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GOVERNOR



# STATE OF CALIFORNIA COMMISSION ON STATE MANDATES

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## REPORT TO THE LEGISLATURE: INCORRECT REDUCTION CLAIMS

January 1, 2017 – December 31, 2017

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## Table of Contents

<b>INTRODUCTION.....</b>	<b>3</b>
<b>SUMMARY OF COMPLETED CLAIMS.....</b>	<b>4</b>
<b>A. Decided Incorrect Reduction Claims.....</b>	<b>4</b>
<i>Animal Adoption, 14-9811-I-03.....</i>	<i>4</i>
<i>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.....</i>	<i>6</i>
<i>Health Fee Elimination, 09-4206-I-25.....</i>	<i>11</i>
<i>Health Fee Elimination, 10-4206-I-32.....</i>	<i>12</i>
<i>Health Fee Elimination, 10-4206-I-35.....</i>	<i>15</i>
<i>Integrated Waste Management, 13-0007-I-02.....</i>	<i>18</i>
<i>Integrated Waste Management, 14-0007-I-04.....</i>	<i>21</i>
<i>Integrated Waste Management, 14-0007-I-05.....</i>	<i>23</i>
<i>Integrated Waste Management, 14-0007-I-06.....</i>	<i>26</i>
<b>B. Withdrawn Incorrect Reduction Claims.....</b>	<b>28</b>
<i>Animal Adoption (98-TC-11).....</i>	<i>28</i>
<i>Health Fee Elimination (CSM 4206).....</i>	<i>28</i>
<i>Integrated Waste Management (00-TC-07).....</i>	<i>28</i>
<b>STRATEGIC APPROACH TO IRC BACKLOG REDUCTION.....</b>	<b>28</b>

## **INTRODUCTION**

Government Code section 17602 requires the Commission on State Mandates (Commission) to report to the Legislature “the number of individual and consolidated incorrect reduction claims decided during the preceding calendar year and whether and why the reduction was upheld or overturned.” This report fulfills that requirement.

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

Government Code Section 17551(d) requires the Commission to hear and decide a claim that the Controller has incorrectly reduced payments to the local agency or school district (incorrect reduction claims or IRCs). 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.

This report includes a summary of the 15 IRCs completed by the Commission between January 1, 2017 and December 31, 2017. This includes six IRCs that were settled and withdrawn as a result of the Commission’s strategic approach to prioritizing for hearing those claims with many cross cutting issues and facilitating the work of the Controller and claimants in reevaluating pending IRCs consistent with the Commission’s decisions.

## SUMMARY OF COMPLETED CLAIMS

### A. Decided Incorrect Reduction Claims

*Animal Adoption*, 14-9811-I-03

Civil Code Sections 1834 and 1846;  
Food and Agriculture Code Sections 31108, 31752, 31752.5, 31753, 32001, and 32003;  
As Added or Amended by Statutes 1998, Chapter 752 (SB 1785)  
Fiscal Years 2001-2002, 2002-2003; 2006-2007, 2007-2008, and 2008-2009

Claimant: Southeast Area Animal Control Authority

Incorrect Reduction Claim Filed: June 8, 2015

Decision Adopted: January 27, 2017

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This IRC was filed in response to an audit by the State Controller's Office (Controller) of the Southeast Area Animal Control Authority's (claimant's) initial reimbursement claims under the *Animal Adoption* program for fiscal years 2001-2002, 2002-2003, 2006-2007, 2007-2008, and 2008-2009. The Controller reduced and recalculated the claims because it found that the claimant did not comply with the Parameters and Guidelines when calculating costs under the actual cost method, claimed unallowable costs and ineligible staff, misstated animal census data, overstated the number of eligible animals, understated the number of reimbursable days, did not claim allowable costs, misstated indirect costs, and overstated offsetting revenues.<sup>1</sup>

The Commission partially approves this IRC, and requests, pursuant to Government Code section 17551(d) and section 1185.9 of the Commission regulations, that the Controller reinstate costs that relate to the following incorrect reductions to the extent the claimant can provide documentation to support the validity of the costs incurred:<sup>2</sup>

- The reduction of costs relating to the exclusion of animals deemed treatable upon arrival at the shelter and later euthanized during the increased holding period because they became non-rehabilitatable.
- The reduction of costs relating to the Controller's recalculation of costs following the *Purifoy v. Howell* decision and its use of an average number of reimbursable days, to the

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<sup>1</sup> See Exhibit A, IRC, page 464 (Cover Letter of Final Audit Report, page 1).

<sup>2</sup> Section VI. of the Parameters and Guidelines require claimants to provide source documents that show the evidence of the validity of such costs and their relationship to the mandate. The supporting documentation must be kept on file by the agency during the audit period required by Government Code section 17558.5. In this respect, claimants are required by Food and Agriculture Code section 32003 to maintain records on animals that are taken up, euthanized, or impounded. Such records shall identify the date the animal was taken up, euthanized, or impounded; the circumstances surrounding these events; and the names of the personnel performing these activities.

The record in this case shows that the claimant started maintaining records using the Paw Trax system in fiscal years 2006-2007 and 2008-2009, and that no records were available for the earlier fiscal years of 2001-2002 and 2002-2003. See Exhibit B, Controller's Late Comments on the IRC, page 15 (State Controller's Office Analysis and Response, page 9). The Controller should, on remand and under its audit authority, re-assess fiscal years 2001-2002 and 2002-2003 in conformity with its reassessment of data for 2006-2007 and 2008-2009 for purposes of reinstating costs incorrectly reduced.

extent the recalculation resulted in an exclusion of “eligible animals” correctly held under the law.

The Commission further finds that all other reductions made by the Controller are correct as a matter of law and are not arbitrary, capricious, or entirely lacking in evidentiary support.

*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 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])<sup>3</sup>  
Fiscal Years 2006-2007, 2007-2008, and 2008-2009

Claimant: County of San Diego

Incorrect Reduction Claim Filed: December 10, 2015

Decision Adopted: May 26, 2017

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This IRC challenges the Controller's findings and reductions in Finding 2 of \$1,387,095, claimed for board and care and treatment services costs of seriously emotionally disturbed (SED) pupils provided by out-of-state, for-profit, residential facilities claimed for fiscal years 2006-2007 through 2008-2009 by the claimant under the *Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services*<sup>4</sup> program.

The Commission's findings are as follows:

**A. The Claimant Timely Filed the IRC.**

On March 7, 2012, the Controller issued the Final Audit Report.<sup>5</sup> On December 18, 2012, the Controller issued the Revised Final Audit Report which "supersedes" the March 7, 2012 Final Audit Report.<sup>6</sup> The claimant filed this IRC on December 10, 2015, more than three years after the Final Audit Report was issued, but within three years after the Revised Final Audit Report was issued.<sup>7</sup> Based on this record, the Commission finds that a new statute of limitations began to accrue with the issuance of the Revised Final Audit Report. The conclusion on the statute of limitations is based on the plain language of the Revised Final Audit Report that it superseded the earlier March 7, 2012 report, the ambiguity in the Commission's regulations at the time the IRC was filed, and on the policy of reaching the merits of the claim as requested by the claimant.

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<sup>3</sup> 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.

<sup>4</sup> 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.

<sup>5</sup> Exhibit B, Controller's Comments on the IRC, page 6.

<sup>6</sup> Exhibit A, IRC, page 76.

<sup>7</sup> Exhibit A, IRC, page 1.

Although the claimant could have filed an IRC on the March 7, 2012 Final Audit Report as early as March 7, 2012 (and before the December 18, 2012 Revised Final Audit Report was issued), the claimant's IRC filing on December 10, 2015, following the superseding Revised Final Audit Report issued December 18, 2012, is timely.

**B. The Controller Timely Initiated the Audit.**

Government Code section 17558.5 requires the Controller to initiate an audit no later than three years after the reimbursement 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 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 either March 29, 2010, or April 14, 2010, as the parties assert, was within three years of the date of payment on the fiscal year 2006-2007 claim. As to the other two fiscal years, the audit was initiated within three years of the date the reimbursement claims were submitted.

