nearly 284,000 authorized personnel-years in 1998-99 (including $4.3 billion and 90,000 personnel-years in higher education). Including benefits (such as contributions to retirement and health insurance), estimated employee compensation expenditures exceed $15 billion for the budget year.

The following employee compensation issues are discussed below:

- The administration's proposals for employee compensation.
- Collective bargaining agreements may again not be settled by the beginning of the budget year.
- Legislative oversight of state employee collective bargaining agreements.

Employee Pay/Benefit Increases

State Civil Service Employees. State employees (other than those in higher education) last received a general pay increase (3 percent) on January 1, 1995. Figure 12 (see next page) shows a history of general salary increases for state civil service employees and the consumer price indices for the United States and California since 1981-82. As shown in the figure, the Governor’s budget includes an amount equivalent to a 3 percent salary increase for these state employees ($279 million). The total consists of $142 million from the General Fund and $68 million each from special funds and nongovernmental cost funds.

The Governor’s budget indicates that the amount ultimately needed for this purpose is dependent on reaching agreement with the 21 employee bargaining units through the collective bargaining process. In recognition of this, the Budget Bill includes provisional language stipulating that (1) the amount in the bill is not to be construed to control or influence the collective bargaining process and (2) the funds are to be distributed in accordance with approved memoranda of understanding (MOU) for represented employees and based on salary and benefit schedules established by the Department of Personnel Administration (DPA) for nonrepresented employees. As discussed below, only one of the 21 employee bargaining units has reached tentative agreement on an MOU, and the Legislature has not approved that tentative agreement.

Figure 12

State General Salary Increases 1981-82 Through 1998-99

(Percent Increase)

Fiscal Year	State General Salary Increase	Consumer Price Index	
		United States	California
1981-82	6.5%	8.8%	10.7%
1982-83	—	4.2	2.3
1983-84	6.0	3.7	3.6
1984-85	8.0	3.9	4.9
1985-86	6.0	2.9	4.0
1986-87	6.0	2.2	3.3
1987-88	3.8	4.1	4.2
1988-89	6.0	4.6	4.8
1989-90	4.0	4.8	5.0
1990-91	5.0	5.5	5.3
1991-92	—	3.2	3.6
1992-93	—	3.1	3.2
1993-94	5.0	2.6	1.8
1994-95	3.0	2.9	1.7
1995-96	—	2.7	1.4
1996-97	—	2.9	2.3
1997-98[a]	—	2.2	2.5
1998-99[a]	3.0[b]	2.2	2.9

[a] Legislative Analyst's Office estimate of consumer price indices.
[b] Governor's budget proposal is equivalent to a 3 percent general salary increase.

Employees in Higher Education. In higher education, the Governor proposes increases to the baseline budgets of the University of California and the California State University (in keeping with the terms of the Governor's four-year "compact") but leaves it to the systems to allocate these funds among compensation and other purposes. Out of this increase, the systems propose to spend $171 million for salary and benefit increases. Figure 13 shows how this amount will be allocated.

Figure 13

Higher Education Salary and Benefit Increases 1998-99 Governor's Budget

General Fund (In Millions)

University of California	
4.5 percent faculty salary increase, effective 10/1/98	$26.3
2 percent staff cost-of-living increase, effective 10/1/98	19.9
Full-year cost of 1997-98 salary increases	15.8
Merit salary adjustments	35.2
Subtotal	($97.2)
California State University	
Salary and benefit increases to be negotiated	$71.3
Full-year cost of 1997-98 salary/ benefit increases	2.4
Subtotal	($73.7)
Higher Education Total	**$170.9**

New Collective Bargaining Agreements Still Under Negotiation

The Department of Personnel Administration should report to the budget committees during budget hearings on the administration's collective bargaining proposals and the status of negotiations.

The DPA began negotiations in 1995 with the 21 bargaining units representing rank-and-file state employees (other than higher education) for new MOUs governing compensation and other terms and conditions of employment. These MOUs are to replace those that, for the most part, expired June 30, 1995. In 1995, the DPA reached agreement with only one of the 21 units, the highway patrol officers. This MOU was approved by the Legislature but it expired on June 30, 1997. In December 1997, the DPA reached an agreement with the California Correctional Peace Officers Association but this proposed MOU had not, at the time this *Analysis* was written, been submitted to the Legislature. Moreover, under the terms of the MOU, even if approved by the Legislature, it would expire on June 30, 1998.

Under current law, the provisions of expired MOUs generally remain in effect pending adoption of replacement MOUs. Unless the DPA can negotiate successfully with one or more of the 21 bargaining units before June 30, 1998, the state will begin another budget year with expired MOUs. Given this situation, we recommend that the DPA report to the budget committees during budget hearings on the administration's collective bargaining proposals and the status of negotiations.

