



January 20, 2017

Ms. Lisa Macchione
County of San Diego
Office of County Counsel
1600 Pacific Highway, Room 355
San Diego, CA 92101

Ms. Jill Kanemasu
Accounting and Reporting
State Controller's Office
3301 C Street, Suite 700
Sacramento, CA 95816

And Parties, Interested Parties, and Interested Persons (See Mailing List)

Re: Draft Proposed Decision, Schedule for Comments, and Notice of Hearing
Handicapped and Disabled Students (04-RL-4282-10); Handicapped and Disabled Students II (02-TC-40/02-TC-49); and Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services (97-TC-05), 15-9705-I-06
Government Code Sections 7571, 7572, 7572.5, 7572.55, 7576, 7581, and 7586 as added by Statutes 1984, Chapter 1747 (AB 3632); and as amended by Statutes 1985, Chapter 1274 (AB 882); Statutes 1994, Chapter 1128 (AB 1892); Statutes 1996, Chapter 654 (AB 2726); California Code of Regulations, Title 2, Division 9, Chapter 1, Sections 60020, 60030, 60040, 60045, 60050, 60055, 60100, 60110, 60200, and 60550 (Emergency regulations effective January 1, 1986 [Register 86, No. 1], and refiled June 30, 1986, designated effective July 12, 1986 [Register 86, No. 28]; and Emergency regulations effective July 1, 1998 [Register 98, No. 26]; final regulations effective August 9, 1999 [Register 99, No. 33])
Fiscal Years: 2006-2007, 2007-2008, and 2008-2009
County of San Diego, Claimant

Dear Ms. Macchione and Ms. Kanemasu:

The Draft Proposed Decision for the above-captioned matter is enclosed for your review and comment.

Written Comments

Written comments may be filed on the Draft Proposed Decision by **February 10, 2017**. Please note that all representations of fact submitted to the Commission must be signed under penalty of perjury by persons who are authorized and competent to do so and must be based upon the declarant's personal knowledge, information, or belief. (Cal. Code Regs., tit. 2, § 1187.5.) Hearsay evidence may be used for the purpose of supplementing or explaining other evidence but shall not be sufficient in itself to support a finding unless it would be admissible over an objection in civil actions. (Cal. Code Regs., tit. 2, § 1187.5.) The Commission's ultimate findings of fact must be supported by substantial evidence in the record.¹

¹ 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.

Ms. Macchione and Ms. Kanemasu
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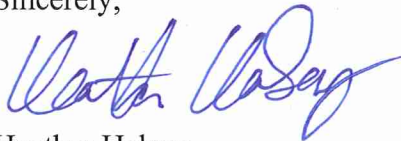
You are advised that comments filed with the Commission on State Mandates (Commission) are required to be simultaneously served on the other interested parties on the mailing list, and to be accompanied by a proof of service. However, this requirement may also be satisfied by electronically filing your documents. Refer to http://www.csm.ca.gov/dropbox_procedures.php on the Commission's website for electronic filing instructions. (Cal. Code Regs., tit. 2, § 1181.3.)

If you would like to request an extension of time to file comments, please refer to section 1187.9(a) of the Commission's regulations.

Hearing

This matter is set for hearing on **Friday, March 24, 2017**, at 10:00 a.m., State Capitol, Room 447, Sacramento, California. The Proposed Decision will be issued on or about March 10, 2017. Please let us know in advance if you or a representative of your agency will testify at the hearing, and if other witnesses will appear. If you would like to request postponement of the hearing, please refer to section 1187.9(b) of the Commission's regulations.

Sincerely,



Heather Halsey
Executive Director

ITEM __
INCORRECT REDUCTION CLAIM
DRAFT PROPOSED DECISION

Government Code Sections 7571, 7572, 7572.5, 7572.55, 7576, 7581, and 7586 as added by Statutes 1984, Chapter 1747 (AB 3632); and as amended by Statutes 1985, Chapter 1274 (AB 882); Statutes 1994, Chapter 1128 (AB 1892); Statutes 1996, Chapter 654 (AB 2726);

California Code of Regulations, Title 2, Division 9, Chapter 1, Sections 60020, 60030, 60040, 60045, 60050, 60055, 60100, 60110, 60200, and 60550

(Emergency regulations effective January 1, 1986 [Register 86, No. 1], and re-filed June 30, 1986, designated effective July 12, 1986 [Register 86, No. 28]; and Emergency regulations effective July 1, 1998 [Register 98, No. 26]; final regulations effective August 9, 1999 [Register 99, No. 33])¹

Handicapped and Disabled Students (04-RL-4282-10); Handicapped and Disabled Students II (02-TC-40/02-TC-49); and Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services (97-TC-05)

Fiscal Years 2006-2007, 2007-2008, and 2008-2009

15-9705-I-06

County of San Diego, Claimant

EXECUTIVE SUMMARY

Overview

This Incorrect Reduction Claim (IRC) challenges the Office of the State Controller's (Controller's) reduction of vendor costs totaling \$1,387,095 (the treatment and board and care costs in Finding 2) claimed for fiscal years 2006-2007 through 2008-2009 by the County of San Diego (claimant) for the *Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services* program.² The Controller reduced vendor costs claimed for board and care and

¹ Note that this caption differs from the Test Claim and Parameters and Guidelines captions in that it includes only those sections that were approved for reimbursement in the Test Claim Decision. Generally, a parameters and guidelines caption should include only the statutes and executive orders and the specific sections approved in the test claim decision. However, that was an oversight in the case of the Parameters and Guidelines at issue in this case.

² Though the consolidated *Handicapped and Disabled Students (04-RL-4282-10); Handicapped and Disabled Students II (02-TC-40/02-TC-49); and Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services (97-TC-05)* Parameters and Guidelines apply to the

treatment services for out-of-state residential placement of SED pupils in facilities organized and operated for-profit. The Parameters and Guidelines and the test claim statutes and regulations only allow vendor payments for the board and care and treatment services for SED pupils placed in out-of-state facilities organized and operated on a *nonprofit* basis.

At the October 28, 2016 Commission meeting, the Commission found that the Revised Final Audit Report, issued December 18, 2012, superseded the previous Final Audit Report for the purpose of the statute of limitations, and therefore this IRC was timely filed.

As explained herein, staff recommends that the Commission on State Mandates (Commission) deny this IRC.

Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services Program

On May 25, 2000, the Commission approved the *Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services*, 97-TC-05 Test Claim, as a reimbursable state-mandated program.³ The test claim statutes and implementing regulations were part of the state's response to the federal Individuals with Disabilities Education Act (IDEA) that guaranteed to disabled pupils, including those with mental health needs, the right to receive a free and appropriate public education, including psychological and other mental health services, designed to meet the pupil's unique educational needs.⁴ As originally enacted, the statutes shifted to counties the responsibility and funding of mental health services required by a pupil's individualized education plan (IEP), but the implementing regulations required that all services provided by the counties be provided *within* the State of California.⁵ In 1996, the Legislature amended Government Code section 7576 to provide that the fiscal and program responsibilities of counties for SED pupils shall be the same regardless of the location of placement, and that the counties shall have fiscal and programmatic responsibility for providing or arranging the provision of necessary services for SED pupils placed in out-of-state residential facilities.⁶ The test claim statutes and regulations address the counties' responsibilities for out-of-state placement of seriously emotionally disturbed pupils.

fiscal years at issue, this IRC solely involves the *Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services* program.

³ Exhibit B, Controller's Comments on the IRC, page 139 (Statement of Decision on 97-TC-05).

⁴ Former Government Code sections 7570, et seq., as enacted and amended by Statutes 1984, Chapter 1747; Statutes 1985, Chapter 1274; California Code of Regulations, title 2, sections 60000-60610 (emergency regulations filed December 31, 1985, designated effective January 1, 1986 (Register 86, No. 1) and refiled June 30, 1986, designated effective July 12, 1986 (Register 86, No. 28)).

⁵ Former California Code of Regulations, title 2, section 60200.

⁶ Statutes 1996, chapter 654.

The Parameters and Guidelines for the *SED* program were adopted on October 26, 2000,⁷ and corrected on July 21, 2006,⁸ with a period of reimbursement beginning January 1, 1997. The Parameters and Guidelines, as originally adopted, authorize reimbursement for the following costs:

To reimburse counties for payments to service vendors providing mental health services to SED pupils in out-of-state residential placements as specified in Government Code section 7576 and Title 2, California Code Regulations, [sections] 60100 and 60110.⁹

The correction adopted on July 21, 2006, added the following sentence: “Included in this activity is the cost for out-of-state residential board and care of SED pupils.” The correction was necessary to clarify the Commission’s finding that the term “payments to service vendors providing mental health services to SED pupils in out-of-state residential placements” includes reimbursement for “residential costs” of out-of-state placements.¹⁰ Thus, the Parameters and Guidelines for *Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services*, 97-TC-05, authorize reimbursement for payments to out-of-state service vendors providing board and care and treatment services for SED pupils “as specified in Government Code section 7576 and Title 2, California Code Regulations, [sections] 60100 and 60110.”

Former section 60100(h) required that “[o]ut-of-state placements shall only be made in residential programs that meet the requirements of Welfare and Institutions Code sections 11460(c)(2) through (c)(3).” Welfare and Institutions Code section 11460, as amended by Statutes of 1995, chapter 724, governed the foster care program from 1996 to 2010. During those years, Welfare and Institutions Code section 11460(c)(3) provided that “State reimbursement for an AFDC-FC rate paid on or after January 1, 1993, shall only be paid to a group home *organized and operated on a nonprofit basis*.” (Emphasis added.) Thus, the nonprofit rule applicable to out-of-state foster care group homes was made expressly applicable to out-of-state residential placements of SED pupils.

On October 26, 2006, the Commission consolidated the Parameters and Guidelines for *Handicapped and Disabled Students (04-RL-4282-10)*; and *Handicapped and Disabled Students II (02-TC-40/02-TC-49)*; and *Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services (97-TC-05)*, for costs incurred commencing with the 2006-2007 fiscal year.¹¹ The reimbursable activities in the consolidated Parameters and Guidelines require counties to determine that the residential placement of SED pupils meets all the criteria established in Welfare and Institutions Code sections 18350 through 18356 before authorizing

⁷ Exhibit A, IRC, page 31.

⁸ Exhibit A, IRC, page 31.

⁹ Exhibit X, Parameters and Guidelines, adopted October 26, 2000.

¹⁰ Exhibit X, Corrected Parameters and Guidelines, dated July 21, 2006.

