



amended and is no longer relevant to OAL.

**AB 88 (Kelley)** would have exempted from the APA the WRCB's adoption or revision of state policy for water quality control and water quality control plans and guidelines; the issuance of waste discharge requirements, permits, and waivers; and the issuance or waiver of water quality certifications (*see supra* AB 3359). This bill died in committee.

## ■ LITIGATION

In *Engelmann v. State Board of Education*, 2 Cal. App. 4th 47 (1991) (certified for partial publication only), the Third District Court of Appeal affirmed the Sacramento County Superior Court's holding that the procedures and criteria used by the State Board of Education in selecting textbooks for use in public schools must be adopted pursuant to the APA. [12:1 CRLR 29] On March 19, the California Supreme Court denied the Board's petition for review, as well as a request for an order directing full publication.

No petition for review has been filed in *Fair Political Practices Commission v. Office of Administrative Law*, No. C010924 (Apr. 27, 1992), in which the Third District Court of Appeal found that the FPPC's regulatory actions are subject to review under the APA only as it existed at the time of the electorate's 1974 approval of the Political Reform Act, which (among other things) created the FPPC. [11:2 CRLR 44]

In other litigation, the state Water Resources Control Board's appeal of the judgment in *State Water Resources Control Board and Regional Quality Control Board, San Francisco Region v. Office of Administrative Law*, No. A054559, is still pending in the First District Court of Appeal. In a judgment favorable to OAL, the trial court held that the wetland rules at issue are regulations within the meaning of the APA; the rules are not exempt from the APA; and since the rules were not adopted pursuant to the APA, they are unenforceable. [12:1 CRLR 29]

## OFFICE OF THE AUDITOR GENERAL

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The Office of the Auditor General (OAG) is the nonpartisan auditing and investigating arm of the California legislature. OAG is under the direction of the

Joint Legislative Audit Committee (JLAC), which is comprised of fourteen members, seven each from the Assembly and Senate. JLAC has the authority to "determine the policies of the Auditor General, ascertain facts, review reports and take action thereon...and make recommendations to the Legislature...concerning the state audit...revenues and expenditures...." (Government Code section 10501.) OAG may "only conduct audits and investigations approved by" JLAC.

Government Code section 10527 authorizes OAG "to examine any and all books, accounts, reports, vouchers, correspondence files, and other records, bank accounts, and money or other property of any agency of the state...and any public entity, including any city, county, and special district which receives state funds...and the records and property of any public or private entity or person subject to review or regulation by the agency or public entity being audited or investigated to the same extent that employees of that agency or public entity have access."

OAG has three divisions: the Financial Audit Division, which performs the traditional CPA fiscal audit; the Investigative Audit Division, which investigates allegations of fraud, waste and abuse in state government received under the Reporting of Improper Governmental Activities Act (Government Code sections 10540 *et seq.*); and the Performance Audit Division, which reviews programs funded by the state to determine if they are efficient and cost effective.

## ■ MAJOR PROJECTS

**Californians to Vote on OAG's Future.** Proposition 159, authored by Senate Minority Leader Ken Maddy, qualified for the November 3 California ballot. This measure would amend the California Constitution to establish OAG with the mandate to conduct independent, non-partisan, professional audits as required by law or requested by the legislature. This initiative would also exempt OAG from the expenditure limits imposed on the legislature by Proposition 140, and require that not more than 50% of the Joint Legislative Audit Committee be composed of members of the same political party. Because OAG is currently folded into the legislature's budget, and the legislature must cut its budget by 38% under Proposition 140, OAG is subject to the threat of funding decreases or entire elimination. [12:1 CRLR 31]

Also appearing on the November ballot is Proposition 158, authored by Senator Dan Boatwright. This measure

would amend the California Constitution to create an independent Office of California Analyst. While this office currently exists as the Office of the Legislative Analyst, that office is also under the financial auspices of the legislature and faces the same threat of fiscal cutback or elimination as does OAG.

## ■ RECENT AUDITS

**Report No. P-115 (May 1992)** analyzes the Department of Corporations' (DOC) management of medical surveys and consumer complaints in its health care service plan division. Pursuant to the Knox-Keene Health Care Service Plan Act of 1975, DOC is responsible for regulating and licensing health care service plans (HCSPs). Among other things, DOC is required to perform various activities to ensure that HCSPs provide quality medical care; these activities include onsite medical surveys of every licensed health plan within specified timeframes. Additionally, DOC assists HCSP members in resolving complaints against their health plans.

As a result of its review, OAG found that DOC has not effectively managed its onsite medical surveys of HCSPs. Although required by law to conduct a survey of each HCSP at least once every five years, DOC told the legislature in 1986 that it attempts to conduct such surveys of most HCSPs every three years. However, OAG found that DOC did not conduct medical surveys every three years for 56% of the state's HCSPs from fiscal year 1987-88 through 1990-91. OAG also found that DOC did not conduct surveys every five years for 10% of the state's HCSPs from fiscal year 1986-87 through 1990-91. As a result, OAG noted that DOC may allow some HCSPs to continue to operate in a manner inconsistent with the law and possibly dangerous to their members' health.