Strengthen Legislature's Collective Bargaining Oversight

We recommend that the Legislature reaffirm the policy adopted in the **Supplemental Report of the 1996-97 Budget Act** ***to assure that the Legislature will have the opportunity to fully review proposed collective bargaining agreements. We recommend further that the Legislature include the same language in the*** **Supplemental Report for the 1998-99 Budget Act.**

In our overview of employee compensation issues in past *Analyses*, we have discussed the need to strengthen the Legislature's oversight of proposed collective bargaining agreements. In order to ensure that the Legislature has the opportunity to appropriately review new MOUs, we have recommended that the Legislature adopt the following policies:

- Review the administration's MOU proposals (including final text and complete fiscal estimates) at the budget hearings and adopt, as appropriate, in the annual Budget Act. Any MOU that is not available in time for in-depth review during budget hearings should be referred to the budget committees and adopted, as appropriate, as an amendment to the Budget Act.

- Require a minimum time period between the submittal of the proposed MOUs to the Legislature and hearings on the proposal. This would give the Legislature sufficient time to study the MOUs to ensure that the fiscal and policy implications of the proposals are fully understood. Given the importance of these agreements, we suggest a 30-day review period.

In response to this recommendation, the Legislature adopted the following language in the *Supplemental Report of the 1996-97 Budget Act*:

> It is legislative intent to refer all memorandum of understanding to the appropriate policy and budget committees in each house. It is further legislative intent to give these committees a total of 30 days to review the policy and fiscal implications of each memorandum of understanding.

We recommend that the Legislature reaffirm the policy stated in the supplemental report and implement it for any MOU that is sent to the Legislature. We also recommend that the Legislature include the same language in the supplemental report for the 1998-99 budget.

CONTROL SECTION 3.60

Public Employees' Retirement System Employer Contribution Rates

We withhold recommendation on employer contribution rates for retirement benefits pending (1) final determination of the actual rates to be applied in the budget year and (2) receipt and review of information regarding the actuarial assumptions underlying the rates.

This control section specifies the contribution rates for the various retirement classes of state employees in the Public Employees' Retirement System (PERS). The section also authorizes the Department of Finance to adjust any appropriation in the Budget Bill as required to conform with changes in these rates. In addition, the section requires the State Controller to offset these contributions with any surplus funds in the employer accounts of the retirement trust fund.

Under current law, the PERS is responsible for developing employer contribution rates each year based on actuarial analyses. At the time this *Analysis* was prepared, a final determination of these rates had not been made.

Consequently, we withhold recommendation pending final determination of 1998-99 rates and receipt and review of information from the PERS regarding the actuarial assumptions underlying the determined rates. This information is typically available in March or April.

TAX RELIEF
(9100)

The state provides local property tax relief, both as subventions to local governments and as direct payments to eligible taxpayers, through seven different programs. The two largest programs are the Homeowners' Property Tax Relief (homeowners' exemption) and the Renters' Tax Relief (renters' credit) programs.

As required by the state Constitution, the homeowners' exemption grants a $7,000 property tax exemption on the assessed value of owner-occupied dwellings, and requires the state to reimburse local governments for the resulting reduction in property tax revenues. The exemption reduces the typical homeowner's taxes by about $75 annually. The Governor's budget proposes an expenditure of $395 million on this program in 1998-99. This is an increase of almost $4 million, or 1 percent, which reflects the expected growth in the number of homeowners claiming the exemption.

Proposal to Eliminate Renters' Credit

The renters' credit provides a refundable tax credit to Californians who rent their principal place of residence. The credit is applied first to income taxes due, with any balance paid directly to the renter as a refund. The amount of the credit is $60 for single renters and $120 for married couples or heads of households. The renters' credit program has been suspended in each year since 1993, but under existing law, the credit is scheduled to be reinstated in 1998. The budget proposes to permanently eliminate the credit, for a budgetary savings of about $540 million in 1998-99.

The renters' credit is primarily claimed by low- and moderate-income taxpayers. According to projections for the 1998 tax year, three-fourths of those eligible to claim the credit will have less than $30,000 in annual income and nearly one-third will have less than $10,000 in annual income (see Figure 14). Given the income of those eligible to claim the renters' credit, many have come to view the program as a means of easing the tax burden of lower-income Californians.

Figure 14

Renters' Credit Claimants by Income[a]

Adjusted Gross Income	Number of Returns (In Thousands)	Percent Of Total
Less than $10,000	1,804	31%
$10,001 to $20,000	1,506	26
$20,001 to $30,000	1,070	18
$30,001 to $40,000	655	11
$40,001 to $50,000	384	7
More than $50,000	424	7
Totals	**5,843**	**100%**

a Based on projections for the 1998 tax year.

