STATE OF CALIFORNIA
EDMUND G. BROWN JR., Governor

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January 27, 2016

Mr. Keith B. Petersen
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Ms. Jill Kanemasu
State Controller's Office
Accounting and Reporting
3301 C Street, Suite 700
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And Parties, Interested Parties, and Interested Persons (See Mailing List)

Re: **Decision**
Notification of Truancy, 13-904133-I-13
Education Code Section 48260.5
Statutes 1983, Chapter 498
Fiscal Years: 2007-2008, 2008-2009, and 2009-2010
Riverside Unified School District, Claimant

Dear Mr. Petersen and Ms. Kanemasu:

On January 22, 2016, the Commission on State Mandates adopted the decision on the above-entitled matter.

Sincerely,

Heather Halsey
Executive Director

BEFORE THE

COMMISSION ON STATE MANDATES

STATE OF CALIFORNIA

IN RE INCORRECT REDUCTION CLAIM ON: Education Code Section 48260.5 Statutes 1983, Chapter 498 Fiscal Years 2007-2008, 2008-2009, and 2009-2010 Riverside Unified School District, Claimant	Case No.: 13-904133-I-13 *Notification of Truancy* DECISION PURSUANT TO GOVERNMENT CODE SECTION 17500 ET SEQ.; CALIFORNIA CODE OF REGULATIONS, TITLE 2, DIVISION 2, CHAPTER 2.5. ARTICLE 7 (*Adopted January 22, 2016*) (*Served January 27, 2016*)

DECISION

The Commission on State Mandates (Commission) heard and decided this incorrect reduction claim (IRC) during a regularly scheduled hearing on January 22, 2016.

The law applicable to the Commission's determination of a reimbursable state-mandated program is article XIII B, section 6 of the California Constitution, Government Code section 17500 et seq., and related case law.

The Commission adopted the proposed decision to deny the IRC on consent, with Commission members Alex, Hariri, Olsen, Ortega, and Ramirez voting to adopt the consent calendar. Commission members Chivaro and Saylor were not present for the vote.

Summary of the Findings

This IRC challenges reductions of $68,410 made by the State Controller's Office (Controller) to reimbursement claims filed by the Riverside Unified School District (claimant) for fiscal years 2007-2008, 2008-2009, and 2009-2010 under the *Notification of Truancy* program.

At issue in this IRC is whether the Controller may:

- Reduce costs claimed for initial truancy notifications distributed for pupils who accumulated fewer than three unexcused absences or tardiness occurrences while between ages six and 18 because they were subject to the compulsory education requirements for only a portion of the school year.
- Reduce costs claimed for initial truancy notifications distributed for pupils who accumulated fewer than three total unexcused absences or tardiness occurrences during the school year; and,
- Use statistical sampling and extrapolation to reduce the costs claimed for initial truancy notifications.

The Commission finds that the reduction totaling $68,410, based on the Controller's sampling and extrapolation methodology, for initial notifications of truancy distributed for pupils who had

fewer than three unexcused absences or tardiness occurrences during the school year and for pupils who accumulated fewer than three absences while between the ages of six and 18 and so were not subject to the compulsory education laws, is correct as a matter of law, and is not arbitrary, capricious, or entirely lacking in evidentiary support.

COMMISSION FINDINGS

I. Chronology

02/16/2010 Claimant signed the reimbursement claim for fiscal year 2007-2008.[1]

02/16/2010 Claimant signed the reimbursement claim for fiscal year 2008-2009.[2]

02/15/2011 Claimant signed the reimbursement claim for fiscal year 2009-2010.[3]

12/19/2012 Controller issued the draft audit report.[4]

01/18/2013 Claimant submitted comments on the draft audit report.[5]

02/22/2013 Controller issued the final audit report.[6]

11/15/2013 Claimant filed this IRC.[7]

10/03/2014 Controller filed late comments on the IRC.[8]

10/28/2015 Commission staff issued the draft proposed decision.[9]

10/30/2015 The Controller filed comments on the draft proposed decision.[10]

11/03/2015 The claimant filed comments on the draft proposed decision.[11]

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[1] Exhibit A, Incorrect Reduction Claim, page 269.

[2] Exhibit A, Incorrect Reduction Claim, page 271.

[3] Exhibit A, Incorrect Reduction Claim, page 273.

[4] Exhibit A, Incorrect Reduction Claim, page 31. The draft audit report is not part of the record.

[5] Exhibit A, Incorrect Reduction Claim, pages 39-40.

[6] Exhibit A, Incorrect Reduction Claim, pages 232-247.

[7] Exhibit A, Incorrect Reduction Claim.

[8] Exhibit B, Controller's Late Comments on the Incorrect Reduction Claim. Note that pursuant to Government Code section 17553(d) "the Controller shall have no more than 90 days after the claim is delivered or mailed to file any rebuttal to an incorrect reduction claim. The failure of the Controller to file a rebuttal to an incorrect reduction claim shall not serve to delay the consideration of the claim by the Commission." However, in this instance, due to the backlog of Incorrect Reduction Claims, these late comments have not delayed consideration of this item and so have been included in the analysis and proposed decision.

[9] Exhibit C, Draft Proposed Decision.

[10] Exhibit D, Controller's comments on the Draft Proposed Decision.

[11] Exhibit E, Claimant's comments on the Draft Proposed Decision.

II. Background

The *Notification of Truancy* Program

Under California's compulsory education laws, children between the ages of six and 18 are required to attend school full-time, with a limited number of specified exceptions.[12] Once a pupil is initially designated a truant, as defined, state law requires schools, districts, counties, and the courts to take progressive intervention measures to ensure that parents and pupils receive services to assist them in complying with the compulsory attendance laws.

The first intervention is required by Education Code section 48260.5, as added by the test claim statute.[13] As originally enacted, section 48260.5 specified:

> (a) Upon a pupil's initial classification as a truant, the school district shall notify the pupil's parent or guardian, by first-class mail or other reasonable means, of the following:
>
> (1) That the pupil is truant.
>
> (2) That the parent or guardian is obligated to compel the attendance of the pupil at school.
>
> (3) That parents or guardians who fail to meet this obligation may be guilty of an infraction and subject to prosecution pursuant to Article 6 (commencing with Section 48290) of Chapter 2 of Part 27.
>
> (b) The district also shall inform parents or guardians of the following:
>
> (1) Alternative educational programs available in the district.
>
> (2) The right to meet with appropriate school personnel to discuss solutions to the pupil's truancy.

On November 29, 1984, the Board of Control, the predecessor to the Commission, determined that Education Code section 48260.5, as added by Statutes 1983, chapter 498, imposed a reimbursable state-mandated program to develop notification forms and provide written notice to the parents or guardians of the truancy. The decision was summarized as follows:

> The Board determined that the statute imposes costs by requiring school districts to develop a notification form, and provide written notice to the parents or guardians of students identified as truants of this fact. It requires that notification contain other specified information and, also, to advise the parent or guardian of their right to meet with school personnel regarding the truant pupil. The Board found these requirements to be new and not previously required of the claimant.[14]

The original parameters and guidelines were adopted on August 27, 1987, and authorized reimbursement for the one-time activities of planning implementation, revising school district

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[12] Education Code section 48200.

[13] Education Code section 48260.5, Statutes 1983, chapter 498.

[14] Exhibit F, Board of Control, Brief Written Statement for Adopted Mandate issued by the Board of Control on the *Notification of Truancy* test claim (SB 90-4133).

policies and procedures, and designing and printing the notification forms. Reimbursement was also authorized for ongoing activities to identify pupils to receive the initial notification and prepare and distribute the notification by first class mail or other reasonable means.

The Commission amended the parameters and guidelines on July 22, 1993, effective July 1, 1992, to add a unit cost of $10.21, adjusted annually by the Implicit Price Deflator, for each initial notification of truancy distributed in lieu of requiring the claimant to provide documentation of actual costs to the Controller. The parameters and guidelines further provide that "school districts incurring unique costs within the scope of the reimbursable mandated activities may submit a request to amend the parameters and guidelines to the Commission for the unique costs to be approved for reimbursement."[15]

The Legislature enacted Statutes 2007, chapter 69, effective January 1, 2008, which was sponsored by the Controller's Office to require the Commission to amend the parameters and guidelines, effective July 1, 2006, to modify the definition of a truant and the required elements to be included in the initial truancy notifications in accordance with Statutes 1994, chapter 1023, and Statutes 1995, chapter 19.[16] These statutes required school districts to add the following information to the truancy notification: that the pupil may be subject to prosecution under Section 48264, that the pupil may be subject to suspension, restriction, or delay of the pupil's driving privilege pursuant to Section 13202.7 of the Vehicle Code, and that it is recommended that the parent or guardian accompany the pupil to school and attend classes with the pupil for one day. The definition of truant was also changed from a pupil with unexcused instances of absence or tardiness for "more than three days" to a pupil "who is absent from school without valid excuse three full days in one school year or tardy or absent for more than any 30 minute period during the schoolday without a valid excuse on three occasions in one school year, or any combination thereof."[17] In 2008, the Commission amended the parameters and guidelines, for costs incurred beginning July 1, 2006, as directed by the Legislature.[18] However, reimbursement for the program under the amended parameters and guidelines remained fixed at a unit cost of $10.21, adjusted annually by the Implicit Price Deflator ($19.63 for fiscal year 2013-14). These are the parameters and guidelines applicable to this claim.

The Controller's Audit and Summary of the Issues

The final audit report of February 22, 2013, determined that $684,558 claimed costs for fiscal years 2007-2008 through 2009-2010 was allowable, and $111,552 was unallowable for various reasons. The claimant only disputes the $68,410 reduction in finding 2 of the audit report based on the Controller's review of a sample of 883 notices issued by the district's elementary and secondary schools out of the 45,091 notices claimed for the audit period.[19] The Controller found that 79 notices included in the sample were not reimbursable because the district claimed:

[15] Exhibit A, Incorrect Reduction Claim, page 69.

[16] Exhibit F, Office of the State Controller, Letter to School Districts re AB 1698, July 17, 2007.

[17] Education Code section 48260 (Stats. 1994, ch. 1023; Stats. 1995, ch. 19).