OAG also found that DOC has not effectively managed the release of its medical survey reports. Specifically, OAG found that from fiscal year 1986-87 through 1990-91, 86% of DOC's confidential reports to HCSPs were not issued within the 90-day period established in DOC policy; instead, DOC took an average of 335 days to issue those confidential reports to the health plans. Also, for 78% of the medical surveys for which DOC could provide both the HCSPs' responses and DOC's public reports, DOC did not release the public reports within 45 days of receipt of the HCSPs' responses, as is required by DOC policy; rather, DOC took an average of 164 days to issue those public reports.



In addition, Health and Safety Code section 1380(h) requires DOC to make public specified deficiencies which are not corrected by HCSPs within thirty days of notification. However, OAG found that in 28% of the corrective action plans reviewed, DOC inappropriately deleted from the public reports deficiencies that the HCSPs had not corrected within that 30-day period. OAG also noted that DOC is required to open for public inspection reports of all surveys, deficiencies, and correction plans except for those deficiencies health plans correct within thirty days. However, OAG found that DOC has not properly maintained its records of medical survey information. For example, during OAG's review of medical surveys, DOC could not locate 153 of 247 documents requested by OAG.

OAG also found that DOC failed to clearly state in 25% of the confidential survey reports reviewed whether or not the HCSPs were complying with health care standards. OAG also found that although DOC has the authority to take follow-up and enforcement action, DOC did not do so in 62% of the medical surveys reviewed to ensure that HCSPs corrected cited deficiencies.

Finally, OAG found that DOC failed to meet its goal of processing complaints made by members against their health plans within 45 days in 52% of the complaints OAG reviewed. OAG also noted that as of January 1992, DOC had a backlog of 599 complaints, some received as long ago as fiscal year 1988-89.

OAG recommended that the DOC Commissioner take the following actions:

- establish management controls to ensure that DOC conducts onsite medical surveys according to its three-year goal and five-year statutory mandate;

- implement the training plan adopted in March 1992 for new analysts and update its procedure manual to ensure that analysts are informed of procedures based on the Policy Manual implemented in March 1992;

- ensure that analysts have consistent supervision and direction in conducting medical surveys and issuing medical survey reports;

- establish and implement policies and guidelines to ensure that analysts write medical survey reports clearly and uniformly;

- establish and implement policies regarding instances when DOC deems it unnecessary to issue medical survey reports;

- formalize DOC's policy to include new terminology describing whether HCSPs meet health care standards;

- ensure that consumer services representatives comply with applicable timelines for processing complaints established in DOC's March 1992 Complaint Manual; and

- ensure that the backlog of pending complaints is reduced to a level consistent with DOC's goal in processing complaints.

**Report No. 213 (July 1992)** is the fourth in a series of semiannual reports concerning how the Department of Health Services (DHS) processes reimbursement requests for certain prescribed drugs under the Medi-Cal program; these reports review DHS' process for counting and compiling data on drug treatment authorization requests (TARs) received and processed from June 1990 through May 1992. [12:2&3 CRLR 44; 11:4 CRLR 48; 11:2 CRLR 45]

OAG found that DHS received approximately 91,000 drug TARs during the six months from December 1991 through May 1992. This represents a 16% increase in drug TARs since OAG's first review covering June 1990 through November 1990. According to OAG, the increase may be attributable to a 25.6% increase in Medi-Cal beneficiaries eligible to obtain drugs through the program.

During the last six months of its review, OAG found that DHS' Medi-Cal drug units processed approximately 13% more drug TARs than they did from June 1990 through November 1990. At the same time, DHS' monthly backlog of drug TARs received by mail increased to approximately 8,900 by the end of May 1992. Beginning in April 1992, the Stockton drug unit became the unit primarily responsible for receiving and processing all mail-in drug TARs. The Stockton unit's average time for processing mail drug TARs exceeded the five-working-day limit required by state law; instead, the unit is averaging 25 days for processing mailed-in drug TARs. This represents an increase over the average of fifteen days reported in November 1991. However, OAG also noted that DHS reported receiving no complaints about its processing of drug TARs from June 1991 through May 1992.

OAG also noted that DHS' recent closure of its San Francisco drug unit reduced the number of personnel available to process drug TARs and transferred the drug unit's primary responsibilities to the two remaining field offices (Stockton and Los Angeles).

**Report No. C-126 (August 1992)**, prepared under contract by Rea & Parker, Inc., estimates the net fiscal impact upon the state and local governments in San

Diego County of providing public services to undocumented immigrants. OAG's study defines undocumented immigrants as foreign nationals residing in the United States without lawful permission, or foreign nationals residing in the United States who have violated the conditions of their initial legal entrant status. The benefits analyzed in the study are those state and local tax payments derived from or attributable to undocumented immigrants. OAG analyzed costs in the areas of education, public health services, criminal justice, and social services delivery.