If the Legislature wished to reinstate the renters' credit but at a lower cost to the state, a number of options would be available, including:

- ***Limit Income Eligibility.*** By setting a maximum income threshold to be eligible for the credit, the Legislature could ease the tax burden of lower-income renters only. This approach was taken by the Legislature in 1991 and 1992 to lower the program's costs. In those years, program costs were reduced by about one-fourth by making higher-income renters ineligible.

- ***Eliminate Refundability***. The Legislature could eliminate the provision of current law that allows taxpayers to receive the credit in the form of a refund. The program's costs could be reduced by about one-half under this option.

The *Analysis of the 1997-98 Budget Bill* addressed a number of other issues regarding the proposed elimination (see pages G-169 through G-172).

COMMISSION ON STATE MANDATES (8885)

The Commission on State Mandates (commission) is responsible for determining whether local government claims for reimbursement of state-mandated local costs should be paid by the state. If the commission determines that a statute, executive order, or regulation contains a reimbursable mandate, the commission develops an estimate of the statewide cost of the mandated program and includes this estimate in a semiannual report. After receipt of this report, the Legislature appropriates funds in a "claims" bill to pay newly approved mandates. Subsequent-year costs of the mandate are then funded through the budget, under each affected department.

The commission is also responsible for reviewing requests from counties to reduce their general assistance grant levels. Specifically, under the "SB 1033" (Chapter 72, Statutes of 1993) process, counties may apply to the commission for a finding of "significant fiscal distress." Upon receipt of such a finding, counties are authorized to reduce their general assistance grant levels for up to three years.

The budget proposes expenditures of $1.1 million for 1998-99. This is $109,000, or 11 percent, more than estimated current-year expenditures. Most of this increase, $100,000, reflects funds for the commission to review two SB 1033 claims in the budget year. In the current year, the commission did not receive any SB 1033 applications and redirected its SB 1033 funds ($50,000) to pay for expenses associated with implementation of SB 11, Ayala (Chapter 945, Statues of 1995), a measure which modified and shortened the mandate test claim process. Because authority for seven counties to reduce their general assistance grant levels will expire in the budget year, it is highly possible that the commission will receive more than two SB 1033 applications in 1998-99. If this occurs, the commission will request additional funds, pursuant to Control Section 27.00, and proposed budget bill language would lengthen the time for application review.

$4 Million Cost for Late Budgets

In order to reduce state costs and legal ambiguity, we recommend the Legislature enact legislation to (1) repeal the 30 mandates that have been suspended consistently for several years , or (2) modify them so that the local government responsibility is optional, fee-financed, or mandatory only if the Legislature provides funding in the Budget Act.

Beginning in the *1991-92 Budget Act*, the Legislature has regularly "suspended" a long series of laws and regulations that impose costs on local governments which the state is required to reimburse. To suspend a mandate, Section 17581 of the Government Code requires the Legislature to identify the law or regulation in the Budget Act and include an appropriation of zero dollars. During the year the Budget Act is in force, local governments are not required to carry out the mandated responsibilities, and are not eligible for state reimbursement. In recent years, the Legislature has eliminated state liabilities regarding 14 of these suspended mandates, generally by repealing the mandated activity, or by making the mandated activity optional or fee financed. Thirty other mandates shown in Figure 15, however, are once again proposed for suspension in the Budget Bill.

The process of "suspending" mandates was developed as a way to reduce state costs, without permanently eliminating the mandate. While awkward, the process works reasonably well, provided the state budget is adopted by July 1. In years when the budget is delayed, however, this process creates significant legal uncertainty, and can result in state costs to reimburse those local governments which carry out the mandated responsibilities during the interim between budgets.

For example, the 1998-99 budget includes $4.1 million to reimburse local governments for their costs to comply with the mandates shown in Figure 15 during the 49 days in 1997 in which the state did not have a budget. The $4.1 million cost—scheduled separately in the budgets for 11 departments—is a rough estimate, based on the $6 million the state paid to compensate local governments for their mandated costs during the 1992 budget delay. These are costs the state will have to pay, yet in our view the state received very little benefit from having these mandates reestablished for a month and a half.

In order to clarify local government responsibilities and avoid incurring costs during budget delays, we recommend the Legislature enact trailer legislation which does one of the following for each mandate proposed for suspension:

- Repeal the mandated responsibility.
- Make the mandated responsibility optional or fee financed.