[18] Statutes 2007, chapter 69 (AB 1698).

[19] Exhibit A, Incorrect Reduction Claim, final audit report, pages 242-243; Exhibit B, Controller's Late Comments on the Incorrect Reduction Claim, page 16.

- 67 notifications sent for pupils with fewer than three unexcused absences or tardiness occurrences while between the ages of six and 18, because they were subject to the compulsory education requirements for only a portion of the school year.
- 12 notifications sent for pupils who accumulated fewer than three total unexcused absences or tardiness occurrences during the school year.[20]

The Controller reduced $68,410 in costs claimed using statistical sampling audit methodology by examining a random sample of initial truancy notices distributed by the claimant, calculating the "sample size based on a 95% confidence level," and determining that 79 of those notices claimed were beyond the scope of the mandate, as described above.[21] The number of unallowable notifications within the sample for each fiscal year was then calculated as an error percentage and extrapolated to the number of notifications issued and identified by the claimant in those fiscal years, to approximate the total number of unallowable notifications claimed. The number of unallowable notices was then multiplied by the unit cost for each fiscal year to calculate the total reduction for the audit period.[22]

III. Positions of the Parties

A. Riverside Unified School District

The claimant argues that the statistical sampling technique used by the Controller should be rejected and that the audit finding should only pertain to the documentation actually reviewed. The claimant states that the audit report cited no statutory or regulatory authority to allow reduction of costs claimed based on extrapolation of a statistical sample.

The claimant asserts that the standard in Government Code section 17561(d)(2) controls the audit (excessive or unreasonable) because it is specific to mandates claims, and that the standard in Government Code section 12410 (correctness, legality, and sufficient provisions of law) does not control the audit. Also, the audit report states that the audit was conducted according to generally accepted government accounting standards (GAGAS) that "recognize statistical sampling as an acceptable method to provide sufficient, appropriate evidence" but claimant states that the audit does not cite specific General Accountability Office (GAO) or GAGAS language in support of the assertion.

Claimant also argues that the GAO auditing guide pertains to audits of federal funds that do not apply to state mandate reimbursement. And the district has no notice of the GAO guide because the Controller does not publish its audit standards. Nor has the GAO guide been adopted pursuant to the Administrative Procedure Act (APA).[23]

Claimant further argues that the sampling process was misapplied in this IRC because the audit actually conducted a review for documentation rather than mandate compliance. According to the claimant, "testing to detect the rate of error within tolerances is the purpose of sampling, but

[20] Exhibit A, Incorrect Reduction Claim, final audit report, page 242; Exhibit B, Controller's Late Comments on the Incorrect Reduction Claim, page 19.

[21] Exhibit B, Controller's Late Comments on the Incorrect Reduction Claim, page 10.

[22] Exhibit A, Incorrect Reduction Claim, pages 242-243.

[23] Exhibit A, Incorrect Reduction Claim, pages 11-13.

it is not a tool to assign an exact dollar amount to the amount of the error which the Controller has inappropriately done . . . here."[24]

Claimant also states that the sample may not be representative of the universe because, for example, kindergarten students in the sample are more likely to be excluded because of the under-age issue, and the possibility of a special education student being under-age or over-age is greater than the entire student body.[25]

And according to claimant, the sampling technique used in the audit is non-representative because the sample size for the audit period is 1.93 percent of the universe. As the claimant states: "The expected error rate is stated to be 50%, which means the total amount adjusted of $68,410 is really just a number exactly between $34,205 (50%) and $102,615 (150%). An interval of possible outcomes cannot be used as a finding of absolute actual cost."[26]

Claimant states that because the statistical sampling and extrapolation fails for legal, quantitative, and qualitative reasons, the audit findings should be limited to the 736 notices actually investigated. Claimant also cites statutory entitlements for pupils under age six or older than 18 to attend school and argues that truancy notifications for them should be reimbursed as "a product of the attendance accounting process and promotes compliance of the compulsory education law and *every pupil's* duty to attend school regularly."[27]

In comments on the draft proposed decision, claimant says it no longer disputes the audit findings on notifications for pupils with fewer than three unexcused absences while between the ages of six and 18, or for pupils who accumulated fewer than three total unexcused absences or tardiness occurrences during the school year. Claimant's agreement with these findings, however, "is limited to the extent of the actual number of sampled notices involved, but not as to the extrapolation of these sampled notices."[28] As to the draft proposed decision's findings upholding the Controller's use of statistical extrapolation, the claimant says the findings are "based on factually unrelated case law, broad legislative grants of authority, and unadopted audit standards intended for other purposes."[29]

B. State Controller's Office

The Controller maintains that the audit is correct and that the IRC should be rejected. The Controller first states that the sample size for secondary schools within the claimant's district was 443 for period attendance,[30] so its total sample size for both elementary and secondary schools was larger than the 736 cited by claimant. The Controller also states that both

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[24] Exhibit A, Incorrect Reduction Claim, page 14.

[25] Exhibit A, Incorrect Reduction Claim, page 15.

[26] Exhibit A, Incorrect Reduction Claim, page 16.

[27] Exhibit A, Incorrect Reduction Claim, pages 22-23. Italics in original.

[28] Exhibit E, Claimant's Comments on the Draft Proposed Decision, page 3.

[29] *Ibid.*

[30] Exhibit B, Controller's Late Comments on the Incorrect Reduction Claim, page 12. The 147 period-attendance initial truancy notifications sampled for 2009-2010 was not listed in the audit report, however. See Exhibit A, Incorrect Reduction Claim, page 243.

Government Code sections 17561(d) and 12410 (correctness, legality, and sufficient provisions of law) control the audit, and section 12410 applies to all claims against the state. And the district's reimbursement claims were neither correct nor legal because costs were claimed for non-reimbursable notices issued. The Controller cites GAGAS section 7.55 that states, "When a representative sample is needed, the use of statistical sampling approaches generally results in stronger evidence. . . ." In response to claimant's observation that the *Government Auditing Standards* have not been adopted pursuant to any state agency rulemaking, the Controller states that its "requirements" are applicable to auditors, not claimants, so state agency rulemaking is irrelevant and has no bearing on how mandate-related activities are performed or reimbursement claims are submitted.[31]

The Controller also argues that its sampling and extrapolation methodology is appropriate and cites the *Handbook of Sampling for Auditing and Accounting*[32] to support its sampling of errors versus non-errors. According to the Controller, a tolerance factor advocated by the claimant is not applicable because estimation sampling was used in the audit. As to the claimant's allegation that the sample is not representative of the universe, the Controller cites section 1185.1(f)(3) of the Commission's regulations that requires assertions or representations of fact to be supported by testimonial or documentary evidence, and states that claimant has provided no such evidence. The Controller also states: "The fact that a particular student's initial truancy notification might more likely be identified as non-reimbursable is irrelevant to the composition of the audit sample itself. It has no bearing on evaluating whether the sample selection is representative of the population."[33] The Controller also defends its selection of a sample size as consistent with basic statistical sampling principles, citing the *Handbook* again for support. As the Controller argues: "While a statistical sample evaluation identifies a range for the population's true error rate, the point estimate provides the best, and thus *reasonable,* single estimate of the population's error rate."[34]

The Controller also points out that the test claim statute applies to pupils "subject to compulsory full-time education or to compulsory continuing education" and that Education Code section 48200 defines those pupils as "each person between the ages of 6 and 18 not exempted." The Controller concludes that absences before age six or after age 18 are not relevant to determining whether a pupil is a truant.

On October 30, 2015, the Controller filed comments concurring with the draft proposed decision.[35]

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[31] Exhibit B, Controller's Late Comments on the Incorrect Reduction Claim, page 13.

[32] Exhibit F, Herbert Arkin, *Handbook of Sampling for Auditing and Accounting,* Third Edition, Prentice Hall, New Jersey, 1984 (selected pages).

[33] Exhibit B, Controller's Late Comments on the Incorrect Reduction Claim, page 15.

[34] Exhibit B, Controller's Late Comments on the Incorrect Reduction Claim, page 17.

[35] Exhibit D, Controller's Comments on the Draft Proposed Decision, page 1.

IV. Discussion

Government Code section 17561(b) authorizes the Controller to audit the claims filed by local agencies and school districts and to reduce any claim for reimbursement of state mandated costs that the Controller determines is excessive or unreasonable.

Government Code Section 17551(d) requires the Commission to hear and decide a claim that the Controller has incorrectly reduced payments to the local agency or school district. If the Commission determines that a reimbursement claim has been incorrectly reduced, section 1185.9 of the Commission's regulations requires the Commission to send the statement of decision to the Controller and request that the costs in the claim be reinstated.

The Commission must review questions of law, including interpretation of the parameters and guidelines, de novo, without consideration of legal conclusions made by the Controller in the context of an audit. The Commission is vested with exclusive authority to adjudicate disputes over the existence of state-mandated programs within the meaning of article XIII B, section 6.[36] The Commission must also interpret the Government Code and implementing regulations in accordance with the broader constitutional and statutory scheme. In making its decisions, the Commission must strictly construe article XIII B, section 6 and not apply it as an "equitable remedy to cure the perceived unfairness resulting from political decisions on funding priorities."[37]

With regard to the Controller's audit decisions, the Commission must determine whether they were arbitrary, capricious, or entirely lacking in evidentiary support. This standard is similar to the standard used by the courts when reviewing an alleged abuse of discretion of a state agency.[38] Under this standard, the courts have found that:

> When reviewing the exercise of discretion, "[t]he scope of review is limited, out of deference to the agency's authority and presumed expertise: 'The court may not reweigh the evidence or substitute its judgment for that of the agency. [Citation.]'" ... "In general ... the inquiry is limited to whether the decision was arbitrary, capricious, or entirely lacking in evidentiary support. . . ." [Citations.] When making that inquiry, the " ' "court must ensure that an agency has adequately considered all relevant factors, and has demonstrated a rational connection between those factors, the choice made, and the purposes of the enabling statute." [Citation.]' "[39]

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[36] *Kinlaw v. State of California* (1991) 54 Cal.3d 326, 331-334; Government Code sections 17551, 17552.

