

BEFORE THE
 COMMISSION ON STATE MANDATES
 STATE OF CALIFORNIA

**IN RE INCORRECT REDUCTION CLAIM
 ON:**

Family Code Sections 3060-3064,
 3130-3134.5, 3408, 3411, and 3421;
 Penal Code Sections 277, 278, and 278.5;
 Welfare and Institutions Code Section 11478.5

Statutes 1976, Chapter 1399; Statutes 1992,
 Chapter 162; Statutes 1996, Chapter 988

Fiscal Years 1999-2000, 2000-2001,
 2001-2002, 2003-2004, 2004-2005,
 2005-2006, and 2006-2007

County of Santa Clara, Claimant

Case Nos.: 08-4237-I-02 and 12-4237-I-03

Child Abduction and Recovery

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

(Adopted March 25, 2016)

(Served March 30, 2016)

DECISION

The Commission on State Mandates (Commission) heard and decided this consolidated incorrect reduction claim (IRC) during a regularly scheduled hearing on March 25, 2016. Jim Spano, Chris Ryan, and Masha Vorobyova appeared on behalf of the State Controller’s Office. The County of Santa Clara did not appear, but filed a letter indicating that it was standing on the record submitted.

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

The Commission adopted the proposed decision to deny this IRC by a vote of 6-0 as follows:

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

Summary of the Findings

Incorrect Reduction Claim (IRC) 08-4237-I-02 (fiscal years 1999-2000, 2000-2001, and 2001-2002) and IRC 12-4237-I-03 (fiscal years 2003-2004, 2004-2005, 2005-2006, and 2006-2007)¹ have been consolidated for hearing. These consolidated IRCs challenge the State Controller's Office (Controller's) reductions to reimbursement claims of the County of Santa Clara (claimant) for the *Child Abduction and Recovery* program.

The only issue remaining in contention for this matter is whether the Controller's reductions totaling \$1,183,619 for unsupported salaries, benefits, and related indirect costs claimed for fiscal years 1999-2000 through 2001-2002 and 2003-2004 are correct as a matter of law and not arbitrary, capricious, or entirely lacking in evidentiary support.

To claim costs for employee salaries and benefits, the parameters and guidelines require that the claimant either specify the actual number of hours devoted to each mandated function and provide source documents or worksheets that show evidence of the validity of the costs, or claim costs based on the average number of hours devoted to each mandated function if supported by a documented time study. Average time accountings to support employee time claimed "can be deemed akin to worksheets."² However, the time study is still required to "show evidence of and the validity of [the] costs [claimed]" for the mandated program.³

The Commission finds that the Controller's reduction of costs claimed for fiscal year 1999-2000 through 2001-2002 is correct as a matter of law, and not arbitrary, capricious, or entirely lacking in evidentiary support. The payroll documentation originally provided by the claimant to the Controller, which does not verify the time spent on the program, does not comply with the documentation requirements of the parameters and guidelines. Moreover, based on the evidence in the record, the Controller's decision to reject the time study that claimant later prepared using data from later fiscal years as inadequate documentation to support the costs claimed for all the employees is not arbitrary, capricious, or entirely lacking in evidentiary support. The record shows that the Controller considered the claimant's arguments and all relevant factors, and has demonstrated a rational connection between those factors and the decision made to reject the time study. The Commission cannot substitute its judgment for that of the Controller on audit decisions.

The Commission also finds that the Controller's reduction of salary and benefit costs for fiscal year 2003-2004 is not arbitrary, capricious, or entirely lacking in evidentiary support. For this reimbursement claim, the claimant resubmitted the same four week time study conducted from November 15, 2004, through December 10, 2004 to support fiscal year 2003-2004 claimed costs, with a summary of the time study results and a projection of the results to a full fiscal year. The Controller determined, however, that the claimant's time study did not adequately support the time claimed for fiscal year 2003-2004 because the time study included three employee classifications that the county did not include in their claim for reimbursement; the time study period included a holiday week when employees worked fewer hours; and actual timesheets kept for January 2005 through June 2005 showed varying changes in staffing levels and workload.

¹ Note that there was no audit for 2002-2003 and that year is not in issue in this IRC.

² *Clovis Unified School Dist. v. Chiang* (2010) 188 Cal.App.4th 794, 804.

³ Exhibit A, Incorrect Reduction Claim 08-4237-I-02, pages 53-60.

Since the claimant did not provide time logs or other adequate documentation supporting the time spent on the mandate in fiscal year 2003-2004, the Controller extrapolated employee hours identified on timesheets for January 2005 through June 2005 to approximate the actual hours spent on the program for the 2003-2004 fiscal year, instead of reducing costs to \$0. The Commission finds that there is no evidence in the record that the Controller's rejection of the claimant's time study or the Controller's calculation of employee costs for fiscal year 2003-2004, is arbitrary, capricious, or entirely lacking in evidentiary support.

Therefore, the Commission denies these IRCs.

I. Chronology

- 03/17/2006 Controller issued the final audit report for fiscal years 1999-2000 through 2001-2002.⁴
- 01/28/2009 Claimant filed IRC 08-4237-I-02.⁵
- 12/04/2009 Controller issued the final audit report for fiscal years 2003-2004 through 2006-2007.⁶
- 11/29/2012 Claimant filed IRC 12-4237-I-03.⁷
- 12/22/2014 Controller filed Late Comments on IRC 08-4237-I-02.⁸
- 12/22/2014 Controller filed Late Comments on IRC 12-4237-I-03.
- 12/31/2014 Controller filed Revised Late Comments on IRC 12-4237-I-03.⁹
- 04/02/2015 Claimant filed Rebuttal to Controller's Late Comments on IRC 08-4237-I-02.¹⁰
- 04/02/2015 Claimant filed Rebuttal to Controller's Late Comments on IRC 12-4237-I-03.¹¹
- 1/13/2016 Commission staff issued the Draft Proposed Decision.¹²
- 1/15/2015 Controller filed Comments on the Draft Proposed Decision.¹³

⁴ Exhibit A, Incorrect Reduction Claim 08-4237-I-02, page 19.

⁵ Exhibit A, Incorrect Reduction Claim 08-4237-I-02, page 1.

⁶ Exhibit B, Incorrect Reduction Claim 12-4237-I-03, page 16.

⁷ Exhibit B, Incorrect Reduction Claim 12-4237-I-03, page 1.

⁸ Exhibit C, Controller's Late Comments on IRC 08-4237-I-02, page 1.

⁹ Exhibit D, Controller's Revised Late Comments on IRC 12-4237-I-03, page 1. Note that these revised comments simply replaced illegible pages with legible ones and these revised comments filed December 31, 2014 replace the late comments filed December 22, 2014.

¹⁰ Exhibit E, Claimant's Rebuttal to Controller's Late Comments on IRC 08-4237-I-02, page 1.

¹¹ Exhibit F, Claimant's Rebuttal to Controller's Late Comments on IRC 12-4237-I-03, page 1.

¹² Exhibit G, Draft Proposed Decision.

¹³ Exhibit H, Controller's Comments on the Draft Proposed Decision.

3/22/2016 Claimant filed a letter with the Commission indicating that a representative of the county would not be present at the hearing and that it stands on the record submitted.

II. Background

A. Child Abduction and Recovery Program

On September 19, 1979, the Board of Control approved a test claim filed by the County of San Bernardino, finding that the test claim statutes imposed a reimbursable state-mandated program on counties by requiring district attorney offices to actively assist in the resolution of child custody problems, including visitation disputes and the enforcement of custody and other orders of the court in a child custody proceeding. These activities include actions necessary to locate and return a child; the enforcement of child custody orders, orders to appear; or any other court order defraying expenses related to the return of an illegally detained, abducted, or concealed child; proceeding with civil court actions; and guaranteeing the appearance of offenders and minor in court actions. Reimbursement was found not to be required for the costs associated with criminal prosecutions under the Penal Code.¹⁴

On January 21, 1981, the Board of Control adopted the parameters and guidelines for this program for costs incurred beginning January 1, 1977. Since the adoption of the original parameters and guidelines, the test claim statutes have been renumbered and some have been amended.¹⁵ In addition, the parameters and guidelines have been amended several times. The parameters and guidelines that govern the reimbursement claims at issue in this case were amended on August 26, 1999, and provide that counties may claim reimbursement for the following activities:

1. Obtaining compliance with court orders relating to child custody or visitation proceedings and the enforcement of child custody or visitation orders, including:
 - a. Contact with child(ren) and other involved persons.

¹⁴ Exhibit A, Incorrect Reduction Claim 08-4237-I-02, pages 43-50 (parameters and guidelines, as amended July 22, 1993), 53-60 (parameters and guidelines, as amended August 26, 1999).

¹⁵ Exhibit A, Incorrect Reduction Claim 08-4237-I-02, pages 53-54 (parameters and guidelines, as amended August 26, 1999), which explain under the Summary of Mandate section of the parameters and guidelines, the statutory changes as follows:

Chapter 990, Statutes of 1983, amended Section 4604 of the Civil Code to clarify that the enforcement requirements of this section applied to visitation decrees as well as custody decrees.

Chapter 162, Statutes of 1992, repealed Sections 4600.1, 4604, 5157, 5160, and 5169 of the Civil Code and without substantial change enacted Sections 3060 to 3064, 3130 to 3134.5, 3408, 3411, and 3421 of the Family Code.

Chapter 988, Statutes of 1996, the Parental Kidnapping Prevention Act, repealed Sections 277, 278 and 278.5 of the Penal Code and enacted in a new statutory scheme in Sections 277, 278 and 278.5 which eliminated the distinction between cases with and cases without a preexisting child custody order.

- (1) Receipt of reports and requests for assistance.
 - (2) Mediating with or advising involved individuals. Mediating services may be provided by other departments. If this is the case, indicate the department.
 - (3) Locating missing or concealed offender and child(ren).
- b. Utilizing any appropriate civil or criminal court action to secure compliance.
- (1) Preparation and investigation of reports and requests for assistance.
 - (2) Seeking physical restraint of offenders and/or the child(ren) to assure compliance with court orders.
 - (3) Process services and attendant court fees and costs.
 - (4) Depositions.
- c. Physically recovering the child(ren).
- (1) Travel expenses, food, lodging, and transportation for the escort and child(ren).
 - (2) Other personal necessities for the child. All such items purchased must be itemized.
2. Court actions and costs in cases involving child custody or visitation orders from another jurisdiction, which may include, but are not limited to, utilization of the Uniform Child Custody Jurisdiction Act (Family Code Sections 3400 through 3425) and actions relating to the Federal Parental Kidnapping Prevention Act (42 USC 1738A) and The Hague Convention of 25 October 1980 on the Civil Aspects of International Child Abduction (Senate Treaty Document 99-11, 99th Congress, 1st Session).
- a. Cost of providing foster care or other short-term care for any child pending return to the out-of-jurisdiction custodian. The reimbursable period of foster home care or other short-term care may not exceed three days unless special circumstances exist.
- Please explain the special circumstances. A maximum of ten days per child is allowable. Costs must be identified per child, per day. This cost must be reduced by the amount of state reimbursement for foster home care which is received by the county for the child(ren) so placed.
- b. Cost of transporting the child(ren) to the out-of-jurisdiction custodian.
- (1) Travel expenses, food, lodging, and transportation for the escort and child(ren).
 - (2) Other personal necessities for the child(ren). All such items purchased must be itemized. Cost recovered from any party, individual or agency, must be shown and used as an offset against costs reported in this section.
 - (3) Securing appearance of offender and/or child(ren) when an arrest warrant has been issued or other order of the court to produce the offender or child(ren).
 - (a) Cost of serving arrest warrant or order and detaining the individual in custody, if necessary, to assure appearance in accordance with the arrest warrant or order.
 - (b) Cost of providing foster home care or other short-term care for any child

requiring such because of the detention of the individual having custody. The number of days for the foster home care or short-term care shall not exceed the number of days of the detention period of the individual having physical custody of the minor.

- (4) Return of an illegally obtained or concealed child(ren) to the legal custodian or agency.
 - (a) Costs of food, lodging, transportation and other personal necessities for the child(ren) from the time he/she is located until he/she is delivered to the legal custodian or agency. All personal necessities purchased must be itemized.
 - (b) Cost of an escort for the child(ren), including costs of food, lodging, transportation and other expenses where such costs are a proper charge against the county. The type of escort utilized must be specified.¹⁶

Section VI. of these parameters and guidelines describe the non-reimbursable costs as follows: “Costs associated with criminal prosecution, commencing with the defendant’s first appearance in a California court, for offenses defined in Sections 278 or 278.5 of the Penal Code, wherein the missing, abducted, or concealed child(ren) has been returned to the lawful person or agency.”

Section VII. of these parameters and guidelines further require that claimed costs “shall be supported” by cost element information, as specified. With respect to claims for salaries and benefits, claimants are required to:

Identify the employee(s), show the classification of the employee(s) involved, describe the mandated functions performed and specify the actual number of hours devoted to each function, the productive hourly rate, and the related benefits. The average number of hours devoted to each function may be claimed if supported by a documented time study. Benefits are reimbursable; however, benefit rates must be itemized. If no itemization is submitted, 21 percent must be used for computation of claimed cost.

Section VIII. further requires that “all costs claimed must be traceable to source documents and/or worksheets that show evidence of and the validity of such costs,” and that these “documents must be kept on file by the agency submitting the claim for [the audit] period specified in Government Code section 17558.5.” However, contemporaneous source documentation was not required by these parameters and guidelines.

B. The Audit Findings of the Controller

The audit report for fiscal years 1999-2000 through 2001-2002 reduced costs by \$1,278,468 because claimant overstated productive hourly rates when calculating employee salaries and benefits (Finding 1) and claimed unsupported salaries, benefits, and related indirect costs (Finding 2).¹⁷ The audit report for fiscal years 2003-2004 through 2006-2007 reduced costs by

¹⁶ Exhibit A, Incorrect Reduction Claim 08-4237-I-02, pages 53-60 (parameters and guidelines, as amended August 26, 1999).

¹⁷ Exhibit A, Incorrect Reduction Claim 08-4237-I-02, pages 18-38. The audit report also reduced costs in Finding 3 for overstated indirect costs, which are not challenged by the claimant.

\$296,732 on similar grounds: the claimant overstated productive hourly wage rates in all audit years (Finding 1) and claimed unsupported salaries, benefits, and related indirect costs in fiscal year 2003-2004 (Finding 2).¹⁸

The claimant originally challenged both findings made by the Controller. After the IRCs were filed, however, the claimant withdrew the challenge to audit Finding 1 in both audit reports relating to the reduction of costs based on overstated productive hourly rates.¹⁹ Thus, the claimant now only challenges the reductions in Finding 2 of the audit reports for unsupported salaries and benefits and related indirect costs claimed for fiscal years 1999-2000 through 2001-2002 and 2003-2004, totaling \$1,183,619, described as follows:²⁰

- The Controller reduced costs for salaries and benefits claimed for fiscal years 1999-2000 through 2001-2002 for two full-time employees in the claimant's Child Abduction and Recovery Unit because the county did not provide any documentation to support mandate-related hours claimed. In addition, one of the full-time employees stated that she spent part of her time assisting with criminal trial preparation after the defendant's first court appearance, which is not eligible for reimbursement. Moreover, the time study later submitted by the claimant shows that the two full-time employees worked between 42.50 and 69.27 percent and 60 and 92.94 percent, respectively, on the mandated program during the four week time study,²¹ which contradicts the claimant's assertion that the full-time employees performed only mandate-related activities during the audit period.

The Controller also partially reduced costs claimed for the remaining employees working part-time on the program in these fiscal years because the county provided time logs that did not support all of the mandate-related hours claimed. The time logs identified mandate-related time, non-mandate related time, and non-productive time, but did not reconcile and support the hours claimed. Subsequently, the claimant submitted a four-week time study conducted in fiscal year 2004-2005 in lieu of the employee time logs, which the Controller rejected because the time study is not competent evidence to replace time logs provided to support the costs claimed for earlier fiscal years. In addition, the Controller found that the county did not identify how the time period studied (four weeks in fiscal year 2004-2005) was representative of the costs incurred in fiscal years 1999-2000 through 2001-2002, and did not show how the results could be projected to approximate actual costs for the audit period. The Controller concluded that a time study

¹⁸ Exhibit B, Incorrect Reduction Claim 12-4237-I-03, pages 15-43. Finding 3 of this audit report also finds understated salaries, benefits, and related indirect costs for one employee, which occurred as result of an input error in the claimant's payroll system. The adjustment in Finding 3 is not disputed.

¹⁹ Exhibit E, Claimant's Rebuttal to Controller's Late Comments on IRC 08-4237-I-02, page 4; Exhibit F, Claimants Rebuttal to Controller's Late Comments on IRC 12-4237-I-03, page 4.

²⁰ Exhibit A, Incorrect Reduction Claim 08-4237-I-02, page 28; Exhibit B, Incorrect Reduction Claim 12-4237-I-03, page 31.

²¹ Exhibit C, Controller's Late Comments on IRC 08-4237-I-02, pages 16 and 43 (Tab 8, Controller's Analysis of Paralegal and Legal Clerk Time Study Hours).

is not appropriate since the entire program requires varying levels of effort and includes activities that are not mandated by the state.

The Controller, therefore, allowed reimbursement for salaries and benefits for fiscal years 1999-2000 through 2001-2002 based on mandate-related hours supported by employee time logs.

- The Controller reduced costs for salaries and benefits claimed for fiscal year 2003-2004 because the claimant did not provide documentation to support the mandate-related hours claimed. Instead, the claimant resubmitted the four week time study from fiscal year 2004-2005 with a summary of the results and a projection of the results to estimate costs for 2003-2004. However, the Controller found that the time study was still not representative of the 2003-2004 costs because the time study included three employee classifications that the county did not include in their claim for reimbursement; the time study period included a holiday week when employees worked fewer hours; and actual timesheets kept from January 2005 through June 2005 showed varying changes in staffing levels and workload.

The Controller, therefore, rejected the claimant's time study and, instead, extrapolated the employee hours identified on the timesheets for January 2005 through June 2005 to approximate the actual hours spent on the program for the 2003-2004 fiscal year.

III. Positions of the Parties

A. County of Santa Clara

The claimant contends that the Controller's reductions for salary, benefits, and related indirect costs are incorrect and should be reinstated. For fiscal years 1999-2000 through 2001-2002, the claimant asserts that the employees working full-time on the mandated program should not be required to provide time logs, and that payroll documentation for these employees is sufficient, alone, to substantiate the hours claimed for full-time employees. The claimant argues in its rebuttal to the Controller's comments that while the "SCO response devalues the time study because it does not show that the County employees worked on mandate-related activities on a full-time basis...it does show that a percentage of these employees time was spent on mandate-related activities and the County should be reimbursed for this time."²²

The claimant also asserts that it provided time logs to substantiate the hours spent in mandate activities for those employees who did not perform mandate-activities full time.²³ The claimant asserts that "to the extent that the SCO believed that the time logs were insufficient, a time study was performed from November 15, 2004 through December 10, 2004."²⁴ The claimant argues that "[t]he county did perform a time study in FY 2004-2005 to support costs claimed for FY 1999-2000, FY 2000-2001, and FY 2001-2002 because the source document requirement was not in the Commission's parameters and guidelines at the time the mandate claim was filed."²⁵ The claimant further argues that to the extent the Controller felt the time logs provided

²² Exhibit E, Claimant's Rebuttal to Controller's Late Comments on IRC 08-4237-I-02, page 5.

²³ Exhibit A, Incorrect Reduction Claim 08-4237-I-02, page 15.

²⁴ Exhibit A, Incorrect Reduction Claim 08-4237-I-02, page 15.

²⁵ Exhibit E, Claimant's Rebuttal to Controller's Late Comments on IRC 08-4237-I-02, page 5.

were insufficient, the time study performed provides a reliable measure of the time needed to perform mandated activities and that the Controller should rely on a current time study to support the hours claimed.²⁶ The claimant argues that the time study relied on contemporaneous documentation of mandated and non-mandated activities to fully account for the time; that it covered four weeks that corresponded with pay periods to assure that the time study documentation could be checked against payroll information; and that all employees performing mandated activities participated in order to eliminate errors due to small sample size or extrapolation. Further, the claimant argues that the time study is representative of a full fiscal year because the activities related to the program are not seasonal and have not changed appreciably over time.²⁷

For fiscal year 2003-2004, the claimant makes similar arguments regarding the appropriateness of the fiscal year 2004-2005 time study to support the costs claimed. The claimant also argues that the time study was done “in close proximity to the claim period and for a reasonable length of time to merit acceptance as representative of the fiscal year.” The claimant asserts that the Controller failed to recognize that the time study substantiated the County’s claims and wrongfully applied its own standard.²⁸

Claimant did not file comments on the draft proposed decision.

B. State Controller’s Office

It is the Controller’s position that the audit adjustments are correct and that these IRCs should be denied. The Controller states that unallowable salary, benefits, and indirect costs were claimed because the claimant did not provide any documentation to support the hours claimed for two full-time employees, and that for other employees the county provided time logs that did not support the hours claimed and included time for non-mandate-related activities. The Controller argues that claimant has not complied with the documentation requirements of the parameters and guidelines by merely providing payroll documentation in support of the costs claimed for full-time employees for fiscal years 1999-2000 through 2001-2002. The Controller further found that for fiscal years 1999-2000, 2000-2001, and 2001-2002, a time study conducted during fiscal year 2004-2005 and provided in lieu of time logs was not competent evidence to replace time logs in support of the costs claimed. For fiscal year 2003-2004, the Controller found that the county did not support costs claimed with source documents showing the evidence of and the validity of such costs and that the 18-day time study in fiscal year 2004-2005, was not representative of the audit period.

On January 15, 2016, the Controller filed comments on the draft proposed decision, supporting the Commission’s conclusion and recommendation.

IV. Discussion

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

²⁶ Exhibit A, Incorrect Reduction Claim 08-4237-I-02, page 15.

²⁷ *Id.*

²⁸ Exhibit B, Incorrect Reduction Claim 12-4237-I-03, page 12.

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 6.²⁹ 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 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 Under this standard, the courts have found that:

When reviewing the exercise of discretion, "[t]he scope of review is limited, out of deference to the agency's authority and presumed expertise: 'The court may not reweigh the evidence or substitute its judgment for that of the agency. [Citation.]'"... "In general...the inquiry is limited to whether the decision was arbitrary, capricious, or entirely lacking in evidentiary support..." [Citations.] When making that inquiry, the " "court must ensure that an agency has adequately considered all relevant factors, and has demonstrated a rational connection between those factors, the choice made, and the purposes of the enabling statute." [Citation.]' "³²

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.³³ In addition, section 1185.1(f)(3) and 1185.2(c) of the Commission's regulations requires that any assertions of fact

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

³⁰ *County of Sonoma v. Commission on State Mandates* (2000) 84 Cal.App.4th 1264, 1280, 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 *American Bd. of Cosmetic Surgery, Inc., v. Medical Bd. of California* (2008) 162 Cal.App.4th 534, 547-548.

³³ *Gilbert v. City of Sunnyvale* (2005) 130 Cal.App.4th 1264, 1274-1275.

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.³⁴

The Controller's Reduction of Costs for Employee Salaries, Benefits, and Related Indirect Costs Is Correct as a Matter of Law and Not Arbitrary, Capricious, or Entirely Lacking in Evidentiary Support.

08-4237-I-02 (fiscal years 1999-2000, 2000-2001, and 2001-2002) and 12-4237-I-03 (fiscal years 2003-2004, 2004-2005, 2005-2006, and 2006-2007)³⁵ have been consolidated for hearing. These consolidated IRCs challenge the Controller's reductions to reimbursement claims filed by claimant for the *Child Abduction and Recovery* program.

The only issue remaining in contention for this matter is whether the Controller's reductions totaling \$1,183,619 for unsupported salaries, benefits, and related indirect costs claimed for fiscal years 1999-2000 through 2001-2002 and 2003-2004 are correct as a matter of law and not arbitrary, capricious, or entirely lacking in evidentiary support.

Reimbursement claims filed with the Controller are required as a matter of law to be filed in accordance with the parameters and guidelines adopted by the Commission.³⁶ Parameters and guidelines provide instructions for eligible claimants to prepare reimbursement claims for the direct and indirect costs of a state-mandated program, and also identify the supporting documentation required to be retained.³⁷

As indicated in the Background, the parameters and guidelines amended by the Commission on August 26, 1999, apply to these reimbursement claims.³⁸ Section VII.A.1. of the parameters and guidelines provide instructions on how to claim costs for employee salaries and benefits as follows:

Identify the employee(s), show the classification of the employee(s) involved, describe the mandated functions performed and specify the actual number of hours devoted to each function, the productive hourly rate, and the related

³⁴ 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.

³⁵ Note that there was no audit for 2002-2003 and it is unclear whether or not a reimbursement claim was filed in that year but that year is not in issue in this IRC.

³⁶ 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.

³⁷ Government Code section 17557; California Code of Regulations, title 2, section 1183.7.

³⁸ Exhibit A, Incorrect Reduction Claim 08-4237-I-02, page 7; Exhibit B, Incorrect Reduction Claim 12-4237-I-03, page 4, Exhibit C, Controller's Late Comments on IRC 08-4237-I-02, page 8; Exhibit D, Controller's Revised Late Comments on IRC 12-4237-I-03, page 9.

benefits. The average number of hours devoted to each function may be claimed if supported by a documented time study. Benefits are reimbursable; however, benefits rates must be itemized. If no itemization is submitted, 21 percent must be used for computation of claimed costs.

Section VIII. of the parameters and guidelines also requires that costs claimed “be traceable to source documents and/or worksheets that show evidence of and the validity of such costs.”³⁹

Therefore the parameters and guidelines require that the claimant either specify the actual number of hours devoted to each mandated function and provide source documents or worksheets that show evidence of the validity of the costs, or claim costs based on the average number of hours devoted to each mandated function if supported by a documented time study. Average time accountings to support employee time claimed “can be deemed akin to worksheets.”⁴⁰ However, the time study is still required to “show evidence of and the validity of [the] costs [claimed]” for the mandated program.⁴¹

For the reasons discussed below, the Commission finds that the reduction costs claimed for employee salaries, benefits, and related indirect costs is correct as a matter of law and not arbitrary, capricious, or entirely lacking in evidentiary support.

A. The Controller’s Reduction of Costs for Fiscal Years 1999-2000 Through 2001-2002 Is Correct as a Matter of Law and Not Arbitrary, Capricious, or Entirely Lacking in Evidentiary Support.

1. Reduction of costs for full-time employees

The Controller reduced salary and benefit costs claimed for fiscal years 1999-2000 through 2001-2002 for two full-time employees because the county did not provide adequate documentation to support mandate-related *hours* claimed. The claimant originally provided payroll documents to support the costs claimed for these employees, and asserts that the provision of payroll documentation for full-time employees should be sufficient to substantiate the hours claimed.⁴² However, payroll documentation does not show the actual number of hours the employees worked on mandated activities, as required by the parameters and guidelines. In addition, the reimbursement claims for fiscal years 1999-2000, 2000-2001, and 2001-2002, list the employee names, job classifications, and a brief description of the activities performed, but do not identify the actual number of hours devoted to each reimbursable function.⁴³ Further, the Controller noted that one of the full-time employees stated during the audit that she did not work full-time on mandate-related activities, and that she assisted in trial preparation after the

³⁹ Exhibit A, Incorrect Reduction Claim 08-4237-I-02, pages 58, 60; Exhibit B, Incorrect Reduction Claim 12-4237-I-03, pages 50, 52.

⁴⁰ *Clovis Unified School Dist. v. Chiang* (2010) 188 Cal.App.4th 794, 804.

⁴¹ Exhibit A, Incorrect Reduction Claim 08-4237-I-02, page 60 (parameters and guidelines, amended August 26, 1999).

⁴² Exhibit A, Incorrect Reduction Claim 08-4237-I-02, page 37.

⁴³ Exhibit A, Incorrect Reduction Claim 08-4237-I-02, pages 82, 117-118, 155.

defendant's first court appearance, which is not eligible for reimbursement.⁴⁴ There is no evidence in the record contradicting this statement.

Therefore, for full-time employees, the payroll documentation provided by the claimant does not comply with the requirements of the parameters and guidelines to support the actual number of hours devoted to each reimbursable function.

The claimant then tried to support the salary and benefit costs claimed for fiscal years 1999-2000, 2000-2001, and 2001-2002 by providing to the Controller a four-week time study of the program, conducted from November 15, 2004, through December 10, 2004. The claimant states that the time study relied on contemporaneous documentation of mandated and non-mandated activities to fully account for the time; that it covered four weeks that corresponded with pay periods to assure that the time study documentation could be checked against payroll information; and that all employees performing mandated activities participated in order to eliminate errors due to small sample size or extrapolation. Further, the claimant argues that the time study is representative of a full fiscal year because the activities related to the program are not seasonal and the time spent on the program has not changed appreciably over time.⁴⁵

The Controller, however, rejected the time study because it does not adequately support the costs claimed for these employees. The Controller found that the time study specifically contradicted the claimant's assertion that the full-time employees worked on mandate activities full-time. The two full-time employees, a paralegal and legal clerk, reported the following percentages of time spent on mandate activities for the time study period:

	<u>Week 1</u>	<u>Week 2</u>	<u>Week 3</u>	<u>Week 4</u>
Paralegal	91.50%	0.00%	60.00%	92.94%
Legal Clerk	47.44%	42.50%	67.78%	69.27% ⁴⁶

The claimant admits that the time study shows less than full-time hours for these employees, but argues that it should be reimbursed for the time identified in the study.⁴⁷ The claimant states that while the "SCO response devalues the time study because it does not show that the County employees worked on mandate-related activities on a full-time basis...it does show that *a percentage of these employees time* was spent on mandate-related activities and the County should be reimbursed for this time."⁴⁸

However, the Controller found that the time study itself, was not representative of the costs claimed for fiscal years 1999-2000, 2000-2001, and 2001-2002. The mandate-related hours

⁴⁴ Exhibit A, Incorrect Reduction Claim 08-4237-I-02, page 30; Exhibit C, Controller's Late Comments on IRC 08-4237-I-02, page 16.

⁴⁵ *Id.*

⁴⁶ Exhibit C, Controller's Late Comments on IRC 08-4237-I-02, pages 16, 43 (Tab 8, Controller's Analysis of Paralegal and Legal Clerk's Time Study Hours).

⁴⁷ Exhibit E, Claimant's Rebuttal to Controller's Late Comments on IRC 08-4237-I-02, page 5.