¹¹ Exhibit A, IRC, pages 30-43 (consolidated Parameters and Guidelines, adopted October 26, 2006).

payment. Former Welfare and Institutions Code section 18350(c) required that “[p]ayments for care and supervision shall be based on rates established in accordance with Sections 11460 to 11467, inclusive.”¹² And, as discussed above, section 11460(c) requires that out-of-state facilities where SED pupils are placed, shall be organized and operated on a nonprofit basis. Thus, reimbursement for the cost of board, care, and treatment services in out-of-state residential facilities remained the same when the program was consolidated with the *Handicapped and Disabled Students* program and during all audit years in question.¹³

The consolidated Parameters and Guidelines also contain instructions for claiming costs. With respect to claims for contract services, claimants are required to provide the name of the contractor who performed the services and show the dates and times when services were performed. The costs claimed must also be supported with contemporaneous source documents. Supporting documents shall be retained “during the period subject to audit.”¹⁴

Statutes 2011, chapter 43 (AB 114) eliminated the mandated programs *Handicapped and Disabled Students* (04-RL-4282-10); *Handicapped and Disabled Students II* (02-TC-40/02-TC-49); and *Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services* (97-TC-05), by transferring responsibility for SED pupils to school districts, effective July 1, 2011.¹⁵ Thus on September 28, 2012, the Commission adopted an amendment to the consolidated Parameters and Guidelines ending reimbursement for these programs effective July 1, 2011.

Procedural History

On April 9, 2008, the claimant filed its fiscal year 2006-2007 annual reimbursement claim.¹⁶ On February 10, 2009, the claimant filed its fiscal year 2007-2008 annual reimbursement claim.¹⁷ On February 8, 2010, the claimant filed its fiscal year 2008-2009 annual reimbursement claim.¹⁸ The Controller asserts that it initiated the audit of the fiscal years 2006-2007 through 2008-2009 reimbursement claims on April 14, 2010.¹⁹ On March 7, 2012, the Controller issued the Final

¹² Exhibit X, Welfare and Institutions Code section 18350, as amended by Statutes 1990, chapter 46, section 12, effective April 10, 1990.

¹³ Exhibit A, IRC, pages 30-43 (consolidated Parameters and Guidelines, adopted October 26, 2006).

¹⁴ Exhibit A, IRC, pages 42 (consolidated Parameters and Guidelines, adopted October 26, 2006).

¹⁵ Exhibit X, Assembly Bill No. 114 (2011-2012 Reg. Sess.), approved by the Governor, June 30, 2011.

¹⁶ Exhibit A, IRC, page 123.

¹⁷ Exhibit A, IRC, page 133.

¹⁸ Exhibit A, IRC, page 145.

¹⁹ Exhibit B, Controller’s Comments on the IRC, page 6.

Audit Report.²⁰ On December 18, 2012, the Controller issued the Revised Final Audit Report, relating to Finding 4 only.²¹ On December 10, 2015, the claimant filed this IRC.²² On December 18, 2015, Commission staff notified the claimant that the IRC filing was deemed untimely filed.²³ On December 28, 2015, claimant filed the Appeal, *Appeal of Executive Director Decision*, 15-AEDD-01.²⁴ On March 25, 2016 and September 23, 2016, the Commission heard the claimant's Appeal, but took no action.²⁵ On October 28, 2016, the Commission granted the claimant's Appeal.²⁶ On December 5, 2016, the Controller filed comments on the IRC.²⁷ The claimant did not file rebuttal comments.

On January 20, 2017, Commission staff issued the Draft Proposed Decision.²⁸

Commission Responsibilities

Government Code section 17561(d) 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 a 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 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 of the California Constitution.²⁹ 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

²⁰ Exhibit A, IRC, page 76.

²¹ Exhibit A, IRC, page 76.

²² Exhibit A, IRC, page 1.

²³ Exhibit X, *Appeal of Executive Director Decision*, 15-AEDD-01, page 1.

²⁴ Exhibit X, *Appeal of Executive Director Decision*, 15-AEDD-01, page 14.

²⁵ 15-AEDD-01 was also set for hearing on May 26, 2016 but was continued, and again on July 22, 2016 but was postponed.

²⁶ Exhibit X, October 28, 2016 Commission hearing minutes and transcript excerpt, page 7.

²⁷ Exhibit B, Controller's Comments on the IRC.

²⁸ Exhibit C, Draft Proposed Decision, issued January 20, 2017.

²⁹ *Kinlaw v. State of California* (1991) 54 Cal.3d 326, 331-334; Government Code sections 17551, 17552.

apply it as an “equitable remedy to cure the perceived unfairness resulting from political decisions on funding priorities.”³⁰

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.³¹

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 claimant.³² In addition, section 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.³³

Claims

The following chart provides a brief summary of the claims and issues raised and staff’s recommendation.

| Issue | Description | Staff Recommendation |
|---|--|---|
| Timeliness of the audit for fiscal years 2006-2007 through 2008-2009. | Government Code section 17558.5 required the Controller to initiate an audit no later than three years after the claim is filed or last amended, or if no payment is made, within 3 years of the date of payment. In either case, the audit must be completed within 2 years after initiation. | <i>The audit was timely initiated and concluded –</i> The audit was initiated on April 14, 2010, less than three years after payment for the 2006-2007 reimbursement claim and within three years from the date the reimbursement claims for fiscal years 2007-2008 and 2008-2009 were filed, and therefore was timely initiated. The Final Audit Report providing the claimant with |

³⁰ *County of Sonoma v. Commission on State Mandates* (2000) 84 Cal.App.4th 1264, 1281, citing *City of San Jose v. State of California* (1996) 45 Cal.App.4th 1802, 1817.

³¹ *Johnston v. Sonoma County Agricultural Preservation and Open Space District* (2002) 100 Cal.App.4th 973, 983-984. See also *American Bd. of Cosmetic Surgery, Inc., v. Medical Bd. of California* (2008) 162 Cal.App.4th 534, 547.

³² *Gilbert v. City of Sunnyvale* (2005) 130 Cal.App.4th 1264, 1274-1275.

³³ 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.

| | | |
|---|--|---|
| | | the claim component adjusted, the amount adjusted, and the reason for the adjustment, was dated March 7, 2012, less than two years after the initiation of the claim on April 14, 2010, and thus was timely completed. |
| Timeliness of the IRC. | <p>The claimant filed this IRC more than three years after the completion of the Final Audit Report, but less than three years after the completion of the Revised Final Audit Report which “superseded” the former report.</p> <p>The claimant must file an IRC within three years of “the date of the Office of State Controller’s final state audit report, letter, remittance advice, or other written notice of adjustment notifying the claimant of a reduction.” Former Cal. Code Regs., title 2, § 1185(b) (effective from May 8, 2007, to June 30, 2014).</p> | <i>The Commission has determined that this IRC was timely filed based on the date of the Revised Final Audit Report which “superseded” the Final Audit Report.³⁴</i> |
| Reduction of costs claimed for vendor payments for board, care, and treatment services for SED pupils placed in an out-of-state facility that is organized and operated for-profit. | The Controller found that a total of \$1,387,095 claimed for board and care and treatment costs for all fiscal years audited was not allowable because, based on the documentation provided by the claimant in this case; the vendor costs claimed were for Charter Provo Canyon, Utah, an out-of-state <i>for-profit</i> residential facility and, thus, the costs were beyond the scope of the mandate. | <i>Correct as a matter of law – During all of the fiscal years at issue in these claims, the Parameters and Guidelines and state law required that residential and treatment costs for SED pupils placed in out-of-state residential facilities be provided by nonprofit facilities and thus, costs claimed for vendor services provided by an out-of-state service vendor that is organized and operated on a for-profit basis is beyond the scope of the mandate and not reimbursable as a matter of law.</i> |

³⁴ Exhibit X, October 28, 2016 Commission hearing minutes and transcript excerpt, page 7.

Staff Analysis

A. The IRC was Timely Filed.

On March 7, 2012, the Controller issued the Final Audit Report with the reductions at issue in this IRC.³⁵ On December 18, 2012, the Controller issued the Revised Final Audit Report which “supersedes” the Final Audit Report because the Controller “recalculated EPSDT revenues for FY 2008-09 and revised Finding 4 to reflect the actual funding percentages based on the final settlement.” The revision had no fiscal effect on allowable total program costs, or on the adjustments in Finding 2.³⁶ The claimant filed this IRC on December 10, 2015, challenging the Controller’s reductions in Finding 2 for out-of-state, for-profit, vendor costs for room and board and treatment incurred for SED pupils for fiscal years 2006-2007, 2007-2008, and 2008-2009.

Based on the facts in this case, the Commission has found that the claimant’s IRC was timely filed because the Revised Final Audit Report issued December 18, 2012 stated that it “supersedes” the Final Audit Report issued March 7, 2012.³⁷ The dictionary definition of supersede is: 1. to replace: supplant; 2. to cause to be set aside or replaced by another.³⁸ Since the December 18, 2012 Revised Final Audit Report superseded the earlier Final Audit Report, it constitutes the last essential element of the audit for purposes of the period of limitation, which put the claimant on notice of the right to file an IRC with the Commission within three years. Thus, based on the date of the Revised Final Audit Report, the claimant had until December 18, 2015 to file the IRC.

The IRC was filed on December 10, 2015 and thus was timely filed.

B. The Controller Timely Initiated and Completed the Audit Pursuant to Government Code Section 17558.5.

The claimant filed the 2006-2007 reimbursement claim on April 9, 2008,³⁹ the 2007-2008 reimbursement claim on February 10, 2009,⁴⁰ and the 2008-2009 reimbursement claim on February 8, 2010.⁴¹ The State paid \$4,106,959 for fiscal year 2006-2007 from the fiscal year 2009-2010 budget.⁴² The Controller initiated the audit on April 14, 2010, at which time the claims for fiscal years 2007-2008 and 2008-2009 had not been paid and within one year of the payment on the 2006-2007 claim in fiscal year 2009-2010.⁴³ The Controller issued the Final

³⁵ Exhibit B, Controller’s Comments on the IRC, page 6.

³⁶ Exhibit A, IRC, page 76.

³⁷ Exhibit X, October 28, 2016 Commission hearing minutes and transcript excerpt, page 7.

³⁸ Webster’s II New College Dictionary (1995) page 1107.

³⁹ Exhibit A, IRC, page 123.

⁴⁰ Exhibit A, IRC, page 133.

⁴¹ Exhibit A, IRC, page 145.

⁴² Exhibit A, IRC, page 84 (footnote 3 in audit report).

⁴³ Exhibit B, Controller’s Comments on the IRC, page 6.