[37] *County of Sonoma, supra,* 84 Cal.App.4th 1264, 1281, citing *City of San Jose v. State of California* (1996) 45 Cal.App.4th 1802, 1817.

[38] *Johnston v. Sonoma County Agricultural* (2002) 100 Cal.App.4th 973, 983-984. See also *American Bd. of Cosmetic Surgery, Inc. v. Medical Bd. of California, supra,* 162 Cal.App.4th 534, 547.

[39] *American Bd. of Cosmetic Surgery, Inc. v. Medical Bd. of California* (2008) 162 Cal.App.4th 534, 547-548.

The Commission must review the Controller's audit in light of the fact that the initial burden of providing evidence for a claim of reimbursement lies with the claimant.[40] In addition, sections 1185.1(f)(3) and 1185.2(c) of the Commission's regulations require that any assertions of fact by the parties to an IRC must be supported by documentary evidence. The Commission's ultimate findings of fact must be supported by substantial evidence in the record.[41]

A. The Audit Reductions in Finding 2 for the 79 Notifications Included in the Sample Are Correct as a Matter of Law.

In the audit of the fiscal year 2007-2008, 2008-2009, and 2009-2010 reimbursement claims, the Controller found that the claimant sent 67 initial truancy notices for pupils with fewer than three unexcused absences while between the ages of six and 18, because they were subject to the compulsory education requirements for only a portion of the school year (i.e. they accrued one or more of the requisite absences while under age six or over age 18),[42] and sent truancy notices for 12 pupils who had fewer than three unexcused absences or tardiness occurrences during the school year.[43] The Controller reduced costs claimed for these notices within the audit sample because the notices go beyond the scope of the mandate and are not reimbursable. For the reasons below, the Commission finds that the Controller's reductions are correct as a matter of law.

1. Reimbursement is not required for truancy notices for pupils with fewer than three unexcused absences or tardiness occurrences while between ages six and 18.

The Controller found that the district claimed 67 notifications that it distributed for pupils who had "accumulated fewer than three unexcused absences or tardiness occurrences while between ages 6 and 18" during the school year. The Controller made reductions for these 67 notifications because it found that distributing initial truancy notices for pupils not subject to compulsory education is beyond the scope of the mandate.[44]

In both its response to the audit and in the IRC, claimant maintains that the notification of truancy requirement applies to pupils younger than age six and older than age 18 because school districts are required to enroll pupils who are five years old at the beginning of the school year,

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[40] *Gilbert v. City of Sunnyvale* (2005) 130 Cal.App.4th 1264, 1274-1275.

[41] Government Code section 17559(b), which provides that a claimant or the state may commence a proceeding in accordance with the provisions of section 1094.5 of the Code of Civil Procedure to set aside a decision of the Commission on the ground that the Commission's decision is not supported by substantial evidence in the record.

[42] Exhibit A, Incorrect Reduction Claim, pages 242-243. For daily attendance accounting during the audit period, 50 notifications were sent for truant pupils not between the ages of six and 18. For period attendance accounting during the audit period, 17 notifications were sent for truant pupils not between the ages of six and 18, for a total of 67 notifications under both accounting methods.

[43] Exhibit A, Incorrect Reduction Claim, pages 242-243. All 12 absences were under daily attendance accounting: six in 2007-2008, five in 2008-2009, and one in 2009-2010.

[44] *Ibid.*

as well as special education pupils through age 21.[45] Specifically, claimant argues that although Education Code sections 48200 and 48400 establish the legal attendance requirements for pupils aged six through 18, there is an entitlement to attend kindergarten pursuant to section 48000, and to attend first grade pursuant to sections 48010 and 48011. Attendance cannot be denied by a school district. And special education pupils are statutorily entitled to education services from ages 3 to 22 pursuant to section 56026.[46] Section 46000 requires the district to keep attendance and record absences for all pupils for purposes of apportionment and compliance with the compulsory education law, subject to regulations by the State Board of Education. Claimant states: "the initial notification of truancy is a product of the attendance accounting process and promotes compliance of the compulsory education law and *every pupil's* duty to attend school regularly."[47] In comments on the draft proposed decision, the claimant states that it no longer disputes this issue.[48]

The Commission finds that providing initial truancy notices for pupils who accumulated fewer than three unexcused absences or tardiness occurrences while between ages six and 18, who by definition were not subject to the compulsory education law when they accrued one or more of the requisite absences or tardiness occurrences, is beyond the scope of the mandate and is not eligible for reimbursement.

The claimant is correct that at the time these reimbursement claims were filed, school districts were required by state law to admit a child to kindergarten if his or her fifth birthday were on or before December 2 of that school year.[49] School districts are also required by state and federal law to provide special education services to "individuals with exceptional needs" until the age of 21 if required by a pupil's individualized education plan.[50] And schools are required by state law to record the attendance of every pupil enrolled in school for apportionment of state funds and "to ensure the *general* compliance with the compulsory education law, and performance by a pupil of his duty to attend school regularly as provided in [California Code of Regulations, title 5] section 300."[51]

However, the truancy laws apply only to pupils who are subject to compulsory full-time education. Education Code section 48260(a) defines a truant as:

> A pupil *subject to compulsory full-time education or to compulsory continuation education* [emphasis added] who is absent from school without a valid excuse

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[45] Exhibit A, Incorrect Reduction Claim, page 251.

[46] Exhibit A, Incorrect Reduction Claim, pages 18-20. Education Code section 56040 requires special education for pupils defined according to section 56026.

[47] Exhibit A, Incorrect Reduction Claim, pages 22-23. Emphasis in original. Claimant cites California Code of Regulations, title 5, section 300.

[48] Exhibit E, Claimant's Comments on the Draft Proposed Decision, page 2.

[49] Education Code section 48000(a), as last amended by Statutes 1991, chapter 381.

[50] Title 20, United States Code, section 1401; Education Code section 56026.

[51] Education Code section 46000; California Code of Regulations, title 5, section 400. Section 300 of the regulations state in relevant part that "every pupil shall attend school punctually and regularly."

> three full days in one school year or tardy or absent for more than a 30-minute period during the schoolday [*sic*] without a valid excuse on three occasions in one school year, or any combination thereof, shall be classified as a truant … .

Education Code section 48200 states: "Each person *between the ages of 6 and 18 years* [emphasis added] not exempted ... is subject to compulsory full-time education."

Education Code section 48260(b) further states that "[n]otwithstanding subdivision (a) [which defines a truant as a pupil subject to compulsory full-time education], it is the intent of the Legislature that school districts shall not change the method of attendance accounting provided for in existing law." Therefore, even though schools are required by state law to report the attendance of all enrolled pupils, the truancy laws, including the notice of initial truancy required by this mandated program, apply only to pupils between the ages of six and 18.

Accordingly, the Controller's reduction of costs claimed for 67 truancy notices within the audit sample for pupils who accumulated fewer than three unexcused absences or tardiness occurrences while between ages six and 18, is correct as a matter of law.

2. Reimbursement is not required for truancy notices for pupils with fewer than three unexcused absences or tardiness occurrences.

Education Code Section 48260[52] defines a truant as a pupil who is absent from or tardy to school without valid excuse "on three occasions in one school year." The Commission amended the parameters and guidelines effective for costs incurred beginning July 1, 2006, to reflect that the mandate to provide a truancy notification is triggered by a pupil who is absent from or tardy to school without valid excuse on three occasions in one school year and these parameters and guidelines apply to this IRC.[53] If a pupil cannot be initially classified as a truant, as defined in section 48260, a notification is not required, and any notification sent to that pupil's parent or guardian is not reimbursable.

The Controller found that, during the audit period, 12 of the sampled notifications were distributed for pupils who accumulated fewer than three unexcused absences or tardiness occurrences during the school year.[54] The claimant has not rebutted these findings, and does not address the 12 notifications in the IRC. In comments on the draft proposed decision, the claimant states that it no longer disputes this issue.[55]

The claimant's request for reimbursement to provide truancy notices for pupils with fewer than three unexcused absences or tardiness occurrences goes beyond the scope of the mandate and is not reimbursable.

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[52] As amended by Statutes 1994, chapter 1023 (SB 1728) and Statutes 1995, chapter 19 (SB 102).

[53] Exhibit A, Incorrect Reduction Claim, pages 31-35.

[54] Exhibit A, Incorrect Reduction Claim, page 242. Exhibit B, Controller's Late Comments on the Incorrect Reduction Claim, page 18. All 12 absences were under daily attendance accounting: six in 2007-2008, five in 2008-2009, and one in 2009-2010.

[55] Exhibit E, Claimant's Comments on the Draft Proposed Decision, page 3.

Accordingly, the Controller's reduction of costs claimed for the 12 truancy notifications provided for pupils with fewer than three unexcused absences or tardiness occurrences is correct as a matter of law.

B. The Audit Reductions in Finding 2 Based on Statistical Sampling and Extrapolation of Findings to All Notices Claimed Are Not Arbitrary, Capricious, or Entirely Lacking in Evidentiary Support.

In its audit, the Controller examined a random sample of initial truancy notices distributed by the claimant for each year to determine the proportion of notifications that were unallowable for the Controller's asserted legal reasons. The sample for all fiscal years totaled 883 notifications distributed by elementary and secondary schools, out of a total of 45,091 claimed for the audit period. The Controller selected its sample "based on a 95% confidence level, a precision rate of ± 8%, and an expected error rate of 50%."[56] The number of unallowable notifications within the sample for each fiscal year was then calculated as an annual error percentage, and extrapolated to the total number of notifications issued by the claimant in each fiscal year to approximate the total number of unallowable notifications for elementary and secondary schools. The number of unallowable notices was then multiplied by the unit cost for each fiscal year to calculate the total reduction for the audit period at $68,410.[57]

Since the Controller has not reviewed all 45,091 initial truancy notifications and their associated records during these fiscal years, the Controller's methodology is an estimate based on statistical probabilities of the amount of costs claimed beyond the scope of the mandate and that the Controller has determined to be excessive or unreasonable. The Controller states that the estimated reduction of costs has an "adjustment range" with a 95 percent confidence level for all three fiscal years between $37,420 and $99,396, and the total reduction ($68,410) for all three years falls within that range and best represents the point estimate from each audit sample's results.[58]

Claimant argues that statistical sampling is misapplied in this IRC and that the audit findings should be limited to the notifications sampled. Claimant continues that the sampling process was misapplied in this IRC because the audit actually conducted a review for documentation rather than mandate compliance. According to the claimant, "testing to detect the rate of error within tolerances is the purpose of sampling, but it is not a tool to assign an exact dollar amount to the amount of the error which the Controller has inappropriately done . . . here."[59]

Claimant also states that the sample may not be representative of the universe because, for example, kindergarten students in the sample are more likely to be excluded because of the under-age issue, and the possibility of a special education student being under age or over age is greater than the entire student body.[60]

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[56] Exhibit A, Incorrect Reduction Claim, page 241.