**C. The Controller Timely Completed the March 7, 2012 Final Audit Report, But Did Not Timely Complete the December 18, 2012 Revised Final Audit Report and, Thus, the December 18, 2012 Revised Final Audit Report Is Void.**

Government Code section 17558.5 requires that an audit be completed no later than two years after the date that the audit was commenced. Here, the Controller's audit was commenced on either March 29, 2010, or April 14, 2010. Therefore, a timely audit must be completed as early as March 29, 2012.

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." Absent evidence to the contrary, the Commission finds that the date of the Final Audit Report provides evidence of when an audit is complete.

In this case, 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 March 29, 2012. The claimant does not dispute that the reduction in Finding 2 was included in the March 7, 2012 Final Audit Report and that Finding 2 did not change in the later-dated revised report.<sup>8</sup> Thus, the March 7, 2012 Final Audit Report was timely completed.

The Controller issued the Revised Final Audit Report on December 18, 2012, after the two year deadline imposed by Government Code section 17558.5 to complete the audit. Therefore, the Commission finds that the Revised Final Audit Report, dated December 18, 2012, is not timely. Although Government Code section 17558.5 does not specify the consequences for failing to meet the deadlines imposed by the statute, the courts have ruled that when a deadline is for the protection of a person or class of persons, and the language of the statute as a whole indicates the Legislature's intent to enforce the deadline, the deadline is mandatory. Therefore, the Commission finds that the failure to meet the deadline makes the Revised Final Audit Report void.

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<sup>8</sup> Exhibit F, pages 4-5 (March 25, 2016 Commission Hearing Transcript Excerpt).

**D. The Controller's Audit Conclusions and Reduction of Costs in Finding 2 for Board and Care and Treatment Services Costs for SED Pupils Provided by Out-of-State, For-Profit, Residential Programs Remains Valid When the Final Audit Report Is Timely, But the Superseding Revised Final Audit Report Is Void.**

Since the Revised Final Audit Report is void because it was not timely completed, the Commission must determine the effect on the March 7, 2012 Final Audit Report.

**1. Although Claimant Now Requests Reinstatement of All Costs Reduced by the Controller, the Commission's Jurisdiction Is Limited to the Reductions for Board and Care and Treatment Services Under Finding 2 Because the Claimant Only Timely Filed an IRC to Challenge Reductions for Board and Care and Treatment Services Under Finding 2, and Did Not Plead the Remaining Audit Reductions in Its IRC.**

The claimant now requests that the Commission determine the effect of the void and superseding Revised Final Audit Report on *all* of the Controller's cost reductions in Findings 1, 2, 3, and 4, most of which the claimant did not challenge in the IRC.<sup>9</sup> The Commission finds that it does not have jurisdiction over costs reduced in the audit which were not alleged to be incorrect by the claimant in the IRC. The claimant's IRC challenged only the reductions in Finding 2 of \$1,387,095: board and care and treatment services for seriously emotionally disturbed pupils provided by out-of-state, for-profit, residential programs. To be timely, an additional IRC or an amendment to the existing IRC to challenge the Findings not challenged in this IRC, had to be filed in accordance with the Commission's regulations by December 18, 2015. No additional IRC or amendment to this IRC was filed.

Accordingly, the Commission's jurisdiction is limited to the reduction of costs in Finding 2 for board and care and treatment services for seriously emotionally disturbed pupils provided by out-of-state, for-profit, residential programs.

**2. The Commission Finds that the Timely Completion of the Audit Was Made with the Controller's March 7, 2012 Final Audit Report. Since the Revised Final Audit Report Was Not Timely Completed and Is Void, It Has No Effect on the March 7, 2012 Reductions Under Finding 2. Therefore, the Commission Must Reach the Merits of Finding 2, As Requested by Claimant in its Appeal of the Executive Director's Decision, 15-AEDD-01. On the Merits, the Commission Finds the Controller's Reduction of Costs Claimed for Board and Care and Treatment Services for Seriously Emotionally Disturbed Pupils Provided by Out-of-State Residential Programs that Are Organized and Operated on a For-Profit Basis, Is Correct as a Matter Of Law.**

- a) The Timely Completion of the Audit Was Made with the Controller's March 7, 2012 Final Audit Report and the Revised Final Audit Report Is Void and Can Have No Effect on the March 7, 2012 Reductions Under Finding 2.

On October 28, 2016, the Commission heard and decided the issue of whether the claimant timely filed this IRC in accordance with the Commission's regulations and found that the statute of limitations for filing the IRC began to accrue with the later December 18, 2012 Revised Final Audit Report. The conclusion on the statute of limitations was based on the policy of reaching the merits of the claim as requested by the claimant, the plain language of the Revised Final Audit Report that it superseded the earlier March 7, 2012 report (and hence provided notice to

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<sup>9</sup> Exhibit E, Claimant's Late Comments on Draft Proposed Decision.

the claimant that it could commence an IRC proceeding), and the ambiguity in the Commission's regulations at the time the IRC was filed. However, the issue of whether the Controller timely completed the audit in accordance with Government Code section 17558.5 was not before the Commission at the October 28, 2016 hearing. Thus, the Commission was not made aware of, and did not address, the timeliness of the Revised Final Audit Report and the effect of that untimely and void report with respect to the validity of the March 7, 2012 Final Audit Report and the reductions made therein. Thus, the Commission did *not* make a finding at that hearing that the March 7, 2012 Final Audit Report was void, as asserted by the claimant. The Commission, instead, agreed to reach the merits of the IRC.

Based on the evidence in the record, the Commission finds that the March 7, 2012 Final Audit Report provided notice to the claimant of the reasons for the reduction and the amount reduced in Finding 2 in accordance with Government Code section 17558.5. No changes were made in the Revised Final Audit Report to Finding 2 and the claimant does not dispute that the reduction amount and reasoning for the reduction in Finding 2 remained the same in the Revised Final Audit Report as it was in the March 7, 2012 Final Audit Report.<sup>10</sup>

Accordingly, the Commission finds that completion of the audit was made with the Controller's March 7, 2012 Final Audit Report and claimant could have filed an IRC at any time beginning on March 7, 2012 to contest the Finding 2 reductions at issue in this claim. Since the March 7, 2012 Final Audit Report was timely completed, and the Revised Final Audit Report is void and can have no effect on Finding 2 since it was completed past the statutory deadline, the Commission must now reach the merits of Finding 2.

- b) The Controller's Reduction of Costs Claimed for Board and Care and Treatment Services for Seriously Emotionally Disturbed Pupils 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 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 board and care and treatment services for SED pupils. Since the facility providing the board and care and treatment services 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

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<sup>10</sup> Exhibit F, pages 4-5 (March 25, 2016 Commission Hearing Transcript Excerpt).

and not applied as an “equitable remedy to cure the perceived unfairness resulting from political decisions on funding priorities.”<sup>11</sup>

Accordingly, the Commission finds that the Controller’s reduction of costs in Finding 2 for board and care and treatment services costs for SED pupils provided by out-of-state, for-profit, residential programs is correct as a matter of law.

The Commission therefore denies this IRC.

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<sup>11</sup> *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.

*Health Fee Elimination, 09-4206-I-25*

Former Education Code Section 72246 (Renumbered as § 76355);<sup>12</sup> Statutes 1984, Chapter 1 (1983-1984 2nd Ex. Sess.) (AB2X 1); and Statutes 1987, Chapter 1118 (AB 2336)

Fiscal Years 2002-2003, 2003-2004, 2004-2005, 2005-2006, and 2006-2007

Claimant: Yosemite Community College District

Incorrect Reduction Claim Filed: October 5, 2009

Decision Adopted: March 24, 2017

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This Decision addresses an IRC filed by the Yosemite Community College District (claimant) regarding reductions made by the State Controller's Office (Controller) to reimbursement claims for costs incurred during fiscal years 2002-2003 through 2006-2007 under the *Health Fee Elimination* program. Reductions of \$451,873 were made based on overstated indirect costs claimed for fiscal years 2005-2006 and 2006-2007, understated offsetting student health service fees authorized to be collected, and understated offsetting savings or reimbursements from earned interest income on the student health fee revenue.