⁴⁸ Exhibit E, Claimant's Rebuttal to Controller's Late Comments on IRC 08-4237-I-02, page 5 (emphasis added).

reported during the time study, 606.5 hours,⁴⁹ extrapolates to approximately 7,885 mandate-related hours annually.⁵⁰ However, for the fiscal year in which the time study was done (2004-2005), the county only claimed 3,335 mandate-related hours.⁵¹ In addition, and as more fully explained in the next section below, the Controller found that the time spent on this state-mandated program varied from year to year and was not constant and, thus, the time study does not adequately support the time spent on the program during these earlier fiscal years.⁵²

The Commission finds that the Controller's full reduction of costs for these employees is correct as a matter of law, and not arbitrary, capricious, or entirely lacking in evidentiary support. As indicated above, the payroll documentation originally provided by the claimant, which does not verify the time spent on the program, does not comply with the documentation requirements of the parameters and guidelines. Moreover, based on the evidence in the record, the Controller's decision to reject the time study as inadequate documentation to support the costs claimed is not arbitrary, capricious, or entirely lacking in evidentiary support. The Commission cannot substitute its judgment for that of the Controller on audit decisions to reject the time study. With respect to audit decisions of the Controller, the Commission need only determine if the Controller "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."⁵³ The Commission finds that the Controller has met this burden. Based on the evidence in the record, the Controller's finding that the time study does not support or "show evidence of and the validity of [the] costs [claimed]" for the full-time employees is not arbitrary, capricious, or entirely lacking in evidentiary support.

Accordingly, the Commission finds that the claimant did not comply with the documentation requirements of the parameters and guidelines and, thus, the Controller's reduction of all costs claimed for the full-time employees is correct as a matter of law, and not arbitrary, capricious, or entirely lacking in evidentiary support.

2. Reduction of costs for the remaining employees

The Controller also partially reduced the costs claimed for the remaining employees that worked on this program part-time in these fiscal years because the county provided time logs, but the time logs did not support all of the mandate-related hours claimed. The time logs identified mandate-related time, non-mandate related time, and non-productive time, but did not reconcile

⁴⁹ Exhibit C, Controller's Late Comments on IRC 08-4237-I-02, page 45 (Tab 9, Analysis of Time Study).

⁵⁰ The time study occurred over a 4 week period, including Thanksgiving Break: 606.5 hour/4 weeks equals: 151.625 mandated-hours per week. Multiplied by 52 weeks is 7884.5 hours. See also, Exhibit C, Controller's Late Comments on IRC 08-4237-I-02, page 16.

⁵¹ Exhibit C, Controller's Late Comments on IRC 08-4237-I-02, pages 16, 56 (Tab 10, Santa Clara County's Total Mandate-Related Hours Claimed).

⁵² Exhibit C, Controller's Late Comments on IRC 08-4237-I-02, pages 16, 51-56 (Tab 10, Santa Clara County's Total Mandate-Related Hours Claimed).

⁵³ *American Bd. of Cosmetic Surgery, Inc.*, *supra*, 162 Cal.App.4th 534, 547-548.

and support the hours claimed. The Controller allowed the time supported by documentation as required by the parameters and guidelines, and reduced the unsupported costs claimed.⁵⁴

Subsequently, the claimant submitted the four-week time study conducted in November and December 2004 *in lieu* of the employee time logs to support the costs claimed for these employees, which the Controller rejected. The Controller found that the time-study (conducted in 2004) was not competent evidence to replace actual time records provided for costs claimed for fiscal years 1999-2000 through 2001-2002, and that the time study results did not represent the time spent on the program in the fiscal years claimed.⁵⁵ Further, in the time study plan overview, the claimant also asserts that “the activities in this mandate do not vary by the time of year.”⁵⁶ However, the Controller found that neither the time study, nor the claimant’s annual reimbursement claims, support the claimant’s assertion that the workload is constant as follows:

[T]he Child Recovery Unit Lieutenant Investigator testified that the unit routinely loaned investigators to other units because of shortages or not enough work in the Child Recovery Unit. Furthermore, the county’s claims show significant workload variance from year to year based on total mandate-related hours that the county reported...

<u>Fiscal Year</u>	<u>Total Mandated-Related Hours Reported</u>
1999-2000	10,694
2000-01	14,150
2001-02	13,531
2002-03	12,814
2003-04	7,783
2004-05	3,334 ⁵⁷

The Commission finds that the Controller’s audit decision to reject the time study as inadequate documentation to support the costs claimed is not arbitrary, capricious, or entirely lacking in evidentiary support. The record shows that the Controller considered the claimant’s arguments and all relevant factors, and has demonstrated a rational connection between those factors and the decision made.⁵⁸ The claimant has not filed any evidence rebutting the Controller’s findings on the variability of time spent on mandated activities in the fiscal years reported. Therefore, the Commission is required to defer to the Controller’s audit decision.⁵⁹

Accordingly, based on the evidence in this record, the Commission finds that the claimant did not comply with the documentation requirements of the parameters and guidelines and, thus, the Controller’s partial reduction of costs claimed for employees working on the program on a part-

⁵⁴ Exhibit A, Incorrect Reduction Claim 08-4237-I-02, pages 28, 58, 60.

⁵⁵ Exhibit A, Incorrect Reduction Claim 08-4237-I-02, pages 30-31.

⁵⁶ Exhibit A, Incorrect Reduction Claim 08-4237-I-02, page 190.

⁵⁷ *Id.*, page 31.

⁵⁸ *American Bd. of Cosmetic Surgery, Inc.*, *supra*, 162 Cal.App.4th 534, 547-548.

⁵⁹ *Ibid.*

time basis in fiscal years 1999-2000, 2000-2001, and 2001-2002 is correct as a matter of law and not arbitrary, capricious, or entirely lacking in evidentiary support.

B. The Controller's Reduction of Costs for Fiscal Year 2003-2004 Is Not Arbitrary, Capricious, or Entirely Lacking in Evidentiary Support.

For fiscal year 2003-2004, the claimant did not provide time logs or payroll documentation to support the costs claimed, but resubmitted the four week time study conducted from November 15, 2004, through December 10, 2004 to support fiscal year 2003-2004 claimed costs, with a summary of the time study results and a projection of the results to a full fiscal year.⁶⁰ However, the Controller found that the time study was still not representative of the 2003-2004 costs because the time study included three employee classifications that the county did not include in their claim for reimbursement; the time study period included a holiday week when employees worked fewer hours; and actual timesheets kept from January 2005 through June 2005 showed varying changes in staffing levels and workload.⁶¹ The Controller, therefore, rejected the claimant's time study and, instead, extrapolated the employee hours identified on the timesheets for January 2005 through June 2005 to approximate the actual hours spent on the program for the 2003-2004 fiscal year.⁶² The Controller's audit resulted in a partial reduction of salary, benefit, and related indirect costs totaling \$169,848.⁶³

The claimant argues that the Controller wrongfully applied its own standard and failed to recognize the time study the claimant provided, which substantiates the claim.⁶⁴ The claimant argues that the time study provided is a reliable measure of the time needed to perform the mandated activities as follows:

The time study relied on contemporaneous documentation of the mandated and non-mandated activities to provide a full accounting of time; it covered four weeks that corresponded with pay periods to assure that the time study documentation could be checked back against payroll information; it was done in close proximity to the claim period and for a reasonable length of time to merit acceptance as representative of the fiscal year; and all employees performing mandated activities participated to eliminate any errors that could have occurred due to small sample size or extrapolation. Moreover, because the activities related to the program are not seasonal and have not changed appreciably over time, the November-December 2004 time study is a reliable indicator of the time spent on the same activities during the claiming period in question.⁶⁵

⁶⁰ Exhibit B, Incorrect Reduction Claim 12-4237-I-03, page 31.

⁶¹ Exhibit B, Incorrect Reduction Claim 12-4237-I-03, page 13, 31.

⁶² Exhibit B, Incorrect Reduction Claim 12-4237-I-03, page 32.

⁶³ Exhibit B, Incorrect Reduction Claim 12-4237-I-03, page 31.

⁶⁴ Exhibit B, Incorrect Reduction Claim 12-4237-I-03, page 12.

⁶⁵ *Id.*

In their response to the draft audit report, the claimant also argues that the time study was conducted close in proximity to the claim period and for a reasonable length of time to be representative of the claim period.⁶⁶

The Controller found the time study does not adequately represent the costs claimed for fiscal year 2003-2004.⁶⁷ The evidence in the record supports the Controller's decision. For example, the four week time study period included the Thanksgiving holiday, in which three employees did not work at all, and the remaining time-studied employees worked fewer hours.⁶⁸ The subsequent timesheets submitted for January 2005 through June 2005 also contradict the claimant's assertion that there were no substantial staffing level or workload changes within the program. County employees maintained actual timesheets for the period of January 2005 through June 2005. During that time, employees documented monthly mandate-related time between 440.5 hours and 662.5 hours, a variance of 50 percent.⁶⁹ The Controller concluded that this variance of 50 percent shows that the time study of 18 work days is not representative of the fiscal year 2003-2004 costs.⁷⁰ Further, the time study results for the seven employees the county claimed do not support the mandate-related hours claimed for fiscal year 2003-2004. For fiscal year 2003-2004 the county claimed 7,783 mandate-related hours attributable to seven employees.⁷¹ However an extrapolation of the time study hours for these same seven employees total only 6,646.25 mandate-related hours.⁷²

The Commission finds that the Controller considered the claimant's arguments and all relevant factors, and has demonstrated a rational connection between those factors and the decision made.⁷³ And the claimant has not filed any evidence rebutting the Controller's findings. Therefore the Controller's conclusion that the time study does not adequately support the actual hours claimed is not arbitrary, capricious, or lacking in evidentiary support.

The Commission further finds that the Controller's decision to estimate fiscal year 2003-2004 salary and benefit costs based on an extrapolation of hours actually spent on the mandate and documented on timesheets from January 2005 through June 2005 is not arbitrary, capricious, or entirely lacking in evidentiary support. As indicated above, the claimant did not provide time logs or other adequate documentation supporting the time spent on the mandate in fiscal year 2003-2004 as required by the parameters and guidelines and, instead of reducing the costs to \$0, the Controller used actual time spent on the program the following year. There is no evidence in

⁶⁶ Exhibit B, Incorrect Reduction Claim 12-4237-I-03, page 40.

⁶⁷ Exhibit B, Incorrect Reduction Claim 12-4237-I-03, page 31.

⁶⁸ Exhibit D, Controller's Revised Late Comments on IRC 12-4237-I-03, page 17.

⁶⁹ Exhibit B, Incorrect Reduction Claim 12-4237-I-03, page 34.

⁷⁰ Exhibit D, Controller's Revised Late Comments on IRC 12-4237-I-03, page 17.

⁷¹ Exhibit D, Controller's Revised Late Comments on IRC 12-4237-I-03, page 18; Exhibit B, Incorrect Reduction Claim 12-4237-I-03, page 81; Exhibit C, Controller's Late Comments on IRC 08-4237-I-02, page 55 (Tab 10, Santa Clara County's Total Mandate-Related Hours Claimed).

⁷² Exhibit D, Controller's Revised Late Comments on IRC 12-4237-I-03, page 18.

⁷³ *American Bd. of Cosmetic Surgery, Inc.*, *supra*, 162 Cal.App.4th 534, 547-548.

the record that the time spent on the mandate in 2005 is not representative of the fiscal year 2003-2004 costs.

The Commission therefore finds that the Controller's reduction of costs for employees' salaries, benefits, and related indirect costs for fiscal year 2003-2004 is not arbitrary, capricious, or entirely lacking in evidentiary support.

V. Conclusion

The Commission finds that the Controller's reductions are correct as a matter of law and not arbitrary, capricious, or entirely lacking in evidentiary support.

Based on the foregoing, the Commission denies this IRC.

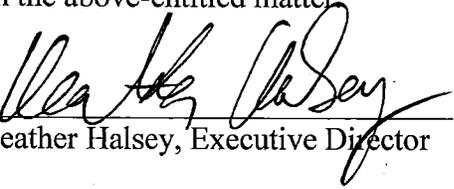
COMMISSION ON STATE MANDATES

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**RE: Decision**

Child Abduction and Recovery, 08-4237-I-02 and 12-4237-I-03
Family Code Sections 3060-3064, 3130-3134.5, 3408, 3411, and 3421;
Penal Code Sections 277, 278, and 278.5; Welfare and Institutions Code Section 11478.5
Statutes 1976, Chapter 1399; Statutes 1992, Chapter 162; Statutes 1996, Chapter 988
Fiscal Years: 1999-2000, 2000-2001, 2001-2002, 2003-2004, 2004-2005, 2005-2006,
and 2006-2007
County of Santa Clara, Claimant

On March 25, 2016, the foregoing decision of the Commission on State Mandates was adopted on the above-entitled matter.


Heather Halsey, Executive Director

Dated: March 30, 2016

BEFORE THE
COMMISSION ON STATE MANDATES
STATE OF CALIFORNIA

IN RE INCORRECT REDUCTION CLAIM
ON:
Penal Code Sections 273.5(e), (f), (g), (h), and
(i); 1000.93, 1000.94, 1000.95, and 1203.097
Statutes 1992, Chapters 183 and 184; Statutes
1994, Chapter 28X; Statutes 1995, Chapter 641
Fiscal Years 1998-1999, 1999-2000, and
2000-2001
County of Santa Clara, Claimant

Case No.: 07-9628101-I-01
*Domestic Violence Treatment Services –
Authorization and Case Management*
DECISION PURSUANT TO
GOVERNMENT CODE SECTION 17500
ET SEQ.; CALIFORNIA CODE OF
REGULATIONS, TITLE 2, DIVISION 2,
CHAPTER 2.5, ARTICLE 7
(Adopted March 25, 2016)
(Served March 30, 2016)

DECISION

The Commission on State Mandates (Commission) heard and decided this incorrect reduction claim (IRC) during a regularly scheduled hearing on March 25, 2016. Jim Spano and Masha Vorobyova appeared on behalf of the State Controller’s Office (Controller). The County of Santa Clara did not appear, but filed a letter indicating that it was standing on the record submitted.

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

The Commission adopted the proposed decision to deny the IRC for lack of jurisdiction by a vote of 6-0 as follows:

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

Summary of the Findings

This IRC addresses reductions made by the State Controller’s Office (Controller) to reimbursement claims of the County of Santa Clara (claimant) for fiscal years 1998-1999,

1999-2000, and 2000-2001 under the *Domestic Violence Treatment Services – Authorization and Case Management* program. The Controller reduced costs claimed based on claimant’s overstatement of productive hourly rates for its probation officers, unsupported or ineligible salaries and benefits claimed, overstated indirect costs claimed based on the claimant’s failure to calculate indirect costs using its revised countywide cost allocation plan, and the claimant’s failure to deduct offsetting fee revenue received from administering the batterer’s treatment program.

Based on the analysis herein, the Commission finds that the three-year period of limitations for filing an IRC began to accrue when the final audit report was issued on February 26, 2004. Because this IRC was filed August 15, 2007, more than three years later, it was not timely filed and therefore the Commission has no jurisdiction to hear and decide this IRC.

COMMISSION FINDINGS

I. Chronology

- 01/18/2000 Claimant signed its reimbursement claim for fiscal year 1998-1999.¹
- 01/11/2001 Claimant signed its original reimbursement claim for fiscal year 1999-2000.²
- 10/25/2001 Claimant signed its amended reimbursement claim for fiscal year 1999-2000.³
- 12/20/2001 Claimant signed its reimbursement claim for fiscal year 2000-2001.⁴
- 10/08/2003 Controller issued the Draft Audit Report.⁵
- 12/12/2003 Claimant filed comments on the Draft Audit Report.⁶
- 02/26/2004 Controller issued the Final Audit Report.⁷
- 08/15/2007 Claimant filed this IRC.⁸
- 09/04/2007 Claimant refiled the IRC to include the Controller’s August 3, 2006 remittance advice.⁹
- 09/07/2007 Commission staff deemed the IRC filing complete.

¹ Exhibit A, IRC, pages 89-109.

² Exhibit A, IRC, pages 110-116.

³ Exhibit A, IRC, pages 117-139.

⁴ Exhibit A, IRC, pages 140-183.

⁵ Exhibit A, IRC, page 26. The Draft Audit Report is not part of the record of this IRC.

⁶ Exhibit A, IRC, pages 41-48.

⁷ Exhibit A, IRC, pages 23-40.

⁸ Exhibit A, IRC.

⁹ Exhibit B, Supplemental filing (remittance advice coversheet). The remittance advice is included in Exhibit A, IRC, page 336.

- 10/30/2009 Controller issued the Revised Audit Report.¹⁰
- 07/03/2015 Controller filed late comments on the IRC.¹¹
- 08/04/2015 Claimant filed late rebuttal comments.¹²
- 08/18/2015 Commission staff requested that claimant provide additional information on the IRC.
- 08/28/2015 Claimant responded to the request for additional information on the IRC.¹³
- 12/22/2015 Commission staff issued the Draft Proposed Decision.¹⁴
- 01/11/2016 Claimant filed comments on the Draft Proposed Decision.¹⁵
- 03/22/2016 Claimant filed a letter with the Commission indicating that a representative of the county would not be present at the hearing and that it stands on the record submitted.

II. Background

A. Domestic Violence Treatment Services Program

On April 23, 1998, the Commission partially approved the *Domestic Violence Treatment Services– Authorization and Case Management* test claim. The test claim statutes provide that if a defendant is convicted of a domestic violence crime and granted probation as part of sentencing, the defendant is required to successfully complete the batterer’s treatment program administered by county probation departments as a condition of probation.¹⁶ The Commission

¹⁰ Exhibit C, Controller’s late comments on the IRC, pages 33-52.

¹¹ Exhibit C, Controller’s late comments on the IRC. Note that pursuant to Government Code section 17553(d) “the Controller shall have no more than 90 days after the claim is delivered or mailed to file any rebuttal to an incorrect reduction claim. The failure of the Controller to file a rebuttal to an incorrect reduction claim shall not serve to delay the consideration of the claim by the Commission.” However, in this instance, due to the backlog of IRCs, these late comments have not delayed consideration of this item and so have been included in the analysis and proposed decision.

¹² Exhibit D, Claimant’s late rebuttal comments on the IRC.

¹³ Exhibit E, Claimant’s response to request for additional information.

¹⁴ Exhibit F, Draft Proposed Decision.

¹⁵ Exhibit G, Claimant’s comments on the Draft Proposed Decision.

¹⁶ See Commission on State Mandates, Statement of Decision on CSM 96-281-01, *Domestic Violence Treatment Services – Authorization and Case Management*. The test claim was filed on statutes enacted in 1992, 1994, and 1995. Before 1992, the Legislature established procedures for the diversion of persons arrested for misdemeanor domestic violence offenses prior to the determination of guilt or innocence. The diversion program created an alternative to criminal prosecution and conviction of the accused batterer. The accused was required to enroll in, and complete, a batterer’s treatment program. The accused could avoid prosecution and conviction if the accused successfully completed the batterer’s program. The 1992 and 1994 legislation

determined that many activities pled in the test claim did not impose costs mandated by the state because the activities associated with the defendant's completion of a batterer's treatment program, which is now a condition of probation, changes the penalty for a crime within the meaning of Government Code section 17556(g).¹⁷ However, the Commission partially approved the claim, finding that the following activities impose a reimbursable state-mandated program on counties:

- Administration and regulation of the batterers' treatment programs (Pen. Code, § 1203.097(c)(1), (c)(2), and (c)(5)), offset by the claimant's fee authority under Penal Code section 1203.097(c)(5)(B);
- Providing services for victims of domestic violence (Pen. Code, § 1203.097(b)(4));
- Assessing the future probability of the defendant committing murder. (Pen. Code, § 1203.097(b)(3)(I)).

The Commission adopted parameters and guidelines on November 30, 1998 that provide reimbursement for the following activities:

- A. Administration and regulation of batterer's treatment programs (Pen. Code, §§ 1203.097(c)(1), (c)(2) and (c)(5)) offset by the claimant's fee authority under Penal Code section 1203.097(c)(5)(B).
 1. Development of an approval and annual renewal process for batterers' programs, not previously claimed under former Penal Code sections 1000.93 and 1000.95. (One-time activity.)
 - a. Meeting and conferring with and soliciting input from criminal justice agencies and domestic violence victim advocacy programs.

required county probation departments to administer and regulate domestic violence batterer's treatment programs and perform other related case management duties for domestic violence divertees and their victims. The 1995 legislation eliminated the diversion program as a pretrial option for an accused batterer and transformed the batterer's treatment program into a condition of probation, if part of the punishment and sentencing following conviction included probation. (Commission on State Mandates, Decision 96-281-01, p. 4.)

¹⁷ *Id.*, pages 7 and 8. The denied activities included the following: referring the defendant to an appropriate alternative batterer's program if the original program is unsuitable; monitoring the defendant's progress in the batterer's program, receiving and reviewing reports of violation, and reporting such findings to the court; requesting a hearing for further sentencing when the defendant is not performing satisfactorily in the assigned program, is not benefiting from the program, has not complied with the condition of probation, or has engaged in criminal conduct; providing information obtained from the investigation of the defendant's history to the batterer's treatment program upon request; investigating the defendant's history to determine the appropriate batterer treatment program, determining which community program would benefit the defendant, and reporting such findings to the court; assessing the defendant after the court orders the defendant to a batterer's program; and determining the amount, means, and manner of restitution the defendant must pay to the victim or battered women's shelter.

- b. Staff training regarding the administration and regulation of batterers' treatment programs. (One-time for each employee performing the mandated activity.)
 2. Processing of initial and annual renewal approvals for vendors, including:
 - a. Application review.
 - b. On-site evaluations.
 - c. Notification of application approval, denial, suspension or revocation.
- B. Victim Notification. (Pen. Code, § 1203.097 (b)(4).)
 1. The probation department shall attempt to:
 - a. Notify victims regarding the requirement for the defendant's participation in a batterer's program.
 - b. Notify victims regarding available victim resources.
 - c. Inform victims that attendance in any program does not guarantee that an abuser will not be violent.
 2. Staff training on the following activities:
 - a. Notify victims regarding the requirement for the defendant's participation in a batterer's program, and inform victims that attendance in any program does not guarantee that an abuser will not be violent. (One-time for each employee performing the mandated activities.)
 - b. Notify victims regarding available victim resources. (Once-a-year training for each employee performing the mandated activity.)
- C. Assessing the future probability of the defendant committing murder. (Pen. Code, § 1203.097(b)(3)(I).)
 1. Evaluation and selection of a homicidal risk assessment instrument.
 2. Purchasing or developing a homicidal risk assessment instrument.
 3. Training staff on the use of the homicidal risk assessment instrument.
 4. Evaluation of the defendant using the homicidal risk assessment instrument, interviews and investigation, to assess the future probability of the defendant committing murder.

In the event a local agency obtains a new homicidal risk assessment instrument, documentation substantiating the improved value of the new instrument is required to be provided with the claim.¹⁸

Section V. of the parameters and guidelines allows reimbursement for employee salaries and benefits, to be claimed as follows:

¹⁸ Exhibit A, IRC, pages 69-70.

Identify the employee(s), and/or show the classification of the employee(s) involved. Describe the reimbursable activities performed and specify the actual time devoted to each reimbursable activity by each employee, productive hourly rate and related fringe benefits.¹⁹

Section V. also allows reimbursement for the cost of training an employee “to perform the mandated activities.” The parameters and guidelines require the claimant to “identify the employee(s) by name and job classification,” and “provide the title and subject of the training session, the date(s) attended and the location.”²⁰

Section VI. of the parameters and guidelines, which addresses the required data to support the claim, states:

For audit purposes, all costs claimed shall be traceable to source documents (e.g. employee time records, invoices, receipts, purchase orders, contracts, worksheets, calendars, declarations, etc.) that show evidence of the validity of such costs and their relationship to the state mandated program. All documentation in support of the claimed costs shall be made available to the State Controller’s Office, as may be requested, and all reimbursement claims are subject to audit during the period specified in Government Code section 17558.5, subdivision (a).²¹

The parameters and guidelines were amended in January 2010 (eff. July 1, 2005) to add boilerplate language requiring claimants to keep contemporaneous source documents. Because the reimbursement claims at issue in this IRC were for costs incurred in fiscal years 1998-1999, 1999-2000, and 2000-2001, the parameters and guidelines applicable to this claim are those adopted on November 30, 1998.

B. The Controller’s Audits and Summary of the Issues

The Controller issued a final audit report on February 26, 2004, reducing costs claimed by \$748,645.²² The claimant filed this IRC on August 15, 2007, and based on additional documentation the claimant submitted with its IRC, the Controller issued a revised final audit report on October 30, 2009, to supersede the prior final audit report. The revised final audit report increases allowable costs by \$100,881 and reduces costs claimed during the audit period by \$647,794.²³ The Controller’s final revised audit reductions and findings are explained below.

Finding One, Reduction of Costs Claimed for Salaries and Benefits

¹⁹ Exhibit A, IRC, page 70.

²⁰ Exhibit A, IRC, page 71.

²¹ Exhibit A, IRC, pages 71-72.

²² Exhibit A, IRC, pages 22-50.

²³ Exhibit C, Controller’s late comments on the IRC, pages 33-64. Although in the revised audit, finding 1 increased allowable costs claimed by \$104,417, the revised finding 2 (on indirect costs) decreased allowable costs by \$3,536, so the net increase in allowable costs from the original to the revised audit totals \$100,881. See Exhibit C, Controller’s late comments on the IRC, pages 9, 11, and 14.

The Controller issued a final audit report on February 26, 2004, reducing salary and benefit costs claimed, and related indirect costs by \$705,080. The Controller found that the claimant incorrectly calculated its productive hourly rate and claimed employee costs that were unsupported or ineligible for reimbursement.²⁴

The claimant has withdrawn from its IRC the challenge to the Controller's reduction of costs based on the claimant's calculation of productive hourly rates.²⁵ However, the findings and reductions based on unsupported or ineligible salary and benefit costs claimed are still disputed. Finding 1 of the revised final audit report and comments filed by the Controller on the IRC summarize the reductions as follows:

A. For administration and regulation of batterer's treatment programs, the county claimed salaries and benefits totaling \$90,949 (\$25,841 for FY 1998-1999, \$56,665 for FY 1999-2000, and \$8,443 for FY 2000-2001) that were unsupported.²⁶ The Controller's reductions and revised findings are as follows:

1. The county estimated five hours per month for each of the 10 officers for fiscal year 1998-1999 (600 hours) and 11 officers for fiscal year 1999-2000 (660 hours) for providing resources over the telephone to victims. No documentation was provided to substantiate the activities performed and time spent on them.

Subsequently, the county conducted a time study in June 2003 and submitted it with the IRC to document the time spent providing resources over the telephone to victims. The time study showed the average time per case was 15 minutes. After reviewing the time study, the Controller accepted the 15-minute time standard, but rejected as unreasonable the application of the time standard to all cases in the Domestic Violence Unit during the year. Once the defendant is assigned to the probation department, the department sends letters notifying victims of available resources. Therefore, the Controller presumed that victim contacts with the department "would ensue" shortly after receiving the letters. The Controller applied the 15-minute time standard to new cases assigned during the year. The Controller allowed 324.25 hours of the 600 hours claimed for fiscal year 1998-1999 and 165 hours of the 660 hours claimed for fiscal year 1999-2000.²⁷

²⁴ Exhibit A, IRC, pages 22-50.

²⁵ Exhibit D, Claimant's late rebuttal comments on the IRC, page 4; Exhibit E, Claimant's response to request for additional information, page 1.

²⁶ The revised audit report reinstated \$46,114 in salaries and benefits. Exhibit C, Controller's late comments on the IRC, page 42.

²⁷ Exhibit C, Controller's late comments on the IRC, pages 16 and 42 (revised final audit report). Page 22 of the Controller's comments show the amounts claimed and reinstated for this activity combined with 1.B.4. (speaking over the phone with victims): "The county overstated the hours of providing resources to victims via telephone contact by 1,270.5 hours for the audit period. The time study standard of 15 minutes applied to new cases in the unit only substantiated 649.50 hours, instead of the 1,920 hours claimed."

2. The county claimed 26 hours for fiscal year 1998-1999 and 30 hours for fiscal year 1999-2000 for its investigative unit to perform activities for the administration and regulation component, which was determined to be unallowable because no documentation was provided to substantiate the activities performed and time spent on the activities. In addition, the auditor's interviews of the investigative officers revealed this is not a function that this unit performs.

Moreover, the Controller determined that the county claimed these hours based on an "inadequate" time study conducted in May 1999. Thirty-one officers participated in the time study. Of the 31 officers recording time, only two officers indicated hours for the administrative component, totaling 2 hours and 15 minutes. The claimant then calculated the employee hours claimed by dividing the 2.25 hours by the 48 cases in the unit for the month of May 1999, which generated a time standard of 0.05 hours for the function. The time standard was multiplied by the total number of cases for each fiscal year to arrive at the claimed hours.²⁸

3. The county claimed 536 hours for fiscal year 1999-2000 and 224 hours for fiscal year 2000-2001 for staff training, for a total of 760 claimed training hours. The county provided course rosters and sign-in sheets to substantiate 456 hours claimed for training by the Probation Department's Certification Unit (232 hours claimed in fiscal year 1999-2000 and 224 hours claimed in fiscal year 2000-2001). The Controller originally reduced many of the hours claimed because Probation Department personnel stated that individuals attending the training did not perform activities related to the administration and regulation of the batterer's treatment program.

Based on the declaration provided with the IRC, the Controller revisited the issue and reviewed the course content of the training, determining that the course topics fell within the allowable training activities of the program's parameters and guidelines. Of the 57 probation officers receiving training, 11 were assigned to the Domestic Violence Treatment Services Program during the audit period, per the declaration of Rita Loncarich. The remaining probation officers were assigned to General Supervision and Investigation, which also handles domestic violence related charges. The Controller determined that 456 documented training hours (of 760 hours claimed) are allowable.²⁹

4. The county claimed 102 hours for fiscal year 1999-2000 and 66 hours for fiscal year 2000-2001 for meeting and conferring with criminal justice agencies. County personnel stated that a different unit within the Probation Department claimed the additional hours and provided a memorandum by the department's supervisor, which included the number of hours and stated that department staff were at meetings. The

²⁸ Exhibit C, Controller's late comments on the IRC, pages 20, 22, and 43 (revised final audit report).

²⁹ Exhibit C, Controller's late comments on the IRC, pages 20, 22, and 43 (revised final audit report). The revised audit reinstated \$18,867 in allowable salaries and benefits and \$18,283 in related indirect costs.

Controller originally found that this documentation did not identify who attended such meetings.