Audit Report with the reductions at issue in this IRC, on March 7, 2012.⁴⁴ The Revised Final Audit report was issued on December 18, 2012.⁴⁵

When the reimbursement claims at issue in this IRC were submitted, Government Code section 17558.5 required the Controller to initiate an audit no later than three years after the claim is filed or last amended. However, if no funds are appropriated or no payment is made to the claimant for the program for the fiscal year at issue, the time for the Controller to initiate the audit is tolled to three years after the date of the initial payment of the claim.

Staff recommends that the Commission find that the Controller timely initiated the audit for all three fiscal years. The fiscal year 2006-2007 reimbursement claim was filed on April 9, 2008, but the claim was not paid until fiscal year 2009-2010. Thus the time for the Controller to initiate the claim was tolled, and the audit initiation date of April 14, 2010 was within three years of the date of payment on the claim. As to the other two fiscal years, the audit was initiated within three years of the date the claims were submitted.

An audit is complete under Government Code section 17558.5(c) when the Controller notifies the claimant of any adjustment to a claim for reimbursement that results from an audit or review. The “notification shall specify the claim components adjusted, the amounts adjusted, interest charges on claims adjusted to reduce the overall reimbursement to the local agency . . . , and the reason for the adjustment.”⁴⁶

Therefore, a timely audit must be completed by April 12, 2012. The Revised Final Audit Report which did not change Finding 2 from the March 7, 2012 Final Audit Report, notified the claimant of the adjustments, the amounts adjusted, and the reason for the adjustment.

Based on the foregoing, staff recommends that the Commission find that the audit was timely completed pursuant to Government Code section 17558.5(a).

C. The Controller’s Reduction of Costs Claimed for Vendor Services Provided by Out-Of-State Residential Treatment and Board and Care Programs That Are Organized and Operated on a For-Profit Basis Is Correct as a Matter of Law.

In Finding 2, costs related to ineligible vendor payment for out-of-state residential placement of SED pupils in programs that are “owned and operated *for-profit*” were reduced. The claimant contends that state law conflicted with federal law during this time period and that federal law did not limit the placement of SED pupils to nonprofit facilities. Absent a decision from the courts on this issue, however, the Commission is required by law to presume that the state statutes and regulations adopted in accordance with the Administrative Procedures Act, are valid. The claimant further argues that decisions issued by the OAH and the U.S. Supreme Court support the position that reimbursement is required if a SED pupil is placed in a for-profit facility that complies with federal IDEA law. However, the claimant has provided no documentation or evidence that the costs claimed in the reimbursement claims at issue in this IRC were incurred as

⁴⁴ Exhibit A, IRC, page 76.

⁴⁵ Exhibit A, IRC, page 76.

⁴⁶ Government Code section 17558.5(c).

a result of a court order finding that no other alternative placement was identified for a SED pupil during the audit years in question, and unlike the court's equitable powers under IDEA, the reimbursement requirements of article XIII B, section 6, of the California Constitution must be strictly construed and not applied as an "equitable remedy to cure the perceived unfairness resulting from political decisions on funding priorities."⁴⁷ Thus, those decisions do not support the claimant's right to reimbursement.

Staff recommends the Commission find that the Controller's reduction of costs claimed for vendor services provided by out-of-state residential programs that are organized and operated on a for-profit basis is correct as a matter of law. The Parameters and Guidelines authorize reimbursement for the payments made by counties to out-of-state care providers of a SED pupil for residential and treatment costs based on rates established by the Department of Social Services in accordance with Welfare and Institutions Code sections 18350 and 18356.⁴⁸ Counties are further required to determine that the residential placement "meets all the criteria established in Welfare and Institutions Code sections 18350 through 18356 before authorizing payment."⁴⁹

During the reimbursement period, Welfare and Institutions Code section 18350(c) required that the payment "for care and supervision shall be based on rates established in accordance with Sections 11460 to 11467" of the Welfare and Institutions Code. Welfare and Institutions Code section 11460 governed the foster care program and subdivision (c)(3) provided that "State reimbursement for an AFDC-FC rate paid on or after January 1, 1993, shall only be paid to a group home *organized and operated on a nonprofit basis.*" (Emphasis added.) Thus, the nonprofit rule applicable to out-of-state foster care group homes was made expressly applicable to out-of-state residential placements of SED pupils. Consistent with these statutes, section 60100(h) of the regulations for this program states that out-of-state residential programs shall meet the requirements in Welfare and Institutions Code section 11640(c)(2) through (3) and, thus, be organized and operated on a nonprofit basis. Thus, the Parameters and Guidelines require that the out-of-state residential facility be operated on a nonprofit basis.

The claimant makes no argument disputing the Controller's findings that Charter Provo Canyon School is a for-profit facility that provided the treatment and board and care services for its SED pupils. Claimant contends, however, that reimbursement is required because it contracted with Mental Health Systems, Inc., a nonprofit corporation, in accordance with the Parameters and Guidelines, and provides a copy of a letter from the IRS verifying that Mental Health Systems, Inc., is a nonprofit entity.⁵⁰ During the course of the audit, the claimant provided a copy of the contracts between Mental Health Systems, Inc., and Charter Provo Canyon School, LLC (later

⁴⁷ *County of Sonoma v. Commission on State Mandates* (2000) 84 Cal.App.4th 1264, 1281, citing *City of San Jose v. State of California* (1996) 45 Cal.App.4th 1802, 1817.

⁴⁸ Exhibit A, IRC, page 37 (consolidated Parameters and Guidelines, adopted October 26, 2006).

⁴⁹ Exhibit A, IRC, page 37 (consolidated Parameters and Guidelines, adopted October 26, 2006).

⁵⁰ Exhibit A, IRC, page 24.

identified as UHS of Provo Canyon) “for the provision of services pursuant to Chapter 26.5 of Division 7 of Title 1 of the Government Code” (the chapter Government Code that includes the test claim statute). The agreement demonstrates that Charter Provo Canyon School provided the services for the claimant, and confirms that Charter Provo Canyon School, LLC is a for-profit limited liability company.

Accordingly, the evidence in the record supports the Controller’s finding that the services were provided by for-profit entities and are outside the scope of the mandate.

Conclusion

Staff finds that the Controller’s reductions are correct as a matter of law.

Staff Recommendation

Staff recommends that the Commission adopt the Proposed Decision to deny this IRC, and authorize staff to make any technical, non-substantive changes following the hearing.

BEFORE THE
COMMISSION ON STATE MANDATES
STATE OF CALIFORNIA

**IN RE INCORRECT REDUCTION CLAIM
ON:**

Government Code Sections 7571, 7572, 7572.5, 7572.55, 7576, 7581, and 7586 as added by Statutes 1984, Chapter 1747 (AB 3632); and as amended by Statutes 1985, Chapter 1274 (AB 882); Statutes 1994, Chapter 1128 (AB 1892); Statutes 1996, Chapter 654 (AB 2726);

California Code of Regulations, Title 2, Division 9, Chapter 1, Sections 60020, 60030, 60040, 60045, 60050, 60055, 60100, 60110, 60200 and 60550

(Emergency regulations effective January 1, 1986 [Register 86, No. 1], and re-filed June 30, 1986, designated effective July 12, 1986 [Register 86, No. 28]; and Emergency regulations effective July 1, 1998 [Register 98, No. 26]; final regulations effective August 9, 1999 [Register 99, No. 33])⁵¹

Fiscal Years 2006-2007, 2007-2008, and 2008-2009

County of San Diego, Claimant

Case No.: 15-9705-I-06

Handicapped and Disabled Students (04-RL-4282-10); Handicapped and Disabled Students II (02-TC-40/02-TC-49); and Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services (97-TC-05)

DECISION PURSUANT TO
GOVERNMENT CODE SECTION 17500 ET
SEQ.; CALIFORNIA CODE OF
REGULATIONS, TITLE 2, DIVISION 2,
CHAPTER 2.5, ARTICLE 7

(Adopted March 24, 2017)

DECISION

The Commission on State Mandates (Commission) heard and decided this Incorrect Reduction Claim (IRC) during a regularly scheduled hearing on March 24, 2017. [Witness list will be included in the adopted Decision.]

⁵¹ Note that this caption differs from the Test Claim and the Parameters and Guidelines captions in that it includes only those sections that were approved for reimbursement in the Test Claim Decision. Generally, a parameters and guidelines caption should include only the statutes and executive orders and the specific sections approved in the test claim decision. However, that was an oversight in the case of the Parameters and Guidelines at issue in this case.

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/modified] the Proposed Decision to [approve/partially approve/deny] this IRC by a vote of [vote count will be included in the adopted Decision] as follows:

| Member | Vote |
|---|-------------|
| Ken Alex, Director of the Office of Planning and Research | |
| Richard Chivaro, Representative of the State Controller | |
| Mark Hariri, Representative of the State Treasurer, Vice Chairperson | |
| Sarah Olsen, Public Member | |
| Eraina Ortega, Representative of the Director of the Department of Finance, Chairperson | |
| Carmen Ramirez, City Council Member | |
| Don Saylor, County Supervisor | |

Summary of the Findings

This IRC challenges the Office of the State Controller’s (Controller’s) findings and reductions of vendor costs, for the treatment and board and care costs in Finding 2 claimed for fiscal years 2006-2007 through 2008-2009 by the County of San Diego (claimant), for the *Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services*⁵² program.

At the October, 28, 2016 Commission meeting, the Commission found that the Revised Final Audit Report, issued December 18, 2012, superseded the Final Audit Report for the purpose of the statute of limitations for filing the IRC and therefore the claim was timely filed.

The Commission now finds that, because the audit reductions were completed on March 7, 2012, within two years from the date the reimbursement claims were filed or paid, the audit was timely as required by section 17558.5 of the Commission’s regulations.

The Commission further finds that the Controller’s reduction of costs claimed for vendor services provided by out-of-state residential programs that are organized and operated on a for-profit basis is correct as a matter of law. During the entire reimbursement period for this program, state law and the Parameters and Guidelines required that out-of-state residential programs that provide board and care and treatment services to SED pupils shall be organized and operated on a nonprofit basis. The Parameters and Guidelines also require the claimant to provide supporting documentation for the costs claimed. In this case, the Controller concluded, based on a service agreement provided by the claimant, that the vendor payments made by the

⁵² Though the consolidated *Handicapped and Disabled Students; Handicapped and Disabled Students II*; and *Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services* parameters and guidelines apply to the fiscal years at issue, this IRC solely involves the *Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services* program.

claimant to Mental Health Systems, Inc., a California nonprofit corporation, are not reimbursable because Mental Health Systems, Inc., contracted with Charter Provo Canyon School, a Delaware for-profit limited liability company, to provide the board and care and treatment services for SED pupils. Since the facility providing the treatment and board and care is a for-profit facility, the Controller correctly found that the costs were not eligible for reimbursement under the Parameters and Guidelines and state law.