The Commission finds that the audit for fiscal years 2002-2003 and 2003-2004 was timely commenced from the date of initial payment of the claims in accordance with Government Code section 17558.5, and that the audit was timely completed within the two-year deadline.

The Commission also finds that the Controller's reduction and recalculation of indirect costs for is correct as a matter of law, and not arbitrary, capricious, or entirely lacking in evidentiary support. The claimant used the FAM29-C methodology to calculate indirect costs for fiscal years 2005-2006 and 2006-2007, but used the prior year's CCFS-311 financial reporting information, instead of the claim year's CCFS-311 financial reporting information as required to report actual costs incurred. Thus, the Controller's reduction is correct as a matter of law. In addition, there is no evidence that the Controller's recalculation of indirect costs is arbitrary, capricious, or entirely lacking in evidentiary support.

Additionally, the Commission finds that the correct calculation and application of offsetting revenue from student health fees has been resolved by the court in *Clovis Unified School Dist.*, which found that to the extent the district "has the authority' to charge for the mandated program or increased level of service, that charge cannot be recovered as a state-mandated cost."<sup>13</sup> Thus a reduction based on fees *authorized* to be charged by Education Code section 76355, rather than fee revenue actually collected, is correct as a matter of law.

Finally, the Commission finds that the Controller's reduction of costs for interest earned on the student health fee revenue collected is correct as a matter of law. The revenue generated from the health fee, including the interest earned, does not constitute proceeds of taxes and is required by law and Section VIII. of the Parameters and Guidelines ("Offsetting Savings and Other Reimbursements") to be identified and deducted from the costs claimed.

Therefore, the Commission denies this IRC.

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<sup>12</sup> Statutes 1993, chapter 8.

<sup>13</sup> *Clovis Unified School Dist. v. Chiang* (2010) 188 Cal.App.4th 794, 812.

*Health Fee Elimination, 10-4206-I-32*

Former Education Code Section 72246 (Renumbered as § 76355);<sup>14</sup> Statutes 1984, Chapter 1 (1983-1984 2nd Ex. Sess.) (AB2X 1); and Statutes 1987, Chapter 1118 (AB 2336) Fiscal Years 2002-2003, 2003-2004, 2004-2005, 2005-2006, and 2006-2007

Claimant: State Center Community College District

Incorrect Reduction Claim Filed: September 1, 2010

Decision Adopted: July 28, 2017

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This Decision addresses the IRC filed by State Center Community College District (claimant) regarding reductions made by the State Controller's Office (Controller) to reimbursement claims for fiscal years 2002-2003 through 2006-2007 under the *Health Fee Elimination* program. Over the five fiscal years in question, the Controller reduced costs totaling \$902,744. The Controller made reductions based on overstated indirect costs and understated health fees authorized to be collected. The Controller in Findings 1, 4, and 5 also made additional findings that did not result in any reductions of costs claimed.

The Commission finds that the Controller timely initiated the audit of the fiscal year 2002-2003, 2003-2004, and 2004-2005 reimbursement claims pursuant to Government Code section 17558.5, since the first payment on the 2002-2003 reimbursement claim was made within three years of the date the audit was initiated, and no payment had been made for the 2003-2004 and 2004-2005 claims at the time the audit was initiated. The audit was complete for all reimbursement claims before the two-year deadline.

On the merits, the Commission finds as follows:

- The Controller's reduction of indirect costs is partially correct. The district claimed indirect costs for fiscal years 2002-2003 and 2003-2004 under the OMB Circular A-21 method, but did not obtain federal approval of the indirect cost rates used for the calculation as required by the OMB itself. Thus, the reduction for these fiscal years is correct as a matter of law. There is no evidence that the Controller's recalculation of indirect costs using the FAM-29C method is arbitrary, capricious, or entirely lacking in evidentiary support.

The reduction of indirect costs for fiscal years 2005-2006 and 2006-2007, however, is incorrect as a matter of law. The Controller adjusted indirect costs claimed using a federally approved indirect cost rate based solely on the ground that the claiming instructions were changed beginning fiscal year 2004-2005 to disallow the use of a federally approved rate to claim indirect costs unless specifically approved in the Commission's Parameters and Guidelines. The Controller's new indirect cost rate rule is included in the Controller's Mandated Cost Manuals, updated December 27, 2005, November 15, 2006, and November 7, 2007, which applied to the fiscal year 2004-2005, 2005-2006, and 2006-2007 reimbursement claims to be filed by January 15, 2006, January 15, 2007, and February 15, 2008, respectively.<sup>15</sup>

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<sup>14</sup> Statutes 1993, chapter 8.

<sup>15</sup> Exhibit F, Excerpts of Mandated Cost Manuals for 2004-2005, 2005-2006, and 2006-2007 reimbursement claims; Government Code section 17560, as amended by Statutes 1998, chapter 681 and Statutes 2007, chapter 129.

Although the new rule allows the use of the federal OMB Circular A-21 “if specifically allowed by a mandated program’s Ps &Gs,” the Parameters and Guidelines for the *Health Fee Elimination* Program do not contain that language and, thus, the Controller’s change to the rule effectively prohibits the use of the federal method for calculating indirect costs for this program. Parameters and guidelines are regulatory in nature and may validly incorporate manuals and other documents by reference as long the incorporated document is adequately identified and available for comment.<sup>16</sup> However, if the manual or document that is incorporated by reference later changes without notice or opportunity for comment, then the new rule or standard of general application in the incorporated document may become an invalid underground regulation.<sup>17</sup> There is no evidence in the record, such as a proof of service or certificate of mailing, that the Controller provided notice of the change in the rule to the claimant or that the claimant received the updated Mandated Cost Manuals prior to filing its 2005-2006 and 2006-2007 reimbursement claims. The record suggests that the claimant first received notice of the change in the rule when the draft audit report was issued in March 2010. By that time, however, the claimant could not file a request to amend the Parameters and Guidelines or a request to review the claiming instructions to specifically allow the use of the federal OMB method to calculate indirect costs retroactively for the fiscal year 2005-2006 and 2006-2007 claims. Accordingly, under these circumstances, the Commission finds that the Controller’s reduction of indirect costs by \$124,261 for fiscal years 2005-2006 and 2006-2007, based solely on the Controller’s change to the claiming instructions with regard to the calculation of indirect cost rates, is incorrect as a matter of law.

Since the Controller’s adjustment to indirect costs for fiscal year 2004-2005 does not result in a reduction, the Commission has no jurisdiction under Government Code section 17551(d) to review the Controller’s audit adjustment for that fiscal year.

- The Controller’s reduction based on the claimant’s unreported offsetting fee authority is correct as a matter of law, and is not arbitrary, capricious, or entirely lacking in evidentiary support. This issue has been conclusively decided in *Clovis Unified School District*,<sup>18</sup> in which the court held that local government is required to identify and deduct the total amount of fees authorized to be charged, and not only the fee revenue actually collected. The court stated that local government could choose not to exercise statutory fee authority to its maximum extent, but not at the state’s expense. The Commission further finds that the Controller’s calculation of the claimant’s authorized offsetting fee revenue is not arbitrary, capricious, or entirely lacking in evidentiary support, since the Controller used the enrollment data available and reported by the claimant. The Controller obtained student enrollment and Board of Governors Grant (BOGG) recipient data from the California Community College’s Chancellor’s Office and calculated the authorized health service fees using the authorized rates approved by the Chancellor’s Office for the fiscal years at issue.<sup>19</sup>

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<sup>16</sup> *Clovis Unified School Dist. v. Chiang* (2010) 188 Cal.App.4th 794, 799; *Kings Rehabilitation Center Inc. v. Premo* (1999) 69 Cal.App.4th 215, 220.

<sup>17</sup> *Kings Rehabilitation Center Inc. v. Premo* (1999) 69 Cal.App.4th 215, 219-220.

<sup>18</sup> *Clovis Unified School District v. Chiang* (2010) 188 Cal.App.4th 794.

<sup>19</sup> Exhibit A, IRC, page 76.