- Specify that local governments are required to carry out the mandated responsibility *only* if funding for the activity is scheduled in the current Budget Act.

Figure 15

Mandated Programs Proposed for Suspension In Budget Bill

Program	Mandates	
Programs Mandated by Law	**Chapter**	**Year**
Substandard housing	238	1974
Voter registration procedures	704	1975
Mineral resources policies	1131	1975
Local coastal plans	1330	1976
Guardianship/conservatorship	1357	1976
Voter registration roll purge	1401	1976
Senior citizen property tax deferral	1242	1977
Absentee ballots	77	1977
Filipino employees	845	1978
Handicapped voter access	494	1979
Short-Doyle case management	815	1979
Deaf teletype equipment	1032	1980
Regional housing	1143	1980
Involuntary lien notices	1281	1980
Victims statements minors	332	1981
Lis Pendens	889	1981
Democratic presidential delegates	103	1982
Mobilehome property tax deferral	1051	1983
Court audits and proration of fines	980	1983
Short-Doyle audits	1327	1984
Domestic violence information	1609	1984
Election materials	1042	1985
Residential care services	1352	1985
Open Meeting Act	541	1986
Property taxation	48	1987
CPR pocket masks	1334	1987
Programs Mandated by the CCR[a]	**Title**	**Section**
Firefighters clothing equipment	8	3401-3410
Personal alarm devices	8	3401(c)
Detention of minors	15	4500-4549
Pretreatment facilities	22	64435(f)

[a] California Code of Regulations.

LOCAL GOVERNMENT FINANCING (9210)

This budget item contains appropriations to local governments for three purposes:

- ***Citizen's Option for Public Safety (COPS).*** The COPS program was created in 1996 to provide local governments with funds for law enforcement. The budget proposes to again fund the program at $100 million for 1998-99.
- ***Special Supplemental Subventions.*** This program reimburses qualifying redevelopment agencies for revenues lost as a result of the repeal of the business inventory exemption subvention in 1984.
- ***State-Mandated Local Programs.*** This item includes funding to reimburse local governments for costs incurred in complying with certain state-mandated programs.

This item also includes spending on the property tax administration loan program. This program was created by Chapter 914, Statutes of 1995 (AB 818, Vasconcellos) and extended through 2000-01 by Chapter 420, Statutes of 1997 (AB 719, Torlakson). This legislation appropriates $60 million each year for loans to counties for additional spending on property tax administration. These loans may be forgiven if counties can demonstrate that they have generated or preserved sufficient property tax revenues for schools to offset the costs of the loan. When the loans are forgiven, a cost is accrued in Item 9210. The budget recognizes a cost of $50 million for this purpose each in 1996-97 and 1997-98. The budget, however, shows no estimated costs for 1998-99, apparently on the basis that it is not known if any loans will be forgiven. It is most likely, though, that the state will incur costs of approximately $50 million in the budget year as loans are forgiven. The loan program and property tax administration are discussed in more detail in Part VI of *The 1997-98 Budget: Perspectives and Issues*. (Please see pages 215 through 226.)

FINDINGS AND RECOMMENDATIONS

General Government

		Analysis Page
	The Year 2000 Computer Problem	
1.	**Departments Report Progress.** Recommend that budget subcommittees require departments to report on their progress in accomplishing Y2K remediation efforts.	G-18
2.	**Deny Fund New Projects.** Recommend denying funding new information technology projects until a department has completed its Y2K remediation efforts.	G-19
3.	**Approve Department of Information Technology's (DOIT's) Funding Augmentation Request.** Recommend the Legislature augment DOIT's budget to provide additional oversight and assistance to departments.	G-20
4.	**Reserve Fund Necessary.** Recommend the Legislature establish a reserve fund from which departments can request monies for yet-to-be identified efforts to address the problems related to the year 2000 conversion.	G-20
	Consumer Affairs	
5.	**Implementation of Smog Check Program Components Needs Plan.** Although the department is re-	G-23

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questing $68 million to implement certain components of the Smog Check program, a clear implementation plan is not evident. The department should provide a complete report before the budget hearings to provide the Legislature with needed information on the current status of all components of the Smog Check program.