[57] Exhibit A, Incorrect Reduction Claim, final audit report, pages 242-243.

[58] Exhibit B, Controller's Late Comments on the Incorrect Reduction Claim, pages 17 and 29-30.

[59] Exhibit A, Incorrect Reduction Claim, page 14.

[60] Exhibit A, Incorrect Reduction Claim, page 15.

And, according to claimant, the sampling technique used in the audit is non-representative because the sample size for the audit period (736 truancy notifications sampled; 440 notifications sampled for daily attendance (elementary schools) and 296 notifications for period attendance (secondary schools) is 1.93 percent of the universe. As the claimant states: "The expected error rate is stated to be 50%, which means the total amount adjusted of $68,410 is really just a number exactly between $34,205 (50%) and $102,615 (150%). An interval of possible outcomes cannot be used as a finding of absolute actual cost."[61]

The Controller explains, in response, that the district incorrectly identifies the population sample size for secondary schools as 296 truancy notifications, thus incorrectly identifying the total sample size at 736 truancy notifications for elementary and secondary schools. The correct number of period attendance truancy notifications sampled by the Controller for secondary schools was 443, rather than 296 as alleged by the claimant, bringing the total notifications sampled to 883.[62] The Controller explains that:

> The district did not identify the FY 2009-10 "Secondary Schools" statistical sample, i.e. period attendance population. We selected, and tested, 147 period attendance initial truancy notifications in FY 2009-10. Our audit found no instances of non-compliance from the FY 2009-10 period attendance testing."[63]

The Controller also states as follows:

> Based on the sampling parameters identified in the report and the individual sample results, our analysis shows that the audit adjustment range is $37,420 to $99,396 **(Tab 4)**. While a statistical sample evaluation identifies a range for the population's true error rate, the point estimate provides the best, and thus *reasonable,* single estimate of the population's error rate. The audit report identifies a $68,410 audit adjustment, which is a cumulative total of the unallowable costs based on point estimates from each audit sample's results.[64]

The Controller further counters that sampling and extrapolation is an audit tool authorized by general accepted government auditing standards and statutes authorizing audits of claims.[65] The Controller also argues that claimant misstates and misunderstands the meaning of an expected error rate and confidence interval. The Controller argues that its method is reasonable, and "the Administrative Procedures [*sic*] Act is not applicable."[66]

Based on the analysis herein, the Commission finds that the evidence in the record does not support the claimant's assertion that the Controller's use of sampling and extrapolation

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[61] Exhibit A, Incorrect Reduction Claim, page 16.

[62] Exhibit B, Controller's Late Comments on the Incorrect Reduction Claim, page 12.

[63] Exhibit B, Controller's Late Comments on the Incorrect Reduction Claim, pages 12 and 16.

[64] Exhibit B, Controller's Late Comments on the Incorrect Reduction Claim, pages 17, 29-30.

[65] Exhibit A, Incorrect Reduction Claim, page 245 (final audit report). Exhibit B, Controller's Late Comments on the Incorrect Reduction Claim, pages 11-12. The Controller cites Government Code sections 17561(d)(2) and 12410.

[66] Exhibit B, Controller's Late Comments on the Incorrect Reduction Claim, pages 12-17.

constitutes an illegal underground regulation, or that the Controller's findings are arbitrary, capricious, or entirely lacking in evidentiary support.

1. The evidence in the record does not support claimant's argument that the statistical sampling and extrapolation method used in the audit constitutes an underground regulation.

The claimant challenges the statistical sampling and extrapolation methodology used by the Controller as an underground regulation not adopted pursuant to the APA, and argues that any findings and reductions extrapolated from the sample reviewed by the Controller should therefore be void.[67]

Section 11340.5 of the APA states in pertinent part:

> No state agency shall issue, utilize, enforce, or attempt to enforce any guideline, criterion, bulletin, manual, instruction, order, standard of general application, or other rule, which is a regulation as defined in Section 11342.600, unless [the rule] has been adopted as a regulation and filed with the Secretary of State pursuant to this chapter.[68]

Section 11342.600 of the APA defines a regulation to mean "…every rule, regulation, order, or standard of general application or the amendment, supplement, or revision of any rule, regulation, order, or standard adopted by any state agency to implement, interpret, or make specific the law enforced or administered by it, or to govern its procedure."[69] And Government Code section 11346 provides that "[e]xcept as provided in Section 11346.1, the provisions of this chapter are applicable to the exercise of any quasi-legislative power conferred by any statute heretofore or hereafter enacted, but nothing in this chapter repeals or diminishes additional requirements imposed by any statute." Section 11346 continues: "This chapter shall not be superseded or modified by any subsequent legislation except to the extent that the legislation shall do so expressly."[70] Therefore, if the Controller's challenged audit methods constitute a regulation not adopted pursuant to the APA, the Commission cannot uphold the reductions.

The seminal authority on so-called "underground regulations" is the California Supreme Court's opinion in *Tidewater Marine Western v. Bradshaw*,[71] in which a group of shipping companies and associations challenged the application of the Industrial Welfare Commission's (IWC's) wage orders to their businesses and employees as an invalid underground regulation, not adopted under the APA.

Tidewater Marine Western, Inc. (Tidewater) and Zapata Gulf Pacific, Inc. (Zapata) were two of the petitioners whose principal business was transporting workers and supplies between oil-drilling platforms in the Santa Barbara Channel and coastal ports. The employees at the center of the dispute were California residents, working 12 hour shifts with intermittent break or rest

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[67] Exhibit A, Incorrect Reduction Claim, page 13-14.

[68] Government Code section 11340.5 (Stats. 2000, ch. 1060).

[69] Government Code section 11342.600 (Stats. 2000, ch. 1060).

[70] Government Code section 11346 (Stats. 1994, ch. 1039; Stats. 2000, ch. 1060).

[71] *Tidewater Marine Western v. Bradshaw* (1996) 14 Cal.4th 557.

periods, at a flat daily rate without overtime pay, which the employers explained was reasonable because: "the demands of work are inconstant, and crew members may spend part of this duty period engaged in leisure activities."[72] The IWC had existing wage orders for transportation employees and for technical and mechanical employees, which required an overtime pay rate when an employee worked more than eight hours in any twenty-four hour period. Beginning in 1978, maritime employees had begun filing claims under these wage orders with the Division of Labor Standards Enforcement (DLSE), which examined those claims on a case-by-case basis, "considering such factors as the type of vessel, the nature of its activities, how far it traveled from the California coast, how long it was at sea, and whether it left from and returned to the same port…"[73] After an unstated number of these claims, "DLSE eventually replaced this case-by-case adjudication with a written enforcement policy, which provides: 'IWC standards apply to crews of fishing boats, cruise boats, and similar vessels operating exclusively between California ports, or returning to the same port, if the employees in question entered into employment contracts in California and are residents of California.'"[74] Initially, this written policy was contained in a "draft policy manual" that DLSE created to guide its deputy labor commissioners, but in 1989, DLSE formalized the policy in its "Operations and Procedures Manual," which was available to the public upon request. The manual, prepared internally and without public input, "reflected 'an effort to organize…interpretive and enforcement policies' of the agency and 'achieve some measure of uniformity from one office to the next.'"[75]

In 1987, the DLSE began applying the IWC's wage order requiring overtime pay to the maritime workers in the Santa Barbara Channel, including those of Tidewater and Zapata, which were among the entities that brought suit to challenge the application of the order on several grounds, including the theory that application of the order constituted an underground regulation.

The Court noted that while "DLSE's primary function is enforcement, not rulemaking," DLSE does have power to promulgate "regulations and rules of practice and procedure."[76] The Court further noted that the Labor Code does not include special rulemaking procedures for DLSE, "nor does it expressly exempt the DLSE from the APA."[77] The Court analyzed the underground regulation challenge raised by Tidewater, beginning with the requirements and underlying purpose of the APA, as follows:

> The APA establishes the procedures by which state agencies may adopt regulations. The agency must give the public notice of its proposed regulatory action (Gov. Code, §§ 11346.4, 11346.5); issue a complete text of the proposed regulation with a statement of the reasons for it (Gov. Code, § 11346.2, subds. (a), (b)); give interested parties an opportunity to comment on the proposed regulation (Gov. Code, § 11346.8); respond in writing to public comments (Gov. Code, §§

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[72] *Tidewater*, *supra*, 14 Cal.4th 557, 561.

[73] *Id.*, page 562.

[74] *Ibid*.

[75] *Ibid*.

[76] *Tidewater*, *supra*, 14 Cal.4th 557, 570.

[77] *Ibid*. [Citing Labor Code § 98.8].