The decisions issued by the Office of Administrative Hearings (OAH) and the United States Supreme Court that claimant relies upon to argue for subvention are not applicable in this case because those cases do not address the subvention requirement of Article XIII B section 6 of the California Constitution. Moreover, the claimant has provided no documentation or evidence that the costs claimed in the subject reimbursement claims were incurred as a result of a court order finding that no other alternative placement was identified for a SED pupil during the audit years in question. Further, unlike the court's equitable powers under the federal Individuals with Disabilities Education Act (IDEA), the reimbursement requirements of article XIII B, section 6, of the California Constitution must be strictly construed and not applied as an "equitable remedy to cure the perceived unfairness resulting from political decisions on funding priorities."⁵³

Therefore, the Commission denies this IRC.

I. Chronology

- 04/09/2008 Claimant filed its fiscal year 2006-2007 annual reimbursement claim.⁵⁴
- 02/10/2009 Claimant filed its fiscal year 2007-2008 annual reimbursement claim.⁵⁵
- 02/08/2010 Claimant filed its fiscal year 2008-2009 annual reimbursement claim.⁵⁶
- 04/14/2010 Date that Controller asserts that it initiated the audit of the fiscal years 2006-2007 through 2008-2009 reimbursement claims.⁵⁷
- 03/07/2012 Controller issued the Final Audit Report.⁵⁸
- 12/18/2012 Controller issued the Revised Final Audit Report, which "superseded" the Final Audit Report.⁵⁹

⁵³ *County of Sonoma v. Commission on State Mandates* (2000) 84 Cal.App.4th 1264, 1281, citing *City of San Jose v. State of California* (1996) 45 Cal.App.4th 1802, 1817.

⁵⁴ Exhibit A, IRC, page 123. In its audit report, the Controller noted the County received payment for their 2006-2007 claim from the 2009-10 budget (see also, Exhibit A, page 84).

⁵⁵ Exhibit A, IRC, page 133.

⁵⁶ Exhibit A, IRC, page 145.

⁵⁷ Exhibit B, Controller's Comments on the IRC, page 6.

⁵⁸ Exhibit A, IRC, page 8.

⁵⁹ Exhibit A, IRC, pages 8 and 76

12/10/2015 Claimant filed this IRC.⁶⁰
12/18/2015 Commission issued a notice that the IRC was deemed untimely filed.
12/28/2015 Claimant filed the *Appeal of Executive Director Decision*, 15-AEDD-01.
03/25/2016 Commission heard 15-AEDD-01, but took no action.
09/23/2016 Commission heard 15-AEDD-01, but took no action.⁶¹
10/28/2016 Commission heard 15-AEDD-01, and granted claimant's Appeal, finding that the IRC was timely filed.⁶²
12/05/2016 Controller filed comments on the IRC.⁶³
01/20/2017 Commission staff issued the Draft Proposed Decision.⁶⁴

II. Background

A. Out-of-State Residential Treatment for Seriously Emotionally Disturbed (SED) Pupils

This IRC addresses reimbursement claims for costs incurred by the County of San Diego for vendor services provided to SED pupils in out-of-state residential facilities from fiscal years 2006-2007, 2007-2008, and 2008-2009. During the audit period, the consolidated Parameters and Guidelines for *Handicapped and Disabled Students* (04-RL-4282-10); *Handicapped and Disabled Students II* (02-TC-40/02-TC-49); and *Seriously Emotionally Disturbed (SED) Pupils: Out of State Mental Health Services* (97-TC-05) governed the program.⁶⁵ The history of this program with respect to out-of-state residential treatment for SED pupils is described below.

Government Code sections (Gov. Code, §§ 7570, et seq.) and implementing regulations (Cal. Code Regs., tit. 2, §§ 60000, et seq.) were part of the state's response to the federal Individuals with Disabilities Education Act (IDEA) that guaranteed to disabled pupils, including those with mental health needs, the right to receive a free and appropriate public education, including psychological and other mental health services, designed to meet the pupil's unique educational needs.⁶⁶ As originally enacted, Government Code sections 7570, et seq. shifted to counties the

⁶⁰ Exhibit A, IRC, page 1.

⁶¹ 15-AEDD-01 was also set for hearing on May 26, 2016 but was continued, and again on July 22, 2016 but was postponed.

⁶² Exhibit X, October 28, 2016 Commission meeting minutes and transcript excerpt, page 7.

⁶³ Exhibit B, Controller's Comments on the IRC, page 1.

⁶⁴ Exhibit C, Draft Proposed Decision, issued January 20, 2017.

⁶⁵ Exhibit A, IRC, page 30 (consolidated Parameters and Guidelines, adopted October 26, 2006).

⁶⁶ Former Government Code sections 7570, et seq., as enacted and amended by Statutes 1984, Chapter 1747; Statutes 1985, Chapter 1274; California Code of Regulations, title 2, sections 60000-60610 (emergency regulations filed December 31, 1985, designated effective

responsibility and funding of mental health services required by a pupil's individualized education plan (IEP), but the implementing regulations required that all services provided by the counties be provided *within* the State of California.⁶⁷ In 1996, the Legislature amended Government Code section 7576 to provide that the fiscal and program responsibilities of counties for SED pupils shall be the same regardless of the location of placement, and that the counties shall have fiscal and programmatic responsibility for providing or arranging the provision of necessary services for SED pupils placed in out-of-state residential facilities.⁶⁸

On May 25, 2000, the Commission approved the *Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services*, 97-TC-05 Test Claim, in which the claimant pled the 1996 amendment to Government Code section 7576 and the regulations that implemented the amendment, as a reimbursable state-mandated program (hereafter referred to as "SED").⁶⁹ In the Test Claim Statement of Decision the Commission found that:

Before the enactment of Chapter 654, counties were only required to provide mental health services to SED pupils placed in out-of-home (in-state) residential facilities. However, section 1 now requires counties to have fiscal and programmatic responsibility for SED pupils regardless of placement – i.e., regardless of whether SED pupils are placed out-of-home (in-state) or out-of-state.

Chapter 654 also added subdivision (g) to Government Code section 7576, which provides:

“Referrals shall be made to the community mental health service in the county in which the pupil lives. If the pupil has been placed into residential care from another county, the community mental health service receiving the referral shall forward the referral immediately to the community mental health service of the county of origin, which shall have fiscal and programmatic responsibility for providing or arranging for provision of necessary services. . . .” (Emphasis added.)

California Code of Regulations, sections 60100 and 60200, amended in response to section 7576, further define counties' "fiscal and programmatic responsibilities" for SED pupils placed in out-of-state residential care. Specifically, section 60100 entitled "LEA Identification and Placement of a Seriously Emotionally Disturbed Pupil" reflects the Legislature's intent behind the Test Claim statute by providing that residential placements for a SED pupil may be made out-of-state only when no in-state facility can meet the pupil's

January 1, 1986 (Register 86, No. 1) and refiled June 30, 1986, designated effective July 12, 1986 (Register 86, No. 28).

⁶⁷ Former California Code of Regulations, title 2, section 60200.

⁶⁸ Statutes 1996, chapter 654.

⁶⁹ Exhibit B, Controller's Comments on the IRC, pages 22-30.

needs. Section 60200 entitled “Financial Responsibilities” details county mental health and LEA financial responsibilities regarding the residential placements of SED pupils.

In particular, amended section 60200 removes the requirement that LEAs be responsible for the out-of-state residential placement of SED pupils. Subdivision (c) of section 60200 now provides that the county mental health agency of origin shall be “responsible for the provision of assessments and mental health services included in an IEP in accordance with [section 60100].” Thus, as amended, section 60200 replaces the LEA with the county of origin as the entity responsible for paying the mental health component of out-of-state residential placement for SED pupils.⁷⁰

As relevant here, the Commission concluded that the following new costs were mandated by the state:

- Payment of out-of-state residential placements for SED pupils. (Gov. Code, § 7576; Cal. Code Regs., tit. 2, §§ 60100, 60110.)
- Program management, which includes parent notifications as required, payment facilitation, and all other activities necessary to ensure a county’s out-of-state residential placement program meets the requirements of Government Code section 7576 and Title 2, California Code of Regulations, sections 60000-60610. (Gov. Code, § 7576; Cal. Code of Regs., tit. 2, §§ 60100, 60110.)⁷¹

Parameters and Guidelines for the *SED* program were adopted on October 26, 2000,⁷² and corrected on July 21, 2006,⁷³ with a period of reimbursement beginning January 1, 1997. The Parameters and Guidelines, as originally adopted, authorize reimbursement for the following costs:

To reimburse counties for payments to service vendors providing mental health services to SED pupils in out-of-state residential placements as specified in Government Code section 7576 and Title 2, California Code Regulations, [sections] 60100 and 60110.⁷⁴

The correction adopted on July 21, 2006 added the following sentence: “Included in this activity is the cost for out-of-state residential board and care of SED pupils.” The correction was necessary to clarify the Commission’s finding when it adopted the Parameters and Guidelines,

⁷⁰ Exhibit B, Controller’s Comments on the IRC, pages 141-142 (Statement of Decision, *Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services*, 97-TC-05).

⁷¹ Exhibit B, Controller’s Comments on the IRC, page 148.

⁷² Exhibit X, Parameters and Guidelines, adopted October 26, 2000.

⁷³ Exhibit X, Corrected Parameters and Guidelines, dated July 21, 2006.

⁷⁴ Exhibit X, Parameters and Guidelines, adopted October 26, 2000.

that the term “payments to service vendors providing mental health services to SED pupils in out-of-state residential placements” includes reimbursement for “residential costs” of out-of-state placements.⁷⁵

Thus, the Parameters and Guidelines authorize reimbursement for payments to out-of-state service vendors providing board and care and treatment services for SED pupils “*as specified in Government Code section 7576 and Title 2, California Code Regulations, [sections] 60100 and 60110.*” Former section 60100(h) required that “[o]ut-of-state placements shall only be made in residential programs that meet the requirements of Welfare and Institutions Code sections 11460(c)(2) through (c)(3).” Welfare and Institutions Code section 11460, as amended by Statutes of 1995, chapter 724, governed the foster care program from 1996 to 2010. During those years, Welfare and Institutions Code section 11460(c)(3) provided that “State reimbursement for an AFDC-FC rate paid on or after January 1, 1993, shall only be paid to a group home *organized and operated on a nonprofit basis.*” (Emphasis added.) Thus, the nonprofit rule applicable to out-of-state foster care group homes was made expressly applicable to out-of-state residential placements of SED pupils.