The Controller revised this finding to reinstate all hours reduced after the IRC was filed because the management information reports submitted with the IRC substantiated all the claimed meeting hours. The revised audit reinstates claimed direct costs of \$6,936, and \$6,757 in related indirect costs.³⁰

B. For victim notification, the county claimed salaries and benefits totaling \$136,569 (\$52,285 for FY 1998-1999, \$36,227 for FY 1999-2000, and \$48,057 for FY 2000-2001) that were unsupported or ineligible for the following reasons:³¹

1. For fiscal years 1998-1999 and 1999-2000, the documentation provided by the county did not support the total number of letters sent to notify victims regarding the requirement for the defendant's participation in the batterer's program, to notify victims regarding available victim resources, and to inform victims that attendance in any program does not guarantee that an abuser will not be violent.³²

In comments on the draft audit report, the claimant stated it "concur[s] with this finding."³³ However, in the IRC, claimant requests the Commission to "reverse the audit findings" and reinstate all the Controller's audit reductions.³⁴

2. For the entire audit period, the county was unable to support all of the hours it claimed for the officers to make field contact with the victims. The county submitted field contact logs to support these hours; however, the total hours claimed did not reconcile to the hours in the field contact logs.

In comments on the IRC, the Controller stated that it allowed the hours validated by the declaration of Ms. Tong submitted with the IRC; i.e., one hour per field contact case supported with field contact logs, which totaled 131 hours for fiscal year 1998-1999, 343 hours for fiscal year 1999-2000, and 435 hours for fiscal year 2000-2001. The Controller determined that 909 cases were allowable for the audit period, which resulted in allowable costs totaling \$37,719 in salaries and benefits and \$36,588 in related indirect costs.³⁵

The Controller further states that the field contact issue primarily pertains to fiscal year 1998-1999, where the Controller disallowed 408 employee hours claimed. The Controller states:

³⁰ Exhibit C, Controller's late comments on the IRC, pages 20 and 43 (revised final audit report).

³¹ For victim notification, the original audit found salaries and benefits totaling \$143,277 (\$52,285 for FY 1998-1999, \$36,227 for FY 1999-2000, and \$48,057 for FY 2000-2001) that were unsupported or ineligible.

³² Exhibit C, Controller's late comments on the IRC, pages 17 and 43 (revised final audit report).

³³ Exhibit A, IRC, page 46.

³⁴ Exhibit A, IRC, pages 2 and 6-7.

³⁵ Exhibit C, Controller's late comments on the IRC, page 20.

From January through June 1999, the auditor validated 111 of the 240 cases reviewed. These 111 cases were allowed for reimbursement. The files were purged for the first half of the fiscal year, July through December. From the county's summary schedule for that period, 182 cases were listed for that time period. The auditor tested 72 cases (approximately 40%) and traced these costs to the county's system to review the field officer's field visit log comments. Out of 72 cases tested, only 8 were validated. This represents a pass rate of 11%, which was applied to the remaining 182 cases to yield an additional 20 cases. This methodology is a more valid approach to approximate valid purged cases

...³⁶

3. For the entire audit period, the county claimed costs for the time spent to prepare letters sent to victims for notification of the defendant's violation of probation, scheduled hearings, and status changes in cases. The Controller found that these activities are not reimbursable under the mandate.³⁷

In comments on the draft audit report, the claimant stated "we concur that this is not a reimbursable activity."³⁸ However, the IRC requests the Commission to "reverse the audit findings" and reinstate all the Controller's audit reductions.³⁹

4. For fiscal year 2000-2001, the county claimed estimated hours spent talking with victims on the telephone. No documentation was provided to substantiate the activities performed or the time spent on such activities.

The claimant submitted additional time study documentation with its IRC. The Controller reviewed the time study and accepted the 15-minute time standard for new cases only. The Controller applied the hours to 641 new cases in the Domestic Violence Unit, resulting in 160.25 allowable hours for victim telephone contacts.⁴⁰

- C. For assessment of future probability of defendant committing murder, the county claimed salaries and benefits totaling \$75,050 (\$12,573 for FY 1998-1999, \$59,434 for FY 1999-2000, and \$3,043 for FY 2000-2001) that were unsupported. The county used a fiscal year 1998-1999 time study of 4.68 hours for each case to support time spent performing the activity in fiscal year 1999-2000. The county did not perform a time study during fiscal year 1999-2000; however it did perform a time study for 2000-2001, which resulted in 1.59 hours for each case, a decline from the previous time study. The county stated that the reduction was due to the learning curve and efficiency of probation officers

³⁶ Exhibit C, Controller's late comments on the IRC, pages 21-22 and 44 (revised final audit report).

³⁷ Exhibit C, Controller's late comments on the IRC, pages 17 and 44 (revised final audit report).

³⁸ Exhibit A, IRC, page 47.

³⁹ Exhibit A, IRC, pages 2 and 6-7.

⁴⁰ Exhibit C, Controller's late comments on the IRC, pages 21 and 44 (revised final audit report). The revised audit report increased allowable salaries and benefits by \$6,708 and related indirect costs by \$6,323 for fiscal year 2000-2001.

performing mandate-related activities. The Controller calculated the costs for fiscal year 1999-2000 using the average of the fiscal year 1998-1999 and 2000-2001 time study results (3.14 hours per case).⁴¹

Finding Two, Overstated Indirect Costs

In finding 2, the Controller reduced \$44,881 in costs claimed for overstated indirect cost rates for the audit period because the claimant revised its countywide cost allocation plan, but did not apply the revised amounts when computing the indirect cost rate. The Controller recalculated indirect costs by multiplying the allowable salaries and benefits by the revised indirect cost rates.⁴²

Finding Three, Offsetting Fee Revenues

In finding 3 of the revised audit report, the Controller reduced costs claimed by \$2,250 for offsetting revenues that claimant received for processing vendor renewals for the batterer treatment programs.⁴³ In comments on the draft audit report, the claimant stated that it concurred with the audit finding.⁴⁴ However, the claimant's IRC requests a determination that all costs reduced by the Controller be reinstated.⁴⁵

III. Positions of the Parties

A. County of Santa Clara

Claimant disputes the Controller's findings, and requests that the Commission direct the Controller to reinstate all costs reduced. The claimant argues that the costs claimed are supported by valid time studies, reports, declarations, and time logs.⁴⁶

After filing the IRC, the claimant withdrew the challenge to the Controller's reduction of costs based on the claimant's calculation of productive hourly rates.⁴⁷ The claimant continues to dispute all other reductions.

In comments on the Draft Proposed Decision, the claimant disagrees that the remittance advice does not provide the notice required by Government Code section 17558.5 to trigger the period

⁴¹ Exhibit C, Controller's late comments on the IRC, pages 21, 22, and 44.

⁴² Exhibit A, IRC, page 38 (final audit report). Exhibit C, Controller's late comments on the IRC, page 51 (revised final audit report). As the Controller said in the revised audit report: "We recalculated the overstated indirect costs based on the revised amounts identified in Finding 1. Consequently, overstated indirect costs increased by \$3,536, from \$41,345 to \$44,881."

⁴³ Exhibit A, IRC, page 39.

⁴⁴ Exhibit A, IRC, page 48 (comments on the final audit report).

⁴⁵ Exhibit A, IRC, pages 2 and 6-7.

⁴⁶ Exhibit A, IRC, pages 11-15, 200-210, 212-213, 215-324, 326, 328-334.

⁴⁷ Exhibit D, Claimant's late rebuttal comments on the IRC, page 4; Exhibit E, Claimant's response to request for additional information, page 1.

of limitations. Claimant argues that because the IRC was deemed complete by Commission staff, the Commission effectively waived any right to later claim the IRC was not timely filed.⁴⁸

B. State Controller's Office

It is the Controller's position that the revised audit adjustments are correct and that this IRC should be denied. The Controller reinstated some of the costs claimed based on documentation submitted with the IRC.

IV. Discussion

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

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

The Commission must review questions of law, including interpretation of the parameters and guidelines, de novo, without consideration of legal conclusions made by the Controller in the context of an audit. The Commission is vested with exclusive authority to adjudicate disputes over the existence of state-mandated programs within the meaning of article XIII B, section 6.⁴⁹ 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."⁵⁰

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.⁵¹ Under this standard, the courts have found that:

When reviewing the exercise of discretion, "[t]he scope of review is limited, out of deference to the agency's authority and presumed expertise: 'The court may not reweigh the evidence or substitute its judgment for that of the agency. [Citation.]'" ... "In general ... the inquiry is limited to whether the decision was

⁴⁸ Exhibit G, Claimant's comments on the Draft Proposed Decision, pages 3-4.

⁴⁹ *Kinlaw v. State of California* (1991) 54 Cal.3d 326, 331-334; Government Code sections 17551, 17552.

⁵⁰ *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.

⁵¹ *Johnston v. Sonoma County Agricultural Preservation and Open Space Dist.* (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.

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.]’ ”⁵²

The Commission must review the Controller’s audit in light of the fact that the initial burden of providing evidence for a claim of reimbursement lies with the claimant.⁵³ In addition, sections 1185.1(f)(3) and 1185.2(c) of the Commission’s regulations require that any assertions of fact by the parties to an IRC must be supported by documentary evidence. The Commission’s ultimate findings of fact must be supported by substantial evidence in the record.⁵⁴

The Commission Does Not Have Jurisdiction to Hear and Decide This Incorrect Reduction Claim Because It Was Not Timely Filed.

The IRC was filed on August 15, 2007,⁵⁵ almost three and one-half years after the final audit report was issued on February 26, 2004.⁵⁶ The IRC was deemed complete, however, based on a later-issued remittance advice, a computer-generated document dated August 3, 2006, which was submitted by the claimant as a supplemental filing.⁵⁷

Claimant argues that the IRC was timely filed based on the remittance advice dated August 3, 2006, and that if the remittance advice was not the type of document needed to trigger the filing of an IRC, then the IRC should have been rejected as incomplete by Commission staff in 2007. Claimant also asserts that by deeming the IRC filing complete, the Commission effectively waived any right to claim the IRC was not timely filed.⁵⁸ The completeness review performed by Commission staff is not a legal review, however. It is simply a check to determine if the elements required for filing an IRC have been met.⁵⁹ Thus, the completeness review cannot be relied on to determine this question of law.

For the reasons below, the Commission finds that the three-year period of limitations for filing an IRC began to accrue when the final audit report was issued on February 26, 2004. Thus, the

⁵² *American Bd. of Cosmetic Surgery, Inc. v. Medical Board of California* (2008) 162 Cal.App.4th 534, 547-548.

⁵³ *Gilbert v. City of Sunnyvale* (2005) 130 Cal.App.4th 1264, 1274-1275.

⁵⁴ 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.

⁵⁵ Exhibit A, IRC, page 2.

⁵⁶ Exhibit A, IRC, page 22-50.

⁵⁷ Exhibit B, Supplemental filing (remittance advice coversheet), dated August 3, 2006, filed September 4, 2007. The remittance advice is attached to the IRC (Exhibit A), page 336.

⁵⁸ Exhibit G, Claimant’s comments on the Draft Proposed Decision, pages 3-4.

⁵⁹ California Code of Regulations, title 2, section 1185.2.

IRC filed August 15, 2007, more than three years later, was not timely filed. Therefore, the Commission does not have jurisdiction to hear and decide this IRC.

Under the statutory mandates scheme, a reimbursement claim 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(a). Government Code section 17558.5(c) then 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 adjustment.”⁶⁰ 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.

Former section 1185(b) of the Commission’s regulations, in effect when the final audit report was issued in this case, required IRCs to be filed “no later than three (3) years following the date of the Office of State Controller’s remittance advice or other notice of adjustment notifying the claimant of a reduction.”⁶¹ The statute of limitations for filing an IRC is currently in section 1185.1(c), which similarly provides that “[a]ll incorrect reduction claims shall be filed with the Commission no later than three years following the date of the Office of State Controller’s final state audit report, letter, remittance advice, or other written notice of adjustment to a reimbursement claim.”

“Critical to applying a statute of limitations is determining the point when the limitations period begins to run.”⁶² Thus, given the multiple documents issued by the Controller in this case, the threshold issue is when the right to file an IRC based on the Controller’s reductions accrued, and consequently when the applicable period of limitations began to run against the claimant.

The goal of any underlying limitations 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.⁶³ The California Supreme Court has described statutes of limitations as follows:

A statute of limitations strikes a balance among conflicting interests. If it is unfair to bar a plaintiff from recovering on a meritorious claim, it is also unfair to require a defendant to defend against possibly false allegations concerning long-forgotten events, when important evidence may no longer be available. Thus, statutes of limitations are not mere technical defenses, allowing wrongdoers to avoid accountability. Rather, they mark the point where, in the judgment of the legislature, the equities tip in favor of the defendant (who may be innocent of wrongdoing) and against the plaintiff (who failed to take prompt action): “[T]he period allowed for instituting suit inevitably reflects a value judgment concerning

⁶⁰ Government Code section 17558.5(c).

⁶¹ Former California Code of Regulations, title 3, section 1185(b) (Register 2003, No. 17).

⁶² *Poosh v. Phillip Morris USA, Inc.* (2011) 51 Cal.4th 788, 797.

⁶³ *Addison v. State of California* (1978) 21 Cal.3d 313, 317; *Jordach Enterprises, Inc. v. Brobeck, Phleger & Harrison* (1998) 18 Cal.4th 739, 761.

the point at which the interests in favor of protecting valid claims are outweighed by the interests in prohibiting the prosecution of stale ones.”⁶⁴

The general rule, supported by a long line of cases, holds that a statute of limitations accrues when a cause of action arises; when the action can be maintained.⁶⁵ Generally, “a plaintiff must file suit within a designated period after the cause of action accrues.”⁶⁶ The cause of action accrues, the Court said, “when [it] is complete with all of its elements.”⁶⁷ Put another way, the courts have held that “[a] cause of action accrues ‘upon the occurrence of the last element essential to the cause of action.’”⁶⁸ Although the courts have carved out some exceptions to the statute of limitations, and have delayed or tolled the accrual of a cause of action when a plaintiff is justifiably unaware of facts essential to a claim or when latent additional injuries later become manifest,⁶⁹ those exceptions are limited and do not apply when a plaintiff has sufficient facts to be on notice or constructive notice that a wrong has occurred and that he or she has been injured.⁷⁰ The courts do not toll a statute of limitations because the full extent of the claim, or its

⁶⁴ *Poosh v. Phillip Morris USA, Inc.*, (2011) 51 Cal.4th 788, 797.

⁶⁵ See, e.g., *Osborn v. Hopkins* (1911) 160 Cal. 501, 506 [“[F]or it is elementary law that the statute of limitations begins to run upon the accrual of the right of action, that is, when a suit may be maintained, and not until that time.”]; *Dillon v. Board of Pension Commissioners* (1941) 18 Cal.2d 427, 430 [“A cause of action accrues when a suit may be maintained thereon, and the statute of limitations therefore begins to run at that time.”].

⁶⁶ *Ibid* [citing Code of Civil Procedure section 312].

⁶⁷ *Ibid* [quoting *Norgart v. Upjohn Co.* (1999) 21 Cal.4th 383, 397].

⁶⁸ *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].

⁶⁹ *Royal Thrift and Loan Co. v. County Escrow, Inc.* (2004) 123 Cal.App.4th 24, 43 [“Generally, statutes of limitation are triggered on the date of injury, and the plaintiff’s ignorance of the injury does not toll the statute... [However,] California courts have long applied the delayed discovery rule to claims involving *difficult-to detect injuries or the breach of fiduciary relationship.*” (Emphasis added.); *Poosh v. Phillip Morris USA, Inc.* (2011) 51 Cal.4th 788, 802, where the court held that for statute of limitations purposes, a later physical injury caused by the same conduct “can, in some circumstances, be considered ‘qualitatively different’.” The court limited its holding to latent disease cases, and did not decide whether the same rule applied in other contexts. (*Id.* at page 792.)

⁷⁰ *Jolly v. Eli Lilly & Co.* (1988) 44 Cal.3d 1103, 1110 [belief that a cause of action for injury from DES could not be maintained against multiple manufacturers when exact identity of defendant was unknown did not toll the statute]; *Goldrich v. Natural Y Surgical Specialties, Inc.* (1994) 25 Cal.App.4th 772, 780 [belief that patient’s body, and not medical devices implanted in it, was to blame for injuries did not toll the statute]; *Campanelli v. Allstate Life Insurance Co.* (9th Cir. 2003) 322 F.3d 1086, 1094 [Fraudulent engineering reports concealing the extent of damage did not toll the statute of limitations, nor provide equitable estoppel defense to the statute of limitations]; *Abari v. State Farm Fire & Casualty Co.* (1988) 205 Cal.App.3d 530, 534 [Absentee landlord’s belated discovery of that his homeowner’s policy might cover damage caused by subsidence was not sufficient reason to toll the statute]. See also *McGee v. Weinberg*

legal significance, or even the identity of a defendant, is not yet known at the time the cause of action accrues.⁷¹

For IRCs, the “last element essential to the cause of action” which begins the running of the period of limitations pursuant to Government Code section 17558.5 and former section 1185 (now § 1185.1) of the Commission’s regulations, is a notice to the claimant of the adjustment that includes the reason for the adjustment. Government Code section 17558.5(c), the substance of which was also in effect at the time the audit report was issued, provides in pertinent part:

The Controller shall notify the claimant in writing within 30 days after issuance of a remittance advice 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 or school district, and the reason for the adjustment...⁷²

An IRC to challenge the Controller’s findings pursuant to Government Code sections 17551 and 17558.7 can be maintained as soon as the Controller issues a notice reducing a claim for reimbursement which specifies the reason for adjustment in accordance with Government Code section 17558.5(c). The Commission’s regulations provide local governments three years following the notice of adjustment required by Government Code section 17558.5(c), in whatever written form provided by the Controller, to file an IRC with the Commission, or otherwise be barred from such action. In addition, the IRC must include a copy of the “written notice of adjustment from the Office of the State Controller that explains the reason(s) for the reduction or disallowance.”⁷³ This interpretation is consistent with previously adopted Commission decisions.⁷⁴

Here, the record shows that the Controller issued a draft audit report on October 8, 2003, which the claimant responded to on December 12, 2003, “agreeing with the audit results with the exception of Finding 1.”⁷⁵ The Controller made no changes to the adjustments or findings

(1979) 97 Cal.App.3d 798, 804 [“It is the occurrence of some ... cognizable event rather than knowledge of its legal significance that starts the running of the statute of limitations.”].

⁷¹ *Scafidi v. Western Loan & Building Co.* (1946) 72 Cal.App.2d 550, 566 [“Our courts have repeatedly affirmed that mere ignorance, not induced by fraud, of the existence of the facts constituting a cause of action on the part of a plaintiff does not prevent the running of the statute of limitations.”]. See also, *Baker v. Beech Aircraft Corp.* (1974) 39 Cal.App.3d 315, 321 [“The general rule is that the applicable statute...begins to run when the cause of action accrues even though the plaintiff is ignorant of the cause of action or of the identity of the wrongdoer.”].

⁷² See former Government Code section 17558.5(b) (Stats. 2002, ch. 1128, eff. Jan. 1, 2003).

⁷³ California Code of Regulations, title 2, section 1185.1(c) and (f)(4); See also, Former California Code of Regulations, title 2, section 1185(c) and (d)(4) (Register 2010, No. 44).

⁷⁴ See Commission on State Mandates, Decision, *Collective Bargaining*, 05-4425-I-11, adopted December 5, 2014, and Decision, *Handicapped and Disabled Students*, 05-4282-I-03 adopted September 25, 2015.

⁷⁵ Exhibit A, IRC, page 26 (final audit report).

following receipt of the claimant's comments, and issued a final audit report on February 26, 2004, stating that "[t]he fiscal impact of the findings reported in the draft report remains unchanged."⁷⁶ The final audit report identifies the amounts reduced for this program for costs claimed for fiscal years 1998-1999, 1999-2000, and 2000-2001, and contains three detailed findings made by the Controller that explain the reasons for the Controller's reductions (Finding 1, unsupported salaries and benefits and related indirect costs; Finding 2, overstated indirect costs; and Finding 3, unreported reimbursements).⁷⁷ There is no evidence that the claimant did not receive the final audit report. The IRC itself states that "[o]n February 26, 2004, the State Controller's Office ("SCO") issued its final audit report on the County of Santa Clara's ("County's") claims for costs incurred based on the legislatively created Domestic Violence Treatment Services Program . . . for July 1, 1998 through June 30, 2001."⁷⁸

The February 26, 2004 final audit report does include an express invitation for the claimant to participate in an additional informal audit review process, and invites the claimant to submit additional documentation to the Controller: "The auditee should submit, in writing, a request for a review and all information pertinent to the disputed issues within 60 days after receiving the final report."⁷⁹ This language could support a finding that the final audit report did not, in fact, constitute the Controller's final determination on the subject claims and thus did not provide the "last essential element to the cause of action" that would begin the running of the statute of limitations.⁸⁰ There is no evidence in the record, however, that the claimant submitted a request for a review or otherwise participated in the additional review process for this audit within the 60-day time period offered by the Controller. Rather, the record shows that the claimant first responded to the Controller's February 26, 2004 final audit report with the filing of this IRC, which included additional documentation in support of its claim for the salaries and benefits reduced in Finding 1 that resulted in the Controller later reinstating some of the costs originally reduced.⁸¹

⁷⁶ Exhibit A, IRC, page 36 (final audit report).

⁷⁷ Exhibit A, IRC, pages 30-38 (Finding 1), 38 (Finding 2), and 39 (Finding 3).

⁷⁸ Exhibit A, IRC, page 6.

⁷⁹ Exhibit A, IRC, page 22 (final audit report).

⁸⁰ California Code of Regulations, title 2, section 1185 (Register 2003, No. 17). See also Adopted Decision, *Handicapped and Disabled Students*, 05-4282-I-03, where the Commission did find that a later remittance advice constituted the first notice of adjustment when the cover letter for the "final audit report" contained the same exact language as here *and* there was evidence in the record that the claimant did participate in the informal audit review process which resulted in the Controller to modifying the reductions and issuing a remittance advice based on the corrected reductions.

⁸¹ The Commission's ultimate findings of fact must be supported by substantial evidence in the record. 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. See also, California Code of

Moreover, the August 3, 2006 remittance advice is a computer-generated document that provides no reason for the audit adjustments and, thus, does not provide the notice required by Government Code section 17558.5(c) to trigger the period of limitations for filing an IRC. Instead, the remittance advice shows that \$0 was due to the claimant for the “reimbursement of state mandated costs” and identifies “payment offsets” relating to adjustments made by the Controller to reimbursement claims filed by the claimant for several state-mandated programs, including the original \$748,645 reduction for the *Domestic Violence Treatment Services* claims at issue here. In any event, the right to file an IRC had already accrued and the limitations period began to run before the remittance advice was issued.

Therefore, based on the evidence in the record, an IRC could have been filed as soon as the final audit report dated February 26, 2004 was issued. The final audit report provides the “last essential element to the cause of action” that began the running of the period of limitations against the claimant. Thus, for the IRC to be timely, it had to be filed by February 26, 2007. Because the IRC was filed on August 15, 2007, it was not timely filed within the three-year period of limitations. Therefore, the Commission does not have jurisdiction to hear and decide this IRC.

V. Conclusion

Based on the foregoing, the Commission finds that the three-year period of limitations for filing an IRC began to accrue when the final audit report was issued on February 26, 2004. Because this IRC was filed August 15, 2007, more than three years later, it was not timely filed and therefore the Commission has no jurisdiction to hear and decide this IRC.

Regulations, title 2, section 1187.5, requiring that all oral or written representations of fact shall be under oath or affirmation.

COMMISSION ON STATE MANDATES

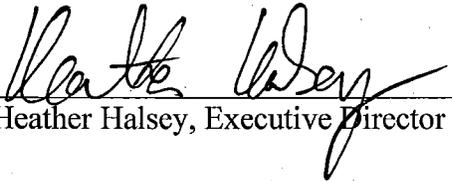
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**RE: Decision**

Domestic Violence Treatment Services – Authorization and Case Management,
07-9628101-I-01

Penal Code Sections 273.5(e), (f), (g), (h), and (i); 1000.93, 1000.94,
1000.95, and 1203.097; Statutes 1992, Chapters 183 and 184;
Statutes 1994, Chapter 28X; Statutes 1995, Chapter 641
Fiscal Years 1998-1999, 1999-2000, and 2000-2001
County of Santa Clara, Claimant

On March 25, 2016, the foregoing decision of the Commission on State Mandates was adopted on the above-entitled matter.


Heather Halsey, Executive Director

Dated: March 30, 2016

BEFORE THE
COMMISSION ON STATE MANDATES
STATE OF CALIFORNIA

**IN RE INCORRECT REDUCTION CLAIM
ON:**

Education Code Section 76300;

Statutes 1984, 2d Ex. Sess., Chapter 1;
Statutes 1984, Chapters 274, and 1401;
Statutes 1985, Chapters 920 and 1454;
Statutes 1986, Chapters 46 and 394;
Statutes 1987, Chapter 1118; Statutes 1989,
Chapter 136; Statutes 1991, Chapter 114;
Statutes 1992, Chapter 703; Statutes 1993,
Chapters 8, 66, 67 and 1124; Statutes 1994,
Chapters 153 and 422; Statutes 1995,
Chapter 308; Statutes 1996, Chapter 63;
Statutes 1999, Chapter 72;

California Code of Regulations, Title 5,
Sections 58501-58503, 58611-58613,
58620, and 58630

Fiscal Years 1998-1999, 1999-2000, 2000-
2001, 2001-2002, 2002-2003, 2003-2004,
2004-2005, 2005-2006, 2006-2007, and
2007-2008

Gavilan Community College District, Claimant

Case No.: 13-9913-I-01

Enrollment Fee Collection and Waivers

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

(Adopted July 22, 2016)

(Served July 26, 2016)

DECISION

The Commission on State Mandates (Commission) heard and decided this Incorrect Reduction Claim (IRC) during a regularly scheduled hearing on July 22, 2016.

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

The Commission adopted the Proposed Decision to approve the IRC on consent, with all Commission members present voting to adopt the Consent Calendar as follows:

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

Summary of the Findings

This IRC challenges the State Controller’s (Controller’s) finding that the Gavilan Community College District (claimant) claimed unallowable costs of \$3,766,932 for the *Enrollment Fee Collection and Waivers* program for fiscal years 1998-1999 through 2007-2008. The Controller found unsupported and ineligible salaries and benefits and contract services claimed, overstated indirect cost rates, and overstated offsetting savings and reimbursements. The claimant disputes the merits of these audit findings, and argues that the audit was not completed within the two-year deadline in Government Code section 17558.5 and is therefore void.

The Commission finds there is no evidence in the record that the audit was completed within the two-year deadline in Government Code section 17558.5, and thus, the audit findings are void.

In late comments on the Draft Proposed Decision, the Controller states it is not challenging the proposed conclusion and recommendation, and has pulled the audit report off of its website and notified the claimant of its withdrawal. According to the Controller, “The State will pay the district for the withdrawn audit findings upon availability of funds.”¹ However, because the IRC has not been withdrawn by the claimant, the Commission must still render a decision.

Therefore, the Commission approves this IRC and requests that the Controller reinstate all costs reduced totaling \$3,766,932, in accordance with Government Code section 17551(d) and section 1185.9 of the Commission regulations.

COMMISSION FINDINGS

I. Chronology

07/11/2006 Claimant signed the reimbursement claim forms for fiscal years 1998-1999, 1999-2000, 2000-2001, 2001-2002, 2002-2003, 2003-2004 and 2004-2005.²

¹ Exhibit D, Controller’s Late Comments on the Draft Proposed Decision, page 1.

² Exhibit A, IRC, pages 212, 248, 297, 345, 397, 451, 506, (dated reimbursement claims). It is unclear from page 212 whether the 1998-1999 was signed on July 1, 2006, or July 11, 2006.

01/08/2007	Claimant signed the reimbursement claim form for fiscal year 2005-2006. ³
01/21/2008	Claimant signed the reimbursement claim form for fiscal year 2006-2007. ⁴
02/12/2009	Claimant signed the reimbursement claim form for fiscal year 2007-2008. ⁵
04/08/2009	The Controller sent the claimant an entrance conference letter dated April 8, 2009. ⁶
04/08/2011	The date of the Final Audit Report cover letter. ⁷
04/18/2011	Claimant received the Final Audit Report. ⁸
03/26/2014	Claimant filed the IRC. ⁹
01/15/2016	Controller filed late comments on the IRC. ¹⁰
05/20/2016	Commission staff issued the Draft Proposed Decision. ¹¹
06/14/2016	Controller filed late comments on the Draft Proposed Decision. ¹²

II. Background

Before 1984, community colleges were authorized but not required to impose student fees for various services, including health services, parking services, transportation services, program changes, late applications, and physical education courses using nondistrict facilities.¹³

³ Exhibit A, IRC, page 571.

⁴ Exhibit A, IRC, page 636.

⁵ Exhibit A, IRC, page 684.

⁶ Exhibit A, IRC, page 203 (audit confirmation letter). Exhibit B, Controller’s Late Comments on the IRC, page 14. Claimant asserts that the audit was initiated by some preliminary communication on or before March 16, 2009, see Exhibit A, IRC, pages 7-10.

⁷ Exhibit A, IRC, page 32 (Final Audit Report cover letter).

⁸ Exhibit A, IRC, pages 8-9, 200-201.

⁹ Exhibit A, IRC.

¹⁰ Exhibit B, Controller’s Late Comments on the IRC. Note that Government Code section 17553(d) states: “the Controller shall have no more than 90 days after the claim is delivered or mailed to file any rebuttal to an incorrect reduction claim. The failure of the Controller to file a rebuttal to an incorrect reduction claim shall not serve to delay the consideration of the claim by the Commission.” However, since the Controller’s comments were received prior to the preparation of the analysis, they have been included in the Proposed Decision.

¹¹ Exhibit C, Draft Proposed Decision.

¹² Exhibit D, Controller’s Late Comments on the Draft Proposed Decision, page 1.

¹³ Fees are authorized under former Education Code section 72246 and current Education Code section 76355 (health services), former Education Code section 72247 and current Education Code section 76360 (parking), former Education Code section 72248 and current Education

The test claim statutes and regulations require community colleges to implement enrollment fees and adopt regulations for their collection.¹⁴ Community colleges retain two percent of the enrollment fees collected;¹⁵ a percentage that has remained constant even though the amount of the enrollment fee has been amended various times. The Los Rios Community College District filed the *Enrollment Fee Collection* Test Claim, 99-TC-13, in June 2000, seeking reimbursement for the activities required to collect the enrollment fee.