The study found that of the 200,000 undocumented immigrants in San Diego County, 176,810 are in the work force; 87,875 of those have taxes withheld from their pay. The study estimated that undocumented immigrants generate over \$60 million annually in the form of payroll taxes, sales taxes, income taxes, gasoline taxes, vehicle license and registration fees, California Lottery ticket sales, and excise taxes.

The study noted that undocumented immigrants generally tend to commit crimes in the same proportion as the overall population and represent approximately 12.5% of total felony arrestees in San Diego County. Based upon the felony arrest percentage for undocumented immigrants, the study found an annual cost of over \$45 million to San Diego County's law enforcement agency resulting from undocumented immigrants' illegal activity. Additionally, OAG applied unit costs for the various judicial stages to the predicted felony and misdemeanor cases involving undocumented immigrants to yield total annual court costs of almost \$7 million. OAG also estimated that costs incurred by the San Diego County District Attorney and the Public Defender relating to undocumented immigrants approach \$19 million annually; the annual cost to the County's Probation Department is \$5 million; total incarceration costs for adults are almost \$29 million; and the total annual cost of prosecution and detention for the juvenile justice system is almost \$1.5 million. Cumulatively, the study reported a total cost of over \$105 million in processing undocumented immigrants through the criminal justice system.

In determining the cost of providing health services for undocumented immigrants, the study addressed those health delivery programs which provide significant services to the undocumented immigrant population, such as emergency and pregnancy-related services under the Medi-Cal program, emergency transport by publicly-funded paramedic services,



and various San Diego County Department of Health Services programs including indigent care at the University of California at San Diego (UCSD) Medical Center, community clinics throughout the County, the treatment of maternal health problems, preventive child care, and communicable disease treatment at County-funded public health clinics. Regarding Medi-Cal, the study noted that undocumented immigrants are eligible for "restricted benefits" for emergency and pregnancy-related medical problems, for a total annual cost of \$30 million, half of which is the responsibility of the state of California and half of which is provided by the federal government. Further indigent care provided by UCSD Medical Center to undocumented immigrants costs San Diego County almost \$2 million annually. The study further estimated that undocumented immigrants utilize 9.1% of all health services in the County; this overall rate consists of undocumented immigrants' utilization of 18.3% of public health and community clinic services and 2.4% of private health care services. The study estimated that the annual cost of public health and community clinic services for undocumented immigrants totals approximately \$8.5 million. The study further applied the overall utilization rate of 9.1% to the County's overall public cost of ambulance and paramedic services to yield an estimated annual cost of almost \$1 million attributable to undocumented immigrants. The study concluded that the total annual state and local public costs of health service delivery to undocumented immigrants is close to \$27 million.

In terms of the cost of providing public education for undocumented immigrants, the study noted that an estimated 12,000 undocumented immigrant children are educated in public elementary and secondary schools in San Diego County annually. Finding that this figure represents approximately 3% of the total San Diego County student population and 19.0% of all students categorized as Limited English Proficient, OAG estimated that the annual cost of providing basic education to these undocumented immigrant students is almost \$50 million. Additionally, an average of \$8 million is spent on providing General Education Grant programs such as special education, gifted and talented programs, and drug education to undocumented immigrants, and \$2.8 million is attributable to providing undocumented immigrant students services provided through Limited English Proficiency Grants. In terms of higher education, the study noted that in San Diego County, costs to the public involve

only the California State University system. The study noted further that with an estimated 85 undocumented immigrants enrolled at San Diego State University and one such student enrolled at California State University at San Marcos, the total subsidy for these students per year is about \$635,000. OAG thus concluded that the annual state and local cost of providing education to undocumented immigrant students in San Diego County is approximately \$60 million.

The study also examined the cost of providing social services for undocumented immigrants, noting that undocumented immigrants utilize publicly-provided social services to a very limited extent given that social services have typically been reserved for legal residents. However, the study examined the two programs which provide the majority of social services to undocumented immigrants: Aid to Families with Dependent Children (AFDC), offered through the state, and the foster care program of the San Diego County Children's Services Bureau. The study found that the total annual state and local amount of AFDC benefits directed to undocumented immigrants is almost \$12 million; the estimated annual County and state cost of providing in-home social services and out-of-home placement for undocumented immigrant children is about \$1.7 million. The study concluded that the total annual state and local cost associated with the provision of social services to undocumented immigrants is \$13 million.

As a result, the study concluded that the cost to state and local governments associated with processing San Diego County's undocumented immigrants through the criminal justice system and with providing health services, education, and social services for this population is \$206 million. Because the state and local governments receive over \$60 million in revenues associated with the employment and consumer spending of undocumented immigrants, the net state and local cost of providing public services to undocumented immigrants in San Diego County is approximately \$146 million.