> 11346.8, subd. (a), 11346.9); and forward a file of all materials on which the agency relied in the regulatory process to the Office of Administrative Law (Gov. Code, § 11347.3, subd. (b)), which reviews the regulation for consistency with the law, clarity, and necessity (Gov. Code, §§ 11349.1, 11349.3).
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> One purpose of the APA is to ensure that those persons or entities whom a regulation will affect have a voice in its creation *(Armistead v. State Personnel Board* (1978) 22 Cal.3d 198, 204-205 (Armistead)), as well as notice of the law's requirements so that they can conform their conduct accordingly (*Ligon v. State Personnel Bd.* (1981) 123 Cal.App.3d 583, 588 (Ligon)). The Legislature wisely perceived that the party subject to regulation is often in the best position, and has the greatest incentive, to inform the agency about possible unintended consequences of a proposed regulation. Moreover, public participation in the regulatory process directs the attention of agency policymakers to the public they serve, thus providing some security against bureaucratic tyranny. (See *San Diego Nursery Co. v. Agricultural Labor Relations Bd.* (1979) 100 Cal.App.3d 128, 142-143.)[78]

The Court in *Tidewater Marine Western* found that the APA "defines 'regulation' very broadly" and explained that a regulation has two principal characteristics:

> First, the agency must intend its rule to apply generally, rather than in a specific case. The rule need not, however, apply universally; a rule applies generally so long as it declares how a *certain class of cases* will be decided. Second, the rule must "implement, interpret, or make specific the law enforced or administered by [the agency], or ... govern [the agency's] procedure."[79]

The Court acknowledged that "interpretations that arise in the course of case-specific adjudication are not regulations, though they may be persuasive as precedents in similar subsequent cases;"[80] and, "[s]imilarly, agencies may provide private parties with advice letters, which are not subject to the rulemaking provisions of the APA."[81] And, the Court reasoned that "if an agency prepares a policy manual that is no more than a restatement or summary, without commentary, of the agency's prior decisions in specific cases and its prior advice letters, the agency is not adopting regulations."[82]

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[78] *Tidewater*, *supra,* 14 Cal.4th 557, 568-569.

[79] *Tidewater, supra,* 14 Cal.4th 557, 571 (emphasis added) [Citing *Roth v. Department of Veteran Affairs* (1980) 110 Cal.App.3d 622, 630; Gov. Code § 11342(g)].

[80] *Ibid*. [Citing *Bendix Forest Products Corp. v. Division of Occupational Safety and Health* (1979) 25 Cal.3d 465, 471; *Carmona v. Division of Industrial Safety* (1975) 13 Cal.3d 303, 309-310; *Taye v. Coye* (1994) 29 Cal.App.4th 1339, 1345; *Aguilar v. Association for Retarded Citizens* (1991) 234 Cal.App.3d 21, 28].

[81] *Tidewater, supra,* 14 Cal.4th 571 [citing Government Code sections 11343; 11346.1].

[82] *Ibid*. [citing Labor Code section 1198.4].

The Court cited a number of examples in which a policy or rule was or was not held to be a regulation,[83] but applying the above reasoning, the Court concluded that the application of the challenged wage orders to the plaintiffs was indeed an invalid underground regulation:

> The policy at issue in this case was expressly intended as a rule of general application to guide deputy labor commissioners on the applicability of IWC wage orders to a particular type of employment. In addition, the policy interprets the law that the DLSE enforces by determining the scope of the IWC wage orders. Finally, the record does not establish that the policy was, either in form or substance, merely a restatement or summary of how the DLSE had applied the IWC wage orders in the past. Accordingly, the DLSE's enforcement policy appears to be a regulation within the meaning of Government Code section 11342, subdivision (g), and therefore void because the DLSE failed to follow APA procedures.[84]

The Court went on to distinguish or disapprove prior cases finding that a challenged policy or position of the DLSE was not an underground regulation,[85] and pointed out that if the current interpretation were the only reasonable interpretation, as argued by DLSE, it would not be necessary to state in a policy manual in order to achieve uniformity in enforcement, which DLSE claimed to be part of its initial motivation for articulating the policy.[86]

In addition to the Court's thorough examination in *Tidewater* of the APA and case law pertaining to underground regulations generally, and specifically in the labor standards enforcement

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[83] *Tidewater*, *supra*, 14 Cal.4th 557, 571-572 ["Examples of policies that courts have held to be regulations subject to the rulemaking procedures of the APA include: (1) an informational "bulletin" defining terms of art and establishing a rebuttable presumption (*Union of American Physicians & Dentists v. Kizer*, [(*UAPD*) (1990)] 223 Cal.App.3d [490,] 501); (2) a "policy of choosing the most closely related classification" for determining prevailing wages for unclassified workers (*Division of Lab. Stds. Enforcement v. Ericsson Information Systems, Inc.* (1990) 221 Cal.App.3d 114, 128); and (3) a policy memorandum declaring that work performed outside one's job classification does not count toward qualifying for a promotion (*Ligon, supra,* 123 Cal.App. [583,] 588). In contrast, examples of policies that courts have held not to be regulations include: (1) a Department of Justice checklist that officers use when administering an intoxilyzer test (*People v. French* (1978) 77 Cal.App.3d 511, 519); (2) the determination whether in a particular case an employer must pay employees whom it requires to be on its premises and on call, but whom it permits to sleep (Aguilar, [*v. Association for Retarded Citizens* (1991)] 234 Cal.App.3d [21,] 25-28); (3) a contractual pooling procedure whereby construction tax revenues are allocated among a county and its cities in the same ratio as sales tax revenues (*City of San Joaquin v. State Bd. of Equalization* (1970) 9 Cal.App.3d 365, 375); and (4) resolutions approving construction of the Richmond-San Rafael Bridge and authorizing issuance of bonds (*Faulkner v. Cal. Toll Bridge Authority* (1953) 40 Cal.2d 317, 323-324."] (Italics supplied).

[84] *Tidewater*, *supra*, 14 Cal.4th 557, 572.

[85] *Skyline Homes, Inc. v. Department of Industrial Relations* (1985) 165 Cal.App.3d 239, 253; *Bono Enterprises, Inc. v. Bradshaw* (1995) 32 Cal.App.4th 968, 978.

[86] *Tidewater*, *supra*, 14 Cal.4th 557, 562.

context, four court of appeal decisions have addressed underground regulation challenges to an auditing methodology: *Grier v. Kizer*[87] (*Grier*); *Union of American Physicians and Dentists v. Kizer*[88] (*UAPD*); *Taye v. Coye*[89](*Taye*) and *Clovis Unified School Dist. v. Chiang* (*Clovis*).

In *Grier* and *UAPD* "the Department conducted audits of Medi-Cal providers by taking a small random sample [to determine the frequency and extent of over- or under-claiming for services provided], then extrapolating that error rate over the total amount received by the provider during the period covered by the audit."[90] The courts found the sampling and extrapolation methodology in that case invalid, solely because of the failure of the Department of Health Services to adopt its methodology in accordance with the APA. The court in *Grier*, *supra*, concurred with the OAL's determination, made in a parallel administrative proceeding, that the challenged method constituted a regulation, and should have been duly adopted. The court observed that "the definition of a regulation is broad, as contrasted with the scope of the internal management exception, which is narrow."[91] And, the court rejected the Department's argument that sampling and extrapolation was the only legally tenable interpretation of its audit authority: "While sampling and extrapolation may be more feasible or cost-effective,...[a] line by line audit is an alternative tenable interpretation of the statutes."[92] The court also noted that the Department "acquiesced" in that determination and in the time between the trial court's determination and the hearing on appeal, it adopted a regulation providing expressly for statistical sampling and extrapolation in the conduct of Medi-Cal audits.[93] Accordingly, the court in *UAPD* assumed, without deciding, that having satisfied the APA, the statistical methodology could be validly applied to pending audits, or remanded audits.[94] Now, with respect to Medi-Cal audits, a statistical sampling methodology is provided for in *both* the Welfare and Institutions Code and in the Department's implementing regulations.[95]

In *Taye*, another health care provider seeking reimbursement under Medi-Cal for services and products supplied to patients was audited, this time by the State Controller's Office.[96] Taye argued that the method of conducting the audit, and in particular the decision to exclude "opening inventory" when calculating the difference between the amount of product purchased

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[87] *Grier v. Kizer* (*Grier*) (1990) 219 Cal.App.3d 422.

[88] *Union of American Physicians and Dentists v. Kizer* (*UAPD*) (1990) 223 Cal.App.3d 490.

[89] *Taye v. Coye* (*Taye*) (1994) 29 Cal.App.4th 1339.

[90] *UAPD*, *supra*, 223 Cal.App.3d 490, 495.

[91] *Grier*, *supra*, 219 Cal.App.3d 422, 435.

[92] *Id.*, pages 438-439.

[93] *Id.*, pages 438-439.

[94] *UAPD*, *supra*, 223 Cal.App.3d 504-505 [finding that the statistical audit methodology did not have retroactive effect because it did not alter the legal significance of past events (i.e., the amount of compensation to which a Medi-Cal provider was entitled)].

[95] See, e.g., Welfare and Institutions Code section 14170(b) (added, Stats. 1992, ch. 722 (SB 485); Code of Regulations, title 22, section 51458.2 (Register 1988, No. 17).

[96] *Taye*, *supra*, 29 Cal.App.4th 1339, 1342.

by Taye during the audit period and the amount of product he billed for during the same period, constituted a "regulation" within the meaning of the APA, and as such could not be applied or enforced until duly adopted as a regulation and filed with the Secretary of State.[97] The court distinguished *Grier* as follows:

> In *Grier*, cited here by Taye, the court found that a challenged method of conducting an audit by extrapolating from a small, select, sample of claims submitted was in fact a regulation. The court concurred in the reasoning of the Office of Administrative Law, determining that the method was a regulation *because it was a standard of general application applied in every Medi-Cal case reviewed by the Department audit teams* and used to determine the amount of the overpayment. [Citation] The auditing method used by LaPlaunt here, in contrast, was not a standard of general application used in all Medi-Cal cases. Thus, LaPlaunt declared: "The audit procedures used to conduct the audit of Pride Home Care Medical were designed to fit the particular conditions that were encountered upon the arrival at the audit site. [¶] ... While all audits are performed along generally accepted audit principles, these principles are not intended to be steadfast rules from which deviation is prohibited. In the twelve years that I have been employed as an auditor for the California State Controller's Office, I have been involved in numerous audits varying in subject and complexity. In these endeavors, I have found that the flexibility to adopt auditing principles to unique situations, including treatment of inventory, is imperative in the successful completion of an audit." It follows that the method was not a "regulation," and no error attended its employment.[98]

This analysis and conclusion was cited approvingly in *Tidewater*, *supra*, as one of several examples of "interpretations that arise in the course of case-specific adjudication" and not subject to the regulatory process.[99]

And finally, in *Clovis Unified*, the court held that the Controller's contemporaneous source document rule (CSDR), which was contained solely in the Controller's claiming instructions and not adopted in the regulatory parameters and guidelines, was applied *generally* to audits of all reimbursement claims for certain programs, in that individual auditors had no discretion to judge on a case-by-case basis whether to apply the rule.[100] As to the second criterion, the court found that the CSDR was more specific, and in some ways inconsistent with the parameters and guidelines for the subject mandated programs. Specifically, the court found that the CSDR defined "source documents" differently and more specifically than the parameters and guidelines, including relegating employee declarations to "corroborating documents, not source documents…", and failing to recognize the appropriate use of a time study.[101] The court therefore held, "[g]iven these substantive differences…we conclude that the CSDR implemented,

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[97] *Id.*, page 1344.