6. **Call Center Augmentations Not Justified.** Recommend the deletion of the proposed augmentations totaling $6.1 million and 109.7 positions for the department's call center because the department has not justified the need for these augmentations. (Reduce various items by a total of $6.1 million and 109.7 positions.) G-28

7. **Barbering and Cosmetology Augmentations Unnecessary.** Recommend deletion of the proposed augmentations because these costs should be accommodated within existing resources using the flexibilities given the department under performance-based budgeting. (Reduce Item 1111-001-0069 by $737,000 and 18.3 positions.) G-31

8. **Bureau of Home Furnishings and Thermal Insulation Laboratory Upgrades Inappropriate.** Recommend the deletion of the proposed augmentation since permanent improvements to a privately owned building should not be funded directly with state dollars. (Reduce Item 1111-001-0752 by $221,000.) G-32

9. **Implementation Plan For Chapter 401, Statutes of 1997 Not Complete.** Recommend deletion of the proposed $326,000 increase in reimbursement authority for the implementation of Chapter 401, Statutes of G-32

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1997 (SB 780, Kelley) since the department is to provide an estimate of ongoing costs at a later date. (Reduce Item 1111-001-0995 by $326,000.)

10. **Private Postsecondary and Vocational Education Program Implementation Plan Needs Legislative Review.** Withhold recommendation on the $6.6 million in special funds, federal funds and reimbursements, and 79.5 positions proposed to assume the responsibilities of the Council for Private Postsecondary and Vocational Education because the department had not implemented the transfer when the budget was prepared. The department needs to provide an implementation plan to the Legislature prior to budget hearings. G-33

11. **Department Should Report on Status of Year 2000 Modifications.** The department should, prior to budget hearings, submit a report to the Legislature on the status of modifications to critical information technology systems. G-34

Fair Employment and Housing

12. **Management Improvements Need to Precede Staff Increases.** Recommend the Legislature not approve the Department of Fair Employment and Housing's request for a $1,250,000 augmentation and 21 positions because of the need for management improvements. Further, we recommend the Legislature adopt supplemental report language directing the department to submit to the Legislature by November 1, 1998, a report on its progress in implementing management changes, the specific performance improvements realized from each change, and other changes/improvements to be implemented. (Reduce Item 1700-001-0001 by $1,250,000.) G-35

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Alcoholic Beverage Control

13. **Alcohol Beverage Control (ABC) Fund Deficit.** Recommend the Legislature enact trailer bill legislation allowing the ABC to increase license fees in an amount higher than proposed by the Governor in order to sustain current enforcement efforts. G-38

14. **Nondocumented Alien Workload. Reduce Item 2100-001-0081 by $928,000.** Recommend deletion of $928,000 and 21.5 positions proposed to verify citizenship of all licensees because the request lacks important details. G-39

Department of Industrial Relations

15. **Targeted Industries Partnership Program (TIPP) Should Not Be Funded From General Fund**. We recommend that the Legislature delete the proposed $2.4 million General Fund augmentation for the TIPP because this would not be a cost-effective use of General Fund money.(Reduce Item 8350-001-0001 by $2,407,000.) G-41

16. **Joint Enforcement Strike Force (JESF) Should Also Not Be Funded by General Fund.** We recommend the Legislature not approve the department's request for a $1.2 million General Fund augmentation to continue the JESF because it has not proven to be a cost-effective mechanism for enforcing payroll tax laws. (Reduce Item 8350-001-0001 by $1,173,000.) G-43

17. **Eliminate Managed Care Unit.** We recommend the Legislature delete $222,000 and 3.3 personnel-years for the Managed Care Unit within the Division of Workers' Compensation because there is little work- G-44

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load and insufficient fee revenue to support the program. (Reduce Item 8350-001-0001 by $222,000, delete Item 8350-001-0132, and transfer the balance in the Workers' Compensation Managed Care Fund to the General Fund.)

18. **Reduce Requested Increase for Rent.** We recommend the Legislature delete the $4,110,000 augmentation for building rent costs because the budget overestimates the rental costs the department will incur when it moves into new state office buildings in San Bernardino, Los Angeles, Oakland and San Francisco. (Reduce Item 8350-001-0001 by $4,111,000.) G-45

19. **Wage Law Enforcement on Public Works Contracts**. We recommend the Legislature delete $191,000 and 2.5 positions requested for enforcement of prevailing wages because under recent legislation should not increase the department's workload. (Reduce Item 8350-001-0001 by $191,000.) G-46

Department of Food and Agriculture

20. **Food Safety Program.** Recommend deletion of the requested $991,000 and eight positions for various food safety program augmentations until the department can present a comprehensive food safety plan to the Legislature for review. (Reduce Item 8570-001-0001 by $991,000.) G-47

21. **Domestic Parcels Inspection Program.** Withhold recommendation on the $1,874,000 from the General Fund and 26.3 personnel-years requested for continuation and augmentation of the Domestic Parcels Inspection Program until the pilot program report—due March 1, 1998—has been submitted and reviewed. G-49