**Report F-105 (June 1992).** As part of its examination of the state's general purpose financial statements for the fiscal year ending June 30, 1991, OAG evaluated the state's internal financial control structure. This study of the control structure was undertaken to allow OAG to express an opinion on the adequacy of the state's general purpose financial statements; determine the extent of compliance with federal grant requirements, laws, and regulations; and determine compliance

with state laws and regulations that could materially affect the general purpose financial statements. The twenty agencies audited represented approximately 61% of the state's revenues and approximately 60% of the state's spending during the fiscal year.

According to OAG, the state loses millions of dollars each year because of inadequate financial control procedures. Additionally, poor accounting practices have caused confusion about the state's financial condition among the state's own financial decisionmakers, the outside investment community, and the federal government. In its review of financial operations of statewide concern, OAG discovered several major shortcomings in the state's internal controls and financial reporting systems. For example, because of the state's failure to use generally accepted accounting principles (GAAP) in its reporting of the execution of its budget, California inconsistently reports its financial condition. The state's true financial condition is also obscured by the use of different accounting principles in the preparation of financial reports by the state Controller's Office and the Department of Finance. In addition, OAG found that the state must make numerous adjustments to its financial statements to prepare them in accordance with nationally recognized GAAP so that they are comparable to the financial statements of other states and acceptable to the investment community and the federal government.

OAG also reported on numerous other problems of statewide concern, including the following:

- California faces a possible liability to the federal government of as much as \$24 million for profits it has accumulated in the state's internal service funds between July 1, 1984, and June 30, 1991.

- For the last six years, the state has been unable to produce financial reports and audited financial statements within six months of the end of the fiscal year, as is required by the Government Finance Officers Association.

- For the past two years, the state has not included combining statements by fund type in its audited financial statements, as is required by the Governmental Accounting and Financial Reporting Standards issued by the Governmental Accounting Standards Board.

- The lack of a central record of information regarding the state's leases requires the state to spend unnecessary additional time to prepare its financial statement disclosures required by GAAP for those lease commitments.

- The state's grants, certain contracts,



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and interagency agreements are not routed through the Department of General Services to assure their validity.

-The state's method of accounting for federal assistance does not provide sufficient information on expenditures of federal funds because it does not record its expenditures by federal program. As a result, the state is unable to present a schedule of federal assistance that shows total expenditures for each federal assistance program, as is required by the federal Office of Management and Budget.

-District Agricultural Associations, which are organized to hold fairs and exhibitions, are not treated as part of the state reporting entity, despite the Legislative Counsel's opinion that such Associations are state agencies and that money they spend is state money.

-The State Administrative Manual fails to require numerous agencies to submit reconciliations and reports of accruals.

The OAG report also provides detailed information on specific weaknesses in control over financial activities and problems in compliance with state and federal regulations in a number of state agencies. For example, in the Business, Transportation and Housing Agency, the Department of Motor Vehicles does not have sufficient control over the collection of dishonored checks, which totalled approximately \$13.4 million as of June 30, 1991, and the Stephen P. Teale Data Center continues to have inadequate methods for inventory and accounting for equipment and intangible assets. In the area of educational programs, OAG notes that the California Student Aid Commission does not ensure the adequacy of efforts to collect on defaulted student loans that the Commission has purchased. As to general government agencies, the Department of Personnel Administration is unable to ensure that it properly accounts for the deferred compensation program. As of March 1992, 21 months after it contracted with a firm to provide recordkeeping services, the Department was not yet able to adequately monitor the program. In the Health and Welfare Agency, the efforts of the Department of Health Services to collect the costs it has incurred in the monitoring and remediation of hazardous waste sites are inadequate. Within the legislative, judicial, and executive areas of state government, OAG noted that the Board of Equalization is unable to ensure that unapplied credit balances are processed in compliance with state law. OAG also identified tax refund problems in the bank and corporate tax system of the Franchise Tax Board in the State and Consumer Services Agency.

**Report No. P-029 (June 1992)** was prepared by OAG to evaluate the Department of Insurance's (DOI) regulatory practices aimed at early detection of problems that can lead to an insurer's insolvency. OAG reviewed the pertinent laws, regulations, and policies relating to DOI's regulatory system; information was gathered by interviewing personnel of DOI's financial analysis division, field examination division, claims services bureau, and conservation and liquidation division. The audit also included an evaluation of the Department's regulatory system through a review of fourteen insolvent insurers, of which nine were incorporated in California.

As part of its duties, DOI is responsible for the protection of policyholders, beneficiaries, and other members of the public from losses arising from insurance company insolvencies. DOI attempts to provide this protection by screening would-be entrants into the field of insurance, analyzing insurers' financial statements, conducting field examinations, regulating insurance rates, investigating consumer complaints, and enforcing compliance with the California Insurance Code. To protect California consumers from losses resulting from the insolvency of insurance companies, DOI regulates nearly 1,900 insurers and approximately 300,000 individuals licensed to conduct insurance business in this state.