On October 26, 2006, the Commission consolidated the Parameters and Guidelines for *Handicapped and Disabled Students (04-RL-4282-10)*; *Handicapped and Disabled Students II (02-TC-40/02-TC-49)*; and *Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services (97-TC-05)* for costs incurred commencing with the 2006-2007 fiscal year.⁷⁶ The reimbursable activities in the consolidated Parameters and Guidelines require counties to determine that the residential placement of SED pupils meets all the criteria established in Welfare and Institutions Code sections 18350 through 18356 before authorizing payment as follows:

G. Authorize payments to in-state or out-of-state residential care providers/ Issue payments to providers of in-state or out-of-state residential care for the residential and noneducational costs of seriously emotionally disturbed pupils (Gov. Code, § 7581; Cal. Code Regs., tit. 2, § 60200, subd. (e))

1. Authorize payments to residential facilities based on rates established by the Department of Social Services in accordance with Welfare and Institutions Code sections 18350 and 18356. *This activity requires counties to determine that the residential placement meets all the criteria established in Welfare and Institutions Code sections 18350 through 18356 before authorizing payment.*⁷⁷

At that time Welfare and Institutions Code section 18350(c) required that “[p]ayments for care and supervision shall be based on rates established in accordance with Sections 11460 to 11467,

⁷⁵ Exhibit X, Corrected Parameters and Guidelines, dated July 21, 2006.

⁷⁶ Exhibit A, IRC, page 30 (consolidated Parameters and Guidelines, adopted October 26, 2006).

⁷⁷ Exhibit A, IRC, page 37 (emphasis added) (consolidated Parameters and Guidelines, adopted October 26, 2006).

inclusive.”⁷⁸ And, as discussed above, section 11460(c) requires that out-of-state facilities where SED pupils are placed, shall be organized and operated on a nonprofit basis. Thus, under the Parameters and Guidelines, reimbursement for the cost of out-of-state residential placement of seriously emotionally disturbed pupils is contingent upon the placement being at a nonprofit facility.

Section V. of the consolidated Parameters and Guidelines instructs claimants to claim for contract services as follows:

Report the name of the contractor and services performed to implement the reimbursable activities. If the contractor bills for time and materials, report the number of hours spent on the activities and all costs charged. If the contract is a fixed price, report the services that were performed during the period covered by the reimbursement claim. If the contract services are also used for purposes other than the reimbursable activities, only the pro-rata portion of the services used to implement the reimbursable activities can be claimed. Submit contract consultant and attorney invoices with the claim and a description of the contract scope of services.⁷⁹

Section IV. of the Parameters and Guidelines then requires that the costs claimed be supported with contemporaneous source documents. Pursuant to Section VI., the supporting documents shall be retained “during the period subject to audit.”⁸⁰

Statutes 2011, chapter 43 (AB 114) eliminated the mandated programs for *Handicapped and Disabled Students (04-RL-4282-10)*; *Handicapped and Disabled Students II (02-TC-40/02-TC-49)*; and *Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services (97-TC-05)*, by transferring responsibility for SED pupils to school districts, effective July 1, 2011.⁸¹ Thus on September 28, 2012, the Commission adopted an amendment to the Parameters and Guidelines ending reimbursement for these programs effective July 1, 2011.

B. The Audit Findings of the Controller

The claimant submitted reimbursement claims totaling \$14,484,766 for fiscal years 2006-2007 through 2008-2009. The Controller audited the claims and reduced them by \$2,832,875 for various reasons. The claimant only disputes the reduction in Finding 2 for \$1,387,095 relating to ineligible vendor payments for board and care and treatment services for out-of-state residential

⁷⁸ Exhibit X, Welfare and Institutions Code section 18350, as amended by Statutes 1990, chapter 46, section 12, effective April 10, 1990.

⁷⁹ Exhibit A, IRC, pages 39-40 (consolidated Parameters and Guidelines, adopted October 26, 2006).

⁸⁰ Exhibit A, IRC, page 42 (consolidated Parameters and Guidelines, adopted October 26, 2006).

⁸¹ Exhibit X, Assembly Bill No. 114 (2011-2012 Reg. Sess.), approved by the Governor, June 30, 2011.

placement of SED pupils in facilities that are “owned and operated *for-profit*.”⁸² The Controller concluded that the vendor payments made by the claimant to Mental Health Systems, Inc., a California nonprofit corporation, are not allowable because Mental Health Systems, Inc., contracted with Charter Provo Canyon School, a Delaware for-profit limited liability company, to provide the out-of-state residential placement services. Since the facility providing the treatment and board and care is a for-profit facility, the Controller found that the costs are not eligible for reimbursement under the Parameters and Guidelines.⁸³

III. Positions of the Parties

A. County of San Diego

The claimant contends that it timely filed its IRC on December 10, 2015, based on the Revised Final Audit Report dated December 18, 2012, which “superseded” the Final Audit Report dated March 7, 2012.

The claimant further contends that the Controller’s reductions for vendor payments for out-of-state residential placement of SED pupils in facilities that are owned and operated for-profit are incorrect and should be reinstated. For all fiscal years at issue, the claimant asserts that the requirements in the Parameters and Guidelines, based on California Code of Regulations, title 2, section 60100(h) and Welfare and Institutions Code section 11460(c)(3), are in conflict with the requirements of federal law, including the Individuals with Disabilities Education Act (IDEA) and section 472(c)(2) of the Social Security Act (42 U.S.C. 672(c)(2)).⁸⁴ In support of this position, the claimant argues the following:

- California law prohibiting placement in for-profit facilities is inconsistent with federal law, which no longer has such limitation, and with IDEA’s requirement that children with disabilities be placed in the most appropriate educational environment out-of-state and not be constrained by nonprofit status.⁸⁵
- Counties will be subject to increased litigation without the same ability as parents to place seriously emotionally disturbed students in appropriate for-profit out-of-state facilities because the U.S. Supreme Court and the Office of Administrative Hearings (OAH) have found that parents were entitled to reimbursement for placing students in appropriate for-profit out-of-state facilities when the IEP prepared by the school district was found to be inadequate and the placement was otherwise proper under IDEA.⁸⁶

⁸² Exhibit A, IRC, page 9.

⁸³ Exhibit A, IRC, page 94; Exhibit B, Controller’s Comments on the IRC, pages 192-202 and 206-216 (see also the contract between Mental Health Systems, Inc., and Charter Provo Canyon School, LLC (later identified as UHS of Provo Canyon, Inc.)).

⁸⁴ Exhibit A, IRC, page 9.

⁸⁵ Exhibit A, IRC, pages 12-13.

⁸⁶ Exhibit A, IRC, pages 14-16.

- The County contracted with a nonprofit entity, Mental Health Services, Inc., to provide the out-of-state residential services subject to the disputed disallowances.⁸⁷
- State and Federal law do not contain requirements regarding the tax identification status of mental health treatment service providers and the county has complied with the legal requirements regarding treatment services, so there is no basis to disallow treatment costs.⁸⁸ California Code of Regulations, title 2, section 60020(i) and (j) describes the type of mental health services to be provided to SED pupils, as well as who shall provide these services to special education students, with no mention of the tax identification status of the services provider.⁸⁹

B. State Controller's Office

It is the Controller's position that the audit adjustments are correct and that this IRC should be denied. The Controller asserts that the unallowable costs resulting from the out-of-state residential placement of SED pupils in for-profit facilities are correct because the Parameters and Guidelines only allow vendor payments for SED pupils placed in a group home organized and operated on a nonprofit basis.⁹⁰ The Controller states that the unallowable treatment and board-and-care vendor payments claimed result from the claimant's placement of SED pupils in a prohibited for-profit out-of-state residential facility.⁹¹

The Controller does not dispute the assertion that California law is more restrictive than federal law in terms of out-of-state residential placement of SED pupils. The Controller also does not dispute that local educational agencies, unlike counties, are not restricted under the Education Code from contracting with for-profit schools for educational services. However the Controller maintains that under the mandated program, costs incurred at out-of-state for-profit residential programs are not reimbursable.⁹²

The Controller also distinguishes the OAH case cited by the claimant, in which the administrative law judge found that not placing the student in an appropriate facility denied the student a free and appropriate public education under federal regulations, which the Controller argues has no bearing or precedent here because the decision does not address the issue of state mandated reimbursement for residential placements made outside of the regulations.⁹³ The Controller also cites an OAH case where the administrative law judge found, consistent with the Parameters and Guidelines, that the county Department of Health could *not* place a student in an out-of-state residential facility that is organized and operated for profit because the county is

⁸⁷ Exhibit A, IRC, pages 16-17.

⁸⁸ Exhibit A, IRC, pages 17-18.

⁸⁹ Exhibit A, IRC, page 17.

⁹⁰ Exhibit B, Controller's Comments on the IRC, page 11.

⁹¹ Exhibit B, Controller's Comments on the IRC, page 11.

⁹² Exhibit B, Controller's Comments on the IRC, page 14.

⁹³ Exhibit B, Controller's Comments on the IRC, page 14.

statutorily prohibited from funding a residential placement in a for-profit facility. There, the administrative law judge also determined that the business relationship between the nonprofit entity, Aspen Solutions, and a for-profit residential facility, Youth Care, did not grant the latter nonprofit status.⁹⁴

IV. Discussion

Government Code section 17561(d) 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 a 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 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 of the California Constitution.⁹⁵ 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."⁹⁶

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.⁹⁷ 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.

⁹⁴ Exhibit B, Controller's Comments on the IRC, page 14 (citing OAH case Nos. N 2007090403 (Exhibit B of the IRC, pages 112-121) and 2005070683 (Tab 14 of the Controller's Comments on the IRC, pages 231-237)).

⁹⁵ *Kinlaw v. State of California* (1991) 54 Cal.3d 326, 331-334; Government Code sections 17551, 17552.

⁹⁶ *County of Sonoma v. Commission on State Mandates* (2000) 84 Cal.App.4th 1264, 1281, citing *City of San Jose v. State of California* (1996) 45 Cal.App.4th 1802, 1817.

⁹⁷ *Johnston v. Sonoma County Agricultural Preservation and Open Space District* (2002) 100 Cal.App.4th 973, 983-984. See also *American Bd. of Cosmetic Surgery, Inc., v. Medical Bd. of California* (2008) 162 Cal.App.4th 534, 547.