[98] *Id.*, page 1345 [emphasis added].

[99] *Tidewater*, *supra*, 14 Cal.4th 557, 571.

[100] *Clovis Unified School District v. Chiang* (2010) 188 Cal.App.4th 794, 803.

[101] *Id.*, pages 803-805.

interpreted, or made specific…" the parameters and guidelines and the Controller's audit authority and was, therefore, an underground regulation.[102]

The necessary inquiry, then, is whether the challenged audit policy or practice is applied "generally," and used to decide a class of cases; and whether the rule "implement[s], interpret[s], or make[s] specific" the law administered by the Controller. Here, that is a close question that turns on the issue of general applicability: if it is the Controller's policy that *all audits* of the *Notification of Truancy* program be conducted using the statistical sampling and extrapolation methods that claimant challenges, then that may meet the standard of a rule applied "generally, rather than in a specific case."[103] On the other hand, if statistical sampling and extrapolation is only one of an auditor's tools, and may or may not be the most practical method for auditing claims involving a unit cost and many thousands of units claimed, it is within the discretion of each auditor to use the challenged methods and the APA does not bar the exercise of that discretion.[104]

In *Clovis Unified School District v. Chiang*, the court held that the Controller's contemporaneous source document rule (CSDR), which was contained solely in the Controller's claiming instructions and not adopted in the regulatory parameters and guidelines, was applied *generally* to audits of all reimbursement claims for certain programs, in that individual auditors had no discretion to judge on a case-by-case basis whether to apply the rule.[105] As to the second criterion, the court found that the CSDR was more specific, and in some ways inconsistent with the parameters and guidelines for the subject mandated programs. Specifically, the court found that the CSDR defined "source documents" differently and more specifically than the parameters and guidelines, including relegating employee declarations to "corroborating documents, not source documents…", and failing to recognize the appropriate use of a time study.[106] The court therefore held, "[g]iven these substantive differences…we conclude that the CSDR implemented, interpreted, or made specific…" the parameters and guidelines and the Controller's statutory audit authority and was, therefore, an underground regulation.[107]

In the Medi-Cal audit context, the courts held the Department of Health Services' statistical sampling and extrapolation methods used to determine the amount of over- or under-payment in reimbursement to health care providers to be an underground regulation, absent compliance with the APA. In *Grier v. Kizer*[108] and *Union of American Physicians and Dentists v. Kizer*,[109]

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[102] *Id.*, page 805.

[103] *Tidewater Marine Western v. Bradshaw* (1996) 14 Cal.4th 557, 571.

[104] See *Taye*, *supra*, 29 Cal.App.4th 1339, 1345. The court found that an auditor's decision was not an underground regulation where it was "designed to fit the particular conditions that were encountered upon arrival at the audit site."

[105] *Clovis Unified School District v. Chiang* (2010) 188 Cal.App.4th 794, 803.

[106] *Id.*, pages 803-805.

[107] *Id.*, page 805.

[108] *Grier v. Kizer* (1990) 219 Cal.App.3d 422 overturned on other grounds in *Tidewater Marine Western v. Bradshaw, supra*, 14 Cal.4th 557.

[109] *Union of American Physicians and Dentists v. Kizer* (1990) 223 Cal.App.3d 490.

(*UAPD*) "the Department conducted audits of Medi-Cal providers by taking a small random sample [to determine the frequency and extent of over- or under-claiming for services provided], then extrapolating that error rate over the total amount received by the provider during the period covered by the audit."[110] The courts found the sampling and extrapolation methodology in that case invalid, solely because of the failure of the Department of Health Services to adopt its methodology in accordance with the APA. The court in *Grier* concurred with an Office of Administrative Law (OAL) determination, made in a parallel administrative proceeding, that the challenged method constituted a regulation, and should have been duly adopted. The court observed that "the definition of a regulation is broad, as contrasted with the scope of the internal management exception, which is narrow."[111] The court rejected the Department's argument that sampling and extrapolation was the only legally tenable interpretation of its audit authority: "While sampling and extrapolation may be more feasible or cost-effective,...[a] line by line audit is an alternative tenable interpretation of the statutes."[112] The court also noted that the Department "acquiesced" in that determination and soon after it adopted a regulation providing expressly for statistical sampling and extrapolation in the conduct of Medi-Cal audits.[113] Accordingly, the court in *Union of American Physicians and Dentists* assumed, without deciding, that having satisfied the APA, the statistical methodology could be validly applied to pending audits, or remanded audits.[114] With respect to Medi-Cal audits, a statistical sampling methodology is provided for in *both* the Welfare and Institutions Code and in the Department's implementing regulations.[115]

In light of the *Clovis Unified*, *Grier* and *UAPD* cases, it is clear that an audit practice may be reasonable and otherwise permissible, yet still impose an illegal underground regulation. However, the Commission does not have substantial evidence in the record that the audit methodology complained of rises to the level of a rule of general application, and no clear "class of cases" to which it applies has been defined. In *Tidewater*, the Court held that a "rule need not, however, apply universally; a rule applies generally so long as it declares how a certain class of cases will be decided."[116] And in the *Clovis Unified* case, the court explained that in the context of the Controller's audits of mandate reimbursement claims:

> As to the first criterion—whether the rule is intended to apply generally—substantial evidence supports the trial court's finding that the CSDR was

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[110] *Id.*, page 495.

[111] *Id.*, page 435.

[112] *Id.*, pages 438-439.

[113] *Ibid.*

[114] *Union of American Physicians and Dentists, supra*, 223 Cal.App.3d 490, 504-505 [finding that the statistical audit methodology did not have retroactive effect because it did not alter the legal significance of past events (i.e., the amount of compensation to which a Medi-Cal provider was entitled)].

[115] See, e.g., Welfare and Institutions Code section 14170(b) (added by Stats. 1992, ch. 722 (SB 485); California Code of Regulations, title 22, section 51458.2 (Register 1988, No. 17).

[116] *Tidewater Marine Western v. Bradshaw, supra*, 14 Cal.4th 557, 571.

> "applie[d] generally to the auditing of reimbursement claims ...; the Controller's auditors ha[d] no discretion to judge on a case[-]by[-]case basis whether to apply the rule."[117]

Therefore, a "class of cases" must be identifiable. In *Grier*, as noted above, the court concurred with OAL's determination that "this particular audit method was a standard of general application 'applied in *every Medi-Cal case* reviewed by [Department] audit teams…'"[118] Here, of the 44 completed audits of the Notification of Truancy mandate, some do not apply a statistical sampling and extrapolation methodology to calculate a reduction;[119] others apply a sampling and extrapolation method to determine whether the notifications issued complied with the eight required elements under section 48260.5;[120] and still others use sampling and extrapolation methods to determine the proportion of notifications issued that were supported by documentation, including attendance records, rather than the proportion unallowable based on absences, as here.[121] The claimant has argued that these examples are not factually relevant, and that "[i]t is not that every audit must be a Tidewater 'case' to support the concept of generality…but more logically it is that if the *factual circumstances* are present that are amenable to the use of sampling and whether sampling was used, rather than another audit method…"[122] The Commission disagrees. In *Taye*, the court gave substantial weight to the declaration of the auditor, LaPlaunt, who explained:

> While all audits are performed along generally accepted audit principles, these principles are not intended to be steadfast rules from which deviation is prohibited. In the twelve years that I have been employed as an auditor for the California State Controller's Office, I have been involved in numerous audits varying in subject and complexity. In these endeavors, I have found that the flexibility to adopt auditing principles to unique situations, including treatment of inventory, is imperative in the successful completion of an audit.[123]

Here, the parameters and guidelines do not specify the methodology the Controller must use to validate program compliance. And, the Controller cites "Government Auditing Standards, as issued by the Comptroller General of the United States," which, the Controller asserts, "specify

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[117] *Clovis, supra*, 188 Cal.App.4th 794, 803.

[118] *Grier, supra*, 29 Cal.App.4th 2, 434-435.

[119] See, e.g., Exhibit F, Audit of Sweetwater Union High School District, *Notification of Truancy*, fiscal years 2006-2007 through 2009-2010 [In this audit report the Controller reduced based on the claimant's failure to comply with the notification requirements of section 48260.5, rather than performing a sampling and estimation audit to determine whether notifications were issued in compliance with section 48260.].

[120] See, e.g., Exhibit F, Audit of Colton Joint Unified School District, *Notification of Truancy*, fiscal years 1999-2000 through 2001-2002, issued November 26, 2003.

[121] See, e.g., Exhibit F, Audit of Bakersfield City School District, *Notification of Truancy*, fiscal years 2007-2008 through 2009-2010, issued October 25, 2012.

[122] Exhibit E, Claimant's Comments on Draft Proposed Decision, page 4. Emphasis in original.

[123] *Taye*, *supra*, 29 Cal.App.4th 1345.

that auditors may use professional judgment in 'selecting the methodology, determining the type and amount of evidence to be gathered, and choosing the tests and procedures for their work.'"[124]

Moreover, the sampling and extrapolation method is not published in the claiming instructions for this mandate, as was the case in *Clovis Unified*; to the extent the sampling and extrapolation methodology implements, interprets, or makes specific the law enforced or administered by the Controller, a published policy might well be dispositive of the issue. In *Tidewater*, *supra*, the DLSE policy at issue was formalized in its "Operations and Procedures Manual," and was "expressly intended as a rule of general application to guide deputy labor commissioners on the applicability of IWC wage orders to a particular type of employment." There is no evidence in this record of any formalized policy, or any intent to require all field auditors to perform their audits in a particular manner.