A.M. Best, an organization that provides ratings and financial information on the insurance industry, defines an insolvent insurance company as any insurer domiciled in the United States against which the insurance department of its state of domicile has taken action for reasons of financial impairment; such state actions include administrative orders, supervision, suspension, receivership, conservatorship, liquidation, or other actions that restrict the insurer's freedom to conduct business. According to an A.M. Best study cited by OAG, 372 property and casualty insolvencies occurred nationwide from 1969 through 1990; California ranked second among the states with 35 insolvencies during that period. Examples of recent California seizures include Great Republic Insurance Company [11:4 CRLR 133], Executive Life Insurance Company, and First Capital Life Insurance Company of San Diego [11:3 CRLR 128]. To combat the problem of insolvent insurers in California, the state established the California Insurance Guarantee Association (CIGA) in 1969 and the California Life Insurance Guarantee Association (CLIGA) in 1991. These two associations exist to pay for covered claims of member

property and casualty and life insurers who become insolvent. All property and casualty insurers transacting business in California must belong to CIGA, and all life insurers doing business in the state must be members of CLIGA. According to OAG, CIGA estimates that, as of June 1990, the projected costs for all property and casualty insolvencies in California since 1985 will total approximately \$1.1 billion. Cost data for the insolvencies of life insurers could not be estimated due to a lack of data available in the short period since the formation of CLIGA.

OAG's audit revealed several problems in DOI's past regulation of potentially insolvent insurers. According to OAG, during 1974-91, DOI did not always take prompt and decisive action when it detected conditions detrimental to an insurer's solvency. These conditions include an insurer's questionable investments, improper reinsurance arrangements, improper affiliate transactions, loss reserve deficiencies, poor underwriting, poor use of managing general agents, and agents' high balances. OAG emphasized that delays in prompt and effective regulatory action can increase the costs of an insurer's insolvencies by allowing the insurer to continue writing new business while no or informal corrective action is pursued; such increased costs are passed on to the policyholders of healthy companies in the form of higher insurance rates.

According to OAG, DOI has consistently failed to take advantage of information available through national agencies and the insurance regulators of other states. Although many state regulators are reluctant to share information on financially troubled insurers, California did not make an adequate effort to gather the information that was available on some troubled insurers, and often waited for the domiciliary state to take action. In some cases, efforts by DOI to screen insurers applying to transact business in California were hampered by flaws in the information gathering system. OAG found that coordination of efforts with agencies such as the Securities and Exchange Commission (SEC) and the National Association of Insurance Commissioners were often ineffective because of DOI's failure to contact these agencies and/or to adequately document the information received.

OAG made a number of recommendations for the improvement of DOI's work related to insolvent insurance companies, including the following:

-DOI should develop guidelines for corrective action plans to address the problems of insurers in danger of insol-



gency. These plans should specify a time-frame for the insurer to correct identified problems and provide an outline of actions DOI will take if the insurer does not comply with the corrective action plan.

—The method of investigation of officers, directors, and major stockholders of insurers applying for new and amended certificates should be revised to include periodic requests for information from other agencies, the development of an identification system for obtaining information from the SEC about specific individuals, and better documentation of the information obtained.

—DOI should establish a more effective and assertive communication system with other state regulators.

—DOI should strengthen its regulatory practices aimed at questionable investments, improper affiliate transactions, loss reserve deficiencies, improper reinsurance, poor use of managing general agents, poor underwriting, and excessive agents' balances.

According to OAG, DOI has already made a number of changes aimed at improving its surveillance and regulation of insurers, including the reorganization of portions of DOI regulatory staff and the drafting of a variety of bills designed to improve regulatory authority over entities and activities identified as factors in past insolvencies. (See *infra* agency report on DOI for related discussion.)

**Report No. P-215 (August 1992)** reviews the University of California's (UC) executive compensation, benefits, and offices. OAG's review of the UC encompassed an evaluation of UC programs that provide compensation and benefits to UC executives; a review of the relocation of the UC's administrative offices from Berkeley to Oakland; and a review of the costs associated with the UC's Office of the President (Office) located in Irvine.

The UC is a public, state-supported institution administered under the authority of the 26-member Board of Regents (Regents). Pursuant to the California Constitution, the Regents have full powers of organization and government of the UC, subject only to the legislative control necessary to ensure the security of the UC's funds and the compliance with endowment terms and certain competitive bidding procedures. The state's general fund is the principal funding source for the UC's instructional programs. Other funding sources include the federal government, which provides funds for research and three U.S. Department of Energy laboratories, private gifts, and investment income. Total UC revenues for fiscal year 1990-91 were approximately \$10.2 bil-

lion, of which approximately \$2.4 billion, or 23.5%, was supplied by the state.