In May 2001, the Glendale Community College District filed the *Enrollment Fee Waivers*, 00-TC-15, Test Claim, seeking reimbursement for the fee-waiver statutes and regulations¹⁶ that specify the groups of students for which fees are waived or exempted, and for whom Board of Governors Grants (BOG grants) are available. A BOG grant is an instrument used by a community college district to process financial assistance to a low-income student.¹⁷ In 1993, the Legislature changed the BOG grant program from a fee-offset grant program to a fee-waiver program (BOG fee waivers).¹⁸ The regulations governing the program were left intact, and were part of the Test Claim.¹⁹

In August 2002, the test claims were consolidated. On April 24, 2003, the Commission determined that the *Enrollment Fee Collection and Waiver* program imposed a partially-reimbursable state-mandated program on community college districts. On January 26, 2006, the Commission adopted the Parameters and Guidelines with the reimbursement period beginning either July 1, 1998 (for enrollment fee collection) or July 1, 1999 (for enrollment fee waivers), for the following activities:

- Adopting policies and procedures for collecting enrollment fees (one-time activity) and related staff training (one-time per employee).

Code section 76361 (transportation), former Education Code sections 72250 – 72250.5 and current California Code of Regulations, title 5, section 58507 (program changes), former Education Code section 72251 (late applications), and former Education Code section 72245 and current Education Code section 76395 (physical education courses using nondistrict facilities).

¹⁴ Education Code section 76300. Statutes 1984, 2d Ex. Sess., chapter 1; Statutes 1984, chapters 274 and 1401; Statutes 1985, chapters 920 and 1454; Statutes 1986, chapters 46 and 394; Statutes 1987, chapter 1118; Statutes 1989, chapter 136; Statutes 1991, chapter 114; Statutes 1992, chapter 703; Statutes 1993, chapters 8, 66, 67, and 1124; Statutes 1994, chapters 153 and 422; Statutes 1995, chapter 308; Statutes 1996, chapter 63; and Statutes 1999, chapter 72. California Code of Regulations, title 5, sections 58501 – 58508, 58611 – 58613, 58620 and 58630.

¹⁵ Education Code Section 76300 (c). This is called a “revenue credit” by the Community College Chancellor’s Office.

¹⁶ Education Code section 76300; California Code of Regulations, title 5, Sections 58600, 58601, 58610 – 58613, 58620, 58630.

¹⁷ California Code of Regulations, title 5, section 58601.

¹⁸ Statutes 1993, chapter 1124 (AB 1561).

¹⁹ California Code of Regulations, title 5, sections 58600 to 58630.

- Calculating and collecting the student enrollment fee for each student enrolled, except for nonresidents and special part-time students as specified.
- Adopting policies and procedures for determining which students are eligible for waiver of the enrollment fees (one-time activity), and related staff training (one-time per employee).
- Adopting procedures that will document all financial assistance provided.
- Recording and maintaining records that document all of the financial assistance for the waiver of enrollment fees.
- Waiving student fees in accordance with groups listed in Education Code section 76300(g) and (h), and waiving fees for students who apply and are eligible for the BOG fee waiver.²⁰

Section IV. of the Parameters and Guidelines further provides that reimbursement may be claimed based on actual costs incurred that are traceable and supported by contemporaneous source documents. Section VI. of the Parameters and Guidelines also requires claimants to keep documentation during the period subject to audit, or until the resolution of any audit findings.²¹ Section VII. of the Parameters and Guidelines governs offsetting savings and reimbursements, requiring claimants to offset their claims by any savings experienced in the same program, or revenues received from any source, including services fees collected, federal funds, and other state funds. Offsetting revenues required to be deducted from the costs claimed include: two percent of the revenue received from the enrollment fees collected, and two percent of the enrollment fees waived for specified categories of students; and after July 5, 2000, \$.91 per credit unit waived for certain categories of students. Offsetting savings also include any budget augmentation received under the Board Financial Assistance Program Administrative Allowance, or any other state budget augmentation received for administering the fee waiver.²²

The Controller's Audit and Summary of the Issues

In a letter dated April 8, 2009, the Controller confirmed that it was initiating a field audit on claimant's fiscal year 1998-1999 through 2007-2008 reimbursement claims, that the entrance conference would take place on April 21, 2009, and that several types of records were requested for the auditor's review.²³

²⁰ Exhibit A, IRC, pages 95-97 (Parameters and Guidelines, adopted Jan. 26, 2006).

²¹ Exhibit A, IRC, pages 94 and 98 (Parameters and Guidelines, adopted Jan. 26, 2006).

²² Exhibit A, IRC, pages 99-100 (Parameters and Guidelines, adopted Jan. 26, 2006).

²³ Exhibit A, IRC, pages 203-205 (entrance conference letter).

The Controller issued a Final Audit Report dated April 8, 2011, which concludes that \$90,288 is allowable and \$3,766,932 is unallowable.²⁴ The evidence in the record indicates that the claimant received the Final Audit Report on April 18, 2011.²⁵

The Final Audit Report consists of five findings, concluding that the district claimed unsupported and ineligible salaries and benefits and contract services, overstated indirect cost rates, and overstated offsetting savings and reimbursements as described below.²⁶

A. *Finding 1*

The unallowable costs include \$652,279 for salaries and benefits for one-time activities for which the claimant did not provide documentation (\$116,550) and for errors in the claimant's time allowances developed from employee surveys that estimated the time taken to perform the ongoing activities (\$535,729).

The one-time activities include \$50,824 claimed for preparing district policies and procedures, of which the Controller found that \$43,388 is unallowable and \$7,436 allowable. The allowable costs were claimed for the first fiscal year for enrollment fee collections (fiscal year 1998-1999) and enrollment fee waivers (fiscal year 1999-2000). For the remaining years, the Controller found that the costs claimed for preparing policies and procedures were not supported with documentation of actual costs incurred, and were the result of discretionary district policy.

The Controller also reduced costs claimed for training, for which \$93,136 was claimed but only \$19,974 was found allowable, primarily for the first fiscal year for which staff members were claimed. The Parameters and Guidelines authorize training costs of one time per employee, but the Controller found costs for some employees were claimed more than once. For 2007-2008, district staff received training from a software vendor for implementing its new Banner system, but the Controller determined that \$63,675, of \$82,358 claimed, was unrelated to the mandate based on district-provided documentation.

Finding 1 also reduced costs claimed for salaries and benefits for 12 on-going activities, supported by the estimated average time in minutes it took an employee to complete the activities per student per year, based on surveys developed by the claimant's mandate consultant. The Controller found that the district estimated the time using the wrong number of students, so the Controller recalculated the costs and found that enrollment fee collection costs were overstated by \$544,326 and enrollment fee waivers were understated by \$8,597, for a net \$535,729 in unallowable costs.²⁷

²⁴ Exhibit A, IRC, page 27 (Final Audit Report).

²⁵ Exhibit A, IRC, page 200 (showing the first page of the Final Audit Report with a date stamp of "APR 18, 2011"), and page 201 (an email dated April 18, 2011, from the claimant to its mandate consultant stating that "[w]e received the state's EFCW audit report today.")

²⁶ Exhibit A, IRC, page 32 (Final Audit Report); Exhibit B, Controller's Late Comments on the IRC, page 7.

²⁷ Exhibit A, IRC, pages 42-43, 49 (Final Audit Report). Exhibit B, Controller's Late Comments on the IRC, page 18.

B. *Finding 2*

The Controller found \$2,097,258 in unallowable costs claimed for salaries and benefits for employees to calculate and collect enrollment fees under Section IV.A(2)(a)(i-iv) of the Parameters and Guidelines. The costs claimed were based on surveys completed by claimant's employees that estimated the average annual time to perform the fee calculation and collection activities per student: 43.1 minutes annually per student for fiscal years 1998-1999 through 2005-2006; 14.5 minutes annually per student for fiscal year 2006-2007; and 31.3 minutes per student for fiscal year 2007-2008.²⁸ The Controller found that the estimated time allowances and costs claimed did not comply with the documentation requirements of the Parameters and Guidelines and were unsupported for the following reasons:

1. The claimant did not explain or support why average time allowances claimed were significantly greater than the time allowances based on the results of the Controller's inquiries and observations.
2. The time allowances recorded by the claimant in fiscal year 2006-2007 were based on estimated time from two employees from the Gilroy Business Office. Gilroy's Admissions and Records Office employees did not complete any survey forms for fiscal year 2006-2007. However, the claimant indicated that most of the fiscal year 2006-2007 collections occurred at the Gilroy office.
3. Based on the minutes recorded by the two employees surveyed at Gilroy's Business Office, the estimated time to perform the activities did not change from fiscal year 1998-1999 through fiscal year 2006-2007.
4. The claimant had an automated telephone registration process, in operation since 2003, and an automated online registration and payment system in operation since May 2006 that were used for the payment of enrollment fees without the assistance of district employees. However, the claimant did not exclude students who paid online when claiming reimbursable costs.
5. The surveys were not developed with sufficient instructions to clarify reimbursable activities.
6. The claimant did not independently verify the uniform time allowances with physical observation and inquiries to ensure that time allowances applied to students were accurate and reasonable.

²⁸ The costs were claimed for: (1) referencing student accounts and printing a list of enrolled courses; (2) calculating the fees, processing the payment, and preparing a payment receipt; (3) answering student questions or referring them to the appropriate person for an answer; (4) updating student records for the enrollment fee information, providing a copy to the student, and copying/filing enrollment fee documentation; (5) collecting delinquent fees; and (6) processing fee refunds for students who establish fee waiver. Exhibit A, IRC, pages 50-54 (Final Audit Report).

7. The claimant did not show that the methodology it used in developing time allowances produced a result that was representative of employees' time spent performing the reimbursable activities.²⁹

C. Finding 3

The Controller further determined that \$73,011 is unallowable, of \$91,273 claimed, for contract services provided by a software vendor that provided training on a new automated Banner system for fiscal year 2007-2008 because the invoices for the claimed costs did not entirely relate to the mandated procedures for collecting enrollment fees or determining which students are eligible for enrollment-fee waivers. The Controller's allocation of eligible costs was based on its review of the individual invoices, and information and discussion with the claimant's staff.³⁰

D. Finding 4

The Controller also found that \$1,002,702, of \$1,091,434 claimed, for overstated indirect costs is unallowable. Of this amount, \$26,102 was due to errors in the calculation of indirect cost rates and \$976,600 was due to the related unallowable direct salary and benefit costs reduced in findings 1 and 2. Claimant used the FAM-29C to calculate indirect costs as authorized by the Parameters and Guidelines, but did not correctly compute the FAM-29C rates in part because the claimant used capital costs to calculate indirect costs, even though the claiming instructions excludes them from the calculation, and because claimant did not include depreciation expenses or use allowances for building and equipment in its calculation of indirect costs.³¹

E. Finding 5

The Controller found that the claimant overstated offsetting savings and reimbursements by \$58,318, (\$74,854 for understated enrollment fee collection and \$16,536 for overstated enrollment fee waivers). Claimant did not accurately report the offsetting two percent of enrollment fee revenue, or the amount waived for enrollment fee waivers. Claimant also reported revenues received that exceeded allowable costs.³²

III. Positions of the Parties

A. Gavilan Community College District

The claimant asserts that the two-year statute of limitations in Government Code section 17558.5(a) to complete the audit expired on April 8, 2011, the date on the Final Audit Report, but that the claimant did not receive the audit report until April 18, 2011 which, "exceeds a normal mailing period in the United States mail. Therefore, the April 8, 2011, date may not be the date the final report actually left the Controller's office."³³ The claimant also asserts that it was on notice that an audit was scheduled for the district on March 16, 2009, or about three

²⁹ Exhibit A, IRC, page 54 (Final Audit Report).

³⁰ Exhibit A, IRC, page 61 (Final Audit Report).

³¹ Exhibit B, Controller's Late Comments on the IRC, pages 28-29.

³² Exhibit A, IRC, pages 65-66 (Final Audit Report).

³³ Exhibit A, IRC, page 9. See also the audit report date-stamped April 18, 2011, on page 200.

weeks before the Controller's audit initiation letter of April 8, 2009. Claimant argues that an audit is initiated when the Controller initially contacts the auditee.³⁴ Because the claimant was on notice of the audit earlier than April 8, 2009, the claimant states that the audit completion deadline was earlier than April 8, 2011, so that the Final Audit Report was issued more than two years after the date the audit commenced.³⁵

The claimant also disputes the audit reductions on several grounds. First, claimant asserts that the Controller uses the wrong audit standards because it conducted a performance audit and used generally accepted government auditing standards (GAGAS), when it should have used the standard in Government Code section 17561(d)(2), which authorizes the Controller to reduce claims only if the costs claimed are excessive or unreasonable.

Claimant argues that the Controller's audit findings inconsistently applied the documentation standards stated in the Parameters and Guidelines. Because the Parameters and Guidelines were adopted and the first claiming instructions were issued seven years after the first fiscal year in the audit period, the claimants were not on notice of the activities approved for reimbursement that should be documented until the eighth year of the eligibility period. Thus, claimant argues that it "would seem patently unreasonable to require contemporaneous documentation of daily staff time for the retroactive initial fiscal years."³⁶ According to the claimant, where its reported time and workload statistics were accepted by the auditor for some activities, the Controller is validating the claimant's good faith method and the mandate consultant's forms as an acceptable method for estimating average time. The claimant also argues that audit report does not document the qualitative criteria for the disallowances and, thus, an independent review of invoices by the Commission will be necessary.

The claimant makes various arguments against audit findings 1, 2, and 3, and also asserts that the reduction of indirect costs is incorrect. The Controller found the claimant overstated its indirect costs because it did not correctly compute the FAM-29C indirect cost rates. The claimant argues that the claiming instructions are not enforceable because they were not adopted in accordance with an administrative rulemaking process. Claimant also argues that in using the FAM-29C, it complied with the Parameters and Guidelines and any differences between its calculation and the Controller's calculation are minor, and that the large differences before fiscal year 2004-2005 are due to the claimant using capital costs and the Controller excluding capital costs from the calculation. Claimant argues that the Controller's requirement to exclude capital costs is unenforceable, so the standard that should be used is the excessive or unreasonable standard in Government Code section 17561(d)(2).

³⁴ Exhibit A, IRC, page 202 (email from Jim Spano to Nancy Patton, Nov. 22, 2011). See also Exhibit E, State Controller's Office Frequently Asked Questions Related to Mandated-Cost Programs, No. 15: "15. Is there a timeline or deadline for the SCO to complete an audit? Pursuant to Government Code section 17558.5, the SCO must complete the audit within two years of the audit start date. The SCO considers the initial telephone contact date with the auditee to be the audit start date." http://www.sco.ca.gov/Files-ARD-Local/mancost_faqsmandates.pdf (Accessed June 22, 2016.)

³⁵ Exhibit A, IRC, page 9.

³⁶ Exhibit A, IRC, page 15.

The claimant also contends that reductions relating to offsetting savings and revenues are incorrect. Since the audit report does not include the source documentation for the amounts reduced, the claimant says there is no way to evaluate the source documentation supporting the Controller's findings. The claimant also "disputes the application of these program revenues to claimed costs for the preparation of policies and procedures and staff training. These costs are not within the scope of costs for which the program funds are applicable."³⁷

Claimant did not file comments on the Draft Proposed Decision.

B. State Controller's Office

It is the Controller's position that the audit was completed within the two-year deadline. An audit is completed, according to the Controller, when the audit report is approved and signed by a representative of the Controller. The Controller argues that the date of mailing or receipt by the auditee are not relevant to the completion date, and there is no legal requirement for the audit report to be mailed or received within two years of the audit commencement date. Because the claimant was contacted on April 8, 2009, and the engagement letter was sent the same day, and the final report was dated April 8, 2011, the audit was completed within two years of its commencement.³⁸

Originally, the Controller maintained that the audit findings were correct and urged the Commission to deny the IRC.³⁹ However, in comments on the Draft Proposed Decision, the Controller states it is not challenging the proposed conclusion and recommendation to approve the IRC, and has pulled the audit report off of its website and notified the claimant of its withdrawal. According to the Controller, "The State will pay the district for the withdrawn audit findings upon availability of funds."⁴⁰

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 the local agency or school district. If the Commission determines that a reimbursement claim has been incorrectly reduced, section 1185.9 of the Commission's regulations requires the Commission to send the 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

³⁷ Exhibit A, IRC, page 25.

³⁸ Exhibit B, Controller's Late Comments on the IRC, page 14.

³⁹ Exhibit B, Controller's Late Comments on the IRC, pages 17.

⁴⁰ Exhibit D, Controller's Late Comments on the Draft Proposed Decision, page 1.

over the existence of state-mandated programs within the meaning of article XIII B, section 6.⁴¹ 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.”⁴²

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.⁴³ Under this standard, the courts have found that:

When reviewing the exercise of discretion, “[t]he scope of review is limited, out of deference to the agency’s authority and presumed expertise: ‘The court may not reweigh the evidence or substitute its judgment for that of the agency. [Citation.]’” ... “In general ... the inquiry is limited to whether the decision was arbitrary, capricious, or entirely lacking in evidentiary support. . . .” [Citations.] When making that inquiry, the “ ‘court must ensure that an agency has adequately considered all relevant factors, and has demonstrated a rational connection between those factors, the choice made, and the purposes of the enabling statute.’” [Citation.]’ ”⁴⁴

The Commission must review the Controller’s audit in light of the fact that the initial burden of providing evidence for a claim of reimbursement lies with the claimant.⁴⁵ In addition, sections 1185.1(f)(3) and 1185.2(c) of the Commission’s regulations require that any assertions of fact by the parties to an IRC must be supported by documentary evidence. The Commission’s ultimate findings of fact must be supported by substantial evidence in the record.⁴⁶

⁴¹ *Kinlaw v. State of California* (1991) 54 Cal.3d 326, 331-334; Government Code sections 17551, 17552.

⁴² *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.

⁴³ *Johnston v. Sonoma County Agricultural Preservation and Open Space Dist.* (2002) 100 Cal.App.4th 973, 983-984. See also *American Bd. of Cosmetic Surgery, Inc. v. Medical Bd. of California, supra*, 162 Cal.App.4th 534, 547.

⁴⁴ *American Bd. of Cosmetic Surgery, Inc. v. Medical Bd. of California* (2008) 162 Cal.App.4th 534, 547-548.

⁴⁵ *Gilbert v. City of Sunnyvale* (2005) 130 Cal.App.4th 1264, 1274-1275.

⁴⁶ 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.

There Is No Evidence in the Record that the Audit Was Completed Within the Two-Year Deadline Required by Government Code Section 17558.5, and thus the Audit Findings Are Void.

The claimant argues that the Controller did not timely complete the audit within the deadlines required by Government Code section 17558.5(a), so the audit is void.

Government Code section 17558.5(a) establishes time limits for the Controller to initiate and to complete an audit “not later than two years after the date the audit is commenced” 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 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. In any case, *an audit shall be completed not later than two years after the date that the audit is commenced.*⁴⁷

Failure to timely initiate or complete an audit within these statutory deadlines is a jurisdictional bar to the Controller’s reductions.⁴⁸

Although the parties dispute the date the Controller initiated the audit, there is no dispute that the audit was timely initiated within three years after the date the initial reimbursement claims were filed. The claimant submitted the initial reimbursement claims in July 2006, and according to the parties, the audit was initiated in either March or April 2009, by contact prior to the April 8, 2009 entrance conference letter.

The Commission, however, must determine the date the audit was initiated in order to decide whether the Controller timely completed the audit “not later than two years after the date that the audit is commenced.”

- A. There is no evidence in the record that the Controller initiated the audit within the meaning of Government Code section 17558.5(a) before the April 8, 2009 entrance conference letter.

The Legislature has not specifically defined the event that initiates the audit and, unlike other auditing agencies that have adopted formal regulations to clarify when the audit begins (which can be viewed as the controlling interpretation of a statute),⁴⁹ the Controller has not adopted a

⁴⁷ Statutes 2004, chapter 890, emphasis added.

⁴⁸ 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. (*People v. McGee* (1977) 19 Cal.3d 948, 962, citing *Morris v. County of Marin* (18 Cal.3d 901, 909-910)). Because the deadlines in Government Code section 17558.5 are mandatory and not directory, the requirement to meet the statutory deadline is jurisdictional.

⁴⁹ See, e.g., regulations adopted by the California Board of Equalization (title 18, section 1698.5, stating that an “audit engagement letter” is a letter “used by Board staff to confirm the start of an audit or establish contact with the taxpayer”).

regulation for the audits of state-mandate reimbursement claims. Because section 17558.5 is silent as to the act or event that initiates an audit, the Commission cannot, as a matter of law, state what the act or event is in all cases, but must determine when the audit was initiated based on the evidence in the record.

The initiation of an audit requires a unilateral act of the Controller. In this respect, the audit initiation provision of Government Code section 17558.5 is better characterized as a statute of repose, rather than a statute of limitations. The statute provides a period during which an audit or review has been commenced, and after which the claimant may enjoy repose, dispose of any evidence or documentation to support their claims, and assert a defense that the audit is not timely and therefore void.

The court in *Giest v. Sequoia Ventures, Inc.*, described a statute of repose as follows:

Unlike an ordinary statute of limitations which begins running upon accrual of the claim, [the] period contained in a statute of repose begins when a *specific event occurs*, regardless of whether a cause of action has accrued or whether any injury has resulted.” [citations] A statute of repose thus is harsher than a statute of limitations in that it cuts off a right of action after a specified period of time, irrespective of accrual or even notice that a legal right has been invaded.⁵⁰

Described by another court in *Inco Development Corp. v. Superior Court*,⁵¹ the characteristics of a statute of repose include that it is “not dependent upon traditional concepts of accrual of a claim, but is tied to an independent, objectively determined and verifiable event...” In addition, the California Supreme Court has said:

[S]tatutes of repose are in fact favored in the law, ‘designed to promote justice by preventing surprises through the revival of claims that have been allowed to slumber until evidence has been lost, memories have faded, and witnesses have disappeared. The theory is that even if one has a just claim it is unjust not to put the adversary on notice to defend within the period of limitation and that the right to be free of stale claims in time comes to prevail over the right to prosecute them.’⁵²

The Parameters and Guidelines for this program further provide that:

All documents used to support the reimbursable activities, as described in Section IV., must be retained during the period subject to audit. If an audit has been initiated by the Controller during the period subject to audit, the retention period is extended until the ultimate resolution of any audit findings.⁵³

Like a statute of limitations to file a civil action, the act or event that must occur before the expiration of the statutory period must be one that can be completed by the affected party alone, without the consent or cooperation of the auditee. This view is consistent with the plain

⁵⁰ *Giest v. Sequoia Ventures, Inc.* (2000) 83 Cal.App.4th 300, 305. Emphasis added.

⁵¹ *Inco Development Corp. v. Superior Court* (2005), 131 Cal.App.4th 1014.

⁵² *Adams v. Paul* (1995) 11 Cal.4th 583, 592.

⁵³ Exhibit A, IRC, page 111 (Parameters and Guidelines, adopted Jan. 26, 2006).

language of section 17558.5 that clearly authorizes the Controller to initiate the audit within the statutory time period, and does not expressly require the action or cooperation of any other party.⁵⁴

However, whether analyzed as a statute of repose, or a statute of limitations, the unilateral act that must occur before the expiration of the statutory period may be interpreted similarly. That is, the filing of a civil action may be interpreted analogously to the initiation of an audit, to the extent that the initiation of the audit, like the commencement of a civil action, terminates the running of the statutory period, and vests authority in the party to proceed.⁵⁵ However, unlike a plaintiff filing a complaint in court within a statutory time period to protect against a statute of limitations defense barring the matter, Government Code section 17558.5 does not require the Controller to lodge a document to *prove* it timely initiated an audit. Nevertheless, because the Controller's authority to audit must be exercised within a specified time, it must be within the Controller's exclusive control to meet or fail to meet the deadline imposed. The Controller has the burden of proof on this issue and must show with evidence in the record that the claimant was notified that an audit was being initiated by the statutory deadline to ensure that the claimant not dispose of any evidence or documentation to support its claim for reimbursement.

In past IRCs, the dispute on this issue centered on whether the entrance conference letter or the entrance conference itself represented the start of the audit. In *Health Fee Elimination*, 05-4206-I-06, the Commission agreed with the Controller that, in that case, the goals of finality and predictability in the operation of a statute of limitations were best served by applying section 17558.5 to the Controller's entrance conference letter and not to the date of an entrance conference itself. The entrance conference is scheduled based on the availability of the parties and the date does not represent a unilateral act by the Controller. The entrance conference letter, to the extent that it can be shown the letter was sent to the claimant for purposes of notice, represents a unilateral act by the Controller to exercise its audit authority before the statutory deadline and provides sufficient, verifiable, notice to a claimant to retain supporting documentation for the claim during the audit.⁵⁶

Here, however, neither party is arguing that the entrance conference, which occurred on April 21, 2009, initiated the audit. Nor are the parties disputing the Controller's assertion that the entrance conference letter, dated April 8, 2009, is also the date the Controller issued the letter to the claimant.⁵⁷ The entrance conference letter is on the Controller's official letterhead, is

⁵⁴ This analysis is consistent with the Commission's IRC Decision in *Collective Bargaining and Collective Bargaining Agreement Disclosure*, 09-4225-I-17 and 10-4425-I-18, adopted March 27, 2015.

⁵⁵ *Liptak v. Diane Apartments, Inc.* (1980) 109 Cal.App.3d 762, 773 ["A party does not have a vested right in the time for the commencement of an action [and nor] does he have a vested right in the running of the statute of limitations prior to its expiration." (citing *Kerchoff-Cuzner Mill and Lumber Company v. Olmstead* (1890) 85 Cal. 80; *Mudd v. McColgan* (1947) 30 Cal.2d 463, 468)].

⁵⁶ *Health Fee Elimination* IRC (05-4206-I-06), adopted March 27, 2015.

⁵⁷ Exhibit B, Controller's Late Comments on the IRC, page 14.

signed by the Controller's audit manager for the Mandated Cost Audit Bureau, and states in relevant part:

This letter confirms that Curt Chiesa has scheduled an audit of the Gavilan Community College District's legislatively mandated Enrollment Fee Collection and Waiver Program cost claims filed for fiscal year (FY) 1998-99 through FY 2007-08. Government Code sections 12410, 17558.5, and 17561 provide the authority for this audit. The entrance conference is scheduled for Tuesday, April 21, 2009, at 11:30 a.m. We will begin audit fieldwork after the entrance conference.⁵⁸

The letter also requests the claimant to provide documentation to support the costs claimed.⁵⁹

The claimant, however, asserts that it was notified of the audit in March 2009, *before* the April 8, 2009 entrance conference letter, and argues that the audit was initiated at that time.⁶⁰ The claimant states that the plain language of the entrance conference letter indicates that the Controller contacted the claimant *before* drafting the letter to confirm the audit, and submits an email dated March 16, 2009, from its mandate consultant (Keith Petersen) to the claimant (nbailey@gavilan.edu) about an audit for the program "next month."⁶¹

Had the entrance conference at Contra Costa this morning *for the same program you are scheduled to be audited for next month, Enrollment Fee Collection and Waiver*. It will probably be the same auditor. This is the first audit of this program, so they weren't able to tell me much about what they will be looking at. They did say that they wanted to interview the Financial Aid director about the BOG waiver process.

Next week I will send you the notes for your entrance conference and Mr. Keeler can then get back to me with his questions.⁶²

⁵⁸ Exhibit A, IRC, page 203.

⁵⁹ Exhibit A, IRC, pages 203-205.

⁶⁰ The claimant supports this contention (that telephonic contact from the Controller to the claimant commences an audit) with an email from the Controller's Office staff to Commission staff, dated November 22, 2011, that states the following:

We consider the event that initiates an audit pursuant to Government Code section 17558.5 to be the date of the initial contact by the SCO to the auditee (generally a telephone contact) to inform them and put them on notice of the SCO's intention to perform the audit. In addition, we consider this same date as the event that commences the two-year period to complete an audit pursuant to Government Code section 17558.5. (Exhibit A, IRC, page 208.)

⁶¹ Exhibit A, IRC, pages 9 and 206.

⁶² Exhibit A, IRC, page 206 (emphasis added). The claimant also filed an email from the Controller's Office staff to Commission staff, dated November 22, 2011, that states that initial contact, generally by telephone, is enough to put the claimant on notice of the audit initiation:

The contents of this email, even if admissible, do not provide any evidence to support the assertion that *the Controller notified the claimant* in March 2009 that an audit was being initiated.⁶³ The email is from the claimant's own consultant and there is no evidence in the record that the Controller provided any notice to the claimant in March 2009 that it was intending to audit these reimbursement claims. Thus, based on this record, the Commission cannot find that the Controller initiated the audit in March 2009.

Moreover, there is no evidence in the record from the Controller's Office to verify that the audit was initiated earlier than the April 8, 2009 entrance conference letter. Accordingly, based on this record, the Commission finds that the Controller initiated the audit within the meaning of Government Code section 17558.5(a) on April 8, 2009.

B. There is no evidence in the record that the audit was timely completed, and thus, the audit is void.

Government Code section 17558.5(a) requires that "an audit shall be completed not later than two years after the date that the audit is commenced." Because the audit in this case was commenced within the meaning of Government Code section 17558.5(a) on April 8, 2009, the date of the entrance conference letter, it would have to be completed no later than April 8, 2011, to be timely.

The Final Audit Report is *dated* April 8, 2011. The claimant states, however, that the Final Audit Report was not received until April 18, 2011, ten days after the two year limitation period; as evidenced by the claimant's date-received stamp on the first page of the Final Audit Report.⁶⁴ The claimant suggests that the audit was not complete until the Final Audit Report was received, and that the ten day difference between the date of the report and the date of receipt "exceeds the normal mailing period in the United States mail."⁶⁵

The Controller argues that it timely completed the audit on April 8, 2011, and that the audit is complete when the audit report is approved and signed, and not when it is mailed or received by the claimant:

We consider the event that initiates an audit pursuant to Government Code section 17558.5 to be the date of the initial contact by the SCO to the auditee (generally a telephone contact) to inform them and put them on notice of the SCO's intention to perform the audit. In addition, we consider this same date as the event that commences the two-year period to complete an audit pursuant to Government Code section 17558.5. (Exhibit A, IRC, page 208.)

⁶³ Hearsay is an out-of-court statement (both oral and written) that is offered for the truth of the matter asserted and is generally inadmissible in court proceedings. (Evid. Code, § 1200.) The Commission's regulations provide that hearsay evidence may be used for purposes of supplementing or explaining other evidence, but shall not be sufficient in itself to support a finding unless it would be admissible over objection in civil actions. (Cal. Code Regs., tit.2, § 1187.5(a).)

⁶⁴ Exhibit A, IRC, pages 8-9, 200-201.

⁶⁵ Exhibit A, IRC, pages 8-9.