[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.]’ ”⁹⁸

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 claimant.⁹⁹ In addition, section 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.¹⁰⁰

A. The IRC was Timely Filed.

On March 7, 2012, the Controller issued the Final Audit Report.¹⁰¹ On December 18, 2012, the Controller issued the Revised Final Audit Report which “supersedes” the Final Audit Report because the Controller “recalculated EPSDT revenues for FY 2008-09 and revised Finding 4 to reflect the actual funding percentages based on the final settlement.” The revision had no fiscal effect on allowable total program costs, or on the adjustments in Finding 2, which are the subject of this IRC.¹⁰² The claimant filed this IRC on December 10, 2015, challenging the Controller’s reductions in Finding 2 for out-of-state, for-profit, vendor costs for room and board and treatment incurred for SED pupils for fiscal years 2006-2007, 2007-2008, and 2008-2009.

Based on the facts in this case, the Commission has found that the claimant’s IRC was timely filed because the Revised Final Audit Report issued December 18, 2012 stated that it “supersedes” the Final Audit Report issued March 7, 2012.¹⁰³

A reimbursement claim for actual costs filed by a local agency is subject to the initiation of an audit by the Controller within the time periods specified in Government Code section 17558.5. Government Code section 17558.5(c) requires the Controller to notify the claimant of any adjustment to a claim for reimbursement that results from an audit or review. The “notification shall specify the claim components adjusted, the amounts adjusted, interest charges on claims adjusted to reduce the overall reimbursement to the local agency . . . , and the reason for the

⁹⁸ *American Bd. of Cosmetic Surgery, Inc., v. Medical Bd. of California* (2008) 162 Cal.App.4th 534, 547-548.

⁹⁹ *Gilbert v. City of Sunnyvale* (2005) 130 Cal.App.4th 1264, 1274-1275.

¹⁰⁰ 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.

¹⁰¹ Exhibit B, Controller’s Comments on the IRC, page 6.

¹⁰² Exhibit A, IRC, page 76.

¹⁰³ Exhibit X, October 28, 2016 Commission hearing minutes and transcript excerpt, page 7.

adjustment.”¹⁰⁴ Government Code sections 17551 and 17558.7 then allow a claimant to file an IRC with the Commission if the Controller reduces a claim for reimbursement.

In 2012, when the Final Audit Report and the Revised Final Audit Report were issued, section 1185.1(c) of the Commission’s regulations, required IRCs to be filed “no later than three (3) years following the date of the Office of State Controller’s final state audit report, letter, remittance advice, or other written notice of adjustment notifying the claimant of a reduction.”¹⁰⁵ Unlike current regulations, section 1185.1(c), as it existed in 2012, did not expressly state that the time for filing an IRC begins to accrue when the claimant *first* receives a notice of adjustment.¹⁰⁶

The goal of any underlying limitation statute or regulation is to require diligent prosecution of known claims so that the parties have the necessary finality and predictability for resolution while evidence remains reasonably available and fresh.¹⁰⁷ Generally, “a plaintiff must file suit within a designated period after the cause of action accrues.”¹⁰⁸ The cause of action accrues “when [it] is complete with all of its elements.”¹⁰⁹ The courts have held that a cause of action accrues and is complete “upon the occurrence of the last element essential to the cause of action.”¹¹⁰

In this case, the period of limitation for filing an IRC accrued and attached to the Revised Final Audit Report issued December 18, 2012, since the Controller stated that the Revised Final Audit Report “supersedes” the March 7, 2012 Final Audit Report. The dictionary definition of

¹⁰⁴ Government Code section 17558.5(c).

¹⁰⁵ California Code of Regulations, title 2, section 1185.1(c) (Register 2010, No. 44).

¹⁰⁶ California Code of Regulations, title 2, section 1185.1(c) (Register 2016, No. 48), which now states the following:

All incorrect reduction claims shall be filed with the Commission no later than three years following the date a claimant *first* receives from the Office of State Controller a final state audit report, letter, or other written notice of adjustment to a reimbursement claim, which complies with Government Code section 17558.5(c) by specifying the claim components adjusted, the amounts adjusted, interest charges on claims adjusted to reduce the overall reimbursement to the claimant, and the reason for the adjustment. The filing shall be returned to the claimant for lack of jurisdiction if this requirement is not met. (Emphasis added.)

¹⁰⁷ *Addison v. State of California* (1978) 21 Cal.3d 313, 317; *Jordach Enterprises, Inc., v. Brobeck, Phleger & Harrison* (1998) 18 Cal.4th 739, 761.

¹⁰⁸ *Ibid.*

¹⁰⁹ *Ibid* [quoting *Norgart v. Upjohn Co.* (1999) 21 Cal.4th 383, 397].

¹¹⁰ *Seelenfreund v. Terminix of Northern California, Inc.*, (1978) 84 Cal.App.3d 133 [citing *Neel v. Magana, Olney, Levy, Cathcart & Gelfand* (1971) 6 Cal.3d 176].

supersede is: 1. to replace: supplant; 2. to cause to be set aside or replaced by another.¹¹¹ Since the December 18, 2012 Revised Final Audit Report superseded the Final Audit Report, it constitutes the last essential element of the audit for purposes of the period of limitation, which put the claimant on notice of the right to file an IRC with the Commission within three years. Thus, based on the date of the Revised Final Audit Report, the claimant had until December 18, 2015 to file the IRC.

The IRC was filed on December 10, 2015 and thus was timely filed.

B. The Controller Timely Initiated and Completed the Audit Pursuant to Government Code Section 17558.5.

The claimant filed the 2006-2007 reimbursement claim on April 9, 2008,¹¹² the 2007-2008 reimbursement claim on February 10, 2009,¹¹³ and the 2008-2009 reimbursement claim on February 8, 2010.¹¹⁴ The State paid \$4,106,959 for fiscal year 2006-2007 from the fiscal year 2009-2010 budget.¹¹⁵ The Controller asserts that it initiated the audit on April 14, 2010 and this is not disputed. At the time the audit was initiated, the claims for fiscal years 2007-2008 and 2008-2009 had not been paid and it was within one year of the payment on the 2006-2007 claim in fiscal year 2009-2010.¹¹⁶ The Controller issued the Final Audit Report on March 7, 2012, less than two years after the date the audit was initiated.¹¹⁷ The Revised Final Audit Report, which did not change the finding in dispute in this IRC, was issued on December 18, 2012.¹¹⁸

1. The audit was timely initiated pursuant to Government Code section 17558.5.

When the reimbursement claims at issue in this IRC were submitted, Government Code section 17558.5 required the Controller to initiate an audit no later than three years after the claim is filed or last amended. However, if no funds are appropriated or no payment is made to the claimant for the program for the fiscal year at issue, the time for the Controller to initiate the audit is tolled to three years after the date of the initial payment of the claim. The statute reads as follows:

A reimbursement claim for actual costs filed by a local agency or school district pursuant to this chapter is subject to the initiation of an audit by the Controller no later than three years after the date that the actual reimbursement claim is filed or last amended, whichever is later. *However, if no funds are appropriated or no*

¹¹¹ Webster's II New College Dictionary (1995) page 1107.

¹¹² Exhibit A, IRC, page 123.

¹¹³ Exhibit A, IRC, page 133.

¹¹⁴ Exhibit A, IRC, page 145.

¹¹⁵ Exhibit A, IRC, page 84 (footnote 3 in audit report).

¹¹⁶ Exhibit B, Controller's Comments on the IRC, page 6.

¹¹⁷ Exhibit A, IRC, page 76.

¹¹⁸ Exhibit A, IRC, page 76.

*payment is made to a claimant for the program for the fiscal year for which the claim is filed, the time for the Controller to initiate an audit shall commence to run from the date of initial payment of the claim.*¹¹⁹

The Commission finds that the Controller timely initiated the audit for all three fiscal years. The fiscal year 2006-2007 reimbursement claim was filed on April 9, 2008, but the claim was not paid until fiscal year 2009-2010. Thus the time for the Controller to initiate the claim was tolled, and the audit initiation date of April 14, 2010 was within three years of the date of payment on the claim. As to the other two fiscal years, the audit was initiated within three years of the date the claims were submitted.

Therefore, the time to initiate an audit in this case was timely pursuant to Government Code section 17558.5(a).

2. *The audit was timely completed pursuant to Government Code section 17558.5.*

Government Code section 17558.5 requires that an audit be completed no later than two years after the date that the audit was commenced.¹²⁰ Here, the Controller's audit was commenced on April 14, 2010. Therefore, a timely audit must be completed by April 12, 2012. The Controller issued the Final Audit Report on March 7, 2012, notifying the claimant of the reduction in Finding 2, before the completion deadline of April 12, 2012. The Controller also issued the Revised Final Audit Report on December 18, 2012, after the completion deadline. For the reasons below, the Commission finds that the Controller timely completed the audit with respect to Finding 2, the only finding in dispute, based on the March 7, 2012 Final Audit Report.

An audit is complete under Government Code section 17558.5(c) when the Controller notifies the claimant of any adjustment to a claim for reimbursement that results from an audit or review. The "notification shall specify the claim components adjusted, the amounts adjusted, interest charges on claims adjusted to reduce the overall reimbursement to the local agency . . . , and the reason for the adjustment."¹²¹

As explained by the Controller and the claimant, the December 18, 2012 Revised Audit Report recalculated offsetting revenues from the Early and Periodic Screening, Diagnosis and Treatment (EPSDT) reimbursements for fiscal year 2008-2009 (in Finding 4) and had no fiscal effect on allowable total program costs for that fiscal year.¹²² No other revisions to the Controller's findings were made, and the reduction in Finding 2 remained the same. The Revised Final Audit

¹¹⁹ Statutes 2005, chapter 890, effective January 1, 2005, emphasis added.

¹²⁰ Statutes 2004, chapter 890, effective January 1, 2005.

¹²¹ Government Code section 17558.5(c).

¹²² Exhibit A, IRC, page 82 (Revised Final Audit Report); Exhibit X, *Appeal of Executive Director Decision*, 15-AEDD-01, page 19 (Cover letter for the Controller's Revised Final Audit Report, page 1); see also, page 3, where appellant states that "[t]he Revised Final Audit Report contained contains [sic] recalculated Revenues for Early and Periodic Screening, Diagnosis and Treatment reimbursements for fiscal year 2008-2009."