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22. **Agricultural Export Program Augmentation.** Recommend deletion of a $464,000 augmentation from the General Fund for the Agricultural Export Program and a one-time equipment purchase for the department's chemical laboratory. The export program activities can be supported within current department resources and the equipment purchase should be funded through laboratory service fees. (Reduce Item 8570-001-0001 by $464,000.) G-50

23. **Marketing Campaign Not Necessary.** Recommend deletion of $82,000 (General Fund) because the proposed marketing campaign should be the responsibility of the agriculture industry. (Reduce Item 8570-001-0001 by $82,000.) G-51

24. **Laboratory Contract Cost Increase Not Justified.** Recommend deletion of a $1,110,000 General Fund augmentation for the department's contract for services from the California Veterinary Diagnostic Laboratory System because the department has not substantiated the higher contract costs. (Reduce Item 8570-001-0001 by $1,110,000.) G-51

Fair Political Practices Commission

25. **Litigation Regarding Political Reform Law.** Withhold recommendation on $1.2 million and 22 personnel-years to carry out the California Political Reform Act because a federal court recently enjoined enforcement of the law. G-54

Board of Equalization

26. **Request for Implementation of Chapter 702, Statutes of 1997 (SB 110, Dills) Premature.** Recommend G-56

	Analysis Page
deletion of the proposed increased in reimbursement authority for the Board of Equalization (BOE) to implement Chapter 702 because the BOE has not approved an implementation plan for this legislation. (Reduce Item 0860-510-0995 by $4,177,000.)	

Franchise Tax Board

27.	**Augmentation for Workload Growth Not Justified.** (Reduce Item 1730-001-0001 by $2,992,000.) Recommend the Legislature delete the proposed augmentation because the Franchise Tax Board has not justified the need for these resources.	G-58
28.	**Separate Preprinted Labels for Tax Returns Unnecessary.** (Reduce Item 1730-001-0001 by $1,231,000.) Recommend the Legislature delete the proposed augmentation to provide a separate preprinted label to taxpayers because taxpayers can provide the necessary information on their tax returns.	G-59
29.	**Department Expects to Miss Critical Failure Date for Year 2000 Implementation.** The department should report to the Legislature on the status of modifying critical information technology systems to accommodate the year 2000 change and include any expected revenue loss.	G-60

Department of Information Technology

30.	**Information Technology Policies Still Needed.** Recommend the adoption of budget bill language appropriating the $437,000 requested when the Department of Information Technology (DOIT) develops a number of specific policies related to the initiation and implementation of information technology projects.	G-62

		Analysis Page
31.	**Project Cost and Schedule Estimates Need Improvement.** Recommend that the Legislature adopt supplemental report language directing DOIT to adopt a policy requiring that feasibility study report transmittal letters and special project reports contain an indication of the administration's assessment of the sensitivity to change of the costs, benefits, and schedules contained in these documents.	G-66
32.	**Advocacy Role Conflicts With Oversight Responsibilities.** Recommend that the Legislature approve DOIT's funding request for additional resources to institute the new funding approval process, but require the resources requested for advocacy be redirected to responsibilities DOIT is required by statute to fulfill.	G-67
33.	**Civil Service Classification System Still Needs Reforming.** Recommend that DOIT report to the Legislature, prior to budget hearings, on its progress and plans to change the civil service classification system to improve the state's access to information technology expertise.	G-68
34.	**Department Continues to Be Leader on Year 2000 Conversion.** Recommend that the Legislature approve DOIT's request for additional resources in 1998-99 for year 2000 conversion. Also recommend that the Legislature direct DOIT to take a number of additional steps with regard to the conversion.	G-68
35.	**Data Center Configuration Policy Needed.** Recommend that the Legislature direct DOIT to develop a five-year strategic plan for configuration of the state's data centers.	G-75

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Health and Welfare Agency Data Center

Data Center Operations

36. **State Should Increase Expertise of State Staff.** Recommend that the Health and Welfare Agency Data Center (HWDC) provide the Legislature with an estimate, prior to budget hearings, on how much it would cost to train state staff to perform services to support the HWDC Router Network that the budget proposes be supported by private consultants. G-76

37. **Acquisition of Data Center Building Premature.** Recommend that the Legislature deny the request to purchase the data center's building in 1998-99 and delete $445,000 proposed in the support budget for maintenance and operating expenses for the building. Instead, recommend that the Legislature appropriate $455,000 to continue the existing lease of the facility. G-77

38. **Data Center Should Seek Review.** Recommend that HWDC report at budget hearings on what tools and resources are needed to renew project management methodologies and legal contracts. G-78

Statewide Automated Welfare System (SAWS)

39. **Requests for Legislative Reports Ignored**. Recommend that the Legislature take no action on $88 million proposed for SAWS until the center submits a series of reports requested by the Legislature in the *1997-98 Budget Act* and in current law. G-83

40. **Welfare Case Data System.** Recommend that the Legislature appropriate the $18 million through budget bill language if (1) the Department of Information Technology certifies that the procurement document G-85

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allows for expansion of the system and (2) the state's oversight role is increased.