In its study, OAG reviewed the salaries and benefits paid by the UC to a sample of 22 top executives. OAG noted that, in an attempt to improve the competitiveness of UC's executive compensation, the Regents have approved a number of salary increases since 1983; for example, of the ten executives who had been in their positions since 1983, nine enjoyed salary increases ranging from 21-40% between July 1983 and July 1984. OAG also found that some approved salary increases for fiscal year 1984-85 may have been greater than UC Regents believed due to a lack of sufficient detail in the document used to propose the increases; the actual average percentage increase in actual salaries paid for seven executives that year was 17.1%, rather than the 10.8% increase UC President David Gardner claimed the executives were receiving. OAG additionally noted that—at the time of its audit—Gardner's total annual compensation, including base salary and various special allowances and supplements, exceeded \$452,000. The annual compensation of the remaining 21 executives in OAG's sample ranged from \$131,293 to \$316,551.

With regard to leaves of absence, OAG found that all six of the executives reviewed failed to report absences related to illness or medical appointments; five of the six failed to report vacation leave taken. In response to OAG's findings, Associate Vice President Richard West stated that, under UC's current legal interpretation of wage and hour law, executives should not be docked for absences of less than one day. However, OAG noted that UC policy does not state that executives may waive the recording of leave time taken in less than one-day increments.

OAG also reviewed President Gardner's housing-related assistance and compensation, noting that when Gardner became UC President in 1983, he was granted an exception from occupying University housing and was provided with a housing allowance to assist him in paying the costs of owning his home. As part of the original housing benefits package Gardner received, the UC agreed to buy his previous home in Utah, provide him with a mortgage loan for his new California home, and pay a cash stipend to cover his house operation costs. OAG notes that subsequent changes to the housing package often resulted in additional benefits to Gardner. OAG discovered that the UC may have paid Gardner more for the Utah home than the value of his equity in it, as Gardner's equity was \$15,000 less

than the UC paid him. OAG also noted that the UC paid Gardner an average of \$25,020 per year as his housing allowance; a separate compensation for house operating expenses given to Gardner during his tenure averaged \$39,600 per year. OAG also found that four other UC executives each receive a housing allowance of approximately \$3,476 per month, or \$41,710 per year.

In terms of moving expenses, OAG found that the UC paid moving expenses for Gardner and four of the eight executives reviewed who were appointed during Gardner's tenure, averaging approximately \$14,800 each. In these five cases, an average of 50.2% of the expenditures was for items not reimbursable under the UC policy in effect at the time; OAG notes that exceptions were granted for these executives. OAG also found that the UC inconsistently reported moving expense payments or reimbursements as taxable gross income to the executives and taxation authorities. For example, in one instance the UC failed to include almost \$6,000 of moving expense payments or reimbursements in one executive's gross income.

In reviewing relocation incentives, OAG determined that two of the 22 executives reviewed were paid relocation incentives in the form of temporary salary supplements during Gardner's tenure. OAG also found that—in violation of UC policy—Gardner and Senior Vice President William Brady approved payment of one such \$30,000 incentive in the absence of Regent approval.

In reviewing special retirement programs, OAG found that in addition to regular contributions to the UC retirement plan, the UC has provided a number of special retirement programs to the executives in OAG's sample. For example, for the Regents' Special Retirement Contribution Program, which is no longer active, the UC changed the contribution rate from 3% of certain executives' salaries to 3% of their salaries plus housing value. OAG further noted that as a result of a change of vesting dates on five non-qualified deferred income plans the UC entered into with Gardner, the UC will pay Gardner an estimated \$492,607 upon his retirement instead of the \$60,850 it would have otherwise been obligated to pay. OAG also discovered that in approving changes in vesting dates on two other retirement program agreements, the UC may be obligated to pay Gardner an additional \$327,478. According to OAG, had the Regents not opted to change the dates on these agreements the UC would not be obligated to provide benefits totaling over \$759,000.



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OAG also noted that the UC provides certain executives with automobile compensation for business purposes. OAG found that as of April 30, eight of the executives reviewed had UC-leased automobiles; seven other executives and one spouse, who is an approved associate of the UC, received automobile allowances. According to OAG, in fiscal year 1990-91, the annual cost of lease payments for automobiles ranged from about \$4,500 to \$8,500.

In auditing entertainment expenditures from July 1990 through April 1992, OAG found that from July 1, 1991 through April 30, 1992, the UC paid \$116,039 from its Administrative Fund for entertainment hosted by twelve of the 22 executives reviewed. OAG noted that entertainment expenditures covered a variety of events, including a party celebrating the wedding of a President's Office employee.

OAG noted that several of the executives in OAG's sample frequently entertained other employees and representatives of the Office of the President exclusively. OAG also found that when only Office employees and representatives were entertained, the entertainment often took place close to UC headquarters. According to OAG, it is not economically prudent to reimburse employees for meals or entertainment when they are at or in the vicinity of their workplace.