Report which did not change Finding 2 from the March 7, 2012 Final Audit Report, notified the claimant of the adjustments, the amounts adjusted, and the reason for the adjustment as follows:

The county overstated residential placement costs by \$1,653,904 for the audit period.

The county claimed board-and-care costs and mental health treatment “patch” costs for residential placements in out-of-state facilities that are operated on a for-profit basis. Only placements in facilities that are operated on a not-for-profit basis are eligible for reimbursement.

...

We adjusted costs claimed for residential placement in out-of-state facilities that are owned and operated on a for-profit basis...¹²³

Based on the foregoing, the Commission finds that the audit was timely completed pursuant to Government Code section 17558.5(a).

C. The Controller’s Reduction of Costs Claimed for Vendor Services Provided by Out-Of-State Residential Treatment and Board and Care Programs That Are Organized and Operated on a For-Profit Basis Is Correct as a Matter of Law.

1. *During all of the fiscal years at issue in these claims, the Parameters and Guidelines and state law required that SED pupils placed in out-of-state residential facilities be placed in nonprofit facilities and thus, costs claimed for vendor services provided by out-of-state service programs that are organized and operated on a for-profit basis are beyond the scope of the mandate.*

As described below, the Commission finds that the Controller’s reduction for vendor service costs claimed for treatment and board and care of SED pupils placed in facilities that are organized and operated for-profit is correct as a matter of law.

Reimbursement claims filed with the Controller are required by law to be filed in accordance with the parameters and guidelines adopted by the Commission.¹²⁴ Parameters and guidelines provide instructions for eligible claimants to prepare reimbursement claims for direct and indirect costs of a state-mandated program.¹²⁵ Parameters and guidelines are regulatory in nature and “APA valid, and absent a court ruling setting them aside, are binding on the parties.”¹²⁶

¹²³ Exhibit A, IRC, page 87.

¹²⁴ Government Code sections 17561(d)(1); 17564(b); and 17571; *Clovis Unified School District v. Chiang* (2010) 188 Cal.App.4th 794, 801, where the court ruled that parameters and guidelines adopted by the Commission are regulatory in nature and are “APA valid”; *California School Boards Association v. State of California* (2009) 171 Cal.App.4th 1183, 1201, where the court found that the Commission’s quasi-judicial decisions are final and binding, just as judicial decisions.

¹²⁵ Government Code section 17557; California Code of Regulations, title 2, section 1183.7(e).

¹²⁶ *Clovis Unified School District v. Chiang* (2010) 188 Cal.App.4th 794, 801; *California School*

As indicated above, the consolidated Parameters and Guidelines authorize reimbursement for the payments made by counties to out-of-state care providers of a SED pupil for residential and treatment costs based on rates established by the Department of Social Services in accordance with Welfare and Institutions Code sections 18350 and 18356. Counties are further required to determine that the residential placement “meets all the criteria established in Welfare and Institutions Code sections 18350 through 18356 before authorizing payment.”

As described in the Background, Welfare and Institutions Code section 18350(c) required that the payment “for care and supervision shall be based on rates established in accordance with Sections 11460 to 11467” of the Welfare and Institutions Code. Welfare and Institutions Code section 11460 governed the foster care program and subdivision (c)(3) provided that “State reimbursement for an AFDC-FC rate paid on or after January 1, 1993, shall only be paid to a group home *organized and operated on a nonprofit basis.*” (Emphasis added.) Thus, the nonprofit rule applicable to out-of-state foster care group homes was made expressly applicable to out-of-state residential placements of SED pupils. Consistent with these statutes, section 60100(h) of the regulations for this program states that out-of-state residential programs shall meet the requirements in Welfare and Institutions Code section 11640(c)(2) through (3) and, thus, be organized and operated on a nonprofit basis.

The claimant argues, however, that there is no requirement in state or federal law regarding the tax identification status of mental health treatment service providers and that the California Code of Regulations, at section 60020(i) and (j), describe the type of mental health services to be provided in the *SED* program, as well as who shall provide it, with no requirement regarding the providers’ tax identification status.¹²⁷ However, section 60020 of the regulations defines “psychotherapy and other mental health services” for SED pupils and is part of the same article containing the provisions in section 60100, which further specifies the requirements for out-of-state residential programs. The definition of “psychotherapy and other mental health services” in section 60020 does not change the requirement that an out-of-state residential facility providing treatment services and board and care for SED pupils is required to be organized and operated on a nonprofit basis under this program.

This is further evidenced by the regulatory history of section 60100. During the regulatory process for the adoption of California Code of Regulation section 60100, comments were filed by interested persons with concerns that referencing Welfare and Institutions Code section 11460 in section 60100 of the regulations to provide that “[o]ut-of-state placements shall only be made in residential programs that meet the requirements of Welfare and Institutions Code sections 11460(c)(2) through (c)(3)” was not clear since state reimbursement for special education residential placements is not an AFDC-Foster Care program. The Departments of Education and Mental Health responded as follows:

Board and care rates for children placed pursuant to Chapter 26.5 of the Government Code are linked in statute to the statutes governing foster care board and care rates. The foster care program and the special education pupils program

Boards Association v. State of California (2009) 171 Cal.App.4th 1183, 1201.

¹²⁷ Exhibit A, IRC, page 17-18.

are quite different in several respects. This creates some difficulties which must be corrected through statutory changes, and cannot be corrected through regulations. Rates are currently set for foster care payments to out-of-state facilities through the process described in WIC Sections 11460(c)(2) through (c)(3). The rates cannot exceed the current level 14 rate *and the program must be non-profit*, and because of the requirements contained in Section WIC 18350, placements for special education pupils must also meet these requirements. The Departments believe these requirements are clearly stated by reference to statute, but we will handbook WIC Sections 11460(c)(2) through (c)(3) for clarity.¹²⁸

In addition, the departments specifically addressed the issue of “out-of-state group homes which are organized as for profit entities, but have beds which are leased by a non-profit shell corporation.”¹²⁹ The departments stated that the issue may need further legal review of documentation of group homes that claim to be nonprofit, but nevertheless “[t]he statute in WIC section 11460 states that state reimbursement shall only be paid to a group home organized and operated on a non-profit basis.”¹³⁰

Subsequent to the adoption of the Test Claim Decision and Parameters and Guidelines for this program, legislation was introduced to address the issue of payment for placement of SED pupils in out-of-state for profit facilities in light of the fact that the federal government eliminated the requirement that a facility be operated as nonprofit in order to receive federal funding. However, as described below, the legislation was not enacted and the law applicable to these claims remained unchanged during the reimbursement period of the program.

In the 2007-2008 legislative session, Senator Wiggins introduced SB 292, which would have authorized payments to out-of-state, for-profit residential facilities that meet applicable licensing requirements in the state in which they operate, for placement of SED pupils placed pursuant to an IEP. The committee analysis for the bill explained that since 1985, California law has tied the requirement for placement of a SED pupil placed out-of-home pursuant to an IEP, to state foster care licensing and rate provisions. However, the analysis notes that the funds for placement of SED pupils are not AFDC-FC funds. California first defined the private group homes that could receive AFDC-FC funding as nonprofits to parallel the federal funding requirement. Because of the connection between foster care and SED placement requirements, this prohibition applies to placements of SED pupils as well. The committee analysis further recognized that the federal

¹²⁸ Exhibit X, Final Statement of Reasons for Joint Regulations for Pupils with Disabilities, page 127 (emphasis added).

¹²⁹ Exhibit X, Final Statement of Reasons for Joint Regulations for Pupils with Disabilities, page 128.

¹³⁰ Exhibit X, Final Statement of Reasons for Joint Regulations for Pupils with Disabilities, page 128.

government eliminated the requirement that a facility be operated as a nonprofit in order to receive federal funding in 1996.¹³¹ However, the bill did not pass the assembly.¹³²

In 2008, AB 1805, a budget trailer bill, containing identical language to SB 292 was vetoed by the governor.¹³³ In his veto message he wrote, "I cannot sign [AB 1805] in its current form because it will allow the open-ended reimbursement of claims, including claims submitted and denied prior to 2006-07. Given our state's ongoing fiscal challenges, I cannot support any bill that exposes the state General Fund to such a liability."¹³⁴

Subsequently, during the 2009-2010 legislative session, Assembly Member Beall introduced AB 421, which authorized payment for 24-hour care of SED pupils placed in out-of-state, for-profit residential facilities. The bill analysis for AB 421 cites the Controller's disallowance of \$1.8 million in mandate claims from San Diego County based on the claims for payments for out-of-state, for-profit residential placement of SED pupils. The analysis states that the purpose of the proposed legislation was to incorporate the allowance made in federal law for reimbursement of costs of placement in for-profit group homes for SED pupils.¹³⁵ Under federal law, for-profit companies were originally excluded from receiving federal funds for placement of foster care children because Congress feared repetition of nursing home scandals in the 1970s, when public funding of these homes triggered growth of a badly monitored industry.¹³⁶ The bill analysis suggests that the reasoning for the current policy in California, limiting payments to nonprofit group homes, ensures that the goal of serving children's interests is not mixed with the goal of private profit. For these reasons, California has continually rejected allowing placements in for-profit group home facilities for both foster care and SED pupils.¹³⁷ The authors and supporters of the legislation contended that out-of-state, for-profit facilities are sometimes the only available placement to meet the needs of the child, as required by federal law.¹³⁸ The author notes the discrepancy between California law and federal law, which allows federal

¹³¹ Exhibit X, Assembly Committee on Human Services, analysis of SB 292 (2007-2008 Reg. Sess.), June 17, 2009, page 2.

¹³² Exhibit X, Complete Bill History, SB 292 (2007-2008 Reg. Sess.).

¹³³ Exhibit X, Assembly Committee on Appropriations, analysis of AB 421 (2009-2010 Reg. Sess.), May 20, 2009, page 3.

¹³⁴ Exhibit X, Governor's Veto Message, AB 1885 (2007-2008), September 30, 2008.

¹³⁵ Exhibit X, Assembly Committee on Appropriations, analysis of AB 421 (2009-2010), May 20, 2009, page 2.

¹³⁶ Exhibit X, Assembly Committee on Appropriations, analysis of AB 421 (2009-2010), May 20, 2009, page 1.

¹³⁷ Exhibit X, Assembly Committee on Appropriations, analysis of AB 421 (2009-2010), May 20, 2009, page 2.