Therefore, because the evidence in the record does not reflect the formalization in written policy or guidance for field auditors of the challenged sampling and extrapolation methodology; and because there is no evidence that auditors were deprived of discretion whether to use the challenged methodology, the record does not support a finding by the Commission that the sampling and extrapolation methodology constitutes a regulation generally applied to a class of cases. Moreover, the Commission takes official notice, as discussed above, that sampling and extrapolation has not been used in every audit of the *Notification of Truancy* program, and where it has been used, it has been applied in a number of different ways, to justify a number of different reductions.[125] Therefore, in light of the applicable case law and the evidence in the record, the Commission finds that the Controller's sampling and extrapolation method, as applied in this case, is not an underground regulation within the meaning of the APA.

2. <u>The Controller's audit findings must be upheld absent evidence that the reductions are arbitrary, capricious, or entirely lacking in evidentiary support.</u>

The claimant argues that there is no statutory or regulatory authority for the Controller to reduce claimed costs based on extrapolation from a statistical sample.[126] The Controller counters that the law does not prohibit the audit methods used. The Controller relies on Government Code section 12410, which requires the Controller to audit all claims against the state and "may audit the disbursement of any state money, for correctness, legality, and for sufficient provisions of law for payment."[127] The Controller also relies on Government Code section 17561, which permits the Controller to reduce any claim that is determined to be excessive or unreasonable:

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[124] Exhibit B, Controller's Late Comments on the Incorrect Reduction Claim, page 17.

[125] See Exhibit F, Audit Reports for the *Notification for Truancy* program. Under the Commission's regulations, the Commission has the authority to take official notice of any fact which may be judicially noticed by the courts. (Cal. Code Regs., tit. 2, § 1187.5(c); Gov. Code, § 11515.) Evidence Code section 452(c) authorizes the court to take judicial notice of the official records and files of the executive branch of state government, including the official records of the State Controller's Office. (See also, *Chas L. Harney, Inc. v. State* (1963) 217 Cal.App.2d 77, 86.)

[126] Exhibit A, Incorrect Reduction Claim, page 11.

[127] Government Code section 12410 (Stats. 1968, ch. 449).

"The SCO conducted appropriate statistical samples that identified a *reasonable* estimate of the non-reimbursable initial truancy notifications, thus properly reducing the claims for the *unreasonable* claimed costs."[128]

The Commission finds that the Controller's audit conclusions must be upheld absent evidence that the Controller's reductions are arbitrary, capricious, or entirely lacking in evidentiary support.

The Controller correctly states that there is no express prohibition in law or regulation of statistical sampling and extrapolation methods being used in an audit. However, the Controller's authority to audit is described in the broadest terms: article XVI, section 7 states that "Money may be drawn from the Treasury only through an appropriation made by law and upon a Controller's duly drawn warrant."[129] Government Code section 12410 provides that the Controller "shall superintend the fiscal concerns of the state…" and "shall audit all claims against the state, and may audit the disbursement of any state money, for correctness, legality, and for sufficient provisions of law for payment."[130]

The Controller's audit authority on mandate reimbursement is more specific. Article XIII B, section 6 provides that "the State shall provide a subvention of funds to reimburse…local government for the costs of the program or increased level of service…" whenever the Legislature or a state agency mandates a new program or higher level of service.[131] Government Code section 17561, accordingly, provides that the state "shall reimburse each local agency and school district for *all* 'costs mandated by the state,' as defined in Section 17514…" At the time the audit of the subject claims began in 2012, section 17561 stated:

> In subsequent fiscal years each local agency or school district shall submit its claims as specified in Section 17560. The Controller shall pay these claims from funds appropriated therefor except as follows: (A) The Controller may audit any of the following: (i) Records of any local agency or school district to verify the actual amount of the mandated costs. (ii) The application of a reasonable reimbursement methodology. (iii) The application of a legislatively enacted reimbursement methodology under Section 17573. (B) The Controller may reduce any claim that the Controller determines is excessive or unreasonable. (C) The Controller shall adjust the payment to correct for any underpayments or overpayments that occurred in previous fiscal years.[132]

The parameters and guidelines for the *Notification of Truancy* mandate predate the statutory authorization for a "reasonable reimbursement methodology," as defined in sections 17518.5 and 17557. However, a unit cost, which was adopted for this program, is included within the

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[128] Exhibit B, Controller's Late Comments on the Incorrect Reduction Claim, page 17 [emphasis in original].

[129] California Constitution, article XVI, section 7 (added November 5, 1974, by Proposition 8).

[130] Statutes 1968, chapter 449.

[131] California Constitution, article XIII B, section 6, Statutes 2004, chapter 133, SCA 4; Proposition 1A, November 2, 2004.

[132] Government Code section 17561, (Stats. 2009-2010, 3rd Ex. Sess., ch. 4.).

definition of a "reasonable reimbursement methodology."[133] Thus the Controller's audit authority in section 17561 expressly authorizes an audit of a claim based on unit cost reimbursement. The statutes, however, do not address how the Controller is to audit and verify the costs mandated by the state.

Additionally, the Controller argues that the audit was properly conducted according to *Government Auditing Standards,* as issued by the Comptroller General of the United States. The Controller cites section 7.55 of the *Generally Accepted Government Auditing Standards* (GAGAS): "[a]uditors must obtain sufficient, appropriate evidence to provide a reasonable basis for their findings and conclusions," in support of the use of statistical sampling.[134] Further the Controller cites section 7.56 of the GAGAS: "[a]ppropriateness is the measure of the quality of evidence…" and section 7.62: "[w]hen a representative sample is needed, the use of statistical sampling approaches generally results in stronger evidence…." The Controller cites to the Government Auditing Standards, as issued by the Comptroller General of the United States, to argue that it properly conducted the audit:

> The SCO conducted its audit according to generally accepted government auditing standards *(Government Auditing Standards,* issued by the U.S. Government Accountability Office, July 2007). *Government Auditing Standards,* section 1.03 states, "The professional standards and guidance contained in this document ... provide a framework for conducting high quality government audits and attestation engagements with competence, integrity, objectivity, and independence." Generally accepted government auditing standards require the auditor to obtain sufficient, appropriate evidence to provide a reasonable basis for the findings and conclusions. The standards recognize statistical sampling as an acceptable method to provide sufficient, appropriate evidence.[135]

While the standards cited do not *expressly* provide for statistical sampling and extrapolation to be applied to mandate reimbursement, they do provide for statistical methods to be used to establish the sufficiency, or validity of evidence.[136] The Controller also cites the "Handbook of Sampling for Auditing and Accounting," by Herbert Arkin, to support its contention that a sampling

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[133] Government Code section 17518.5 (added by Stats. 2004, ch. 890); Government Code section 17557 (as amended, Stats. 2004, ch. 890; Stats. 2007, ch. 329).

[134] Exhibit A, Incorrect Reduction Claim, page 245. The Controller cites to: U.S. Government Accountability Office, *Government Auditing Standards,* July 2007.

[135] Exhibit A, Incorrect Reduction Claim, page 245 (final audit report). The Controller cites to sections 7.55, 7.56 and 7.62 of U.S. Government Accounting Office, *Government Auditing Standards,* July 2007.

[136] Exhibit F, U.S. Government Accounting Office, *Government Auditing Standards*, 2003, page 13.

methodology to determine the frequency of errors in the population (i.e., notifications that were not reimbursable for an asserted legal reason) is a widely used approach to auditing.[137]

In accordance with the Controller's audit authority and duties under the Government Code, it is not the Commission's purview to direct the Controller to employ a specific audit method, including when the audit pertains to the application of a unit cost, as here. The Commission's determination is limited to whether the Controller's audit decisions and reduction of costs claimed based on audit decisions is arbitrary, capricious, or entirely lacking in evidentiary support.[138] Based on the standards and texts cited by the Controller, statistical methods are a commonly-used tool in auditing. The claimant concedes that "statistically valid sample methodology is a recognized audit tool for some purposes."[139]

In fact, statistical sampling methods such as those employed here are used in a number of other contexts and have not been held, in themselves, to be arbitrary and capricious, or incorrect as a matter of law. For example, the Department of Health Services has used statistical sampling and extrapolation to determine the amount of over- or under-payment in the context of Medi-Cal reimbursement to health care providers. In *Grier v. Kizer*[140] and *UAPD*,[141] "the Department conducted audits of Medi-Cal providers by taking a small random sample [to determine the frequency and extent of over- or under-claiming for services provided], then extrapolating that error rate over the total amount received by the provider during the period covered by the audit."[142] The methods used by the Department of Health Services were disapproved by the courts in *Grier* and *UAPD* only because they constituted a regulation not adopted in accordance with the APA (as discussed above), rather than on the substantive question whether statistical sampling and extrapolation was a permissible methodology for auditing.[143] Once the Department adopted a regulation in accordance with the APA – a reaction to the proceedings in *Grier* – the court in *UAPD* had no objection to the statistical methodology on its merits.[144] After

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[137] Exhibit B, Controller's Late Comments on the Incorrect Reduction Claim, pages 16-17. The handbook cited is: Herbert Arkin, *Handbook of Sampling for Auditing and Accounting,* Third Edition, Prentice Hall, New Jersey, 1984.

[138] *American Bd. of Cosmetic Surgery, Inc, supra*, 162 Cal.App.4th 534, 547-548.

[139] Exhibit A, Incorrect Reduction Claim, page 12.

[140] *Grier v. Kizer, supra,* 219 Cal.App.3d 422, overturned on other grounds in *Tidewater Marine Western v. Bradshaw, supra,* 14 Cal.4th 557.

[141] *UAPD, supra,* 223 Cal.App.3d 490.

[142] *Id.*, page 495.

[143] E.g., *Grier v. Kizer, supra,* 219 Cal.App.3d 422, 439-440.

[144] *UAPD, supra,* 223 Cal.App.3d 490, 504-505 [finding that the statistical audit methodology did not have retroactive effect because it did not alter the legal significance of past events (i.e., the amount of compensation to which a Medi-Cal provider was entitled)].