An audit is completed when the final audit report is approved and signed by an authorized SCO representative. The dates that reports are mailed and/or received are irrelevant for determining when an audit is considered to be completed. There is no legal requirement for the SCO to mail an audit report within two years or for claimants to physically receive an audit report within two years of the audit commencement date.⁶⁶

The Commission finds there is no evidence in the record that the audit was timely completed.

The completion of the audit under Government Code section 17558.5(a), like the initiation of the audit, requires the unilateral act of the Controller. The statutory deadline to complete the audit, like the deadline to initiate the audit, acts as a statute of repose that provides a period during which the Controller is authorized to audit and, once commenced, must complete the audit within two years. After the audit period, the claimants may enjoy repose and dispose of any evidence or documentation to support their claims for reimbursement. As stated in the Parameters and Guidelines for this program, all documents used to support the reimbursable activities must be retained “until the ultimate resolution of any audit findings.”⁶⁷ Because the Controller’s authority to audit must be exercised within a specified time, it is within the Controller’s exclusive control to meet or fail to meet the statutory two-year deadline. The Controller has the burden of proof to show with evidence in the record that the claimant was notified that the audit was completed by the statutory deadline to ensure that the claimant not dispose of any evidence or documentation before “the ultimate resolution of any audit findings.”

This conclusion is further supported by Government Code section 17558.5(c), which expressly provides that if any audit adjustments are made, the Controller is required to notify the claimant in writing explaining the adjustments as follows:

The Controller *shall notify* the claimant in writing within 30 days after issuance of a remittance advice 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 overall reimbursement to the local agency or school district, and the reason for the adjustment. . . . [Emphasis added.]

Therefore, under the statutory scheme, an audit resulting in adjustments is complete when the Controller notifies the claimant that the audit is complete by this written notice of adjustment, and not when an audit report is simply approved and signed by an authorized employee of the Controller’s Office as asserted by the Controller. For the notice to be timely, it must be given “not later than two years after the date that the audit is commenced.”

The question remains, however, when the Controller provided notice in this case. As stated above, the Controller initiated the audit of the reimbursement claims on April 8, 2009. The Controller adjusted the reimbursement claims and provided written notice to the claimant explaining the adjustments in the Final Audit Report dated April 8, 2011. Claimant received the Final Audit Report *by mail* on April 18, 2011, ten days past the deadline. Although the

⁶⁶ Exhibit B, Controller’s Late Comments on the IRC, page 14.

⁶⁷ Exhibit A, IRC, page 111 (Parameters and Guidelines, adopted Jan. 26, 2006).

Controller's practice has been to send Final Audit Reports by mail, there is nothing in the Government Code, and the Controller has not adopted regulations, that authorize the service of the written notice required by Government Code section 17558.5(c) by mail, or imputes notice to the claimant as of the date of mailing. Government Code section 17558.5(c) simply states that "[t]he Controller *shall notify* the claimant in writing ... of the reasons for the reduction,"

Unlike section 17558.5(c), the Legislature has expressly authorized service of notice by mail in other statutes, and when service of notice is authorized by mail, service is complete at the time the notice is deposited in the mailbox. For example, Code of Civil Procedure section 1013(a), which applies to service of documents in civil proceedings pending in court, states:

In case of service by mail, the notice or other paper shall be deposited in a post office, mailbox, subpost office, substation, or mail chute, or other like facility regularly maintained by the United States Postal Service, in a sealed envelope, with postage paid, addressed to the person on whom it is to be served, at the office address as last given by that person on any document filed in the cause and served on the party making service by mail; otherwise at that party's place of residence. Service is complete at the time of the deposit . . .

If service is authorized by mail, a proof of service that the notice was properly mailed creates the presumption under the law that the notice was complete at the time of the deposit in the mailbox and was received in the ordinary course of mail absent evidence to the contrary.⁶⁸ Code of Civil Procedure section 1013(a) further makes allowances for the uncertainties of mail delivery by giving recipients of mailed notices longer time to act or to exercise their rights that flow from the notice. Thus, if the place of address and the place of mailing are within the State of California, then the time for any response, right, or duty triggered by the notice, and which must be performed within a statutory time period, "shall be extended *five* calendar days."

There is no evidence in this case, however, of the date the Final Audit Report was mailed and, thus, the Commission cannot presume that the notice was timely served. The Final Audit Report was received *ten* calendar days after the date of the report, April 8, 2011, which may suggest that it was not actually deposited in the mail on the date of the report. Thus, the Commission cannot find that the audit was timely completed on April 8, 2011, as urged by the Controller.

Moreover, some courts have held that when the law is silent on how service shall be made, a notice served by mail is not effective unless and until it is received. For example, in *Johnson v. Barreiro*, a personal injury case stemming from an automobile accident, the dispute centered on the determination of the owner of the vehicle that caused the accident.⁶⁹ On December 24, the appellant sold the vehicle with a conditional sales contract to the driver who caused the accident. The driver was in possession of the car at the time of the January 1 accident, but no notice of sale or registration of transfer was filed with or received by the Department of Motor Vehicles (DMV) prior to the accident. The appellant argued that it mailed the notice of transfer to the DMV on December 31. However, there was no proof of service or evidence of mailing, and the notice was not received by the DMV until January 2, after the accident. In addition, the plaintiff

⁶⁸ Code of Civil Procedure sections 1013(a) and 1013a; Evidence Code section 641; *Bear Creek Master Ass'n. v. Edwards* (2005) 130 Cal.App.4th 1470, 1486.

⁶⁹ *Johnson v. Barreiro* (1943) 59 Cal.App.2d 213.

presented evidence that the appellant, with other vehicle sales made on December 31, did not report those sales to DMV until January 4, 7, and 13.⁷⁰ The court held the appellant responsible for the damages, finding that “in the absence of a statute authorizing the service of a notice by mail, a notice so served is ineffective unless and until it is received” as follows:

Upon evidence before it we think that the trial court was justified in concluding that the notice was not transmitted until January 2nd, and that its finding to that effect is sufficiently sustained. Even if mailed on the 31st of December, said papers were not received by the department until the 2nd of January; and there is nothing in the applicable statutes to the effect that the deposit of said papers in the mail on the 31st would impute notice to the department as of that date so as to relieve appellant of liability as owner. Generally speaking, substituted and constructive notices are not favored in law and are countenanced only as a matter of necessity or extreme expediency. (20 Cal.Jur. 243.) And in the absence of a statute authorizing the service of a notice by mail, a notice so served is ineffective unless and until it is received. (39 Am.Jur. 249 . . .) Also proof of service of notice by mail should show compliance with the conditions of its existence, and show that the notice properly addressed, with postage prepaid, was duly deposited in the mail. (39 Am.Jur. 252.) There was no such proof in this case.⁷¹

The court’s holding in *Johnson* was later applied in *Hoschler v. Sacramento City Unified School District*, where the court interpreted Education Code section 44929.1, which requires a school district to notify a probationary employee in a position requiring certification, on or before March 15 of the employee’s second year of employment with the district, of the district’s decision to reelect or not reelect the employee for the next succeeding school year to the position. In the event that the governing board does not give timely notice, the employee is deemed reelected for the next succeeding school year.⁷² The school district mailed a notice of probationary release on March 12, and the employee, who undisputedly did not willfully refuse to pick up his mail, did not receive a copy of the notice until well after the deadline on May 8. The court held that the employee was not timely notified by the March 15 deadline and was allowed to keep his job for the next school year.⁷³ The court stated:

Section 44929.1 is silent as to a method of giving the required notice. Under settled principles of statutory construction, “[a] statute requiring that a notice shall be given, but which is silent as to the manner of giving such notice, contemplates personal service thereof.” [Citations omitted.] As the court noted in *Long*: “It may be broadly stated that where a statute or contract requires the giving of notice, and there is nothing in context, or in the circumstances of the case, to show that any other form of notice was intended, personal notice will be required. [Citation.] This is true because the law always favors a personal notice, and countenances

⁷⁰ *Id.*, pages 214-216.

⁷¹ *Id.*, pages 218-219.

⁷² *Hoschler v. Sacramento City Unified School Dist.* (2007) 149 Cal.App.4th 258, 264.

⁷³ *Id.*, page 272.

substituted and constructive notices as matters of necessity or extreme expediency.” [Citation.]

Since the District claims it sent notice of Hoschler’s nonretention by certified mail, and the evidence is undisputed that he did not receive the notice until well after March 15, the notice of nonrenewal was untimely. (*Johnson, supra*, 59 Cal.App.2d at pp. 218-219 . . . [where statute does not prescribe method of service, notice served by mail not effective until received.].)⁷⁴

These cases can be distinguished from *Matthew v. Civil Service Commission of City and County of San Francisco*, where a city charter was silent as to the manner of giving notice, but the court found that service by mail was contemplated by the charter since the charter made references to “mail” and notice being “sent” as follows:

Ordinarily, ‘As to the matter of notice, it may be said that where a statute requires notice and does not specify how it shall be given, the presumption is that personal service is required’ (*Colyear v. Tobriner*, 7 Cal.2d 735 at page 743, 62 P.2d 741, at page 745, 109 A.L.R. 191). ‘It may be broadly stated that, where a statute or contract requires giving of notice, and there is nothing in the context or circumstances of the case, to show that any other form of notice was intended, personal notice will be required’ (*Stockton Automobile Co. v. Confer*, 154 Cal. 402 at page 408, 97 P. 881, at page 884). While Section 148 of the charter is silent as to the manner of giving notice, Rule 23 in which reference is made to ‘mail’ and notice being ‘sent’ quite obviously contemplates that the notice may be mailed. The context and circumstances of the case as governed by the rules adopted pursuant to the charter and to supplement its provisions in the operation of the civil service system show that a form of notice other than personal was intended. This interpretation is supported by the rule of administrative interpretation over a period of 24 years or so, during all of which time such notices were all sent by ordinary mail.⁷⁵

Unlike the rule in the city charter in the *Matthew* case, Government Code section 17558.5(c) simply requires that the “Controller *shall notify* the claimant in writing” There are no requirements in the statute on how the notice must be served. Thus, based on the *Johnson* line of cases, the audit was not complete until the claimant received the notice of reductions (in the Final Audit Report) on April 18, 2011, ten days past the two-year audit completion deadline.

Because there is no evidence in the record that the Controller timely completed the audit by the April 8, 2011 deadline, the Commission finds that the audit is void.

V. Conclusion

Based on the foregoing, the Commission approves this IRC and requests that the Controller reinstate all costs that were reduced, totaling \$3,766,932, in accordance with Government Code section 17551(d) and section 1185.9 of the Commission regulations.

⁷⁴ *Id.*, page 264.

⁷⁵ *Matthew v. Civil Service Commission of City and County of San Francisco* (1958) 158 Cal.App.2d 169, 173-174.



RE: **Decision**

Enrollment Fee Collection and Waivers, 13-9913-I-01

Education Code Section 76300; Statutes 1984, 2d Ex. Sess., Chapter 1;
Statutes 1984, Chapters 274 and 1401; Statutes 1985, Chapters 920 and 1454;
Statutes 1986, Chapters 46 and 394; Statutes 1987, Chapter 1118;
Statutes 1989, Chapter 136; Statutes 1991, Chapter 114; Statutes 1992, Chapter 703;
Statutes 1993, Chapters 8, 66, 67, and 1124; Statutes 1994, Chapters 153 and 422;
Statutes 1995, Chapter 308; Statutes 1996, Chapter 63; Statutes 1999, Chapter 72;
California Code of Regulations, Title 5, Sections 58501-58503,
58611-58613, 58620, and 58630
Fiscal Years: 1998-1999, 1999-2000, 2000-2001, 2001-2002,
2002-2003, 2003-2004, 2004-2005, 2005-2006, 2006-2007, and 2007-2008
Gavilan Community College District, Claimant

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



Heather Halsey, Executive Director

Dated: July 26, 2016

BEFORE THE
COMMISSION ON STATE MANDATES
STATE OF CALIFORNIA

**IN RE INCORRECT REDUCTION CLAIM
ON:**

Government Code Sections 7572.55 and 7576;
Statutes 1994, Chapter 1128 (AB 1892);
Statutes 1996, Chapter 654 (AB 2726);
California Code of Regulations, Title 2,
Chapter 1, Sections 60020, 60030, 60040,
60045, 60050, 60055, 60100, 60110, 60200¹
(Emergency regulations effective July 1, 1998
[Register 98, No. 26], final regulations
effective August 9, 1999 [Register 99, No. 33])

Fiscal Years 2002-2003 and 2003-2004

County of Los Angeles, Claimant

Case No.: 12-0240-I-01

Handicapped and Disabled Students II

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

(Adopted July 22, 2016)

(Served July 27, 2016)

DECISION

The Commission on State Mandates (Commission) heard and decided this Incorrect Reduction Claim (IRC) during a regularly scheduled hearing on July 22, 2016. Edward Jewik and Hasmik Yaghobyan appeared on behalf of County of Los Angeles. Jim Spano and Chris Ryan appeared for the State Controller's Office.

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

The Commission adopted the Proposed Decision to deny this IRC by a vote of 6-0 as follows:

¹ 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 specific sections of the statutes and executive orders that were approved in the test claim decision. However, that was an oversight in the case of the Parameters and Guidelines at issue in this case.

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

Summary of the Findings

This IRC was filed in response to an audit by the State Controller’s Office (Controller) of the County of Los Angeles’s (claimant’s) initial reimbursement claims under the *Handicapped and Disabled Students II* program for fiscal years 2002-2003 and 2003-2004. The Controller reduced the claims because it found the claimant: (1) overstated costs by using inaccurate units of service, and (2) overstated offsetting revenues.² In this IRC, the claimant contends that the Controller’s reductions were incorrect and requests, as a remedy, that the Commission reinstate the following cost amounts, which would then become subject to the Program’s reimbursement formula:

FY2002-2003: \$216,793
FY2003-2004: \$231,409³

After a review of the record and the applicable law, the Commission finds that the IRC was untimely filed. Accordingly, the Commission denies this IRC.

I. Chronology

- 05/08/2006 Claimant dated the reimbursement claim for fiscal year 2002-2003.⁴
- 05/08/2006 Claimant dated the reimbursement claim for fiscal year 2003-2004.⁵
- 08/12/2008 Controller dated a letter to claimant confirming the start of the audit.⁶

² See, e.g., Exhibit A, IRC, page 96 (Letter from Jeffrey V. Brownfield to Gloria Molina, dated May 28, 2010).

³ Exhibit A, IRC, page 1.

⁴ Exhibit A, IRC, page 113 (cover letter), page 117 (Form FAM-27).

⁵ Exhibit A, IRC, page 113 (cover letter), page 254 (Form FAM-27).

⁶ Exhibit B, Controller’s Late Comments on the IRC, page 148-149 (Letter from Christopher Ryan to Wendy L. Watanabe, dated August 12, 2008). See also Exhibit B, Controller’s Late Comments on the IRC, page 19, which asserts “The SCO contacted the county by phone on July 28, 2008, to initiate the audit” However, this assertion is not supported by a declaration of a person with personal knowledge or any other evidence in the record.

- 03/26/2010 Controller issued the Draft Audit Report, dated March 26, 2010.⁷
- 04/30/2010 Claimant sent a letter to Controller dated April 30, 2010, in response to the Draft Audit Report.⁸
- 05/28/2010 Controller issued the Final Audit Report dated May 28, 2010.⁹
- 06/11/2013 Claimant filed this IRC.¹⁰
- 11/25/2014 Controller filed late comments on the IRC.¹¹
- 12/23/2014 Claimant filed a request for extension of time to file rebuttal comments which was granted for good cause.
- 03/26/2015 Claimant filed rebuttal comments.¹²
- 05/20/2016 Commission staff issued the Draft Proposed Decision.¹³
- 06/06/2016 Controller filed comments on the Draft Proposed Decision.¹⁴
- 06/10/2016 Claimant filed comments on the Draft Proposed Decision.¹⁵

II. Background

In 1975, Congress enacted the Education for All Handicapped Children Act (EHA) with the stated purpose of assuring that “all handicapped children have available to them . . . a free appropriate public education which emphasizes special education and related services designed to meet their unique needs”¹⁶ Among other things, the EHA authorized the payment of federal funds to states which complied with specified criteria regarding the provision of special education and related services to handicapped and disabled students.¹⁷ The EHA was ultimately renamed the Individuals with Disability Education Act (IDEA) and guarantees to disabled pupils, including those with mental health needs, the right to receive a free and appropriate public

⁷ Exhibit A, IRC, page 101.

⁸ Exhibit A, IRC, pages 107-109 (Letter from Wendy L. Watanabe to Jeffrey V. Brownfield, dated April 30, 2010).

⁹ Exhibit A, IRC, page 96 (cover letter), pages 95-110 (Final Audit Report).

¹⁰ Exhibit A, IRC, pages 1, 3.

¹¹ Exhibit B, Controller’s Late Comments on the IRC, page 1.

¹² Exhibit C, Claimant’s Rebuttal Comments, page 1.

¹³ Exhibit D, Draft Proposed Decision.

¹⁴ Exhibit E, Controller’s Comments on the Draft Proposed Decision, page 1.

¹⁵ Exhibit F, Claimant’s Comments on the Draft Proposed Decision, page 1.

¹⁶ Public Law 94-142, section 1, section 3(a) (Nov. 29, 1975) 89 U.S. Statutes at Large 773, 775. See also 20 U.S.C. § 1400(d) (current version).

¹⁷ Public Law 94-142, section 5(a) (Nov. 29, 1975) 89 U.S. Statutes at Large 773, 793. See also 20 U.S.C. 1411(a)(1) (current version).

education, including psychological and other mental health services, designed to meet the pupil's unique educational needs.¹⁸

The *Handicapped and Disabled Students* Mandate

In California, the responsibility of providing both “special education” and “related services” was initially shared by local education agencies (broadly defined) and by the state government.¹⁹ However, in 1984, the Legislature enacted AB 3632, which amended Government Code chapter 26.5 relating to “interagency responsibilities for providing services to handicapped children” which created separate spheres of responsibility.²⁰ And, in 1985, the Legislature further amended chapter 26.5.²¹

The impact of the 1984 and 1985 amendments — sometimes referred to collectively as “Chapter 26.5 services” — was to transfer the responsibility to provide mental health services for disabled pupils from school districts to county mental health departments.²²

In 1990 and 1991, the Commission adopted the Statement of Decision and the Parameters and Guidelines approving the Test Claim *Handicapped and Disabled Students*, CSM 4282, as a reimbursable state-mandated program within the meaning of article XIII B, section 6 of the California Constitution.²³ The Commission found that the activities of providing mental health assessments; participation in the individualized education plan (IEP) process; and providing psychotherapy and other mental health treatment services were reimbursable and that providing mental health treatment services was funded as part of the Short-Doyle Act, based on a cost-sharing formula with the state.²⁴ Beginning July 1, 2001, however, the cost-sharing ratio for providing psychotherapy and other mental health treatment services no longer applied, and

¹⁸ Public Law 101-476, section 901(a)(1) (October 30, 1999) 104 U.S. Statutes at Large 1103, 1141-1142.

¹⁹ *California School Boards Ass'n v. Brown* (2011) 192 Cal.App.4th 1507, 1514.

²⁰ Statutes of 1984, chapter 1747.

²¹ Statutes of 1985, chapter 1274.

²² “With the passage of AB 3632 (fn.), California’s approach to mental health services was restructured with the intent to address the increasing number of emotionally disabled students who were in need of mental health services. Instead of relying on LEAs [local education agencies] to acquire qualified staff to handle the needs of these students, the state sought to have CMH [county mental health] agencies — who were already in the business of providing mental health services to emotionally disturbed youth and adults — assume the responsibility for providing needed mental health services to children who qualified for special education.” Stanford Law School Youth and Education Law Clinic, *Challenge and Opportunity: An Analysis of Chapter 26.5 and the System for Delivering Mental Health Services to Special Education Students in California*, May 2004, page 12.

²³ “As local mental health agencies had not previously been required to provide Chapter 26.5 services to special education students, local mental health agencies argued that these requirements constituted a reimbursable state mandate.” (*California School Boards Ass'n v. Brown* (2011) 192 Cal.App.4th 1507, 1515.)

²⁴ Former Welfare and Institutions Code sections 5600 et seq.

counties were entitled to receive reimbursement for 100 percent of the costs to perform these services.²⁵

In 2004, the Legislature directed the Commission to reconsider *Handicapped and Disabled Students*, CSM 4282.²⁶ In May 2005, the Commission adopted the Statement of Decision on Reconsideration, 04-RL-4282-10, and determined that the original Statement of Decision correctly concluded that the test claim statutes and regulations impose a reimbursable state-mandated program on counties pursuant to article XIII B, section 6. The Commission concluded, however, that the 1990 Statement of Decision did not fully identify all of the activities mandated by the state or the offsetting revenue applicable to the program. Thus, for costs incurred beginning July 1, 2004, the Commission identified the activities expressly required by the test claim statutes and regulations that were reimbursable, identified the offsetting revenue applicable to the program, and updated the new funding provisions enacted in 2002 that required 100 percent reimbursement for mental health treatment services.

The *Handicapped and Disabled Students II* Mandate

In May 2005, the Commission also adopted the Statement of Decision on *Handicapped and Disabled Students II*, 02-TC-40/02-TC-49, a Test Claim addressing statutory amendments enacted between the years 1986 and 2002 to Government Code sections 7570 et seq., and 1998 amendments to the joint regulations adopted by the Departments of Education and Mental Health.²⁷

The Controller's Audit and Reduction of Costs

The Controller issued a Draft Audit Report dated March 26, 2010, and provided a copy to the claimant for comment.²⁸

In a three-page letter dated April 30, 2016, the claimant responded to the Draft Audit Report, agreeing with the audit's findings and accepting its recommendations.²⁹ The first page of this three-page letter contains the following statement:

The County's response, which is attached, indicates agreement with the audit findings and the actions that the County will take to implement policies and

²⁵ Statutes 2002, chapter 1167 (AB 2781, §§ 38, 41).

²⁶ Statutes 2004, chapter 493 (SB 1895).

²⁷ Statutes 2011, chapter 43 (AB 114) eliminated the mandated programs for *Handicapped and Disabled Students* (4282, 04-RL-4282-10) and *Handicapped and Disabled Students II* (02-TC-40/02-TC-49) by transferring responsibility for providing mental health services under IDEA back to school districts, effective July 1, 2011. On September 28, 2012, the Commission adopted an amendment to the parameters and guidelines ending reimbursement effective July 1, 2011.

²⁸ Exhibit A, IRC, page 101.

²⁹ Exhibit A, IRC, pages 107-109 (Letter from Wendy L. Watanabe to Jeffrey V. Brownfield, dated April 30, 2010).

procedures to ensure that the costs claimed under HDSII are eligible, mandate related, and supported.³⁰

The following two pages of the three-page letter contain further statements of agreement with the Controller's findings and recommendations.

In response to the Controller's Finding No. 1 that the claimant overstated medication support costs by more than \$1.1 million, the claimant responded:

We agree with the recommendation. The County will review and establish policies and procedures to ensure that only actual units of service for eligible clients are claimed in accordance with the mandate program.³¹

In response to the Controller's Finding No. 2 that the claimant overstated indirect costs by more than \$80,000, the claimant responded:

We agree with the recommendation. The County will review and establish policies and procedures to ensure that indirect cost rates are applied to eligible and supported direct costs.³²

In response to the Controller's Finding No. 3 that the claimant overstated offsetting reimbursements by more than \$500,000, the claimant responded:

We agree with the recommendation. The County will review and establish policies and procedures to ensure that revenues are applied to valid program costs, appropriate SD/MC and EPSDT reimbursement percentage rates are applied to eligible costs, and supporting documentation for applicable offsetting revenues are maintained.³³

In a separate two-page letter also dated April 30, 2010, the claimant addressed its compliance with the audit and the status of any remaining reimbursement claims.³⁴ Material statements in the two-page letter include:

- "We maintain accurate financial records and data to support the mandated cost claims submitted to the SCO."³⁵

³⁰ Exhibit A, IRC, page 107 (Letter from Wendy L. Watanabe to Jeffrey V. Brownfield, dated April 30, 2010) (emphasis added).

³¹ Exhibit A, IRC, page 108 (Letter from Wendy L. Watanabe to Jeffrey V. Brownfield, dated April 30, 2010).

³² Exhibit A, IRC, page 108 (Letter from Wendy L. Watanabe to Jeffrey V. Brownfield, dated April 30, 2010).

³³ Exhibit A, IRC, page 109 (Letter from Wendy L. Watanabe to Jeffrey V. Brownfield, dated April 30, 2010).

³⁴ Exhibit B, Controller's Late Comments on the IRC, pages 152-153 (Letter from Wendy L. Watanabe to Jim L. Spano, dated April 30, 2010).

³⁵ Exhibit B, Controller's Late Comments on the IRC, pages 152-153 (Letter from Wendy L. Watanabe to Jim L. Spano, dated April 30, 2010, paragraph 1).

- “We designed and implemented the County’s accounting system to ensure accurate and timely records.”³⁶
- “We claimed mandated costs based on actual expenditures allowable per the Handicapped and Disabled Students II Program’s parameters and guidelines.”³⁷
- “We made available to the SCO’s audit staff all financial records, correspondence, and other data pertinent to the mandated cost claims.”³⁸
- “We are not aware of any . . . Relevant, material transactions that were not properly recorded in the accounting records that could have a material effect on the mandated cost claims.”³⁹
- “There are no unasserted claims or assessments that our lawyer has advised us are probable of assertion that would have a material effect on the mandated cost claims.”⁴⁰
- “We are not aware of any events that occurred after the audit period that would require us to adjust the mandated cost claims.”⁴¹

On May 28, 2010, the Controller issued the Final Audit Report.⁴² The Controller reduced the claims because the claimant: (1) overstated costs by using inaccurate units of service, (2) and overstated offsetting revenues.⁴³

On June 11, 2013, the claimant filed this IRC with the Commission.⁴⁴

III. Positions of the Parties

A. County of Los Angeles

³⁶ Exhibit B, Controller’s Late Comments on the IRC, page 152 (Letter from Wendy L. Watanabe to Jim L. Spano, dated April 30, 2010, paragraph 2).

³⁷ Exhibit B, Controller’s Late Comments on the IRC, page 152 (Letter from Wendy L. Watanabe to Jim L. Spano, dated April 30, 2010, paragraph 4).

³⁸ Exhibit B, Controller’s Late Comments on the IRC, page 152 (Letter from Wendy L. Watanabe to Jim L. Spano, dated April 30, 2010, paragraph 5).

³⁹ Exhibit B, Controller’s Late Comments on the IRC, page 153 (Letter from Wendy L. Watanabe to Jim L. Spano, dated April 30, 2010, paragraph 7(d)).

⁴⁰ Exhibit B, Controller’s Late Comments on the IRC, page 153 (Letter from Wendy L. Watanabe to Jim L. Spano, dated April 30, 2010, paragraph 8).

⁴¹ Exhibit B, Controller’s Late Comments on the IRC, page 153 (Letter from Wendy L. Watanabe to Jim L. Spano, dated April 30, 2010, paragraph 9).

⁴² Exhibit A, IRC, page 96 (cover letter), pages 95-110 (Final Audit Report).

⁴³ See, e.g., Exhibit A, IRC, page 96 (Letter from Jeffrey V. Brownfield to Gloria Molina, dated May 28, 2010).

⁴⁴ Exhibit A, IRC, pages 1, 3.

The claimant objects to reductions totaling \$448,202 to the claimant's reimbursement claims for fiscal years 2002-2003 and 2003-2004.

The claimant takes the following principal positions:

1. The Controller reviewed and utilized incomplete and inaccurate data and documentation when it conducted its audit.⁴⁵
2. The claimant's claims were timely filed.⁴⁶
3. Under the principle of equitable offset, the claimant may submit new claims for reimbursement supported by previously un-submitted documentation.⁴⁷

On June 10, 2016, the claimant filed comments on the Draft Proposed Decision, arguing that the IRC should be considered timely filed because the claimant relied upon statements made by the Controller that it had three years to file an IRC from the notices dated June 12, 2010, as follows:

The County relied upon the statements and the actions of the SCO in making its determinations. In its cover letter to the County accompanying the audit report, the SCO states that the County must file an IRC within three years of the SCO notifying the County of a claim reduction. The SCO then refers to the notices as notices of claim reduction. The SCO then specifically referred to the dates of the notices upon which the County relied as the dates they notified the County of a claim reduction.⁴⁸

The claimant also argued that the limitations period should be reset or suspended because the Controller engaged in a reconsideration of the audit results.⁴⁹

B. State Controller's Office

The Controller contends that it acted according to the law when it made \$448,202 in reductions to the claimant's fiscal year 2002-2003 and 2003-2004 reimbursement claims.

The Controller takes the following principal positions:

1. The claimant failed to provide support for its claims in a format which could be verified.⁵⁰
2. The claimant agreed to the findings of the audit.⁵¹

⁴⁵ Exhibit A, IRC, pages 6-8, 10-12.

⁴⁶ Exhibit A, IRC, pages 13-17 (the "Notice of Claim Adjustment" dated June 12, 2010, filed as a supplement to this IRC to establish alleged timeliness).

⁴⁷ Exhibit A, IRC, pages 8-10.

⁴⁸ Exhibit F, Claimant's Comments on the Draft Proposed Decision, page 3. The letter the claimant is referring to is the letter at Exhibit A, IRC, pages 485-486, from Jim Spano to Robin C. Kay, dated May 7, 2013.

⁴⁹ Exhibit F, Claimant's Comments on the Draft Proposed Decision, page 3.

⁵⁰ Exhibit B, Controller's Late Comments on the IRC, pages 20-22.

⁵¹ Exhibit B, Controller's Late Comments on the IRC, pages 19, 22.

3. The claimant may not, under the principle of equitable offset, submit new claims for reimbursement supported by previously un-submitted documentation.⁵²

On June 6, 2016, the Controller filed comments agreeing with the Draft Proposed Decision.⁵³

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 the local agency or school district. If the Commission determines that a reimbursement claim has been incorrectly reduced, section 1185.9 of the Commission's regulations requires the Commission to send the 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.⁵⁴ 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."⁵⁵

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.⁵⁶ Under this standard, the courts have found that:

When reviewing the exercise of discretion, "[t]he scope of review is limited out of deference to the agency's authority and presumed expertise: 'The court may not reweigh the evidence or substitute its judgment for that of the agency. [Citation.]' " ... "In general ... the inquiry is limited to whether the decision was arbitrary, capricious, or entirely lacking in evidentiary support. . . ." [Citations.] When making that inquiry, the " "court must ensure that an agency has adequately

⁵² Exhibit B, Controller's Late Comments on the IRC, page 19, 21-22.