- The Commission has no jurisdiction under Government Code section 17551(d) to hear and determine whether Findings 1, 4, and 5, are incorrect because these findings did not result in any reductions of costs claimed. These findings address the Controller's conclusions that \$89,593 in salaries, benefits, services and supplies, and related indirect costs for psychological interns and costs funded with Lottery revenue could have been claimed in fiscal year 2004-2005, but were not; and the advisory findings regarding the claimant's reporting of base-year and current-year services, and alleged insufficient documentation of services provided.

The Commission, therefore, partially approves this IRC and requests, pursuant to Government Code section 17551(d) and section 1185.9 of the Commission's regulations, that the Controller reinstate indirect costs of \$124,261 for fiscal years 2005-2006 and 2006-2007 to the claimant.

*Health Fee Elimination, 10-4206-I-35*

Former Education Code Section 72246 (Renumbered as § 76355);<sup>20</sup> Statutes 1984, Chapter 1 (1983-1984 2nd Ex. Sess.) (AB2X 1); and Statutes 1987, Chapter 1118 (AB 2336) Fiscal Years 2002-2003, 2003-2004, 2004-2005, 2005-2006, and 2006-2007

Claimant: San Mateo County Community College District

Incorrect Reduction Claim Filed: November 29, 2010

Decision Adopted: May 26, 2017

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This Decision addresses the IRC filed by San Mateo County Community College District (claimant) regarding reductions made by the State Controller's Office (Controller) to reimbursement claims for fiscal years 2002-2003 through 2006-2007 under the *Health Fee Elimination* program. Over the five fiscal years in question, the Controller reduced costs totaling \$781,934, of which \$732,846 is in dispute. The Controller made reductions based on its findings of unallowable costs for services and supplies (gift certificates, food, and other promotional items distributed during health fairs); unallowable costs for uncollected student health fees as a bad debt expense; overstated indirect costs; and understated health fees authorized to be collected.

The Commission finds that the Controller timely initiated the audit of the fiscal year 2002-2003 and 2003-2004 reimbursement claims pursuant to Government Code section 17558.5, since payment on the 2002-2003 reimbursement claim was made within three years of the date the audit was initiated, and no payment had been made for the 2003-2004 claim at the time the audit was initiated. The audit was complete for all reimbursement claims before the two-year deadline.

On the merits, the Commission finds as follows:

- The Controller's reduction of costs for gift certificates, food, and other promotional items distributed during health fairs is correct as a matter of law, and is not arbitrary, capricious, or without evidentiary support. The Parameters and Guidelines authorize reimbursement for the costs to provide health services to students in the claim year, including the costs for health fairs to distribute information to students, *to the extent* the district provided the service in fiscal year 1986-1987.<sup>21</sup> Thus, to the extent that these promotional items were not provided by the district in the base year, these costs go beyond the scope of the mandate. Here, the record contains invoices supporting the costs incurred in the claim year for gift certificates, food, and other promotional items distributed during health fairs.<sup>22</sup> However, claimant has not argued or submitted any evidence, as required by the Parameters and Guidelines, that it provided these promotional items in the base year as an integral part of its health fairs.
- The Controller's reduction of costs claimed as a bad debt expense resulting from uncollected student health fees is correct as a matter of law. The Parameters and Guidelines authorize reimbursement for the costs of providing health supervision and services and direct and indirect medical and hospitalization services to students, and the operation of student health centers, to the extent the community college provided these

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<sup>20</sup> Statutes 1993, chapter 8.

<sup>21</sup> Exhibit A, IRC, page 40, emphasis added.

<sup>22</sup> Exhibit B, Controller's Late Comments on the IRC, pages 89-109.

services in fiscal year 1986-1987. Health service fees authorized by statute to be charged, but uncollectible, are not costs identified in the Parameters and Guidelines as eligible for reimbursement.

- The Controller's reduction of indirect costs is partially correct. The district claimed indirect costs for all fiscal years under the OMB Circular A-21 based on a federally approved rate of 30 percent, developed using a base of "Direct salaries and wages including all fringe benefits."<sup>23</sup> For fiscal years 2002-2003 and 2003-2004, the Controller found that the claimant overstated indirect costs because it incorrectly applied the indirect cost rate to a base of total direct costs, rather than to a base of salaries and benefits only, as approved by the federal government. This reduction is correct as a matter of law. Section H(2)(e) of the OMB Circular A-21 requires the rate to be applied only to direct salaries and wages.<sup>24</sup> Thus, the claimant did not comply with the OMB Circular A-21 or the negotiated agreement with the federal government and, instead, applied the rate to all direct costs. Moreover, there is no evidence that the Controller's recalculation is arbitrary, capricious, or entirely lacking in evidentiary support.

The reduction for fiscal year 2004-2005, however, is incorrect as a matter of law. The Controller adjusted indirect costs based solely on the ground that the claiming instructions were changed beginning with the fiscal year 2004-2005 reimbursement claims, to not allow the use of a federally approved rate to claim indirect costs unless specifically approved in the Commission's Parameters and Guidelines. The Controller's new indirect cost rate rule is included in the Controller's Mandated Cost Manual, "updated December 27, 2005," which applied to fiscal year 2004-2005 reimbursement claims to be filed by January 15, 2006, just two weeks later.<sup>25</sup> Although the new rule allows the use of the federal OMB Circular A-21 "if specifically allowed by a mandated program's Ps & Gs," the Parameters and Guidelines for the *Health Fee Elimination* Program do not contain that language and, thus, the Controller's change to the rule effectively prohibits the use of the federal method for calculating indirect costs for this program in fiscal year 2004-2005. Parameters and guidelines are regulatory in nature and may validly incorporate manuals and other documents by reference as long the incorporated document is adequately identified and available for comment.<sup>26</sup> However, if the manual or document that is incorporated by reference later changes without notice or opportunity for comment, then the new rule or standard of general application in the incorporated document may become an invalid underground regulation.<sup>27</sup> There is no evidence in the record, such as a proof of service or certificate of mailing, that the Controller provided notice of the change in the rule to the claimant or that the Claimant received the updated Mandated Cost Manual prior to filing its 2004-2005 reimbursement

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<sup>23</sup> Exhibit A, IRC, pages 13, and 109 and 120 (federal approval letter of indirect cost rate, dated March 11, 2003, and effective for the period of July 1, 2003, through June 30, 2008); Exhibit B, Controller's Late Comments on the IRC, pages 48-51 (federal approval letter of indirect cost rate, dated February 4, 1999, and effective for the period of July 1, 1999 through June 30, 2004).

<sup>24</sup> Exhibit F, OMB Circular A-21, page 39 (emphasis added).

<sup>25</sup> Exhibit F, Mandated Cost Manual updated December 27, 2005; Government Code section 17560, as amended by Statutes 1998, chapter 681.

<sup>26</sup> *Clovis Unified School Dist. v. Chiang* (2010) 188 Cal.App.4th 794, 799; *Kings Rehabilitation Center Inc. v. Premo* (1999) 69 Cal.App.4th 215, 220.

<sup>27</sup> *Kings Rehabilitation Center Inc. v. Premo* (1999) 69 Cal.App.4th 215, 219-220.

claim. Even if the updated Mandated Cost Manual was, in fact, issued to community college districts on December 27, 2005 (the date of the manual), the claimant would not have had sufficient notice or opportunity to comment before the 2004-2005 reimbursement claim was due on January 15, 2006. Thus, the Commission finds that the Controller's reduction of indirect costs in fiscal year 2004-2005, based solely on the Controller's change to the claiming instructions and its use of the new indirect cost rate rule, without evidence that notice and an opportunity for comment was provided to the claimant, is an invalid underground regulation and the costs reduced should be reinstated to the claimant.

Since the Controller's adjustment to indirect costs in fiscal years 2005-2006 and 2006-2007 does not result in a reduction, the Commission has no jurisdiction under Government Code section 17551(d) to review the Controller's audit adjustment for those fiscal years.