Statewide Automated Child Support System (SACSS)

41. **Child Support Project Canceled; New Project Offers Opportunities, Challenges.** Recommend that the Legislature require the alternative procurement method be used for the new project, in which the state outlines its desired outcomes rather than specifying a particular technology. Recommend that HWDC report at budget hearings on the status of federal funding for the new project. G-87

42. **Counties Need Assistance With Year 2000.** Recommend that the HWDC and DSS report during budget hearings on the progress of the counties in modifying existing child support systems to understand the year 2000. G-89

Child Welfare Services Case Management System (CWS/CMS)

43. **Contract Increases Not Justified.** Recommend the Legislature delete the proposed augmentation because the vendor, not the state, should pay additional monies to make the CWS/CMS work. (Reduce Item 4130-001-0632 by $15.1 million.) G-90

Other Issues

44. **Statewide Fingerprint Imaging System (SFIS) Expansion Not Justified.** Withhold recommendation on $8.9 million requested for SFIS, pending receipt and review of the justification for the request. G-92

	Analysis Page
45. **Electronic Benefits Transfer (EBT) System Delayed.** Recommend that HWDC report during budget hearings on its progress in implementing this project.	G-92
46. **Automated Tape Library (ATL) Not Yet Justified.** Withhold recommendation on $671,000 requested for the Automated Tape Library, pending receipt and review of the justification for the request.	G-93
47. **Year 2000 Funding Request Not Yet Justified**. Withhold recommendation on $3.6 million requested for HWDC's Year 2000 project pending receipt and review of the justification for the request.	G-93

Office of Emergency Services

48. **Law Enforcement Branch.** Recommend that the Office of Emergency Services (OES) retain law enforcement coordination responsibilities. Also recommend approval of request for two additional law enforcement coordinator positions.	G-95
49. **Disaster Claims Processing to Stay at OES.** The OES reviewed the feasibility of transferring its disaster claims processing to another state agency, as was required by recent legislation and determined that it would be more costly and less efficient to transfer these responsibilities.	G-97

State Controller

50. **Statewide Travel Reimbursement Project Not Mission Critical.** Recommend reduction for the development of an automated statewide travel reimbursement project because it is not mission critical nor mandated, and information technology efforts should be focused on converting computers to accommodate	G-99

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the year 2000. Reduce Item 0840-001-0001 by $689,000.

51. **Additional Information Needed for Local Government Reporting System.** Withhold recommendation on $724,000 requested to replace the current Local Government Reporting Systems, pending receipt of additional information on the critical failure dates for the current systems and a plan to include users of the proposed system in the development process. G-100

Secretary of State

52. **Delay in Voter Registration Computer System.** Recommend legislation to delay the date the Secretary of State must repay a $3.5 million state loan to develop a new statewide voter registration tracking system. G-103

53. **Proposition 208 Ruling May Invalidate Funding Request.** Withhold recommendation on $286,000 to implement new political reform law in light of federal court ruling enjoining its enforcement. G-104

Department of General Services

54. **Surplus Property Warehouse Efforts Fall Short of Legislature's Request**. Recommend that the department report during budget hearings on how it intends to comply with provisions of the *Supplemental Report of the 1997-98 Budget Act* which directed it to phase out the operations of surplus property warehouses. G-107

55. **Update on CALNET Procurement**. Because of its value and impact on state government, recommend that the Department of General Services report to the G-107

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Legislature during budget hearings on its progress in awarding this contract.

56. **Department Unnecessarily Expanding Pilot.** Recommend reduction to ensure the pilot project is carried out as provided in authorizing legislation. (Reduce Item 1760-101-0022 by $710,000.) G-108

57. **Surplus Property Assessments.** Recommend a reduction of $925,000 because several proposed consultants studies should not be undertaken in 1998-99. Also withhold recommendation on $250,000 for a master plan for the Lanterman Developmental Center pending completion and review of consulting work funded in the current year. (Reduce Item 1760-015-0002 by $925,000.) G-109

Housing and Community Development

58. **High Costs to Administer Homeless Grants.** Recommend that the Legislature enact legislation simplifying the administration of the Emergency Housing Assistance Program in order to maximize the dollars going for direct homeless assistance. G-112

59. **Alien Verification Fee Plan Lacks Necessary Federal Guidance.** Recommend that the Legislature not approve a department request for an alien verification and fee system until federal guidelines are provided. G-115