Further, OAG noted that the UC also uses the Administrative Fund to reimburse UC executives for contributions, gifts, and miscellaneous expenses. OAG found that from July 1, 1991 through April 30, 1992, reimbursed expenditures of the executives reviewed totalled \$2,473 for contributions, \$11,578 for gifts, and \$21,211 for miscellaneous expenditures.

In its audit of the UC's system of compensating executives for business-related travel expenses, OAG found that the UC's general travel policies were not always helpful in determining whether costs were legitimate. For example, OAG claimed that the UC policy which states that only those travel expenses that are "ordinary and necessary" are eligible for reimbursement does not clearly define that phrase. Although OAG found no policies governing the use of frequent-flyer miles earned while traveling on business, OAG believes that it is reasonable to expect that these types of earned miles be used for UC business; OAG noted one instance when Gardner used frequent-flyer miles earned while on UC business to purchase a round-trip flight to Hong Kong valued at \$3,880 for his daughter.

According to OAG, there were several instances where executives claimed un-

necessary lodging expenses. For example, Gardner stayed at a San Francisco hotel for two nights during a Regents meeting at a cost to the UC of \$370, even though the location of the meeting was approximately ten miles from the UC's Oakland headquarters. OAG also noted that some executives used their Administrative Fund allocation to pay for first-class travel on business flights; according to OAG, it does not benefit the UC when its employees choose first-class travel if more economical means are available.

Finally, OAG reviewed the circumstances surrounding the move of the President's Office to new administrative offices. OAG noted that beginning in 1988, the Office consolidated its operations in the Kaiser building in Oakland from seven locations in Berkeley. According to OAG, the UC perceived the move as a way to reduce the overall long-term cost of its leased space, resolve organizational problems of managing a staff located on multiple sites, and provide the UC's Berkeley campus with much needed space. In addition, an office in Irvine was leased in order to establish a UC presence in southern California and provide space for other university functions. OAG noted that the total cost of the Irvine office over the UC's five-year lease, including lease payments, tenant improvements, and furnishings, exceeds \$1.2 million, or an average of \$240,000 per year. OAG further noted that because of budget considerations, the UC intends to abandon the Irvine lease when it expires in January 1993.

To ensure that the UC fulfills its responsibility to the public and governments that contribute to its funding, OAG recommended that the UC and, as appropriate, the Regents, take the following actions in regard to compensation and benefits for UC executives:

- ensure that any officials approving executive compensation and benefits receive accurate and complete information so that the officials can make well-informed decisions and staff can implement the decisions as the officials intended;

- charge leave balances for unreported leave taken;

- clarify its policy requiring leave reporting;

- ensure that the proper officials approve any compensation payments and exceptions that require approval;

- ensure that it consistently reports all taxable compensation or reimbursements for executives to the taxation authorities;

- ensure that it does not grant relocation incentives to executives who do not relocate as a condition of their employment;

- clarify its policies regarding appropriate entertainment and travel expenditures and decide whether, or the extent to which, the Administrative Fund should be used to reimburse meals and lodging within the vicinity of UC employees' headquarters;

- clarify its policies regarding whether, or the extent to which, the Administrative Fund should be used to entertain employees of the Office of the President exclusively;

- ensure that contributions, gifts, and other miscellaneous expenses that it reimburses are clearly documented and appropriately made; and

- ensure that frequent-flyer bonuses that executives receive while on official business are used for the UC's benefit and not for individual benefit.

While the UC agreed with some of OAG's recommendations and immediately commenced addressing those recommendations, it disagreed with the following OAG conclusions:

- while OAG questions the accuracy and sufficiency of information provided to the Regents when the Regents approved fiscal year 1984-85 salary increases for certain executives, the UC believes the information was correctly conveyed by Gardner;

- while the UC acknowledges that it paid two executives at rates higher than those approved by the Regents, the UC believes that it paid the executives amounts to which they were entitled and will seek retroactive approval from the Regents;

- the UC does not agree that executives should be required to report absences in increments of less than one day or that the UC should reconsider the amount of sick leave it allows executives to accrue;

- the UC does not agree that it should reevaluate its policies regarding reimbursement of extraordinary travel and entertainment expenses; and

- the UC does not agree that it should ensure that its employees use frequent-flyer awards that they earn while on UC business for business purposes only.

Gardner was succeeded as UC President on October 1 by UC Irvine Chancellor Jack Peltason. Just prior to his departure, Gardner issued new rules on spending in response to OAG's report; these policies include a ban on most first-class air travel—unless absolutely necessary—and a requirement that entertainment paid with administrative funds serve "a clear university business purpose." Although OAG's findings were described by one Regent as "extraordinarily immaterial," other Regents acknowledged that the audit





showed "a complete breakdown" in financial oversight and that the Regents had fallen into "a state of disrepute" with the public.