- The Controller's reduction based on the claimant's unreported offsetting fee authority is correct as a matter of law, and is not arbitrary, capricious, or entirely lacking in evidentiary support. This issue has been conclusively decided in *Clovis Unified School District*,<sup>28</sup> in which the court held that local government is required to identify and deduct the total amount of fees authorized to be charged, and not only the fee revenue actually collected. The court stated that local government could choose not to exercise statutory fee authority to its maximum extent, but not at the state's expense. The Commission further finds that the Controller's calculation of the claimant's authorized offsetting fee revenue is not arbitrary, capricious, or entirely lacking in evidentiary support, since the Controller used the enrollment data available and reported by the claimant. The Controller obtained student enrollment and Board of Governors Grant (BOGG) recipient data from the California Community College's Chancellor's Office and calculated the authorized health service fees using the authorized rates approved by the Chancellor's Office for the fiscal years at issue.<sup>29</sup>

The Commission, therefore, partially approves this IRC and requests that the Controller reinstate \$4,896 to the claimant.

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<sup>28</sup> *Clovis Unified School District v. Chiang* (2010) 188 Cal.App.4th 794.

<sup>29</sup> Exhibit A, IRC, page 80.

*Integrated Waste Management, 13-0007-I-02*

Public Resources Code Sections 40148, 40196.3, 42920-42928; Public Contract Code Sections 12167 and 12167.1; Statutes 1992, Chapter 1116 (AB 3521); Statutes 1999, Chapter 764 (AB 75); State Agency Model Integrated Waste Management Plan (February 2000)  
Fiscal Years 1999-2000, 2000-2001; 2003-2004, 2004-2005, 2005-2006,  
2006-2007, 2007-2008, 2008-2009, and 2009-2010

Claimant: Sierra Joint Community College District

Incorrect Reduction Claim Filed: June 19, 2014

Decision Adopted: July 28, 2017

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This IRC addresses the Controller's reductions to reimbursement claims of the Sierra Joint Community College District (claimant) for fiscal years 1999-2000, 2000-2001, and 2003-2004 through 2009-2010 under the *Integrated Waste Management* program, 00-TC-07. The reductions were made because the claimant did not identify and deduct from its claims offsetting savings from its diversion of solid waste and the associated reduced or avoided costs of landfill disposal fees. The Commission finds that the audit reductions are partially incorrect.

The Controller correctly presumed, consistent with the test claim statutes and the court's interpretation of those statutes, and without any evidence to the contrary, that cost savings, resulting from the diversion of waste from landfills, were realized by the claimant during the audit period. Therefore, the finding of cost savings and the associated reduction of costs claimed is correct as a matter of law.

The Commission further finds, based on the evidence in the record, that the Controller's calculation of offsetting cost savings for fiscal years 1999-2000, 2000-2001, the second half of fiscal year 2003-2004, and fiscal years 2004-2005 through 2009-2010 is not arbitrary, capricious, or entirely lacking evidentiary support. In these fiscal years, the claimant exceeded the mandate and diverted more solid waste than required by law. Thus, instead of using 100 percent of the diversion percentage actually achieved, the Controller's cost savings formula "allocated" the diversion percentage by dividing the percentage of solid waste required to be diverted, either 25 or 50 percent, by the actual percentage of solid waste diverted, as reported by the claimant to California Integrated Waste Management Board (CIWMB). The resulting quotient is then multiplied by the tons of solid waste diverted, as annually reported by the claimant to CIWMB, multiplied by the avoided landfill disposal fee (based on the statewide average fee).<sup>30</sup> The formula allocates cost savings based on the mandated levels of diversion, and is intended to prevent penalizing the claimant for diverting more solid waste than the amount mandated by law.<sup>31</sup> The claimant has not filed any evidence to rebut the statutory presumption of cost savings or to show that the statewide average disposal fee is incorrect, or arbitrary. Thus, the Controller's reduction of costs claimed for these fiscal years is correct.

However, the Controller's reduction of costs claimed for the *first* half of fiscal year 2003-2004 is incorrect as a matter of law and is arbitrary, capricious, and entirely lacking in evidentiary support. The Controller found that the claimant did not achieve the mandated "50 percent" diversion for the first half of fiscal year 2003-2004, when the mandated diversion rate for all of

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<sup>30</sup> Exhibit A, IRC, pages 33-35; Exhibit B, Controller's Late Comments on the IRC, pages 19 and 20.

<sup>31</sup> Exhibit B, Controller's Late Comments on the IRC, page 19.

2003 was in fact 25 percent, which the claimant exceeded.<sup>32</sup> As a result of applying the wrong mandated diversion rate, the Controller used 100 percent of the tonnage diverted by the claimant to calculate offsetting cost savings, resulting in a reduction of \$7,513 (204 tons of diverted waste multiplied by the avoided statewide average landfill disposal fee of \$36.83).<sup>33</sup>

The Controller admits that “as there is no state mandate to exceed solid waste diversion for amounts in excess of 25% for calendar years 2000 through 2003 or 50% for calendar year 2004 and later, there is no basis for calculating offsetting savings realized for actual diversion percentages that exceed the levels set by statute.”<sup>34</sup> However, in comments on the Draft Proposed Decision, the Controller now argues for the first time that calculating offsetting savings for the first half of fiscal year 2003-2004 at \$7,513, using 100 percent of the actual diversion rate achieved by the claimant of 45.59 percent, rather than an allocated rate, is correct because there is no evidence that the claimant prorated or allocated the direct costs claimed to perform the mandate.<sup>35</sup> However, the deadline to complete the audit or give new reasons for reductions has long past.

Additionally, the Controller’s position is not supported by the Parameters and Guidelines or the record. Although the Controller is correct that there is no evidence that the claimant prorated or allocated the direct costs claimed for the first half of fiscal year 2003-2004, there is no evidence that the claimant did so for any other years in the audit period. The Parameters and Guidelines require claimants to report in their reimbursement claims all costs incurred to comply with the reimbursable activities (which includes the activities and costs to divert at least 25 or 50 percent of all solid waste from landfill disposal) and the cost savings from the avoided landfill disposal fees, to claim the net increased costs.<sup>36</sup> It is presumed that the reimbursement claim, submitted under penalty of perjury, claimed only those direct costs mandated by the state, absent any finding by the Controller in the audit to the contrary. And here, there is no indication in the audit report that direct costs were over claimed, nor was over claiming of direct costs a reason given for the reduction in the audit report. In this case, the claimant failed to report cost savings, despite evidence in the record that it diverted solid waste; and for all fiscal years in the audit *except* the first half of fiscal year 2003-2004, the Controller’s offsetting savings formula allocated the diversion percentage based on the mandated percentage to prevent penalizing the claimant for exceeding the diversion requirement.<sup>37</sup> There is no evidence in the record, nor does the Controller specify any reason, to conclude that the calculation of offsetting savings for the first half of fiscal year 2003-2004 should be treated differently than the other fiscal years in the audit period.

Applying the Controller’s formula for the calculation of cost savings (for years when the claimant exceeds the mandate) to the first half of fiscal year 2003-2004, results in offsetting cost savings of \$4,120 (25 percent mandated diversion rate divided by 45.59 percent actual diversion rate, multiplied by 204 tons diverted, multiplied by the avoided statewide average landfill

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<sup>32</sup> Exhibit B, Controller’s Late Comments on the IRC, page 71.

<sup>33</sup> Exhibit A, IRC, page 31, footnote 2 (Final Audit Report); Exhibit B, Controller’s Late Comments on the IRC, page 71.

<sup>34</sup> Exhibit B, Controller’s Late Comments on the IRC, page 19.

<sup>35</sup> Exhibit D, Controller’s Comments on the Draft Proposed Decision.

<sup>36</sup> Exhibit A, IRC, page 54 (Parameters and Guidelines).

<sup>37</sup> Exhibit B, Controller’s Late Comments on the IRC, page 19.

disposal fee of \$36.83),<sup>38</sup> rather than the \$7,513 calculated by the Controller, and the difference of \$3,393 has been incorrectly reduced. Accordingly, the Commission finds that the reduction of \$7,513 for the first half of fiscal year 2004-2004 is incorrect as a matter of law, and is arbitrary, capricious, and entirely lacking in evidentiary support.