¹³⁸ Exhibit X, Assembly Committee on Appropriations, analysis of AB 421 (2009-2010), May 20, 2009, page 2.

funding of for-profit group home placements.¹³⁹ However, the bill did not pass the Assembly and therefore did not move forward.¹⁴⁰

Thus, during the entire reimbursement period for this program, reimbursement was authorized only for out-of-state residential facilities organized and operated on a nonprofit basis. Although the claimant contends that state law conflicted with federal law during this time period, there is no law or evidence in the record that the nonprofit requirement for out-of-state residential programs conflicts with federal law or results in a failure for a pupil to receive a free and appropriate education. Absent a decision from the courts on this issue, the Commission is required by law to presume that the statutes and regulations for this program, which were adopted in accordance with the Administrative Procedures Act, are valid.¹⁴¹

Accordingly, pursuant to the law and the Parameters and Guidelines, reimbursement is required only if the out-of-state service vendor operates on a nonprofit basis. As indicated above, the Parameters and Guidelines are binding.¹⁴² Therefore, costs claimed for out-of-state service vendors that are organized and operated on a for-profit basis are beyond the scope of the mandate.

2. *The claimant's reference to decisions issued by the Supreme Court and administrative bodies allowing placement in for-profit residential programs is misplaced.*

The claimant argues that:

In California, during the audit period, if counties were unable to access for-profit out-of-state programs, they may not be able to offer an appropriate placement for a pupil that had a high level of unique mental health needs that may only be treated in a specialized program. If that program was for-profit, that county would have been subject to litigation from parents, who through litigation, may access the appropriate program for their child regardless of the program's tax identification status.

...

Consistent with IDEA, during the audit period, counties should have been able to place special education students in the most appropriate program that met their unique needs without consideration for the programs for-profit or nonprofit status

¹³⁹ Exhibit X, Assembly Committee on Appropriations, analysis of AB 421 (2009-2010), May 20, 2009.

¹⁴⁰ Exhibit X, Complete Bill History, AB 421 (2009-2010).

¹⁴¹ California Constitution, article III, section 3.5; *Robin J. v. Superior Court* (2004) 124 Cal.App.4th 414, 425.

¹⁴² *Clovis Unified School District v. Chiang* (2010) 188 Cal.App.4th 794, 801; *California School Boards Association v. State of California* (2009) 171 Cal.App.4th 1183, 1201.

so that students would be placed appropriately and counties would not be subject to needless litigation as evidenced in the Riverside case above.¹⁴³

The Riverside OAH decision relied upon by claimants, involved a SED pupil who was deaf, had impaired vision, and an orthopedic condition, was assessed as having borderline cognitive ability, and had a long history of social and behavioral difficulties. His only mode of communication was American Sign Language. The parties agreed that the National Deaf Academy would provide the student with a free and appropriate public education, as required by federal law. The facility accepted students with borderline cognitive abilities and nearly all service providers are fluent in American Sign Language. However, the school district and county mental health department took the position that they could not place the student at the National Deaf Academy because it is operated by a for-profit entity. OAH found that the state was not prohibited from placing the student at this out-of-state for-profit facility because the facility was the only one identified as an appropriate placement.¹⁴⁴ Upon appeal, the District Court affirmed the OAH order directing the school district and the county mental health department to provide the student with compensatory education consisting of immediate placement at the National Deaf Academy and through the 2008-2009 school year.¹⁴⁵

The claimant also relies on the U.S. Supreme Court decision in *Florence County School District Four v. Carter*,¹⁴⁶ for the proposition that local government will be subject to increased litigation with the Controller's interpretation. In the *Florence* case, the court held that parents can be reimbursed under IDEA when they unilaterally withdraw their child from an inappropriate placement in a public school and place their child in a private school, even if the placement in the private school does not meet all state standards or is not state approved. Although the court found that parents are entitled to reimbursement under such circumstances only if a federal court concludes both that the public placement violated IDEA and the private school placement was proper under IDEA, the court's decision in such cases is *equitable*. "IDEA's grant of equitable authority empowers a court 'to order school authorities to reimburse parents for their expenditures on private special education for a child if the court ultimately determines that such placement, rather than a proposed IEP, is proper under the Act.'"¹⁴⁷ Unlike the court's equitable powers under IDEA, the reimbursement requirements of article XIII B, section 6, of the

¹⁴³ Exhibit A, IRC, pages 14-15.

¹⁴⁴ Exhibit A, IRC, pages 112-121 (*Student v. Riverside Unified School District and Riverside County Department of Mental Health*, OAH Case No. 2007090403, dated January 15, 2008).

¹⁴⁵ Exhibit X, *Riverside County Department of Mental Health v. Sullivan* (E.D.Cal. 2009) EDCV 08-0503-SGL.

¹⁴⁶ *Florence County School District v. Carter* (1993) 510 U.S. 7.

¹⁴⁷ *Florence County School District v. Carter* (1993) 510 U.S. 7, 12 (citing its prior decision in *School Comm. of Burlington v. Department of Ed. of Mass.* (1985) 471 U.S. 359, 369).

California Constitution must be strictly construed and not applied as an “equitable remedy to cure the perceived unfairness resulting from political decisions on funding priorities.”¹⁴⁸

In this case, the claimant has provided no documentation or evidence that the costs claimed were incurred as a result of a court order finding that no other alternative placement was identified for a SED pupil during the audit years in question. Thus, the Commission does not need to reach the issue of whether reimbursement under article XIII B, section 6 of the California Constitution would be required in such cases. Therefore, these decisions do not support the claimant’s right to reimbursement.

Accordingly, the Commission finds that the Controller’s reduction of costs for vendor service payments for treatment and board and care for SED pupils placed in out-of-state residential programs organized and operated for-profit, is consistent with the Commission’s Parameters and Guidelines and is correct as a matter of law.

3. *The documentation in the record supports the Controller’s findings that services were provided by for-profit residential programs.*

The claimant makes no argument disputing the Controller’s findings that Charter Provo Canyon School is a for-profit facility that provided the treatment and board and care services for its SED pupils. Claimant contends, however, that reimbursement is required because it contracted with Mental Health Systems, Inc., a nonprofit corporation, in accordance with the Parameters and Guidelines, and provides a copy of a letter from the IRS verifying that Mental Health Systems, Inc., is a nonprofit entity.¹⁴⁹ Claimant further argues that

The State never provided any guidance to counties as to how to access or contract with appropriate out-of-state facilities that meet State criteria or qualifications. The State never provided counties a list of appropriate out-of-state facilities that meet State requirements. County should not be penalized now for fulfilling the requirements of the law with little or no guidance from the State.¹⁵⁰

In this case, the Controller concluded that the vendor payments made by the claimant to Mental Health Systems, Inc., a California nonprofit corporation are not reimbursable because Mental Health Systems, Inc., contracted with Charter Provo Canyon School, a Delaware for-profit limited liability company, to provide the board and care and treatment services for SED pupils. Since the facility providing the treatment and board and care is a for-profit facility, the Controller found that the costs were not eligible for reimbursement under the Parameters and Guidelines.¹⁵¹ As indicated above, reimbursement is required only if the out-of-state service vendor that provides board and care and treatment services to SED pupils is organized and operated on a nonprofit basis. Costs claimed for out-of-state service vendors that are organized and operated

¹⁴⁸ *County of Sonoma v. Commission on State Mandates* (2000) 84 Cal.App.4th 1264, 1281 (citing *City of San Jose v. State* (1996) 45 Cal.App.4th 1802, 1817).

¹⁴⁹ Exhibit A, IRC, page 24.

¹⁵⁰ Exhibit A, IRC, pages 16-17.

¹⁵¹ Exhibit A, IRC, page 94.

on a for-profit basis are beyond the scope of the mandate and are not eligible for reimbursement as a matter of law.

During the course of the audit, claimant provided a copy of the contracts between Mental Health Systems, Inc., and Charter Provo Canyon School, LLC (later identified as UHS of Provo Canyon) “for the provision of services pursuant to Chapter 26.5 of Division 7 of Title 1 of the Government Code” (the chapter Government Code that includes the test claim statute). The agreement demonstrates that Charter Provo Canyon School provided the services for the claimant, and confirms that Charter Provo Canyon School, LLC is a for-profit limited liability company. The contract title itself expresses that it is an “Agreement to Provide Mental Health Services” and the recitals state “Provo Canyon has agreed to provide the services of qualified professionals to provide care to those persons authorized to receive mental health services.”¹⁵² In addition, the reimbursement claims filed for 2006-2007 and 2007-2008 identify the vendor as “Mental Health Systems-Provo Canyon” and for 2008-2009 as “MHS-Provo Canyon.”¹⁵³

Accordingly, the evidence in the record supports the Controller’s finding that the services were provided by for-profit entities and are outside the scope of the mandate.

V. Conclusion

Based on the foregoing, the Commission finds that the Controller’s reductions are correct as a matter of law and denies this IRC.

¹⁵² Exhibit B, Controller’s Comments on the IRC, pages 192-204 and 206-216.

¹⁵³ Exhibit A, IRC, pages 127, 138, and 150.

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 20, 2017, I served the:

Draft Proposed Decision, Schedule for Comments, and Notice of Hearing
Handicapped and Disabled Students (04-RL-4282-10); Handicapped and Disabled Students II, (02-TC-40/02-TC-49); and Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services (97-TC-05), 15-9705-I-06
Government Code Sections 7571, 7572, 7572.5, 7572.55, 7576, 7581, and 7586 as added by Statutes 1984, Chapter 1747 (AB 3632); and as amended by Statutes 1985, Chapter 1274 (AB 882); Statutes 1994, Chapter 1128 (AB 1892); Statutes 1996, Chapter 654 (AB 2726);
California Code of Regulations, Title 2, Division 9, Chapter 1, Sections 60020, 60030, 60040, 60045, 60050, 60055, 60100, 60110, 60200, and 60550
(Emergency regulations effective January 1, 1986 [Register 86, No. 1], and refiled June 30, 1986, designated effective July 12, 1986 [Register 86, No. 28]; and Emergency regulations effective July 1, 1998 [Register 98, No. 26]; final regulations effective August 9, 1999 [Register 99, No. 33])
Fiscal Years: 2006-2007, 2007-2008, and 2008-2009
County of San Diego, 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 20, 2017 at Sacramento, California.



Jill L. Magee
Commission on State Mandates
980 Ninth Street, Suite 300
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COMMISSION ON STATE MANDATES

Mailing List

Last Updated: 1/18/17

Claim Number: 15-9705-I-06

Matter: Handicapped and Disabled Students (04-RL-4282-10); Handicapped and Disabled Students II (02-TC-40/02-TC-49); Seriously Emotionally Disturbed Pupils (SED); Out-of-State Mental Health Services (97-TC-05)

Claimant: County of San Diego

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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