**Other Audits.** Additionally, OAG produced the following reports during the past few months:

- **Report No. P-135 (June 1992)** reviews the Department of General Services' procurement and material management practices;

- **Report No. F-104 (June 1992)** reviews the State Treasurer's Statement of Securities Accountability as of June 30, 1991;

- **Report No. P-134 (July 1992)** reviews court services in San Bernardino County;

- **Report No. P-142 (July 1992)** reviews selected areas of the Chino Unified School District's Building Program;

- **Report No. I-214 (August 1992)** summarizes OAG's investigations between January 1991 and July 1992 of improper activities ranging from the misuse of state resources to abuse of official position; and

- **Report No. P-141 (September 1992)** reviews the Judges' Retirement System.

## ■ LEGISLATION

**AB 3036 (Eaves)** would have required the Auditor General to study the long-term financial impact on the State Highway Account of the conversion of motor vehicles to low- or zero-emission alternative fuels. This bill died in committee.

## COMMISSION ON CALIFORNIA STATE GOVERNMENT ORGANIZATION AND ECONOMY (LITTLE HOOVER COMMISSION)

*Executive Director:*

*Jeannine L. English*

*Chairperson: Nathan Shapell*

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The Little Hoover Commission was created by the legislature in 1961 and became operational in the spring of 1962. (Government Code sections 8501 *et seq.*) Although considered to be within the executive branch of state government for budgetary purposes, the law states that "the Commission shall not be subject to the control or direction of any officer or employee of the executive branch except

in connection with the appropriation of funds approved by the Legislature." (Government Code section 8502.)

Statute provides that no more than seven of the thirteen members of the Commission may be from the same political party. The Governor appoints five citizen members, and the legislature appoints four citizen members. The balance of the membership is comprised of two Senators and two Assemblymembers.

This unique formulation enables the Commission to be California's only truly independent watchdog agency. However, in spite of its statutory independence, the Commission remains a purely advisory entity only empowered to make recommendations.

The purpose and duties of the Commission are set forth in Government Code section 8521. The Code states: "It is the purpose of the Legislature in creating the Commission, to secure assistance from the Governor and itself in promoting economy, efficiency and improved service in the transaction of the public business in the various departments, agencies, and instrumentalities of the executive branch of the state government, and in making the operation of all state departments, agencies, and instrumentalities and all expenditures of public funds, more directly responsive to the wishes of the people as expressed by their elected representatives...."

The Commission seeks to achieve these ends by conducting studies and making recommendations as to the adoption of methods and procedures to reduce government expenditures, the elimination of functional and service duplication, the abolition of unnecessary services, programs and functions, the definition or redefinition of public officials' duties and responsibilities, and the reorganization and/or restructuring of state entities and programs. The Commission holds hearings about once a month on topics that come to its attention from citizens, legislators, and other sources.

## ■ MAJOR PROJECTS

**No Room for Johnny: A New Approach to the School Facilities Crisis** (June 1992). According to this Little Hoover Commission report, California schools face a dramatic increase in the K-12 student population through the end of this decade, with today's 5.1 million students expected to balloon to 7 million by the year 2000. Estimates of the construction costs to provide school facilities for these children range from \$30-\$35 billion, if no cost-saving alternatives are used. The Commission notes that during a

period when the state must decide where to spend its limited resources, schools must compete with many other infrastructure demands. Additionally, school districts are hindered by a complex facilities project approval process involving multiple state agencies, certain state policies which make it difficult for districts to pursue proactive asset management, and a lack of cohesive communities of interest to support school construction projects.

According to the Commission, the state's role as the provider of funds for school facilities is inappropriate; the state should not be a "bottomless pocket" for school facilities spending while the authority for decisions regarding school facilities funding is firmly vested at the local school district level. In spite of the local control over education, numerous court decisions have indicated that the state must act to protect the right of students to equal access to education; it is California's responsibility to ensure that the state's various school facilities are equitable. The Commission suggested that the Governor and legislature take the following actions regarding the facilities funding process:

- modify the Leroy F. Greene State School Building Lease Purchase program to return the responsibility of funding new school facilities to the local school districts, thereby limiting the state's financial role to assuring equity and providing a safety net;

- require the state Department of Education to convene a task force to determine advisory (rather than prescriptive) standards for adequate, modern school facilities that can be adopted by the state in place of the current minimum standards; and

- place a constitutional amendment before voters to modify the approval threshold of general obligation bonds in a manner consistent with the most cost-effective use of the bonds issued.

Even with adequate funds available for construction of new school facilities, the Commission found that the state has created a cumbersome program that micromanages school construction projects, thus delaying the completion and driving up the cost of new school facilities. The state's permit review and planning process for new school facilities may take 18 months or longer, during which a project is reviewed by the local school district, the Department of Education, the Office of Local Assistance, the State Allocation Board, and the Office of the State Architect. Delays caused by this process often add to the cost for new facilities in both rising land values and in higher con-