Therefore, the Commission partially approves this IRC and requests, pursuant to Government Code section 17551(d) and section 1185.9 of the Commission's regulations, that the Controller reinstate \$3,393 to the claimant.

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<sup>38</sup> Exhibit B, Controller's Late Comments on the IRC, pages 37 and 71.

*Integrated Waste Management*, 14-0007-I-04

Public Resources Code Sections 40148, 40196.3, 42920-42928; Public Contract Code Sections 12167 and 12167.1; Statutes 1992, Chapter 1116 (AB 3521); Statutes 1999, Chapter 764 (AB 75); State Agency Model Integrated Waste Management Plan (February 2000) Fiscal Years 1999-2000, 2000-2001, 2003-2004, 2004-2005, 2005-2006, 2006-2007, 2007-2008, 2008-2009, 2009-2010, and 2010-2011

Claimant: Gavilan Joint Community College District

Incorrect Reduction Claim Filed: July 14, 2014

Decision Adopted: September 22, 2017

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This IRC addresses reductions made by the Controller to reimbursement claims of the Gavilan Joint Community College District (claimant) for fiscal years 1999-2000, 2000-2001, and 2003-2004 through 2010-2011, under the *Integrated Waste Management* program, 00-TC-07. The Controller made the audit reductions because the claimant did not identify and deduct from its reimbursement claims offsetting cost savings from its diversion of solid waste and the associated reduced or avoided landfill disposal costs.

The Commission finds that the Controller timely initiated the audit of the fiscal year 2000-2001 reimbursement claim and timely completed the audit for all claims pursuant to Government Code section 17558.5. Government Code section 17558.5(a) tolls the time to initiate the audit to three years from the date of initial payment on the claim, rather three years from the date the claim was filed, “if no funds are appropriated or no payment is made to a claimant for the program for the fiscal year for which the claim is filed.” The record shows that payment on the 2000-2001 reimbursement claim was first made by the Controller on either January 18, 2011,<sup>39</sup> or January 28, 2011,<sup>40</sup> within three years of the date the audit was initiated on January 17, 2014. Thus, the audit was timely initiated. The audit was complete for all reimbursement claims when the final audit report was issued April 11, 2014,<sup>41</sup> well before the two-year deadline of January 17, 2016.

On the merits, the Commission finds that the audit reductions are partially correct. The Controller correctly presumed, consistent with the test claim statutes and the court’s interpretation of those statutes, and without any evidence to the contrary, that the claimant realized cost savings during the audit period equal to the avoided landfill disposal fee per ton of waste required to be diverted.

The Commission further finds, based on the evidence in the record, that the Controller’s calculation of offsetting cost savings for fiscal years 1999-2000, 2000-2001, the second half of fiscal year 2003-2004, and fiscal years 2004-2005 through 2010-2011, is correct as a matter of law and is not arbitrary, capricious, or entirely lacking in evidentiary support. Because the claimant exceeded the mandate and diverted more solid waste than required by law, the Controller’s cost savings formula “allocated” the diversion percentage by dividing the percentage of solid waste required to be diverted, either 25 or 50 percent, by the actual percentage of solid waste diverted, as reported by the claimant to the California Integrated Waste Management Board (CIWMB). The resulting quotient was then multiplied by the tons of solid waste diverted, as annually reported by the claimant to CIWMB, multiplied by the avoided

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<sup>39</sup> Exhibit A, IRC, page 292.

<sup>40</sup> Exhibit B, Controller’s Late Comments on the IRC, page 36.

<sup>41</sup> Exhibit A, IRC, page 24 (Final Audit Report).

landfill disposal fee (based on the statewide average fee).<sup>42</sup> The formula allocates cost savings based on the mandated rates of diversion, and was intended to prevent penalizing the claimant for diverting more solid waste than the amount mandated by law.<sup>43</sup> The claimant has not filed any evidence to rebut the statutory presumption of cost savings or to show that the statewide average disposal fee is incorrect or arbitrary. Thus, the Controller's reduction of costs claimed for these fiscal years is correct.

However, the Controller's reduction of costs claimed for the first half of fiscal year 2003-2004 is incorrect as a matter of law because the Controller calculated offsetting savings using an incorrect required diversion rate. During this period, the claimant achieved an actual diversion percentage of 75.43 percent.<sup>44</sup> The Controller allocated the diversion rate for the first half of fiscal year 2003-2004, as it had done for the other fiscal years, because the claimant exceeded the mandate. However, the Controller used a 50 percent rate to calculate the allocated diversion rate, although the test claim statutes required only 25 percent diversion in calendar year 2003. The requirement to divert 50 percent of solid waste did not become operative until January 1, 2004.<sup>45</sup> Applying the Controller's calculation of cost savings (using 25 percent to calculate the allocated diversion rate) to the first half of fiscal year 2003-2004, results in offsetting costs savings of \$3,822 (25 percent mandated diversion rate divided by 75.43 percent actual diversion rate equals a 33.14 percent allocated rate, multiplied by 313.1 tons diverted, multiplied by the avoided statewide average landfill disposal fee of \$36.83),<sup>46</sup> rather than the \$7,644 calculated by the Controller using a 50 percent diversion rate.

Accordingly, the Commission finds that the law and the record support offsetting cost savings for the first half of fiscal year 2003-2004 of \$3,822, rather than \$7,644, and that the difference of \$3,822 has been incorrectly reduced.

Therefore, the Commission partially approves this IRC, and requests, pursuant to Government Code section 17551(d) and section 1185.9 of the Commission's regulations, that the Controller reinstate \$3,822 to the claimant.

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<sup>42</sup> Exhibit A, IRC, pages 33-35 (Final Audit Report); Exhibit B, Controller's Late Comments on the IRC, page 21.

<sup>43</sup> Exhibit B, Controller's Late Comments on the IRC, page 21.

<sup>44</sup> Exhibit B, Controller's Late Comments on the IRC, page 77.

<sup>45</sup> Public Resources Code sections 42921; Exhibit A, IRC, page 43 (Parameters and Guidelines, adopted March 30, 2005).

<sup>46</sup> Exhibit B, Controller's Late Comments on the IRC, page 77.

*Integrated Waste Management*, 14-0007-I-05

Public Resources Code Sections 40148, 40196.3, 42920-42928; Public Contract Code Sections 12167 and 12167.1; Statutes 1992, Chapter 1116 (AB 3521); Statutes 1999, Chapter 764 (AB 75); State Agency Model Integrated Waste Management Plan (February 2000) Fiscal Years 1999-2000, 2000-2001, 2003-2004, 2004-2005, 2005-2006, 2006-2007, 2007-2008, 2008-2009, 2009-2010, and 2010-2011

Claimant: State Center Community College District

Incorrect Reduction Claim Filed: July 14, 2014

Decision Adopted: December 1, 2017

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This IRC addresses reductions made by the Controller to reimbursement claims of the State Center Community College District (claimant) for fiscal years 1999-2000, 2000-2001, and 2003-2004 through 2010-2011 under the *Integrated Waste Management* program, 00-TC-07. The Controller made the audit reductions because the claimant (in the two colleges within the district: Reedley College and Fresno City College (FCC)) did not identify and deduct from its reimbursement claims offsetting cost savings from its diversion of solid waste and the associated reduced or avoided costs of landfill disposal fees.

The Commission finds that the audit reductions are partially correct.

During the audit period, the claimant diverted solid waste, as required by the test claim statutes, and exceeded the mandated diversion rate in all years except calendar year 2000. The Controller correctly presumed, consistent with the test claim statutes and the court's interpretation of those statutes, and without any evidence to the contrary, that the claimant realized cost savings during the audit period equal to the avoided landfill disposal fee per ton of waste required to be diverted.