⁵³ Exhibit E, Controller's Comments on the Draft Proposed Decision, page 1.

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

⁵⁵ *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.

⁵⁶ *Johnston v. Sonoma County Agricultural Preservation and Open Space Dist.* (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.

considered all relevant factors, and has demonstrated a rational connection between those factors, the choice made, and the purposes of the enabling statute.” [Citation.]’ ”⁵⁷

The Commission must review the Controller’s audit in light of the fact that the initial burden of providing evidence for a claim of reimbursement lies with the claimant.⁵⁸ In addition, sections 1185.1(f)(3) and 1185.2(c) of the Commission’s regulations require that any assertions of fact by the parties to an IRC must be supported by documentary evidence. The Commission’s ultimate findings of fact must be supported by substantial evidence in the record.⁵⁹

A. The IRC Was Untimely Filed.

At the time the reimbursement claims were audited and when this IRC was filed, the regulation containing the limitations period read:

All incorrect reduction claims shall be filed with the commission 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.⁶⁰

Applying the plain language of the limitations regulation — that the IRC must have been filed no later than three years after “the date” of the Final Audit Report — the IRC was untimely. The Controller’s Final Audit Report is dated May 28, 2010.⁶¹ Three years later was Tuesday, May 28, 2013. Instead of filing this IRC by the deadline of Tuesday, May 28, 2013, the claimant filed this IRC with the Commission on Tuesday, June 11, 2013 — 14 days later.⁶²

The claimant attempts to save its IRC by calculating the commencement of the limitations period from June 12, 2010, the date of two documents sent by the Controller which the claimant dubs a “Notice of Claim Adjustment.”⁶³ In the Written Narrative portion of the IRC, the claimant writes, “The SCO issued its audit report on May 28, 2010. The report was followed by a Notice

⁵⁷ *American Bd. of Cosmetic Surgery, Inc., v. Medical Bd. of California* (2008) 162 Cal.App.4th 534, 547-548.

⁵⁸ *Gilbert v. City of Sunnyvale* (2005) 130 Cal.App.4th 1264, 1274-1275.

⁵⁹ 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.

⁶⁰ Former Code of California Regulations, title 2, section 1185(b), which was renumbered section 1185(c) as of January 1, 2011. Effective July 1, 2014, the regulation was amended to state as follows: “All incorrect reduction claims shall be filed with the Commission no later than three years following the date of the Office of State Controller’s final state audit report, letter, remittance advice, or other written notice of adjustment to a reimbursement claim.” Code of California Regulations, title 2, section 1185.1(c).

⁶¹ Exhibit A, IRC, pages 96 (cover letter), 95-110 (Final Audit Report).

⁶² Exhibit A, IRC, page 1.

⁶³ See Exhibit A, IRC, pages 13-17 (“Notice of Claim Adjustment”).

of Claim Adjustment dated June 12, 2010.”⁶⁴ Although the claimant reads the document dated June 12, 2010, as a single document, the Commission reads it as two documents — specifically, two letters each containing a separate “Dear Claimant” salutation, of which the main text of the second letter is reproduced twice.⁶⁵

The claimant’s argument fails because: (1) the two documents were not notices of claim adjustment; and (2) even if they were, the limitations period commenced upon the date of the Final Audit Report and did not re-commence upon the receipt of the later two documents.

1. The Two Documents Dated June 12, 2010, Are Not Notices of Claim Adjustment.

For purposes of state mandates law, the Legislature has enacted a statutory definition of what constitutes a notice of claim adjustment.

Government Code section 17558.5(c) reads in relevant part:

The Controller shall notify the claimant in writing within 30 days after issuance of a remittance advice 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 or school district, and the reason for the adjustment.

In other words, a notice of claim adjustment is a document which contains four elements: (1) a specification of the claim components adjusted, (2) the amounts adjusted, (3) interest charges, and (4) the reason for the adjustment.

Both of the two documents which the claimant dubs a “Notice of Claim Adjustment” contain the amount adjusted, but the other three required elements are absent. Neither of the two documents specifies the claim components adjusted; each provides merely a lump-sum total of all *Handicapped and Disabled Students II* program costs adjusted for the entirety of the relevant fiscal year. Neither of the two documents contains interest charges. Perhaps most importantly, neither of the two documents enunciates any reason for the adjustment.⁶⁶

In addition to their failure to satisfy the statutory definition, the two documents cannot be notices of claim adjustment because neither of the documents adjusts anything. The two documents restate, in the most cursory fashion, the bottom-line findings contained in the Controller’s Final Audit Report.⁶⁷ The claimant asserts that if the documents dated August 6, 2010 do not

⁶⁴ Exhibit A, IRC, page 5.

⁶⁵ The two “Dear Claimant” salutations appear at Exhibit A, IRC, pages 13 and 15. The main text of Exhibit A, IRC, page 17, appears to be identical to the main text of Exhibit A, IRC, pages 15 and 16.

⁶⁶ Exhibit A, IRC, pages 13-17 (“Notice of Claim Adjustment”).

⁶⁷ Compare Exhibit A, IRC, pages 13-17 (the “Notice of Claim Adjustment”) with Exhibit A, IRC, page 102 (“Schedule 1 — Summary of Program Costs” in the Final Audit Report). The bottom-line totals are identical.

constitute notices of claim adjustment, then the Controller never provided notice.⁶⁸ The Final Audit Report provides abundant notice.

Neither of the two documents provides the claimant with notice of any new finding. The Final Audit Report contained the dollar amounts which would not be reimbursed.⁶⁹ The two later documents merely repeat information which was already contained in the Final Audit Report. The two documents do not provide any new and material information nor do they contain any previously unannounced adjustments.⁷⁰

For these reasons, the two documents are not notices of adjustment within the meaning of Government Code section 17558.5(c).

2. The Limitations Period Begins to Run Upon the Occurrence of the Earliest Event Which Would Have Allowed the Claimant to File a Claim.

The Commission's regulation setting out the limitation period lists several events which could potentially trigger the running of the limitations period. Specifically, the limitations regulation lists, as potentially triggering events, the date of a final audit report, the date of a letter, the date of a remittance advice, and the date of a written notice of adjustment. The claimant argues that, if more than one of these events occurred, then the limitations period should begin to run upon the occurrence of the event which occurred last in time.⁷¹ The Commission reaches (and has, many times in the past, reached) the opposite conclusion; the limitations period begins to run from the occurrence of the earliest event which would have allowed the claimant to file a claim. Subsequent events do not reset the limitations clock.

At the time the reimbursement claims were audited and when this IRC was filed, the Commission's regulation containing the limitations period read:

All incorrect reduction claims shall be filed with the commission 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.⁷²

Under a legal doctrine with the potentially confusing name of the "last essential element" rule, a limitations period begins to run upon the occurrence of the *earliest* event in time which creates a

⁶⁸ Exhibit F, Claimant's Comments on the Draft Proposed Decision, page 3.

⁶⁹ The Final Audit Report is dated May 28, 2010. (Exhibit A, IRC, pages 96, 101.)

⁷⁰ Moreover, the governing statute provides that a remittance advice or a document which merely provides notice of a payment action is not a notice of adjustment. (Government Code section 17558.5(c) ["Remittance advices and other notices of payment action shall not constitute notice of adjustment from an audit or review."]) Whatever term may accurately be used to characterize the two documents identified by the claimant, the two documents are not "notices of claim adjustment" under state mandate law.

⁷¹ Exhibit F, Claimant's Comments on the Draft Proposed Decision, pages 2-3.

⁷² Former Code of California Regulations, title 2, section 1185(b), effective May 8, 2007, renumbered as 1185(c) effective January 1, 2011.

complete claim. Under this rule, a right accrues — and the limitations period begins to run — from the earliest point in time when the claim can be filed and maintained.

As recently summarized by the California Supreme Court:

The limitations period, the period in which a plaintiff must bring suit or be barred, runs from the moment a claim accrues. (See Code Civ. Proc., § 312 [an action must “be commenced within the periods prescribed in this title, after the cause of action shall have accrued”]; (Citations.). Traditionally at common law, a “cause of action accrues ‘when [it] is complete with all of its elements’ — those elements being wrongdoing, harm, and causation.” (Citations.) This is the “last element” accrual rule: ordinarily, the statute of limitations runs from “the occurrence of the last element essential to the cause of action.” (Citations.)⁷³

In determining when a limitations period begins to run, the California Supreme Court looks to the earliest point in time when a litigant could have filed and maintained the claim:

Generally, a cause of action accrues and the statute of limitation begins to run when a suit may be maintained. [Citations.] “Ordinarily this is when the wrongful act is done and the obligation or the liability arises, but it does not ‘accrue until the party owning it is entitled to begin and prosecute an action thereon.’ ” [Citation.] In other words, “[a] cause of action accrues ‘upon the occurrence of the last element essential to the cause of action.’ ” [Citations.]⁷⁴

Under these principles, the claimant’s three-year limitations period began to run from the date of the Final Audit Report. As of that day, the claimant could have filed an IRC, because, as of that day, the claimant had been, from its perspective, harmed by a claim reduction. The Controller’s subsequent issuance of a letter or other notice that does not change the reason for the reduction does not start a new limitations clock; the limitations period starts to run from the earliest point in time when the claimant could have filed an IRC — and the limitations period expires three years after that earliest point in time.

This finding is consistent with two recent Commission decisions regarding the three-year period in which a claimant can file an IRC.

In the *Collective Bargaining* Program IRC Decision adopted on December 5, 2014, the claimant argued that the limitations period should begin to run from the date of the *last* notice of claim adjustment in the record.⁷⁵ This argument parallels that of the claimant in this instant IRC, who argues that between the Final Audit Report dated May 28, 2010, and the two letters dated June 12, 2010, the *later* event should commence the running of the limitations period.

In the *Collective Bargaining* Decision, the Commission rejected the argument. The Commission held that the limitations period began to run on the *earliest* applicable event because that was when the claim was complete as to all of its elements.⁷⁶ “Accordingly, the claimant cannot

⁷³ *Aryeh v. Canon Business Solutions, Inc.* (2013) 55 Cal.4th 1185, 1191.

⁷⁴ *Howard Jarvis Taxpayers Ass’n v. City of La Habra* (2001) 25 Cal. 4th 809, 815.

⁷⁵ Decision, *Collective Bargaining*, 05-4425-I-11 (adopted December 5, 2014), pages 20-22.

⁷⁶ Decision, *Collective Bargaining*, 05-4425-I-11 (adopted December 5, 2014), pages 20-22.

allege that the earliest notice did not provide sufficient information to initiate the IRC, and the later adjustment notices that the claimant proffers do not toll or suspend the operation of the period of limitation,” the Commission held.⁷⁷

In the *Domestic Violence Treatment Services — Authorization and Case Management* program IRC Decision adopted on March 25, 2016, the Commission held, “For IRCs, the ‘last element essential to the cause of action’ which begins the running of the period of limitations . . . is a notice to the claimant of the adjustment that includes the reason for the adjustment.”⁷⁸ In the instant IRC, the limitations period therefore began to run from the Final Audit Report, which is the notice that informed the claimant of the adjustment and of the reasons for the adjustment.

Furthermore, the Commission’s finding in the instant IRC is not inconsistent with a recent Commission ruling regarding the timeliness of filing an IRC.

In the *Handicapped and Disabled Students* Program IRC Decision adopted September 25, 2015, the Commission found that an IRC filed by a claimant was timely because the limitations period began to run from the date of a remittance advice letter which was issued after the Controller’s Final Audit Report.⁷⁹ The Decision is distinguishable because the Controller’s cover letter accompanying the audit report to the claimant in that case requested additional information and implied that the attached audit report was not final.⁸⁰ In the instant IRC, by contrast, the Controller’s cover letter contained no such statement or implication; rather, the Controller’s cover letter stated that, if the claimant disagreed with the attached Final Audit Report, the claimant would need to file an IRC within three years.⁸¹

The finding in this instant IRC is therefore consistent with recent Commission rulings regarding the three-year IRC limitations period.⁸²

⁷⁷ Decision, *Collective Bargaining*, 05-4425-I-11 (adopted December 5, 2014), page 21.

⁷⁸ Decision, *Domestic Violence Treatment Services — Authorization and Case Management*, 07-9628101-I-01 (adopted March 25, 2016), page 16.

⁷⁹ Decision, *Handicapped and Disabled Students*, 05-4282-I-03 (adopted September 25, 2015), pages 11-14.

⁸⁰ Decision, *Handicapped and Disabled Students*, 05-4282-I-03 (adopted September 25, 2015), pages 11-14. In the proceeding which resulted in this 2015 Decision, the cover letter from the Controller to the claimant is reproduced at Page 71 of the administrative record. In that letter, the Controller stated, “The SCO has established an informal audit review process to resolve a dispute of facts. The auditee should submit, in writing, a request for a review and all information pertinent to the disputed issues within 60 days after receiving the final report.” The Controller’s cover letter in the instant IRC contains no such language. Exhibit A, IRC, page 96 (Letter from Jeffrey V. Brownfield to Gloria Molina, dated May 28, 2010).

⁸¹ Exhibit A, IRC, page 96.

⁸² All that being said, an administrative agency’s adjudications need not be consistent so long as they are not arbitrary. See, e.g., *Weiss v. State Board of Equalization* (1953) 40 Cal.2d 772, 777 (“The administrator is expected to treat experience not as a jailer but as a teacher.”); *California Employment Commission v. Black-Foxe Military Institute* (1941) 43 Cal.App.2d Supp. 868, 876

In comments on the Draft Proposed Decision, the claimant argues that the Commission should not apply the “last essential element” rule because Regulation 1185 used the disjunctive “or” when listing the events which triggered the running of the limitations period.⁸³ The claimant provides no legal authority for its argument or evidence that Regulation 1185 was intended to be read in such a manner. The Commission therefore rejects the argument.

The Commission also notes that the claimant’s interpretation would yield the absurd result of repeatedly resetting the limitations period. Under the claimant’s theory, a statute of limitations containing a disjunctive “or” restarts whenever one of the other events in the list occurs. In other words, if a regulation states that a three-year limitations period begins to run upon the occurrence of X, Y, or Z, then (under the claimant’s theory), X can occur, a decade can elapse, and then the belated occurrence of Y or Z restarts the limitations clock. This interpretation cannot be correct, particularly in the context of monetary claims against the State’s treasury. The “last essential element” rule provides the claimant with the opportunity to timely file a claim while protecting the State from reanimated liability.

Consequently, the Commission concludes that the limitations period begins to run from the occurrence of the earliest event which would have allowed the claimant to file a claim. That event, in this case, was the date of the Final Audit Report. Since more than three years elapsed between that date and filing of the IRC, the IRC was untimely.

3. The Controller’s Misstatement of Law (Specifically, the Controller’s Erroneous Statement That the Limitations Period Began to Run as of the Three Documents Dated June 12, 2010) Does Not Result in an Equitable Estoppel That Makes the IRC Timely.

In its comments on the Draft Proposed Decision, the claimant argues that the IRC should be considered timely because the claimant relied upon statements made by the Controller. “The County relied upon the statements and the actions of the SCO in making its determinations. In its cover letter to the County accompanying the audit report, the SCO states that the County must file an IRC within three years of the SCO notifying the County of a claim reduction. The SCO then refers to the notices as notices of claim reduction. The SCO then specifically referred to the dates of the notices upon which the County relied as the dates they notified the County of a claim reduction.”⁸⁴

Although the claimant does not use the precise term (and does not conduct the requisite legal analysis), the claimant is arguing that the Controller should be equitably estopped from benefiting from the statute of limitations, and that the Commission should find the IRC timely. The claimant is arguing that, if the filing deadline provided by the Controller was erroneous, then

(“even were the plaintiff guilty of occupying inconsistent positions, we know of no rule of statute or constitution which prevents such an administrative board from doing so.”).

⁸³ Exhibit F, Claimant’s Comments on the Draft Proposed Decision, page 3.

⁸⁴ Exhibit F, Claimant’s Comments on the Draft Proposed Decision, page 3. The letter the claimant is referring to is the letter at Exhibit A, IRC, pages 20-21 from Jim Spano to Robin C. Kay, dated May 7, 2013.

the claimant should be forgiven for filing late because the claimant was relying upon the Controller's statements.

A state administrative agency may possess⁸⁵ — but does not necessarily possess⁸⁶ — the authority to adjudicate claims of equitable estoppel. The Commission possesses the authority to adjudicate claims of equitable estoppel because, without limitation, the Commission is vested with exclusive and original jurisdiction and the Commission is obligated to create a full record for the Superior Court to review in the event that a party seeks a writ of administrative mandamus.⁸⁷

The general elements of estoppel are well-established. “Whenever a party has, by his own statement or conduct, intentionally and deliberately led another to believe a particular thing true and to act upon such belief, he is not, in any litigation arising out of such statement or conduct, permitted to contradict it.”⁸⁸ “Generally speaking, four elements must be present in order to apply the doctrine of equitable estoppel: (1) the party to be estopped must be apprised of the facts; (2) he must intend that his conduct shall be acted upon, or must so act that the party asserting the estoppel had a right to believe it was so intended; (3) the other party must be ignorant of the true state of facts; and (4) he must rely upon the conduct to his injury.”⁸⁹

“The doctrine of estoppel is available against the government “where justice and right require it.” (Citation.)”⁹⁰ However, “estoppel will not be applied against the government if to do so would nullify a strong rule of policy adopted for the benefit of the public.”⁹¹ Estoppel against the government is to be limited to “exceptional conditions,” “special cases,” an “exceptional case,” or applied in a manner which creates an “extremely narrow precedent.”⁹²

Furthermore, the party to be estopped must have engaged in some quantum of turpitude. “We have in fact indicated that some element of turpitude on the part of the party to be estopped is requisite even in cases not involving title to land,” the California Supreme Court noted.⁹³ In the

⁸⁵ *Lentz v. McMahon* (1989) 49 Cal.3d 393, 406.

⁸⁶ *Foster v. Snyder* (1999) 76 Cal.App.4th 264, 268 (“The holding in *Lentz* does not stand for the all-encompassing conclusion that equitable principles apply to all administrative proceedings.”).

⁸⁷ *Lentz v. McMahon* (1989) 49 Cal.3d 393, 404 (regarding exclusive jurisdiction) & fn. 8 (regarding duty to create full record for review). See also Government Code section 17552 (exclusive jurisdiction); Government Code section 17559(b) (aggrieved party may seek writ of administrative mandamus).

⁸⁸ Evidence Code section 623.

⁸⁹ *Driscoll v. City of Los Angeles* (1967) 67 Cal.2d 297, 305.

⁹⁰ *Robinson v. Fair Employment and Housing Commission* (1992) 2 Cal.4th 226, 244, quoting *Lentz v. McMahon* (1989) 49 Cal.3d 393, 399, quoting *City of Los Angeles v. Cohn* (1894) 101 Cal. 373, 377.

⁹¹ *Lusardi Construction Co. v. Aubry* (1992) 1 Cal.4th 976, 994–995.

⁹² *City of Long Beach v. Mansell* (1970) 3 Cal.3d 462, 496 & fn. 30, 500.

⁹³ *City of Long Beach v. Mansell* (1970) 3 Cal.3d 462, 490 fn. 24.

federal courts, equitable estoppel against the government “must rest upon affirmative misconduct going beyond mere negligence.”⁹⁴

Upon a consideration of all of the facts and argument in the record, the Commission concludes for the following reasons that the Controller is not equitably estopped from benefiting from the statute of limitations.

The Commission interprets the evidence in the record as presenting a mutual mistake of law by both the Controller and the claimant. On the date of the Controller’s erroneous letter (May 7, 2013), the three-year limitations period had been in effect and had been published since at least May 2007.⁹⁵ Despite the fact that the limitations period had been in effect for several years, both the claimant and the Controller incorrectly calculated the IRC filing deadline as starting from the date of the two documents dated June 12, 2010, when, for the reasons explained in this Decision, the filing deadline started to run as of the date of the Final Audit Report.

A situation in which a government agency and a third party both misinterpret the law does not allow for an estoppel against the government — because the third party should have taken the time to learn what the law actually said. “Acts or conduct performed under a mutual mistake of law do not constitute grounds for estoppel. (Citation.) It is presumed the party claiming estoppel had an equal opportunity to discover the law.”⁹⁶ “Where the facts and law are known to both parties, there can be no estoppel. (Citation.) Even an expression as to a matter of law, in the absence of a confidential relationship, is not a basis for an estoppel.”⁹⁷ “Persons dealing with the government are charged with knowing government statutes and regulations, and they assume the risk that government agents may exceed their authority and provide misinformation.”⁹⁸

In point of fact, the Controller had earlier provided the claimant with general IRC filing information and had admonished the claimant to visit the Commission’s website. In the cover letter dated May 28, 2010, the Controller summarized the audit findings and then stated, “If you disagree with the audit findings, you may file an Incorrect Reduction Claim (IRC) with the Commission on State Mandates (CSM). The IRC must be filed within three years following the date that we notify you of a claim reduction. You may obtain IRC information at the CSM’s Web site at www.csm.ca.gov/docs/IRCform.pdf.”⁹⁹ In other words, as of May or June 2010, the claimant had been informed in general terms of the filing deadline and had been directed to the Commission’s website. The fact that the claimant failed to do so and the fact that the Controller made an erroneous statement more than two years later does not somehow make the claimant’s IRC timely.

⁹⁴ *Morgan v. Heckler* (1985) 779 F.2d 544, 545 (Kennedy, J.). See also *Mukherjee v. I.N.S.* (9th Cir. 1986) 793 F.2d 1006, 1009 (defining affirmative misconduct as “a deliberate lie . . . or a pattern of false promises”).

⁹⁵ Title 2, California Code of Regulations section 1185; California Regulatory Code Supplement, Register 2007, No. 19 (May 11, 2007), page 212.1 [version operative May 8, 2007].

⁹⁶ *Adams v. County of Sacramento* (1991) 235 Cal.App.3d 872, 883-884.

⁹⁷ *People v. Stuyvesant Ins. Co.* (1968) 261 Cal.App.2d 773, 784.

⁹⁸ *Lavin v. Marsh* (9th Cir. 1981) 644 F.2d 1378, 1383.

⁹⁹ Exhibit A, IRC, page 96.

Separately and independently, the record does not indicate that the Controller engaged in some quantum of turpitude. There is no evidence, for example, that the Controller acted with an intent to mislead.

Finally, the finding of an estoppel under this situation would nullify a strong rule of policy adopted for the benefit of the public, specifically, the policy that limitations periods exist “to encourage the timely presentation of claims and prevent windfall benefits.”¹⁰⁰

For each of these reasons, the claimant’s argument of equitable estoppel is denied.

The Commission is also unpersuaded that the events which the claimant characterizes as the Controller’s reconsideration of the audit act to extend, reset, suspend or otherwise affect the limitations period.¹⁰¹ While the claimant contends that the Controller reconsidered the audit findings and then withdrew from the reconsideration,¹⁰² the Controller contends that it did not engage in a reconsideration, but instead denied the claimant’s request for a reconsideration.¹⁰³ On this point, the factual evidence in the record, within the letter from the Controller dated May 7, 2013, provides, “This letter confirms that we denied the county’s reconsideration request”¹⁰⁴ The limitations period cannot be affected by a reconsideration which did not occur. Separately, the process which the claimant characterizes as a reconsideration did not commence until a June 2012 delivery of documents,¹⁰⁵ by which time the limitations period had been running for about two years. The claimant does not cite to legal authority or otherwise persuasively explain how the Controller’s alleged reconsideration stopped or reset the already-ticking limitations clock.

Accordingly, the IRC is denied as untimely filed.

V. Conclusion

The Commission finds that claimant’s IRC was untimely filed. The Commission therefore denies this IRC.

¹⁰⁰ *Lentz v. McMahon* (1989) 49 Cal.3d 393, 401.

¹⁰¹ Exhibit F, Claimant’s Comments on the Draft Proposed Decision, pages 2-3.

¹⁰² Exhibit F, Claimant’s Comments on the Draft Proposed Decision, pages 2-3.

¹⁰³ Exhibit A, IRC, page 20.

¹⁰⁴ Exhibit A, IRC, page 20.

¹⁰⁵ Exhibit A, IRC, page 20.



RE: **Decision**

Handicapped and Disabled Students II, 12-0240-I-01

Government Code Sections 7572.55 and 7576

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

(Emergency regulations effective July 1, 1998 [Register 98, No. 26], final regulations effective August 9, 1999 [Register 99, No. 33])

Fiscal Years: 2002-2003 and 2003-2004

County of Los Angeles, Claimant

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

Heather Halsey, Executive Director

Dated: July 27, 2016

BEFORE THE
COMMISSION ON STATE MANDATES
STATE OF CALIFORNIA

IN RE INCORRECT REDUCTION CLAIM
ON:

Government Code Sections 7572 and 7572.5;
Statutes 1984, Chapter 1747 (AB 3632);
Statutes 1985, Chapter 1274 (AB 882);
California Code of Regulations, Title 2,
Division 9, Chapter 1, Section 60040
(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])¹

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

County of Los Angeles, Claimant

Case No.: 13-4282-I-06

Handicapped and Disabled Students

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

(Adopted July 22, 2016)

(Served July 27, 2016)

DECISION

The Commission on State Mandates (Commission) heard and decided this Incorrect Reduction Claim (IRC) during a regularly scheduled hearing on July 22, 2016. Edward Jewik and Hasmik Yaghobyan appeared on behalf of the County of Los Angeles. Jim Spano and Chris Ryan appeared for the State Controller's Office.

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

The Commission adopted the Proposed Decision to deny this IRC by a vote of 6-0 as follows:

¹ 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 specific sections of the statutes and executive orders that were approved in the underlying test claim decision. However, that was an oversight in the case of the Parameters and Guidelines at issue in this case.

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

Summary of the Findings

This IRC was filed in response to an audit by the State Controller’s Office (Controller) of the County of Los Angeles’s (claimant’s) initial reimbursement claims under the *Handicapped and Disabled Students* program for fiscal years 2003-2004, 2004-2005, and 2005-2006. The Controller reduced the claims because it found that the claimant: (1) claimed ineligible, unsupported, and duplicate services related to assessment and treatment costs and administrative costs; (2) overstated indirect costs by applying indirect cost rates toward ineligible direct costs; and (3) overstated offsetting revenues by using inaccurate Medi-Cal units, by applying incorrect funding percentages for Early and Periodic, Screening, Diagnosis, and Treatment (EPSDT) for fiscal year (FY) 2005-06, including unsupported revenues, and by applying revenue to ineligible direct and indirect costs.² In this IRC, the claimant contends that the Controller’s reductions were incorrect and requests, as a remedy, that the Commission reinstate the following cost amounts (which would then become subject to the program’s reimbursement formula):

FY2003-2004:	\$5,247,918
FY2004-2005:	\$6,396,075
FY2005-2006:	\$6,536,836 ³

After a review of the record and the applicable law, the Commission found that the IRC was untimely filed.

Accordingly, the Commission denies this IRC.

I. Chronology

01/05/2005 Claimant dated the reimbursement claim for fiscal year 2003-2004.⁴

² See, e.g., Exhibit A, IRC, page 542 (Letter from Jeffrey V. Brownfield to Gloria Molina, dated June 30, 2010).

³ Exhibit A, IRC, page 1. In footnotes 1 to 4, inclusive, of the Written Narrative portion of the IRC, the claimant explains why it is requesting reinstatement of cost amounts which are greater than the amounts that the Controller reduced. Exhibit A, IRC, page 4.

⁴ Exhibit A, IRC, page 564 (cover letter), page 571 (Form FAM-27).

01/10/2006 Claimant dated the reimbursement claim for fiscal year 2004-2005.⁵

04/05/2007 Claimant dated the amended reimbursement claim for fiscal year 2005-2006.⁶

08/12/2008 Controller sent a letter to claimant dated August 12, 2008 confirming the start of the audit.⁷

05/19/2010 Controller issued the Draft Audit Report dated May 19, 2010.⁸

06/16/2010 Claimant sent a letter to Controller dated June 16, 2010 in response to the Draft Audit Report.⁹

06/16/2010 Claimant sent a letter to Controller dated June 16, 2010, with regard to the claims and audit procedure.¹⁰

06/30/2010 Controller issued the Final Audit Report dated June 30, 2010.¹¹

08/02/2013 Claimant filed this IRC.¹²

11/25/2014 Controller filed late comments on the IRC.¹³

12/23/2014 Claimant filed a request for extension of time to file rebuttal comments which was granted for good cause.

03/26/2015 Claimant filed rebuttal comments.¹⁴

05/20/2016 Commission staff issued the Draft Proposed Decision.¹⁵

⁵ Exhibit A, IRC, page 859 (cover letter), page 862 (Form FAM-27). The cover letter is dated one day before the date of the Form FAM-27; the discrepancy is immaterial, and this Decision will utilize the date of the cover letter (January 10, 2006) as the relevant date.

⁶ Exhibit A, IRC, page 1047 (cover letter), page 1050 (Form FAM-27).

⁷ Exhibit B, Controller's Late Comments on the IRC, page 181 (Letter from Christopher Ryan to Wendy L. Watanabe, dated August 12, 2008). The Controller also asserts on page 25 of its comments that "The SCO contacted the county by phone on July 28, 2008, to initiate the audit...." However, this assertion of fact is not supported by a declaration of a person with personal knowledge or any other evidence in the record.

⁸ Exhibit A, IRC, page 547.

⁹ Exhibit A, IRC, pages 558-561 (Letter from Wendy L. Watanabe to Jeffrey V. Brownfield, dated June 16, 2010).

¹⁰ Exhibit B, Controller's Late Comments on the IRC, pages 185-186 (Letter from Wendy L. Watanabe to Jim L. Spano, dated June 16, 2010).

¹¹ Exhibit A, IRC, page 542 (cover letter), pages 541-562 (Final Audit Report).

¹² Exhibit A, IRC, pages 1, 3.

¹³ Exhibit B, Controller's Late Comments on the IRC, page 1.

¹⁴ Exhibit C, Claimant's Rebuttal Comments, page 1.

¹⁵ Exhibit D, Draft Proposed Decision, pages 1, 34.