Trade and Commerce

60. **New and Expanded Foreign Offices.** Recommend deletion of $1,053,000 requested for four new foreign offices and expansion of other foreign offices because (a) establishing foreign offices should be considered as a policy issue through legislation other than the G-117

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Budget Bill and (b) additional funds are not needed to sustain the current level of activity in existing offices. (Reduce Item 2920-012-0001 by $1,053,000)

61. **Agency Needs to Set Priorities Within Existing Resources.** Withhold recommendation on $7.8 million in various augmentation requests (a) until the agency reassesses the need for these increases by setting priorities within current resources and (b) pending the agency submitting information identifying the specific expected outcomes from spending additional funds and how these outcomes will be measured. G-120

Department of Finance

62. **Highlight Information Technology Expenditures.** Recommend that the Legislature adopt supplemental report language directing Department of Finance (DOF) to identify information technology expenditures and projects in the *1999-00 Governor's Budget*. G-122

63. **Audit of Data Centers.** Recommend DOF report during budget hearings on the Health and Welfare Agency Data Center and the Stephen P. Teale Data Center on the findings of the recent financial audit of the two centers. G-123

Office of Administrative Law

64. **No Funding Proposed to Meet Statutory Requirement.** The Office of Administrative Law's proposed budget contains no appropriation or proposed redirection of existing resources to publish the regulations on the Internet, as required by statute. G-124

	Analysis Page
Department of Veterans Affairs and Veterans' Homes of California	
65. **Rethinking Veterans' Assistance.** Recommend adoption of budget bill and supplemental report language initiating a review of the potential timing, availability, and priority use of surplus funds in the Cal-Vet Farm and Home Purchase Program for other programs of benefit to veterans and taxpayers.	G-125
66. **Substandard Nursing Care at Yountville Home.** Recommend that Department of Veterans' Affairs and Department of Health Services report at budget hearings on actions taken to address substandard care and status of regulatory actions and fines.	G-128
67. **Yountville Veterans' Home Augmentations.** Modify funding and staffing sought for the home contingent upon adoption of budget bill language and receipt of additional information by the Legislature. Also recommend a Bureau of State Audits study of the mix of nursing beds at the facility. Reduce Item 8960-011-0001 by $1,882,000, Reduce Federal Funds by $255,000 and Reduce Reimbursements by $273,000.	G-130
68. **Barstow Veterans' Home Beds Still Vacant.** Withhold recommend on the budget for the veterans' home due to the large number of vacant beds at the Barstow facility and the potential availability of federal funds and collections from insurers.	G-134
Interest Payments to the Federal Government	
69. **Interest Liability Settle-Up.** We withhold recommendation on interest payments to the federal government pending resolution of a dispute between the	G-136

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state and the federal government on the amount owed.

Control Section 24.10— Penalty Assessment Fund

70. **Legislature Should Consider Options.** The budget proposes to redirect penalty assessment revenues that will result in a General Fund revenue loss of $12 million. Redirected funds would defray increasing local assistance demands on the fund that pays for peace officer training. The Legislature should weigh the needs of all of the local peace officer training programs as it considers how to use the revenues. Other alternatives include reducing revenues by lowering penalty assessments or transferring surpluses to the Motor Vehicle Account. G-139

Health and Dental Benefits for Annuitants

71. **Budget-Year Costs Are Uncertain.** Withhold recommendation on the $302.3 million General Fund request for health and dental benefits for annuitants pending final determination of premium rates and a possible adjustment for the number of annuitants in the program. G-143

Overview of Employee Compensation

72. **Legislature Needs Report on Status of Collective Bargaining Negotiations.** The Department of Personnel Administration should report to the budget committees during budget hearings on the administration's collective bargaining proposals and the status of negotiations. G-147

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73. **Strengthen Legislature's Collective Bargaining Oversight.** Recommend that the Legislature reaffirm the policies stated in the *Supplemental Report of the 1996-97 Budget Act* to assure that the Legislature will have the opportunity to fully review proposed collective bargaining agreements. Further recommend that the Legislature include the same language in the supplemental report this year. G-148

Control Section 3.60

74. **Public Employees' Retirement System Employer Contribution Rates**. Withhold recommendation on employer contribution rates for retirement benefits pending (1) final determination of the actual rates to be applied in the budget year and (2) receipt and review of information regarding the actuarial assumptions underlying the rates. G-150

Commission on State Mandates

75. **Suspended Mandates Lead to State Costs and Legal Confusion.** Recommend the Legislature enact trailer legislation regarding the 30 mandates proposed for suspension. G-154