The Commission further finds, based on the evidence in the record, that the Controller's calculation of offsetting cost savings for fiscal years 1999-2000, 2000-2001, the second half of fiscal year 2003-2004, and fiscal years 2004-2005 through 2010-2011 is correct as a matter of law and not arbitrary, capricious, or entirely lacking in evidentiary support. During the audit period, the claimant exceeded the mandated diversion rate in all years except calendar year 2000.<sup>47</sup> Instead of using 100 percent of the diversion percentage achieved in years when the claimant diverted more solid waste than the amount mandated by the test claim statutes, the Controller's cost savings formula "allocated" the diversion by dividing the percentage of solid waste required to be diverted, either 25 or 50 percent, by the actual percentage of solid waste diverted, as reported by the claimant to California Integrated Waste Management Board (CIWMB). The resulting quotient was then multiplied by the tons of solid waste diverted, as annually reported by the claimant to CIWMB, multiplied by the avoided landfill disposal fee (based on the statewide average fee).<sup>48</sup> The formula allocates cost savings based on the mandated levels of diversion, and is intended to prevent penalizing the claimant for diverting

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<sup>47</sup> The Controller found that Fresno City College exceeded the mandate in all years in the audit period, but that Reedley College did not exceed the mandate in calendar years 2000 and 2003. In years that Reedley College did not exceed the mandated (25 or 50 percent) diversion level, the Controller did not allocate the diversion rate, but used 100 percent of the tonnage diverted to calculate offsetting savings. See Exhibit B, Controller's Late Comments on the IRC, pages 92-93.

<sup>48</sup> Exhibit A, IRC, pages 33-35 (Final Audit Report); Exhibit B, Controller's Late Comments on the IRC, page 21.

more solid waste than the amount mandated by law.<sup>49</sup> The claimant has not filed any evidence to rebut the statutory presumption of cost savings or to show that the statewide average disposal fee is incorrect or arbitrary. Thus, the Controller's reduction of costs claimed for these fiscal years is correct.

In calendar year 2000, the claimant's Reedley College achieved a 24.57 diversion rate, which was less than the 25 percent required, so the Controller did not allocate the diversion rate, but multiplied 100 percent of the solid waste diverted by the claimant by the avoided landfill disposal fee (based on the statewide average fee).

These formulas are consistent with the statutory presumption of cost savings and correctly presume, without any evidence to the contrary, that the percentage of waste diverted results in offsetting cost savings in an amount equal to the avoided landfill fee per ton of waste required to be diverted. In years when the claimant exceeded the mandated diversion rates, the Controller's formula limits the offset to the mandated levels.<sup>50</sup>

However, the Controller's reduction of costs claimed for the first half of fiscal year 2003-2004 for both colleges is incorrect as a matter of law, and is arbitrary, capricious, and entirely lacking in evidentiary support. For the first half of fiscal year 2003-2004, Reedley College achieved an actual diversion rate of 26.11 percent. The Controller found that Reedley College did not achieve the mandated "50 percent" diversion rate, although only 25 percent diversion was mandated in the first half of fiscal year 2003-2004. Thus, for this period at Reedley College, the Controller did not allocate the diversion percentage to calculate cost savings, but used 100 percent of the reported diversion to calculate offsetting savings.<sup>51</sup> In addition, FCC achieved an actual diversion rate of 53.59 percent in the first half of fiscal year 2003-2004.<sup>52</sup> The Controller allocated the diversion rate for FCC, as it had done for the other fiscal years because the claimant exceeded the mandate, but used a 50 percent rate to calculate the allocated diversion rate, when the test claim statutes mandated only 25 percent diversion in calendar year 2003.<sup>53</sup> The requirement to divert 50 percent of all solid waste did not become operative until January 1, 2004.<sup>54</sup> Therefore, the Controller's calculation of cost savings, which applied a 50 percent diversion rate to the period from July 1, 2003, through December 31, 2003, for both colleges, instead of the mandated 25 percent diversion rate, is incorrect as a matter of law. In addition, the Controller's calculation, which did not reduce cost savings by allocating the diversion percentage to the 25 percent mandated diversion rate as it did for other years when the claimant exceeded the mandate, is arbitrary, capricious, and entirely lacking in evidentiary support. Applying the Controller's formula to the first half of fiscal year 2003-2004 for both colleges within the claimant's district, using the 25 percent diversion requirement, results in offsetting costs savings of:

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<sup>49</sup> Exhibit B, Controller's Late Comments on the IRC, pages 20-21.

<sup>50</sup> Exhibit A, IRC, page 35, footnote 2 (Final Audit Report); Exhibit B, Controller's Late Comments on the IRC, page 93.

<sup>51</sup> Exhibit A, IRC, page 35, footnote 2 (Final Audit Report); Exhibit B, Controller's Late Comments on the IRC, page 93.

<sup>52</sup> Exhibit B, Controller's Late Comments on the IRC, pages 92-93.

<sup>53</sup> Exhibit B, Controller's Late Comments on the IRC, pages 92-93.

<sup>54</sup> Public Resources Code sections 42921; Exhibit A, IRC, page 95 (Parameters and Guidelines).

- \$7,166 for Reedley College (25 percent divided by 26.11 percent, multiplied by 203.2 tons diverted multiplied by the statewide average landfill disposal fee of \$36.83) rather than \$7,484 calculated by the Controller using a 100 percent diversion rate of the solid waste diverted; and
- \$3,039 for FCC (25 percent divided by 53.59 percent, multiplied by 176.9 tons diverted multiplied by the statewide average landfill disposal fee of \$36.83) rather than \$6,079 calculated by the Controller using a 50 percent diversion rate.

Thus, the Commission finds that the law and the record support offsetting savings for the first half of fiscal year 2003-2004 of \$10,205 rather than \$13,563, and the difference of \$3,358 has been incorrectly reduced.<sup>55</sup>

Therefore, the Commission partially approves this IRC, and requests, pursuant to Government Code section 17551(d) and section 1185.9 of the Commission's regulations, that the Controller reinstate \$3,358 to the claimant.

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<sup>55</sup> Exhibit B, Controller's Late Comments on the IRC, pages 37 (FCC 2003 Annual Report), 60 (Reedley 2003 Annual Report) and 92-93.

*Integrated Waste Management*, 14-0007-I-06

Public Resources Code Sections 40148, 40196.3, 42920-42928; Public Contract Code Sections 12167 and 12167.1; Statutes 1992, Chapter 1116 (AB 3521); Statutes 1999, Chapter 764 (AB 75); State Agency Model Integrated Waste Management Plan (February 2000) Fiscal Years 1999-2000, 2000-2001, 2001-2002, 2002-2003, 2003-2004, 2004-2005, 2005-2006, 2006-2007, 2007-2008, 2008-2009, and 2009-2010

Claimant: Victor Valley Community College District

Incorrect Reduction Claim Filed: July 14, 2014

Decision Adopted: December 1, 2017

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This IRC addresses reductions made by the Controller to reimbursement claims of the Victor Valley Community College District (claimant) for fiscal years 1999-2000 through 2009-2010, under the *Integrated Waste Management* program, 00-TC-07. The Controller made the audit reductions because the claimant did not identify and deduct from its reimbursement claims offsetting cost savings from its diversion of solid waste and the associated reduced or avoided landfill disposal costs.

The Commission finds that the Controller timely initiated the audit of the fiscal year 1999-2000, 2003-2004, and 2005-2006 reimbursement claims and timely completed the audit for all of the reimbursement claims at issue in this matter pursuant to Government Code section 17558.5. Government Code section 17558.5(a) tolls the time to initiate the audit to three years from the date of initial payment on the claim, rather than three years from the date the claim was filed, “if no funds are appropriated or no payment is made to a claimant for the program for the fiscal year for which the claim is filed.” The record shows that the Controller first made payment on the 1999-2000, 2003-2004, and 2005-2006 reimbursement claims on either January 18, 2011,<sup>56</sup> or January 28, 2011,<sup>57</sup> within three years of the date the audit was initiated on January 17, 2014,<sup>58</sup> so the audit was timely initiated. The audit was complete for all reimbursement claims when the final audit report was issued on April 9, 2014,<sup>59</sup> well before the two-year deadline of January 17, 2016.