06/06/2016 Controller filed comments on the Draft Proposed Decision.¹⁶

06/10/2016 Claimant filed comments on the Draft Proposed Decision.¹⁷

II. Background

In 1975, Congress enacted the Education for All Handicapped Children Act (EHA) with the stated purpose of assuring that “all handicapped children have available to them . . . a free appropriate public education which emphasizes special education and related services designed to meet their unique needs”¹⁸ Among other things, the EHA authorized the payment of federal funds to states which complied with specified criteria regarding the provision of special education and related services to handicapped and disabled students.¹⁹ The EHA was ultimately renamed the Individuals with Disability Education Act (IDEA) and guarantees 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.²⁰

In California, the responsibility of providing both “special education” and “related services” was initially shared by local education agencies (broadly defined) and by the state government.²¹ However, in 1984, the Legislature enacted AB 3632, which amended Government Code chapter 26.5 relating to “interagency responsibilities for providing services to handicapped children” which created separate spheres of responsibility.²² And, in 1985, the Legislature further amended chapter 26.5.²³

The impact of the 1984 and 1985 amendments — sometimes referred to collectively as “Chapter 26.5 services” — was to transfer the responsibility to provide mental health services for disabled pupils from school districts to county mental health departments.²⁴

¹⁶ Exhibit E, Controller’s Comments on the Draft Proposed Decision, page 1.

¹⁷ Exhibit F, Claimant’s Comments on the Draft Proposed Decision, page 1.

¹⁸ Public Law 94-142, section 1, section 3(a) (Nov. 29, 1975) 89 U.S. Statutes at Large 773, 775. See also 20 U.S.C. § 1400(d) [current version].

¹⁹ Public Law 94-142, section 5(a) (Nov. 29, 1975) 89 U.S. Statutes at Large 773, 793. See also 20 U.S.C. 1411(a)(1) [current version].

²⁰ Public Law 101-476, section 901(a)(1) (October 30, 1999) 104 U.S. Statutes at Large 1103, 1141-1142.

²¹ *California School Boards Ass’n v. Brown* (2011) 192 Cal.App.4th 1507, 1514.

²² Statutes 1984, chapter 1747.

²³ Statutes 1985, chapter 1274.

²⁴ “With the passage of AB 3632 (fn.), California’s approach to mental health services was restructured with the intent to address the increasing number of emotionally disabled students who were in need of mental health services. Instead of relying on LEAs [local education agencies] to acquire qualified staff to handle the needs of these students, the state sought to have CMH [county mental health] agencies — who were already in the business of providing mental health services to emotionally disturbed youth and adults — assume the responsibility for

In 1990 and 1991, the Commission adopted the Test Claim Statement of Decision and the Parameters and Guidelines, approving *Handicapped and Disabled Students*, CSM 4282, as a reimbursable state-mandated program within the meaning of article XIII B, section 6 of the California Constitution.²⁵ The Commission found that the activities of providing mental health assessments; participation in the IEP process; and providing psychotherapy and other mental health treatment services were reimbursable and that providing mental health treatment services was funded as part of the Short-Doyle Act, based on a cost-sharing formula with the state.²⁶ Beginning July 1, 2001, however, the cost-sharing ratio for providing psychotherapy and other mental health treatment services no longer applied, and counties were entitled to receive reimbursement for 100 percent of the costs to perform these services.²⁷

In 2004, the Legislature directed the Commission to reconsider *Handicapped and Disabled Students*, CSM 4282.²⁸ In May 2005, the Commission adopted the Statement of Decision on Reconsideration, 04-RL-4282-10, and determined that the original Statement of Decision correctly concluded that the test claim statutes and regulations impose a reimbursable state-mandated program on counties pursuant to article XIII B, section 6. The Commission concluded, however, that the 1990 Statement of Decision did not fully identify all of the activities mandated by the state or the offsetting revenue applicable to the program. Thus, for costs incurred beginning July 1, 2004, the Commission identified the activities expressly required by the test claim statutes and regulations that were reimbursable, identified the offsetting revenue applicable to the program, and updated the new funding provisions enacted in 2002 that required 100 percent reimbursement for mental health treatment services.²⁹

Statutes 2011, chapter 43 (AB 114) eliminated the mandated programs for *Handicapped and Disabled Students*, 04-RL-4282-10 and 02-TC-40/02-TC-49, by transferring responsibility for

providing needed mental health services to children who qualified for special education.” Stanford Law School Youth and Education Law Clinic, *Challenge and Opportunity: An Analysis of Chapter 26.5 and the System for Delivering Mental Health Services to Special Education Students in California*, May 2004, page 12.

²⁵ “As local mental health agencies had not previously been required to provide Chapter 26.5 services to special education students, local mental health agencies argued that these requirements constituted a reimbursable state mandate.” (*California School Boards Ass’n v. Brown* (2011) 192 Cal.App.4th 1507, 1515.)

²⁶ Former Welfare and Institutions Code sections 5600 et seq.

²⁷ Statutes 2002, chapter 1167 (AB 2781, §§ 38, 41).

²⁸ Statutes 2004, chapter 493 (SB 1895).

²⁹ In May 2005, the Commission also adopted a Statement of Decision on *Handicapped and Disabled Students II* (02-TC-40/02-TC-49), a test claim addressing statutory amendments enacted between the years 1986 and 2002 to Government Code sections 7570 et seq., and 1998 amendments to the joint regulations adopted by the Departments of Education and Mental Health. The period of reimbursement for *Handicapped and Disabled Students II* (02-TC-40/02-TC-49) began July 1, 2001.

providing mental health services under IDEA back to school districts, effective July 1, 2011.³⁰ On September 28, 2012, the Commission adopted an amendment to the Parameters and Guidelines ending reimbursement effective July 1, 2011.

The Controller's Audit and Reduction of Costs

The Controller issued the Draft Audit Report dated May 19, 2010, and provided a copy to the claimant for comment.³¹

In a four-page letter dated June 16, 2010, the claimant responded directly to the Draft Audit Report, agreed with its findings, and accepted its recommendations.³² The first page of this four-page letter contains the following statement:

*The County's attached response indicates agreement with the audit findings and the actions that the County will take to implement policies and procedures to ensure that the costs claimed under HDS are eligible, mandate related, and supported.*³³

The following three pages of the four-page letter contain further statements of agreement with the Controller's findings and recommendations.

In response to the Controller's Finding No. 1, that the claimant overstated assessment and treatment costs by more than \$27 million, the claimant responded in relevant part:

We agree with the recommendation. The County will strengthen the policies and procedures to ensure that only actual units of service for eligible clients are claimed in accordance with the mandated program. The County will ensure all staff members are trained on the applicable policies and procedures.

The County has agreed to the audit disallowances for Case Management Support Costs.³⁴

In response to the Controller's Finding No. 2, that the claimant overstated administrative costs by more than \$5 million, the claimant responded in relevant part:

We agree with the recommendation. As stated in the County's Response for Finding 1, the County will strengthen the policies and procedures to ensure that only actual units of service for eligible clients are claimed in accordance with the mandated program and will ensure the administrative cost rates are applied appropriately. At the time of claim preparation, it was the County's understanding that the administrative cost rates were applied to eligible and supported direct

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

³¹ Exhibit A, IRC, page 547.

³² Exhibit A, IRC, pages 558-561 (Letter from Wendy L. Watanabe to Jeffrey V. Brownfield, dated June 16, 2010).

³³ Exhibit A, IRC, page 558 (Letter from Wendy L. Watanabe to Jeffrey V. Brownfield, dated June 16, 2010) (emphasis added).

³⁴ Exhibit A, IRC, pages 559-560 (Letter from Wendy L. Watanabe to Jeffrey V. Brownfield, dated June 16, 2010).

costs. The State auditor's discovery of ineligible units of service resulted in the ineligibility of the administrative costs.³⁵

In response to the Controller's Finding No. 3, that the claimant overstated offsetting revenues by more than \$13 million, the claimant responded in relevant part:

We agree with the recommendation. It is always the County's intent to apply the applicable offsetting revenues (including federal, state, and local reimbursements) to eligible costs, which are supported by source documentation.³⁶

In a separate two-page letter also dated June 16, 2010, the claimant addressed its compliance with the audit and the status of any remaining reimbursement claims.³⁷ Material statements in the two-page letter include:

- "We maintain accurate financial records and data to support the mandated cost claims submitted to the SCO."³⁸
- "We designed and implemented the County's accounting system to ensure accurate and timely records."³⁹
- "We claimed mandated costs based on actual expenditures allowable per the Handicapped and Disabled Students Program's parameters and guidelines."⁴⁰
- "We made available to the SCO's audit staff all financial records, correspondence, and other data pertinent to the mandated cost claims."⁴¹
- "We are not aware of any . . . Relevant, material transactions that were not properly recorded in the accounting records that could have a material effect on the mandated cost claims."⁴²

³⁵ Exhibit A, IRC, page 560 (Letter from Wendy L. Watanabe to Jeffrey V. Brownfield, dated June 16, 2010).

³⁶ Exhibit A, IRC, page 561 (Letter from Wendy L. Watanabe to Jeffrey V. Brownfield, dated June 16, 2010).

³⁷ Exhibit B, Controller's Late Comments on the IRC, pages 185-186 (Letter from Wendy L. Watanabe to Jim L. Spano, dated June 16, 2010).

³⁸ Exhibit B, Controller's Late Comments on the IRC, pages 185 (Letter from Wendy L. Watanabe to Jim L. Spano, dated June 16, 2010, paragraph 1).

³⁹ Exhibit B, Controller's Late Comments on the IRC, pages 185 (Letter from Wendy L. Watanabe to Jim L. Spano, dated June 16, 2010, paragraph 2).

⁴⁰ Exhibit B, Controller's Late Comments on the IRC, pages 185 (Letter from Wendy L. Watanabe to Jim L. Spano, dated June 16, 2010, paragraph 4).

⁴¹ Exhibit B, Controller's Late Comments on the IRC, pages 185 (Letter from Wendy L. Watanabe to Jim L. Spano, dated June 16, 2010, paragraph 5).

⁴² Exhibit B, Controller's Late Comments on the IRC, pages 186 (Letter from Wendy L. Watanabe to Jim L. Spano, dated June 16, 2010, paragraph 7).

- “There are no unasserted claims or assessments that our lawyer has advised us are probable of assertion that would have a material effect on the mandated cost claims.”⁴³
- “We are not aware of any events that occurred after the audit period that would require us to adjust the mandated cost claims.”⁴⁴

On June 30, 2010, the Controller issued the Final Audit Report.⁴⁵ The Controller reduced the claims because the claimant: (1) claimed ineligible, unsupported, and duplicate services related to assessment and treatment costs and administrative costs; (2) overstated indirect costs by applying indirect cost rates toward ineligible direct costs; and (3) overstated offsetting revenues by using inaccurate Medi-Cal units, by applying incorrect funding percentages for Early and Periodic, Screening, Diagnosis and Treatment (EPSDT) for FY 2005-2006, including unsupported revenues, and by applying revenue to ineligible direct and indirect costs.⁴⁶

On August 2, 2013, the claimant filed this IRC with the Commission.⁴⁷

III. Positions of the Parties

A. County of Los Angeles

The claimant objects to \$18,180,829 in reductions. The claimant asserts that the Controller audited the claim as if the claimant used the actual increased cost method to prepare the reimbursement claim, instead of the cost report method the claimant states it used. Thus, the claimant takes the following principal positions:

1. The Controller lacked the legal authority to audit the claimant’s reimbursement claims because the claimant used the cost report method for claiming costs. The cost report method is a reasonable reimbursement methodology (RRM) based on approximations of local costs and, thus, the Controller has no authority to audit RRMs. The Controller’s authority to audit is limited to actual cost claims.⁴⁸
2. Even if the Controller has the authority to audit the reimbursement claims, the Controller was limited to reviewing only the documents required by the California Department of

⁴³ Exhibit B, Controller’s Late Comments on the IRC, pages 186 (Letter from Wendy L. Watanabe to Jim L. Spano, dated June 16, 2010, paragraph 8).

⁴⁴ Exhibit B, Controller’s Late Comments on the IRC, pages 186 (Letter from Wendy L. Watanabe to Jim L. Spano, dated June 16, 2010, paragraph 9).

⁴⁵ Exhibit B, Controller’s Late Comments on the IRC, page 6 (Declaration of Jim L. Spano, dated Nov. 17, 2014, paragraph 7); Exhibit A, IRC, page 542 (cover letter), pages 541-562 (Final Audit Report).

⁴⁶ See, e.g., Exhibit A, IRC, page 542 (Letter from Jeffrey V. Brownfield to Gloria Molina, dated June 30, 2010).

⁴⁷ Exhibit A, IRC, pages 1, 3.

⁴⁸ Exhibit A, IRC, pages 10-11.

Mental Health's cost report instructions, and not request supporting data from the county's Mental Health Management Information System.⁴⁹

3. The Controller also has the obligation to permit the actual costs incurred on review of the claimant's supporting documentation. However, the data set used by the Controller to determine allowable costs was incomplete and did not accurately capture the costs of services rendered.⁵⁰
4. Under the principle of equitable offset, the claimant may submit new claims for reimbursement supported by previously un-submitted documentation.⁵¹

The claimant also asserts that the Controller improperly shifted IDEA funds and double-counted certain assessment costs.⁵²

On June 10, 2016, the claimant filed comments on the Draft Proposed Decision, arguing that the IRC should be considered timely filed because the claimant relied upon statements made by the Controller that it had three years to file an IRC from the notices dated August 6, 2010, as follows:

The County relied upon the statements and the actions of the SCO in making its determinations. In its cover letter to the County accompanying the audit report, the SCO states that the County must file an IRC within three years of the SCO notifying the County of a claim reduction. The SCO then refers to the notices as notices of claim reduction. The SCO then specifically referred to the dates of the notices upon which the County relied as the dates they notified the County of a claim reduction.⁵³

The claimant also argued that the limitations period should be reset or suspended because the Controller engaged in a reconsideration of the audit results.⁵⁴

B. State Controller's Office

The Controller contends that it acted according to the law when it made \$18,180,829 in reductions to the claimant's reimbursement claims for fiscal years 2003-2004, 2004-2005, and 2005-2006.

⁴⁹ Exhibit A, IRC, pages 11-12.

⁵⁰ Exhibit A, IRC, pages 12-15, 17-18.

⁵¹ Exhibit A, IRC, pages 15-17.

⁵² Exhibit A, IRC, page 4 fn. 1 through 4 ("The amounts are further offset because the SCO, in calculating the County's claimed amount, added the amounts associated with refiling of claims based on the CSM's Reconsideration Decision to the original claims submitted for Fiscal Years 2004-05 and 2005-06, thus double-counting certain assessment costs for those fiscal years.").

⁵³ Exhibit F, Claimant's Comments on the Draft Proposed Decision, page 3. The letter the claimant is referring to is the letter at Exhibit A, IRC, pages 485-486, from Jim Spano to Robin C. Kay, dated May 7, 2013.

⁵⁴ Exhibit F, Claimant's Comments on the Draft Proposed Decision, page 3.

The Controller takes the following principal positions:

1. The Controller possesses the legal authority to audit the claimant's reimbursement claims, even if the claims were made using a cost report method as opposed to an actual cost method.⁵⁵
2. The documentation provided by the claimant did not verify the claimed costs.⁵⁶
3. The claimant provided a management representation letter stating that the claimant had provided to the Controller all pertinent information in support of its claims.⁵⁷
4. The claimant may not, under the principle of equitable offset, submit new claims for reimbursement supported by previously un-submitted documentation.⁵⁸

On June 6, 2016, the Controller filed comments agreeing with the Draft Proposed Decision.⁵⁹

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 the local agency or school district. If the Commission determines that a reimbursement claim has been incorrectly reduced, section 1185.9 of the Commission's regulations requires the Commission to send the 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.⁶⁰ 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

⁵⁵ Exhibit B, Controller's Late Comments on the IRC, page 27. But see Exhibit C, Claimant's Rebuttal Comments, page 2 ("The SCO states it disagrees with the County's contention that the SCO did not have the legal authority to audit the program during these three fiscal years. However, it offers no argument or support for its position."). The Commission is not aided by the Controller's failure to substantively address a legal issue raised by the IRC.

⁵⁶ Exhibit B, Controller's Late Comments on the IRC, pages 27-29.

⁵⁷ Exhibit B, Controller's Late Comments on the IRC, page 29.

⁵⁸ Exhibit B, Controller's Late Comments on the IRC, page 28.

⁵⁹ Exhibit E, Controller's Comments on the Draft Proposed Decision.

⁶⁰ *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.”⁶¹

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.⁶² Under this standard, the courts have found:

When reviewing the exercise of discretion, “[t]he scope of review is limited out of deference to the agency’s authority and presumed expertise: ‘The court may not reweigh the evidence or substitute its judgment for that of the agency. [Citation.]’” ... “In general ... the inquiry is limited to whether the decision was arbitrary, capricious, or entirely lacking in evidentiary support. . . .” [Citations.] When making that inquiry, the “ ‘ ‘court must ensure that an agency has adequately considered all relevant factors, and has demonstrated a rational connection between those factors, the choice made, and the purposes of the enabling statute.’” [Citation.]’ ”⁶³

The Commission must review the Controller’s audit in light of the fact that the initial burden of providing evidence for a claim of reimbursement lies with the claimant.⁶⁴ In addition, sections 1185.1(f)(3) and 1185.2(c) of the Commission’s regulations require that any assertions of fact by the parties to an IRC must be supported by documentary evidence. The Commission’s ultimate findings of fact must be supported by substantial evidence in the record.⁶⁵

A. The IRC Was Untimely Filed.

The threshold issue is whether this IRC was timely filed.⁶⁶

⁶¹ *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.

⁶² *Johnston v. Sonoma County Agricultural Preservation and Open Space Dist.* (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.

⁶³ *American Bd. of Cosmetic Surgery, Inc. v. Medical Bd. of California* (2008) 162 Cal.App.4th 534, 547-548.

⁶⁴ *Gilbert v. City of Sunnyvale* (2005) 130 Cal.App.4th 1264, 1274-1275.

⁶⁵ 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.

⁶⁶ In its comments on the IRC (Exhibit B), the Controller did not raise the issue of whether the IRC was timely filed. However, the Commission’s limitations period is jurisdictional, and, as such, the Commission is obligated to review the limitations issue sua sponte. (See *John R. Sand & Gravel Co. v. United States* (2008) 552 U.S. 130, 132 [128 S. Ct. 750, 752].)

“The statute of limitations is an affirmative defense” (*Ladd v. Warner Bros. Entertainment, Inc.* (2010) 184 Cal.App.4th 1298, 1309), and, in civil cases, an affirmative defense must be

At the time the reimbursement claims were audited and when this IRC was filed, the Commission’s regulation containing the limitations period read:

All incorrect reduction claims shall be filed with the commission 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.⁶⁷

Thus, the applicable limitations period is “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.”⁶⁸

Applying the plain language of the limitations regulation — that the IRC must have been filed no later than three years after “the date” of the Final Audit Report — the IRC was untimely. The Controller’s Final Audit Report is dated June 30, 2010.⁶⁹ Three years later was June 30, 2013. Since June 30, 2013, was a Sunday, the claimant’s deadline to file this IRC moved to Monday, July 1, 2013.⁷⁰ Instead of filing this IRC by the deadline of Monday, July 1, 2013, the claimant filed this IRC with the Commission on Friday, August 2, 2013 — 32 days later.⁷¹

The claimant attempts to save its IRC by calculating the commencement of the limitations period from the date of three documents which bear the date August 6, 2010, and which were issued by the Controller; the claimant refers to these three documents as “Notices of Claim Adjustment.”⁷²

established by a preponderance of the evidence (31 Cal.Jur.3d, Evidence, section 97 [collecting cases]; *People ex. rel. Dept. of Public Works v. Lagiss* (1963) 223 Cal.App.2d 23, 37). See also Evidence Code section 115 (“Except as otherwise provided by law, the burden of proof requires proof by a preponderance of the evidence.”).

⁶⁷ Former Code of California Regulations, title 2, section 1185(b), which was renumbered section 1185(c) effective January 1, 2011. Effective July 1, 2014, the regulation was amended to state the following: “All incorrect reduction claims shall be filed with the Commission no later than three years following the date of the Office of State Controller’s final state audit report, letter, remittance advice, or other written notice of adjustment to a reimbursement claim.” Code of California Regulations, title 2, section 1185.1(c).

⁶⁸ Former Code of California Regulations, title 2, section 1185(b).

⁶⁹ Exhibit A, IRC, page 547 (Final Audit Report).

⁷⁰ See California Code of Regulations, title 2, section 1183.18(a)(1); Code of Civil Procedure section 12a(a) (“If the last day for the performance of any act provided or required by law to be performed within a specified period of time is a holiday, then that period is hereby extended to and including the next day that is not a holiday.”); Government Code section 6700(a)(1) (“The holidays in this state are: Every Sunday...”); and Code of Civil Procedure section 12a(b) (“This section applies . . . to all other provisions of law providing or requiring an act to be performed on a particular day or within a specified period of time, whether expressed in this or any other code or statute, ordinance, rule, or regulation.”).

⁷¹ Exhibit A, IRC, page 1.

⁷² Exhibit A, IRC, pages 21-27.

In the Written Narrative portion of the IRC, the claimant writes, “The SCO issued its audit report on June 30, 2010. The report was followed by Notices of Claim Adjustment dated August 6, 2010 (see Exhibit A).”⁷³ The claimant further argues that the Commission should find that the IRC was timely filed based on statements made by the Controller’s Office that an IRC could be filed three years from the August 6, 2010, notices.⁷⁴

The claimant’s argument fails because: (1) the three documents dated August 6, 2010, were not notices of claim adjustment; (2) the limitations period commences to run upon the earliest event in time which would have allowed the claimant to file a claim; and (3) the Controller’s misstatement of law (specifically, the Controller’s erroneous statement that the limitations period for filing an IRC began to run as of the three documents dated August 6, 2010) does not result in an equitable estoppel that makes the IRC timely.

1. The Three Documents Dated August 6, 2010, Are Not Notices of Adjustment.

For purposes of state mandate law, the Legislature has enacted a statutory definition of what constitutes a “notice of adjustment.”

Government Code section 17558.5(c) reads in relevant part, “The Controller shall notify the claimant in writing within 30 days after issuance of a remittance advice 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 or school district, and the reason for the adjustment.”

In other words, a notice of adjustment is a document which contains four elements: (1) a specification of the claim components adjusted, (2) the amounts adjusted, (3) interest charges, and (4) the reason for the adjustment.

Each of the three documents which the claimant dubs “Notices of Claim Adjustment” contains the amount adjusted, but the other three required elements are absent. None of the three documents specifies the claim components adjusted; each provides merely a lump-sum total of all *Handicapped and Disabled Students* program costs adjusted for the entirety of the relevant fiscal year. None of the three documents contains interest charges. Perhaps most importantly, none of the three documents enunciates a reason for the adjustment.⁷⁵

In addition to their failure to satisfy the statutory definition, the three documents cannot be notices of adjustment because none of the documents adjusts anything. The three documents restate, in the most cursory fashion, the bottom-line findings contained in the Controller’s Final

⁷³ Exhibit A, IRC, page 6.

⁷⁴ Exhibit F, Claimant’s Comments on the Draft Proposed Decision, pages 2-3.

⁷⁵ Exhibit A, IRC, pages 21-27 (the “Notices of Claim Adjustment”). See also Decision, *Domestic Violence Treatment Services — Authorization and Case Management*, Commission on State Mandates Case No. 07-9628101-I-01, adopted March 25, 2016, page 16 (“For IRCs, the ‘last element essential to the cause of action’ which begins the running of the period of limitations . . . is a notice to the claimant of the adjustment that includes the reason for the adjustment.”).

Audit Report.⁷⁶ The claimant asserts that, if the documents dated August 6, 2010, do not constitute notices of claim adjustment, then the Controller never provided notice.⁷⁷ The Final Audit Report provides abundant notice.

None of the three documents provides the claimant with notice of any new finding. The Final Audit Report informed the claimant of the dollar amounts which would not be reimbursed and the dollar amounts which the Controller contended that the claimant owed the State.⁷⁸ The Final Audit Report informed the claimant that the Controller would offset unpaid amounts from future mandate reimbursements if payment was not remitted.⁷⁹ The three documents merely repeat this information. The three documents do not provide notice of any new and material information, and the three documents do not contain any previously unannounced adjustments.⁸⁰

For these reasons, the three documents are not notices of adjustment within the meaning of Government Code section 17558.5(c).

2. The Limitations Period Begins to Run Upon the Occurrence of the Earliest Event Which Would Have Allowed the Claimant to File a Claim.

The Commission's regulation setting out the limitation period lists several events which could potentially trigger the running of the limitations period. Specifically, the limitations regulation lists, as potentially triggering events, the date of a final audit report, the date of a letter, the date of a remittance advice, and the date of a written notice of adjustment. The claimant argues that, if more than one of these events occurred, then the limitations period should begin to run upon the occurrence of the event which occurred last in time.⁸¹ The Commission reaches (and has, many times in the past, reached) the opposite conclusion; the limitations period begins to run from the occurrence of the earliest event which would have allowed the claimant to file a claim. Subsequent events do not reset the limitations clock.

⁷⁶ Compare Exhibit A, IRC, pages 21-27 (the "Notices of Claim Adjustment") with Exhibit A, IRC, pages 548-550 ("Schedule 1 — Summary of Program Costs" in the Final Audit Report). The bottom-line totals are identical.

⁷⁷ Exhibit F, Claimant's Comments on the Draft Proposed Decision, page 3.

⁷⁸ The Final Audit Report and the Controller's cover letter to the Final Audit Report are each dated June 30, 2010. Exhibit A, IRC, pages 542, 547. In addition, the claimant has admitted that the Controller issued the Final Audit Report on June 30, 2010, and that the three documents dated August 6, 2010 "followed" the Final Audit Report. Exhibit A, IRC, page 6.

⁷⁹ Exhibit A, IRC, page 547.

⁸⁰ Moreover, the governing statute provides that a remittance advice or a document which merely provides notice of a payment action is not a notice of adjustment. Government Code section 17558.5(c) ("Remittance advices and other notices of payment action shall not constitute notice of adjustment from an audit or review."). Whatever term may accurately be used to characterize the three documents identified by the claimant, the three documents are not "notices of adjustment" under state mandate law.

⁸¹ Exhibit F, Claimant's Comments on the Draft Proposed Decision, pages 2-3.

At the time the reimbursement claims were audited and when this IRC was filed, the Commission’s regulation containing the limitations period read:

All incorrect reduction claims shall be filed with the commission 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.⁸²

Under a legal doctrine with the somewhat confusing name of the “last essential element” rule, a limitations period begins to run upon the occurrence of the *earliest* event in time which creates a claim. Under this rule, a right accrues — and the limitations period begins to run — from the earliest point in time when the claim could have been filed and maintained.

As recently summarized by the California Supreme Court:

The limitations period, the period in which a plaintiff must bring suit or be barred, runs from the moment a claim accrues. (See Code Civ. Proc., § 312 [an action must “be commenced within the periods prescribed in this title, after the cause of action shall have accrued”]; (Citations.). Traditionally at common law, a “cause of action accrues ‘when [it] is complete with all of its elements’ — those elements being wrongdoing, harm, and causation.” (Citations.) This is the “last element” accrual rule: ordinarily, the statute of limitations runs from “the occurrence of the last element essential to the cause of action.” (Citations.)⁸³

In determining when a limitations period begins to run, the California Supreme Court looks to the earliest point in time when a litigant could have filed and maintained the claim:

Generally, a cause of action accrues and the statute of limitation begins to run when a suit may be maintained. [Citations.] “Ordinarily this is when the wrongful act is done and the obligation or the liability arises, but it does not ‘accrue until the party owning it is entitled to begin and prosecute an action thereon.’ ” [Citation.] In other words, “[a] cause of action accrues ‘upon the occurrence of the last element essential to the cause of action.’ ” [Citations.]⁸⁴

Under these principles, the claimant’s three-year limitations period began to run from the date of the Final Audit Report. As of that date, the claimant could have filed an IRC pursuant to Government Code sections 17551 and 17558.7, because, as of that date, the claimant had been (from its perspective) harmed by a claim reduction. The Controller’s subsequent issuance of a letter or other notice that does not change the reason for the reduction does not start a new limitations clock. The limitations period starts to run from the earliest point in time when the

⁸² Former Code of California Regulations, title 2, section 1185(b) (Regulation 1185), which was renumbered section 1185(c) effective January 1, 2011. Effective July 1, 2014, the regulation was amended to state the following: “All incorrect reduction claims shall be filed with the Commission no later than three years following the date of the Office of State Controller’s final state audit report, letter, remittance advice, or other written notice of adjustment to a reimbursement claim.” Code of California Regulations, title 2, section 1185.1(c).

⁸³ *Aryeh v. Canon Business Solutions, Inc.* (2013) 55 Cal.4th 1185, 1191.

⁸⁴ *Howard Jarvis Taxpayers Ass’n v. City of La Habra* (2001) 25 Cal.4th 809, 815.

claimant could have filed an IRC — and the limitations period expires three years after that earliest point in time.

This finding is consistent with two recent Commission decisions regarding the three-year period in which a claimant can file an IRC.

In the *Collective Bargaining* program IRC Decision adopted on December 5, 2014, the claimant argued that the limitations period should begin to run from the date of the *last* notice of adjustment in the record.⁸⁵ This argument parallels that of the claimant in this instant IRC, who argues that between the Final Audit Report dated June 30, 2010, and the three documents dated August 6, 2010, the *later* event should commence the running of the limitations period.

In the *Collective Bargaining* Decision, the Commission rejected the argument. The Commission held that the limitations period began to run on the *earliest* applicable event because that was when the claim was complete as to all of its elements.⁸⁶ “Accordingly, the claimant cannot allege that the earliest notice did not provide sufficient information to initiate the IRC, and the later adjustment notices that the claimant proffers do not toll or suspend the operation of the period of limitation,” the Commission held.⁸⁷

In the *Domestic Violence Treatment Services — Authorization and Case Management* program IRC Decision adopted on March 25, 2016, the Commission held, “For IRCs, the ‘last element essential to the cause of action’ which begins the running of the period of limitations . . . is a notice to the claimant of the adjustment that includes the reason for the adjustment.”⁸⁸ In the instant IRC, the limitations period therefore began to run from the Final Audit Report, which is the notice that informed the claimant of the adjustment and of the reasons for the adjustment.

Furthermore, the Commission’s finding in the instant IRC is not inconsistent with a recent Commission ruling regarding the timeliness of filing an IRC.

In the *Handicapped and Disabled Students* IRC Decision adopted September 25, 2015, the Commission found that an IRC filed by a claimant was timely because the limitations period began to run from the date of a remittance advice letter which was sent after the Controller’s Final Audit Report.⁸⁹ This Decision is distinguishable because, in that claim, the Controller’s cover letter (accompanying the audit report) to the claimant requested additional information and implied that the attached audit report was not final.⁹⁰ In the instant IRC, by contrast, the

⁸⁵ Decision, *Collective Bargaining*, 05-4425-I-11 (adopted December 5, 2014), pages 20-22.

⁸⁶ Decision, *Collective Bargaining*, 05-4425-I-11 (adopted December 5, 2014), pages 20-22.