Grier, the Department has both regulatory and statutory authority for its sampling and extrapolation audit process.[145]

In addition to the Medi-Cal reimbursement context, the courts have declined to reject the use of statistical sampling and extrapolation to calculate plaintiffs' damages in a class action or other mass tort action.[146] In a case addressing audits of county welfare agencies, the court declined to consider whether the sampling and extrapolation procedures were legally proper, instead finding that counties were not required to be solely responsible for errors "which seem to be inherent in public welfare administration."[147]

On that basis, and giving due consideration to the discretion of the Controller to audit the fiscal affairs of the state,[148] the Commission finds it must uphold the Controller's auditing decisions absent evidence that the audit reductions are arbitrary, capricious, or entirely lacking in evidentiary support.

3. There is no evidence in the record that the Controller's findings using the sampling and extrapolation methodology are not representative of all notices claimed during the audit period or that the findings are arbitrary, capricious, or entirely lacking in evidentiary support.

In addition to challenging the legal sufficiency of the Controller's sampling and extrapolation methodology, the claimant also challenges the qualitative and quantitative reliability and fairness of using statistical sampling and extrapolation to evaluate reimbursement. The claimant states that the risk of extrapolating findings from a sample is that the conclusions obtained from the sample may not be representative of the universe. For example, the claimant asserts that a kindergarten pupil is more likely to be under-age and a special education pupil is more likely to be over-age so that the extrapolation from the samples would not be representative of the universe.[149] The claimant further contends that the sampling technique used by the Controller is also quantitatively non-representative because less than two percent of the total number of notices were audited, the stated precision rate was plus or minus eight percent even though the sample size (ranging from 146 to 148) is essentially identical for all three fiscal years, and that the audited number of notices claimed for daily accounting (elementary schools) in fiscal year 2008-2009 (6,996) is 17 percent larger than the size in fiscal year 2009-2010 (5,995). The claimant concludes by stating that "[t]he expected error rate is stated to be 50%, which means the total amount adjusted $68,410 [for the 3-year audit period] is really just a number exactly between $34,205 (50%) and $102,615 (150%)."[150]

The Controller disagrees with the claimant's assertions that the sampling is non-representative of all notices claimed. The Controller states "that a particular student's initial truancy notification

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[145] See, e.g., Welfare and Institutions Code section 14170(b) as added by Statutes 1992, chapter 722 (SB 485). California Code of Regulations, title 22, section 51458.2 (Register 1988, No. 17).

[146] See, e.g., *Bell v. Farmers Insurance Exchange* (2004) 115 Cal.App.4th 715.

[147] *County of Marin v. Martin* (1974) 43 Cal.App.3d 1, 7.

[148] Government Code section 12410.

[149] Exhibit A, Incorrect Reduction Claim, page 15.

[150] Exhibit A, Incorrect Reduction Claim, page 16.

might more likely be identified as non-reimbursable is irrelevant to the composition of the audit sample itself. It has no bearing on evaluating whether the sample selection is representative of the population" because the sample was random.[151] Citing to the *Handbook of Sampling for Auditing and Accounting*, page 9, the Controller states:

> Since the [statistical] sample is objective and unbiased, it is not subject to questions that might be raised relative to a judgment sample. Certainly a complaint that the auditor had looked only at the worst items and therefore biased the results would have no standing. This results from the fact that an important feature of this method of sampling is that all entries or documents have an equal opportunity for inclusion in the sample.[152]

The Controller further states that the district apparently reached the conclusion that the sampling was quantitatively non-representative because the sample sizes were essentially consistent, while the applicable population size varied. The Controller argues that the absolute size of the sample, not the relative size, is more important under "basic statistical sampling principles." The Controller explains that an "expected error rate" in this context is an assumption used to determine the appropriate sample size, rather than a measure of the ultimate accuracy of the result. In other words, when "the auditor has no idea whatsoever of what to expect as the maximum rate of occurrence or does not care to make an estimate…" an expected error rate of 50 percent as the beginning assumption will provide "the most conservative possible sample size estimate" in order to achieve the precision desired.[153] In addition, the desired accuracy of the result, which might be called a "margin of error," is determined by the auditor before calculating the sample size (shown below as "SE = desired sample precision"). Therefore, the "margin of error" of the Controller's resulting percentage is a known value. The Controller relies on the following formula outlined in Arkin's *Handbook of Sampling for Auditing and Accounting* to calculate the sample size:

$$n = \frac{p(1-p)}{\left(\frac{SE}{t}\right)^2 + \left(\frac{p(1-p)}{N}\right)}$$

n = sample size
p = percent of occurrence in population (expected error rate)
SE = desired sample precision
t = confidence level factor
N = population size[154]

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[151] Exhibit B, Controller's Late Comments on the Incorrect Reduction Claim, page 15.

[152] *Ibid.*

[153] Exhibit B, Controller's Late Comments on the Incorrect Reduction Claim, pages 16-17, Citing to Herbert Arkin, *Handbook of Sampling for Auditing and Accounting*, Third Edition, Prentice Hall, New Jersey, 1984, page 89.

[154] *Id.*, page 16. [Citing to Herbert Arkin, *Handbook of Sampling for Auditing and Accounting*, Third Edition, Prentice Hall, New Jersey, 1984, page 56].

Thus, applying the formula above to the population of elementary and secondary notices in this case, with a 50 percent expected error rate (the "most conservative sample size estimate" when an error rate is not known) and a desired eight percent margin of error, as stated in the audit report, shows that an appropriate sample size for each level of elementary and secondary schools is between 146 and 148 notices for populations ranging from 5,995 to 6,996 notifications issued annually by elementary schools, and 6,897 to 9,496 notifications issued annually by secondary schools during the audit period.[155]

Moreover, there is no evidence in the record that the results are biased or unrepresentative "because a kindergarten pupil is more likely to be under-age and a special education pupil is more likely to be over-age," as asserted by claimant. There is no dispute that the samples were randomly obtained and reviewed by the Controller. According to the *Handbook of Sampling for Auditing and Accounting*, all notices randomly sampled have an equal opportunity for inclusion in the sample so the result is statistically objective and unbiased.[156] Moreover, absent evidence, the Commission must presume that the schools within the claimant's district complied with the mandate in the same way.

In addition, the adjustment range for the population's true error rate within the 95 percent confidence interval is between $30,986 to $30,990, added or subtracted from the point estimate of $68,410.[157] For the claimed costs reduced, this adjustment range represents less than four percent (3.8%) plus or minus of the total amount claimed in fiscal years 2007-2008, 2008-2009, and 2009-2010 ($796,110).[158] Although there is a possibility that the $68,410 reduction may result in more or less reimbursement to the claimant than the actual costs correctly claimed,

Therefore, the Commission finds no evidence that the Controller's reduction of costs claimed, based on the statistical sampling method as applied in this case, is unrepresentative of all notices claimed. The Controller's showing that its method is statistically significant and mathematically valid is sufficient. Based on this analysis, the Commission finds that the Controller's reductions based on statistical sampling methodology as applied in this IRC are not arbitrary, capricious, or entirely lacking in evidentiary support.

V. Conclusion

The Commission finds that the reduction of $68,410 for the audit period, based on the Controller's sampling and extrapolation methodology for initial notices of truancy distributed for pupils who had fewer than three unexcused absences or tardiness occurrences during the school year and for pupils who accumulated fewer than three unexcused absences or tardiness occurrences while between the ages of six and 18 and so were not subject to the compulsory

[155] Exhibit B, Controller's Late Comments on the Incorrect Reduction Claim, page 29.

[156] Exhibit F, Herbert Arkin, *Handbook of Sampling for Auditing and Accounting*, Third Edition, Prentice Hall, New Jersey, 1984, page 9.

[157] Exhibit B, Controller's Late Comments on the Incorrect Reduction Claim, page 17. "Based on the sampling parameters identified in the report and the individual sample results, our analysis shows that the audit adjustment range is $37,420 to $99,396."

[158] Exhibit A, Incorrect Reduction Claim, page 236.

education laws, is correct as a matter of law, and is not arbitrary, capricious, or entirely lacking in evidentiary support.

Accordingly, the Commission denies this IRC.

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RE: **Decision**

Notification of Truancy, 13-904133-I-13
Education Code Section 48260.5
Statutes 1983, Chapter 498
Fiscal Years: 2007-2008, 2008-2009, and 2009-2010
Riverside Unified School District, Claimant

On January 22, 2016, the foregoing decision of the Commission on State Mandates was adopted on the above-entitled matter.

Heather Halsey, Executive Director

Dated: January 27, 2016

DECLARATION OF SERVICE BY EMAIL

I, the undersigned, declare as follows:

I am a resident of the County of Sacramento and I am over the age of 18 years, and not a party to the within action. My place of employment is 980 Ninth Street, Suite 300, Sacramento, California 95814.

On January 27, 2016, I served the:

Decision
Notification of Truancy, 13-904133-I-13
Education Code Section 48260.5
Statutes 1983, Chapter 498
Fiscal Years: 2007-2008, 2008-2009, and 2009-2010
Riverside Unified School District, Claimant

by making it available on the Commission's website and providing notice of how to locate it to the email addresses provided on the attached mailing list.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct, and that this declaration was executed on January 27, 2016 at Sacramento, California.

Jill L. Magee
Commission on State Mandates
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COMMISSION ON STATE MANDATES

Mailing List

Last Updated: 1/14/16

Claim Number: 13-904133-I-13

Matter: Notification of Truancy

Claimant: Riverside Unified School District

TO ALL PARTIES, INTERESTED PARTIES, AND INTERESTED PERSONS:

Each commission mailing list is continuously updated as requests are received to include or remove any party or person on the mailing list. A current mailing list is provided with commission correspondence, and a copy of the current mailing list is available upon request at any time. Except as provided otherwise by commission rule, when a party or interested party files any written material with the commission concerning a claim, it shall simultaneously serve a copy of the written material on the parties and interested parties to the claim identified on the mailing list provided by the commission. (Cal. Code Regs., tit. 2, § 1181.3.)

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