On the merits, the Commission finds that the audit reductions are partially correct. During the audit period, the claimant diverted solid waste, as required by the test claim statutes, and exceeded the mandated diversion rate (25 or 50 percent) in all years of the audit period. Thus, the Controller correctly presumed, consistent with the test claim statutes and the court’s interpretation of those statutes, and without any evidence to the contrary, that the claimant realized cost savings during the audit period equal to the avoided landfill disposal fee per ton of waste required to be diverted.

The Commission further finds, based on the evidence in the record, that the Controller’s calculation of offsetting cost savings for all calendar years in the audit period, except 2002 and 2003, is correct as a matter of law and not arbitrary, capricious, or entirely lacking in evidentiary support. Because the claimant exceeded the mandate and diverted more solid waste than required by law, the Controller’s cost savings formula “allocated” the diversion by dividing the

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<sup>56</sup> Exhibit A, IRC, page 275.

<sup>57</sup> Exhibit B, Controller’s Late Comments on the IRC, pages 38-40.

<sup>58</sup> Exhibit B, Controller’s Late Comments on the IRC, pages 5, 36. Exhibit A, IRC, page 10.

<sup>59</sup> Exhibit A, IRC, page 26 (Final Audit Report).

percentage of solid waste required to be diverted, either 25 or 50 percent, by the actual percentage of solid waste diverted, as reported by the claimant to the California Integrated Waste Management Board (CIWMB). The resulting quotient was then multiplied by the tons of solid waste diverted, as annually reported by the claimant to CIWMB, multiplied by the avoided landfill disposal fee (based on the statewide average fee).<sup>60</sup> The formula allocates cost savings based on the mandated rates of diversion, and was intended to prevent penalizing the claimant for diverting more solid waste than the amount mandated by law.<sup>61</sup> The claimant has not filed any evidence to rebut the statutory presumption of cost savings or to show that the statewide average disposal fee is incorrect or arbitrary. Thus, the Controller's reduction of costs claimed for these fiscal years is correct.

However, the Controller's reduction of costs claimed for calendar years 2002 and 2003 (the second half of fiscal year 2001-2002, all of fiscal year 2002-2003, and the first half of fiscal year 2003-2004) is incorrect as a matter of law and arbitrary, capricious, and entirely lacking in evidentiary support. During 2002, the claimant achieved a 46.97 percent diversion rate, and in 2003, a 46.3 percent diversion rate.<sup>62</sup> The Controller found that the claimant did not achieve the mandated "50 percent" diversion rate in calendar years 2002 and 2003, although the mandate is to divert at least 25 percent of all solid waste by January 1, 2002, and at least 50 percent of all solid waste by January 1, 2004.<sup>63</sup> Thus, in calendar years 2002 and 2003, community college districts were required to divert only 25 percent, which the claimant exceeded. Therefore, the Controller's finding, that the claimant did not divert the required rate in calendar years 2002 and 2003 is incorrect as a matter of law. Moreover, the Controller's calculation of offsetting savings for this time period, which used 100 percent of the reported diversion and did not reduce cost savings by allocating the diversion to reflect the mandate as it did for other years when the claimant exceeded the mandate, is arbitrary, capricious, or entirely lacking in evidentiary support. Applying the Controller's calculation of cost savings (using 25 percent to calculate the allocated diversion) to calendar years 2002 and 2003, results in offsetting savings of:

- \$6,746 for 2002 (25 percent divided by 46.97 percent, multiplied by 350.4 tons diverted multiplied by the statewide average landfill disposal fee of \$36.17) rather than \$12,674; and
- \$7,105 for 2003 (25 percent divided by 46.3 percent, multiplied by 357.3 tons diverted multiplied by the statewide average landfill disposal fee of \$36.83) rather than \$13,160.

The Commission finds that the law and the record support offsetting cost savings for calendar years 2002 and 2003 of \$13,851, and the difference of \$11,983 has been incorrectly reduced. Therefore, the Commission partially approves this IRC, and requests, pursuant to Government Code section 17551(d) and section 1185.9 of the Commission's regulations, that the Controller reinstate \$11,983 to the claimant.

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<sup>60</sup> Exhibit A, IRC, pages 37-38; Exhibit B, Controller's Late Comments on the IRC, page 22.

<sup>61</sup> Exhibit B, Controller's Late Comments on the IRC, page 22.

<sup>62</sup> Exhibit B, Controller's Late Comments on the IRC, pages 48-53, 94.

<sup>63</sup> Exhibit A, IRC, page 58 (Parameters and Guidelines). This is based on Public Resources Code sections 42921.

## **B. Withdrawn Incorrect Reduction Claims**

The process for resolving IRCs can be complex, and differs with each claim. For some claims, once the claimant files an IRC, an informal conference is conducted where Commission staff mediates the issues in dispute between the claimant and the Controller. If the issues are resolved in the informal conference, the IRC is settled and the claimant withdraws the IRC. The claimant and the Controller can also negotiate a resolution independent of Commission staff. For other claims, an IRC is withdrawn after Commission staff has issued a draft proposed decision but before the proposed decision is heard by the Commission. Even though the IRC is withdrawn, there is still a significant amount of staff resources committed to the preparation of the draft proposed decision.

A total of six IRCs were withdrawn by the claimant between January 1, 2017 and December 31, 2017. Below is a breakdown of those withdrawn IRCs:

### ***Animal Adoption (98-TC-11)***

- 11-9811-I-01
- 13-9811-I-02

### ***Health Fee Elimination (CSM 4206)***

- 09-4206-I-21 and 10-4206-I-36
- 10-4206-I-31

### ***Integrated Waste Management (00-TC-07)***

- 14-0007-I-03

## **STRATEGIC APPROACH TO IRC BACKLOG REDUCTION**

The remaining 13 IRCs are currently tentatively scheduled for hearing between January 2018 and January 2019. However, because IRCs have the lowest priority for hearing, their scheduling may be pushed to a later date if other items with higher priority, such as test claims, are filed. Whether elimination of the IRC backlog will take more time than current staff expectation will depend on a variety of factors, including the time involved to resolve the currently pending and recently reactivated stormwater permit (NPDES) test claims. Fourteen pending test claims addressing stormwater are now active, after a decision was issued by the California Supreme Court on the Los Angeles Municipal Stormwater test claim, and will be prioritized over pending IRCs. These test claims are perhaps the largest (with records exceeding 100,000 pages) and most complex claims that have come before the Commission, and they will take significantly more time and Commission resources than average claims. This already has and will continue to delay completion of the IRC backlog, though continued progress is expected.

The Commission remains committed to continuing to eliminate the entire IRC backlog by generally adhering to the first-in-time policy, unless circumstances justify an exception. The following are strategies the Commission is employing to more efficiently decide matters, with a goal of eliminating the backlog as soon as possible: (1) claim consolidation; and (2) cross cutting issues.

- Claim Consolidation – It may be appropriate in some cases to consolidate IRCs so that one analysis and decision adopted by the Commission support multiple claims. Government Code section 17558.8 and section 1185.6 of the Commission’s regulations allow the executive director to consolidate IRCs. However, consolidation has been used sparingly for IRCs because it only works if the issues of law and fact are the same, and

the Controller's auditors were consistent in making claim reductions based on similar documentation. Commission staff is working with Controller staff and the claimant community to identify situations where claims can be consolidated.

- Cross Cutting Issues – Commission staff is working with the Controller and members of the claimant community to identify issues that are common to multiple IRCs. If the Commission decides an issue in one matter that is contested in other matters, the time required to complete those other matters will be reduced. For example, in 2010, the Commission adopted decisions on the County of Los Angeles and the City of Tustin *Investment Reports* IRCs. Commission staff also conducted several informal conferences with the parties to encourage the informal resolution of the remaining claims. Commission staff prepared stipulations, which were signed by many of the parties, in which the Controller agreed to reevaluate the IRCs on the *Investment Reports* program consistent with the Commission's prior decisions on the IRCs with cross cutting issues. The claimants also agreed to make available to the Controller, as may be requested, all documentation in support of claimed costs. In doing so, the Commission resolved certain issues that were common to nearly all of the *Investment Reports* IRCs and which helped to spur the resolution of the remaining IRCs on that program.