⁸⁷ Decision, *Collective Bargaining*, 05-4425-I-11 (adopted December 5, 2014), page 21.

⁸⁸ Decision, *Domestic Violence Treatment Services — Authorization and Case Management*, 07-9628101-I-01 (adopted March 25, 2016), page 16.

⁸⁹ Decision, *Handicapped and Disabled Students*, 05-4282-I-03 (adopted September 25, 2015), pages 11-14.

⁹⁰ Decision, *Handicapped and Disabled Students*, 05-4282-I-03 (adopted September 25, 2015), pages 11-14. In the proceeding which resulted in this 2015 Decision, the cover letter from the Controller to the claimant is reproduced at Page 71 of the administrative record. In that letter, the Controller stated, “The SCO has established an informal audit review process to resolve a dispute of facts. The auditee should submit, in writing, a request for a review and all information

Controller's cover letter contained no such statement or implication; rather, the Controller's cover letter stated that, if the claimant disagreed with the attached Final Audit Report, the claimant would need to file an IRC within three years.⁹¹

The finding in this instant IRC is therefore consistent with recent Commission rulings regarding the three-year IRC limitations period.⁹²

In comments on the Draft Proposed Decision, the claimant argues that the Commission should not apply the "last essential element" rule because Regulation 1185 used the disjunctive "or" when listing the events which triggered the running of the limitations period.⁹³ The claimant provides no legal authority for its argument or evidence that Regulation 1185 was intended to be read in such a manner. The Commission therefore rejects the argument.

The Commission also notes that the claimant's interpretation would yield the absurd result of repeatedly resetting the limitations period. Under the claimant's theory, a statute of limitations containing a disjunctive "or" restarts whenever one of the other events in the list occurs. In other words, if a regulation states that a three-year limitations period begins to run upon the occurrence of X, Y, or Z, then (under the claimant's theory), X can occur, a decade can elapse, and then the belated occurrence of Y or Z restarts the limitations clock. This interpretation cannot be correct, particularly in the context of monetary claims against the State's treasury. The "last essential element" rule provides the claimant with the opportunity to timely file a claim while protecting the State from reanimated liability.

Consequently, the Commission concludes that the limitations period begins to run from the occurrence of the earliest event which would have allowed the claimant to file a claim. That event, in this case, was the date of the Final Audit Report. Since more than three years elapsed between that date and filing of the IRC, the IRC was untimely.

3. The Controller's Misstatement of Law (Specifically, the Controller's Erroneous Statement That the Limitations Period Began to Run as of the Three Documents Dated August 6, 2010) Does Not Result in an Equitable Estoppel That Makes the IRC Timely.

In its comments on the Draft Proposed Decision, the claimant argues that the IRC should be considered timely because the claimant relied upon statements made by the Controller. "The County relied upon the statements and the actions of the SCO in making its determinations. In

pertinent to the disputed issues within 60 days after receiving the final report." The Controller's cover letter in the instant IRC contains no such language. Exhibit A, IRC, page 542 (Letter from Jeffrey V. Brownfield to Gloria Molina, dated June 30, 2010).

⁹¹ Exhibit A, IRC, page 542.

⁹² All that being said, an administrative agency's adjudications need not be consistent. See, e.g., *Weiss v. State Board of Equalization* (1953) 40 Cal.2d 772, 777 ("The administrator is expected to treat experience not as a jailer but as a teacher."); *California Employment Commission v. Black-Foxe Military Institute* (1941) 43 Cal.App.2d Supp. 868, 876 ("even were the plaintiff guilty of occupying inconsistent positions, we know of no rule of statute or constitution which prevents such an administrative board from doing so.").

⁹³ Exhibit F, Claimant's Comments on the Draft Proposed Decision, page 3.

its cover letter to the County accompanying the audit report, the SCO states that the County must file an IRC within three years of the SCO notifying the County of a claim reduction. The SCO then refers to the notices as notices of claim reduction. The SCO then specifically referred to the dates of the notices upon which the County relied as the dates they notified the County of a claim reduction.”⁹⁴

Although the claimant does not use the precise term (and does not conduct the requisite legal analysis), the claimant is arguing that the Controller should be equitably estopped from benefiting from the statute of limitations, and that the Commission should find the IRC timely. The claimant is arguing that, if the filing deadline provided by the Controller was erroneous, then the claimant should be forgiven for filing late because the claimant was relying upon the Controller’s statements.

A state administrative agency may possess⁹⁵ — but does not necessarily possess⁹⁶ — the authority to adjudicate claims of equitable estoppel. The Commission possesses the authority to adjudicate claims of equitable estoppel because, without limitation, the Commission is vested with exclusive and original jurisdiction and the Commission is obligated to create a full record for the Superior Court to review in the event that a party seeks a writ of administrative mandamus.⁹⁷

The general elements of estoppel are well-established. “Whenever a party has, by his own statement or conduct, intentionally and deliberately led another to believe a particular thing true and to act upon such belief, he is not, in any litigation arising out of such statement or conduct, permitted to contradict it.”⁹⁸ “Generally speaking, four elements must be present in order to apply the doctrine of equitable estoppel: (1) the party to be estopped must be apprised of the facts; (2) he must intend that his conduct shall be acted upon, or must so act that the party asserting the estoppel had a right to believe it was so intended; (3) the other party must be ignorant of the true state of facts; and (4) he must rely upon the conduct to his injury.”⁹⁹

⁹⁴ Exhibit F, Claimant’s Comments on the Draft Proposed Decision, page 3. The letter the claimant is referring to is the letter at Exhibit A, IRC, pages 485-486 from Jim Spano to Robin C. Kay, dated May 7, 2013.

⁹⁵ *Lentz v. McMahon* (1989) 49 Cal.3d 393, 406.

⁹⁶ *Foster v. Snyder* (1999) 76 Cal.App.4th 264, 268 (“The holding in *Lentz* does not stand for the all-encompassing conclusion that equitable principles apply to all administrative proceedings.”).

⁹⁷ *Lentz v. McMahon* (1989) 49 Cal.3d 393, 404 (regarding exclusive jurisdiction) & fn. 8 (regarding duty to create full record for review). See also Government Code section 17552 (exclusive jurisdiction); Government Code section 17559(b) (aggrieved party may seek writ of administrative mandamus).

⁹⁸ Evidence Code section 623.

⁹⁹ *Driscoll v. City of Los Angeles* (1967) 67 Cal.2d 297, 305.

“The doctrine of estoppel is available against the government “where justice and right require it.” (Citation.)”¹⁰⁰ However, “estoppel will not be applied against the government if to do so would nullify a strong rule of policy adopted for the benefit of the public.”¹⁰¹ Estoppel against the government is to be limited to “exceptional conditions,” “special cases,” an “exceptional case,” or applied in a manner which creates an “extremely narrow precedent.”¹⁰²

Furthermore, the party to be estopped must have engaged in some quantum of turpitude. “We have in fact indicated that some element of turpitude on the part of the party to be estopped is requisite even in cases not involving title to land,” the California Supreme Court noted.¹⁰³ In the federal courts, equitable estoppel against the government “must rest upon affirmative misconduct going beyond mere negligence.”¹⁰⁴

Upon a consideration of all of the facts and argument in the record, the Commission concludes for the following reasons that the Controller is not equitably estopped from benefiting from the statute of limitations.

The Commission interprets the evidence in the record as presenting a mutual mistake of law by both the Controller and the claimant. On the date of the Controller’s erroneous letter (May 7, 2013), Regulation 1185’s three-year limitations period had been in effect and had been published since at least May 2007.¹⁰⁵ Despite the fact that the limitations period had been in effect for several years, both the claimant and the Controller incorrectly calculated the IRC filing deadline as starting from the date of the three documents dated August 6, 2010, when, for the reasons explained in this Decision, the filing deadline started to run as of the date of the Final Audit Report.

A situation in which a government agency and a third party both misinterpret the law does not allow for an estoppel against the government — because the third party should have taken the time to learn what the law actually said. “Acts or conduct performed under a mutual mistake of law do not constitute grounds for estoppel. (Citation.) It is presumed the party claiming estoppel had an equal opportunity to discover the law.”¹⁰⁶ “Where the facts and law are known to both parties, there can be no estoppel. (Citation.) Even an expression as to a matter of law, in the

¹⁰⁰ *Robinson v. Fair Employment and Housing Commission* (1992) 2 Cal.4th 226, 244, quoting *Lentz v. McMahon* (1989) 49 Cal.3d 393, 399, quoting *City of Los Angeles v. Cohn* (1894) 101 Cal. 373, 377.

¹⁰¹ *Lusardi Construction Co. v. Aubry* (1992) 1 Cal.4th 976, 994–995.

¹⁰² *City of Long Beach v. Mansell* (1970) 3 Cal.3d 462, 496 & fn. 30, 500.

¹⁰³ *City of Long Beach v. Mansell* (1970) 3 Cal.3d 462, 490 fn. 24.

¹⁰⁴ *Morgan v. Heckler* (1985) 779 F.2d 544, 545 (Kennedy, J.). See also *Mukherjee v. I.N.S.* (9th Cir. 1986) 793 F.2d 1006, 1009 (defining affirmative misconduct as “a deliberate lie . . . or a pattern of false promises”).

¹⁰⁵ California Regulatory Code Supplement, Register 2007, No. 19 (May 11, 2007), page 212.1 [version operative May 8, 2007].

¹⁰⁶ *Adams v. County of Sacramento* (1991) 235 Cal.App.3d 872, 883–884.

absence of a confidential relationship, is not a basis for an estoppel.”¹⁰⁷ “Persons dealing with the government are charged with knowing government statutes and regulations, and they assume the risk that government agents may exceed their authority and provide misinformation.”¹⁰⁸

In point of fact, the Controller had earlier provided the claimant with general IRC filing information and had admonished the claimant to visit the Commission’s website. In the cover letter dated June 30, 2010, the Controller summarized the audit findings and then stated, “If you disagree with the audit findings, you may file an Incorrect Reduction Claim (IRC) with the Commission on State Mandates (CSM). The IRC must be filed within three years following the date that we notify you of a claim reduction. You may obtain IRC information at the CSM’s Web site at www.csm.ca.gov/docs/IRCform.pdf.”¹⁰⁹ In other words, as of June or July 2010, the claimant had been informed in general terms of the filing deadline and had been directed to the Commission. The fact that the claimant failed to do so and the fact that the Controller made an erroneous statement more than two years later does not somehow make the claimant’s IRC timely.

Separately and independently, the record does not indicate that the Controller engaged in some quantum of turpitude. There is no evidence, for example, that the Controller acted with an intent to mislead.

Finally, the finding of an estoppel under this situation would nullify a strong rule of policy adopted for the benefit of the public, specifically, the policy that limitations periods exist “to encourage the timely presentation of claims and prevent windfall benefits.”¹¹⁰

For each of these reasons, the claimant’s argument of equitable estoppel is denied.

The Commission is also unpersuaded that the events which the claimant characterizes as the Controller’s reconsideration of the audit act to extend, reset, suspend or otherwise affect the limitations period.¹¹¹ While the claimant contends that the Controller reconsidered the audit findings and then withdrew from the reconsideration,¹¹² the Controller contends that it did not engage in a reconsideration, but instead denied the claimant’s request for a reconsideration.¹¹³ On this point, the factual evidence in the record, within the letter from the Controller dated May 7, 2013, provides, “This letter confirms that we denied the county’s reconsideration request”¹¹⁴ The limitations period cannot be affected by a reconsideration which did not occur. Separately, the process which the claimant characterizes as a reconsideration did not commence

¹⁰⁷ *People v. Stuyvesant Ins. Co.* (1968) 261 Cal.App.2d 773, 784.

¹⁰⁸ *Lavin v. Marsh* (9th Cir. 1981) 644 F.2d 1378, 1383.

¹⁰⁹ Exhibit A, IRC, page 542.

¹¹⁰ *Lentz v. McMahon* (1989) 49 Cal.3d 393, 401.

¹¹¹ Exhibit F, Claimant’s Comments on the Draft Proposed Decision, pages 2-3.

¹¹² Exhibit F, Claimant’s Comments on the Draft Proposed Decision, pages 2-3.

¹¹³ Exhibit A, IRC, page 485.

¹¹⁴ Exhibit A, IRC, page 485.

until a June 2012 delivery of documents,¹¹⁵ by which time the limitations period had been running for about two years. The claimant does not cite to legal authority or otherwise persuasively explain how the Controller's alleged reconsideration stopped or reset the already-ticking limitations clock.

Accordingly, the IRC is denied as untimely filed.

V. Conclusion

The Commission finds that claimant's IRC was untimely filed.

Therefore, the Commission denies this IRC.

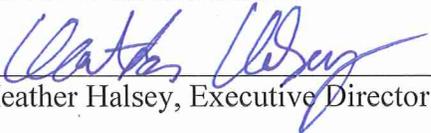
¹¹⁵ Exhibit A, IRC, page 485.



RE: **Decision**

Handicapped and Disabled Students, 13-4282-I-06
Government Code Sections 7572 and 7572.5
Statutes 1984, Chapter 1747 (AB 3632); Statutes 1985, Chapter 1274 (AB 882);
California Code of Regulations, Title 2, Division 9, Chapter 1, Section 60040
(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])
Fiscal Years: 2003-2004, 2004-2005, and 2005-2006
County of Los Angeles, Claimant

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



Heather Halsey, Executive Director

Dated: July 27, 2016

BEFORE THE
COMMISSION ON STATE MANDATES
STATE OF CALIFORNIA

IN RE INCORRECT REDUCTION CLAIMS
ON:

Government Code Section 7576 as amended by
Statutes 1996, Chapter 654 (AB 2726);

California Code of Regulations, Title 2, Division
9, Chapter 1, Sections 60100 and 60110

Fiscal Years 2000-2001, 2001-2002, 2002-2003,
2003-2004, 2004-2005, and 2005-2006

AND

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])¹

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

County of Orange, Claimant

Case Nos.: 11-9705-I-02 and 12-9705-I-03

*Seriously Emotionally Disturbed Pupils:
Out-of-State Mental Health Services, and*

*Handicapped and Disabled Students;
Handicapped and Disabled Students II; and
Seriously Emotionally Disturbed (SED) Pupils:
Out-of-State Mental Health Services*

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

(Adopted September 23, 2016)

(Served September 28, 2016)

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.

DECISION

The Commission on State Mandates (Commission) heard and decided these consolidated Incorrect Reduction Claims (IRCs) during a regularly scheduled hearing on September 23, 2016. James Harman appeared on behalf of the County of Orange. Jim Spano and Chris Ryan appeared on behalf of the State Controller's Office (Controller).

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

The Commission adopted the Proposed Decision to deny these IRCs by a vote of 6-0 as follows:

Member	Vote
Richard Chivaro, Representative of the State Controller	Yes
Mark Hariri, Representative of the State Treasurer, Vice Chairperson	Yes
Scott Morgan, Deputy Director of Administration and State Clearinghouse Director, Governor's Office of Planning and Research	Yes
Sarah Olsen, Public Member	Yes
Eraina Ortega, Representative of the Director of the Department of Finance, Chairperson	Yes
Carmen Ramirez, City Council Member	Absent
Don Saylor, County Supervisor	Yes

Summary of the Findings

The Commission finds that the Office of the State Controller's (Controller's) reduction of costs claimed by the County of Orange (claimant) for board and care and treatment services for out-of-state residential placement of SED pupils in facilities organized and operated for-profit 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 further require the claimant to provide supporting documentation for the costs claimed. Based on the documentation provided by the claimant in this case, the Controller found that the vendor costs claimed for eight out-of-state residential facilities were beyond the scope of the mandate and not allowable. Some of the residential facilities were not organized and operated on a nonprofit basis.² Other vendor payments made by the claimant were made to nonprofit corporations, but those corporations contracted with for-profit facilities

² Exhibit D, Controller's Late Comments on IRC 11-9705-I-02, page 14 (claimant did not support that costs claimed for eight out-of-state facilities were incurred for placement of SED pupils in nonprofit residential placement facilities); Exhibit E, Controller's Late Comments on IRC 12-9705-I-03, page 18 (claimant did not support that costs claimed for six out-of-state facilities were incurred for placement of SED pupils in nonprofit residential facilities).

to provide the services. And the claimant did not provide any documentation to support the nonprofit status of some of the facilities, and admitted the for-profit status of the other facilities. The Office of Administrative Hearings (OAH) and the federal court decisions relied upon by claimant are not applicable because they do not address whether the subvention requirement under article XIII B, section 6 applies. Moreover, claimant has provided no documentation or evidence, nor has claimant alleged, 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. 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, must be strictly construed and not applied as an "equitable remedy to cure the perceived unfairness resulting from political decisions on funding priorities."³

Accordingly, the Commission finds that the Controller's reduction of costs claimed for vendor service payments is consistent with the Commission's Parameters and Guidelines and is correct as a matter of law. Therefore, the Commission denies these IRCs.

I. Chronology

- 11/12/2008 Controller issued the final audit report for fiscal years 2000-2001 through 2001-2002.⁴
- 11/12/2008 Controller issued the final audit report for fiscal years 2002-2003 through 2004-2005.⁵
- 09/17/2010 Controller issued the final audit report for fiscal year 2005-2006.⁶
- 11/09/2011 Claimant filed IRC 11-9705-I-02.⁷
- 03/07/2012 Controller issued a final audit report for fiscal years 2006-2007 through 2008-2009.⁸
- 12/03/2012 Controller issued a revised final audit report for fiscal years 2006-2007 through 2008-2009.⁹

³ *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).

⁴ Exhibit A, Incorrect Reduction Claim 11-9705-I-02, page 73.

⁵ Exhibit A, Incorrect Reduction Claim 11-9705-I-02, page 114

⁶ Exhibit A, Incorrect Reduction Claim 11-9705-I-02, page 155.

⁷ Exhibit A, Incorrect Reduction Claim 11-9705-I-02, page 1. On October 21, 2013, in response to a Commission notice of incomplete filing, claimant resubmitted the claim form, specifying county as the claimant and providing an authorized signature of the county's Manager of Financial Reporting on the claim certification. Exhibit A reflects the completed test claim filing.

⁸ Exhibit B, Incorrect Reduction Claim 12-9705-I-03, page 109.

⁹ Exhibit B, Incorrect Reduction Claim 12-9705-I-03, page 103.

03/08/2013 Claimant filed IRC 12-9705-I-03.¹⁰

03/21/2013 Claimant filed supplemental materials for IRC 12-9705-I-03.¹¹

10/03/2014 Controller filed late comments on IRC 11-9705-I-02.¹²

10/03/2014 Controller filed late comments on IRC 12-9705-I-03.¹³

10/31/2014 Claimant filed a request for an extension of time to file rebuttal comments on both IRCs.¹⁴

03/04/2015 Claimant filed late rebuttal comments to Controller's Late Comments on IRC 11-9705-I-02 and Controller's Late Comments on IRC 12-9705-I-03.¹⁵

02/04/2016 Commission staff issued the Notice of Proposed Consolidation of IRCs 11-9705-I-02 and 12-9705-I-03.

05/13/2016 Commission staff issued the Draft Proposed Decision, and scheduled the hearing for July 22, 2016.¹⁶

05/17/2016 Controller filed comments on the Draft Proposed Decision.¹⁷

06/03/2016 Claimant filed comments on the Draft Proposed Decision.¹⁸

07/06/2016 Commission staff issued the Proposed Decision for hearing.

07/11/2016 Claimant filed a request for postponement of hearing.

07/13/2016 The executive director granted claimant's request for good cause and scheduled the hearing for September 23, 2016.

¹⁰ Exhibit B, Incorrect Reduction Claim 12-9705-I-03, page 1. On October 21, 2013, in response to a Commission notice of incomplete filing, claimant resubmitted the claim form, specifying county as the claimant and providing an authorized signature of the county's Manager of Financial Reporting on the claim certification. Exhibit B reflects the completed test claim filing.

¹¹ Exhibit C, Claimant's Supplement to IRC 12-9705-I-03, page 1.

¹² Exhibit D, Controller's Late Comments on IRC 11-9705-I-02, page 1.

¹³ Exhibit E, Controller's Late Comments on IRC 12-9705-I-03, page 1.

¹⁴ Exhibit F, Claimant's Request for Extension to file Rebuttal to Controller's Comments on the IRCs, filed October 31, 2014.

¹⁵ Exhibit G, Claimant's Late Rebuttal Comments to Controller's Comments on the IRCs, filed March 4, 2015.

¹⁶ Exhibit H, Draft Proposed Decision.

¹⁷ Exhibit I, Controller's Comments on the Draft Proposed Decision, filed May 17, 2016.

¹⁸ Exhibit J, Claimant's Comments on the Draft Proposed Decision, filed June 3, 2016.

II. Background

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

These consolidated IRCs address reimbursement claims for costs incurred by the County of Orange for vendor services provided to SED pupils in out-of-state residential facilities from fiscal years 2000-2001 through 2008-2009. During this audit period, two sets of Parameters and Guidelines governed the program.¹⁹

Generally, the statutes (Gov. Code, §§ 7570, *et seq.*) and implementing regulations at issue (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.²⁰ 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 required that all services provided by the counties be provided *within* the State of California.²¹ 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.²²

On May 25, 2000, the Commission approved the Test Claim *Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services*, 97-TC-05, which 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").²³ 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

¹⁹ Exhibit D, Controller's Late Comments on IRC 11-9705-I-02, pages 48-52 (corrected Parameters and Guidelines, adopted July 21, 2006); Exhibit E, Controller's Late Comments on IRC 12-9705-I-03, pages 156-169 (consolidated Parameters and Guidelines, adopted October 26, 2006.)

²⁰ 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).

²¹ Former California Code of Regulations, title 2, section 60200.

²² Statutes 1996, chapter 654.

²³ Exhibit D, Controller's Late Comments on IRC 11-9705-I-02, pages 22-30.

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 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.²⁴

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

²⁴ Exhibit D, Controller’s Late Comments on IRC 11-9705-I-02, pages 23-24 (Statement of Decision, *Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services*, 97-TC-05); Exhibit E, Controller’s Late Comments on IRC 12-9705-I-03, pages 147-148 (Statement of Decision, *Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services*, 97-TC-05).

- 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.)²⁵

Parameters and Guidelines for the *SED* program were adopted on October 26, 2000,²⁶ and corrected on July 21, 2006,²⁷ 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 60110.²⁸

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, 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.²⁹

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

²⁵ Exhibit D, Controller’s Late Comments on IRC 11-9705-I-02, page 30; Exhibit E, Controller’s Late Comments on IRC 12-9705-I-03, page 154.

²⁶ Exhibit A, Incorrect Reduction Claim 11-9705-I-02, pages 60-64; Exhibit D, Controller’s Late Comments on IRC 11-9705-I-01, pages 33-48.

²⁷ Exhibit D, Controller’s Late Comments on IRC 11-9705-I-02, pages 46-52.

²⁸ Exhibit A, Incorrect Reduction Claim 11-9705-I-02, page 61.

²⁹ Corrected Parameters and Guidelines, dated July 21, 2006; Exhibit D, Controller’s Late Comments on IRC 11-9705-I-02, pages 46-49.

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 *SED, Handicapped and Disabled Students*, CSM 4282 and 04-RL-4282-10, and *Handicapped and Disabled Students II*, 02-TC-40/02-TC-49, for costs incurred commencing with the 2006-2007 fiscal year.³⁰ 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 non-educational 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.*³¹

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.”³² 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.³³

Both sets of Parameters and Guidelines also contain instructions for claiming costs. Section V. of the original Parameters and Guidelines require that claimed costs for fiscal years 2000-2001 through 2005-2006 “shall be supported by” cost element information, as specified. With respect to claims for contract services, claimants are required to:

³⁰ Exhibit E, Controller’s Late Comments on IRC 12-9705-I-03, page 156 (consolidated Parameters and Guidelines, adopted October 26, 2006).

³¹ Exhibit E, Controller’s Late Comments on IRC 12-9705-I-02, page 163 (emphasis added) (consolidated Parameters and Guidelines, adopted October 26, 2006).

³² Exhibit K, Welfare and Institutions Code section 18350, as amended by Statutes 1990, chapter 46, section 12, effective April 10, 1990.

³³ Exhibit E, Controller’s Late Comments on IRC 12-9705-I-02, page 163 (consolidated Parameters and Guidelines, adopted October 26, 2006).

Provide the name(s) of the contractor(s) who performed the services, including any fixed contract for services. Describe the reimbursable activity(ies) performed by each named contractor and give the number of actual hours spent on the activities, if applicable. Show the inclusive dates when services were performed and itemize all costs for those services.³⁴

Section VI. of the original Parameters and Guidelines requires documentation to support the costs claimed as follows:

For auditing purposes, all costs claimed be traceable to source documents (e.g., invoices, receipts, purchase orders, contracts, worksheets, calendars, declarations, etc.) that show the evidence and validity of such costs and their relationship to the state mandated program. All documentation in support of the claimed costs shall be made available to the State Controller's Office, as may be requested...[T]hese documents must be kept on file by the agency submitting the claim for a period of no less than two years after the later of (1) the end of the calendar year in which the reimbursement claim is filed or last amended, or (2) if no funds are appropriated for the fiscal year for which the claim is made, the date of initial payment of the claim.

Beginning with fiscal year 2006-2007, 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.³⁵

Section IV. of the consolidated 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."³⁶

³⁴ Exhibit A, Incorrect Reduction Claim 11-9705-I-02, page 63 (Parameters and Guidelines, adopted October 26, 2000); Exhibit D, Controller's Late Comments on IRC 11-9705-I-02, pages 50-51 (corrected Parameters and Guidelines, adopted July 21, 2006).

³⁵ Exhibit E, Controller's Late Comments on IRC 12-9705-I-03, pages 165-166 (consolidated Parameters and Guidelines, adopted October 26, 2006).

³⁶ Exhibit E, Controller's Late Comments on IRC 12-9705-I-03, pages 165-168 (consolidated Parameters and Guidelines, adopted October 26, 2006).

Statutes 2011, chapter 43 (AB 114) eliminated the mandated programs for *Handicapped and Disabled Students*, CSM 4282 and 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, 2011.³⁷ 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 Controller audited and reduced the reimbursement claims for various reasons. The claimant only disputes the reduction totaling \$6,711,871 for all fiscal years at issue in Finding 1 of both audit reports relating to ineligible vendor payments for board and care and treatment services for out-of-state residential placement of SED pupils in facilities that are “owned and operated *for-profit*.”³⁸ In this respect, the Controller found unallowable costs for all fiscal years based on the following costs claimed for eight residential facilities:

- For two of the facilities (Youth Care of Utah and Charter Provo Canyon School), the county claimed payments made to Mental Health Systems, Inc., and Aspen Solutions Inc., both California nonprofit corporations. However, the Controller found the costs not allowable because these nonprofit corporations contracted with Youth Care of Utah and Charter Provo Canyon, both of which are organized and operated as for-profit facilities, to provide the out-of-state residential placement services.³⁹
- For four of the facilities (Aspen Ranch, Island View, SunHawk Academy and Logan River, LLC), the county asserted that the for-profit facilities had similar contractual arrangements with either Aspen Solutions, Inc. or Mental Health Systems, Inc. (nonprofit businesses incorporated in California). The county, however, did not provide any documentation to support the nonprofit status of the residential facilities providing the services, or provide documentation illustrating a business relationship between the residential facilities and the California nonprofit entities.⁴⁰

³⁷ Exhibit K, Assembly Bill No. 114 (2011-2012 Reg. Sess.), approved by the Governor, June 30, 2011.

³⁸ Exhibit A, Incorrect Reduction Claim 11-9705-I-02, page 8; Exhibit B, Incorrect Reduction Claim 12-9705-I-03, page 9. (Emphasis added.) Both the audit reports and IRC’s use the terms “owned and operated for-profit.” However the statute states “organized and operated for-profit”; our analysis tracks the statutory language.

³⁹ Exhibit D, Controller’s Late Comments on IRC 11-9705-I-02, page 17; Exhibit E, Controller’s Late Comments on IRC 12-9705-I-03, pages 19-20.

⁴⁰ Exhibit D, Controller’s Late Comments on IRC 11-9705-I-02, page 17; Exhibit E, Controller’s Late Comments on IRC 12-9705-I-03, page 20.

- For National Deaf Academy, the county acknowledged it is a for-profit entity, and did not provide any documentation in support of its nonprofit status.⁴¹
- The claimant also contracted with For Kids Behavioral Health of Alaska, Inc., who then contracted with Copper Hills Youth Center to provide the services. Claimant argued that For Kids Behavioral Health of Alaska, Inc. was a nonprofit facility and provided a Certificate of Good Standing from the State of Alaska and a Certificate of Registration from the State of Utah seeking nonprofit status, which was filed and approved December 7, 2007, relating to only a portion of the audit period. In addition, the claimant did not provide any documentation regarding the business relationship between Kids Behavioral Health of Alaska and Copper Hills Youth Center, the residential facility where the pupils were placed. According to a Utah government website, the business named Copper Hills Youth Center was registered November 5, 2004 and remained in business through November 4, 2009, operating as a health services facility.⁴² However, claimant provided no documentation to support a finding that Copper Hills was a nonprofit entity.

III. Positions of the Parties

A. County of Orange

The claimant 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)).⁴³ 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 the IDEA's requirement that children with disabilities be placed in the most appropriate educational environment out-of-state and not be constrained by non-profit status.⁴⁴
- During the periods at issue, the County contracted with nonprofit entities: Mental Health Services, Inc. (facilities include: Provo Canyon School and Logan River Academy),

⁴¹ Exhibit D, Controller's Late Comments on IRC 11-9704-I-02, page 17.

⁴² Exhibit D, Controller's Late Comments on IRC 11-9705-I-02, page 17; Exhibit E, Controller's Late Comments on IRC 12-9705-I-03, page 20.

⁴³ Exhibit A, Incorrect Reduction Claim 11-9705-I-02, page 9; Exhibit B, Incorrect Reduction Claim 12-9705-I-03, page 9.

⁴⁴ Exhibit A, Incorrect Reduction Claim 11-9705-I-02, pages 9-10; Exhibit B, Incorrect Reduction Claim 12-9705-I-03, pages 10-11.

Aspen Solutions, Inc. (facilities include: Island View, Aspen Ranch, Youth Care of Utah, and SunHawk Academy), and Kids Behavior Health of Alaska, Inc. (facility: Copper Hills Youth Center) to provide the out-of-state residential services subject to the disputed disallowances.⁴⁵

- 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, the U.S. District Court, Central District of California, 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.⁴⁶
- 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. 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.⁴⁷
- The Controller’s interpretation of Welfare and Institutions Code section 11460(c)(3) would result in higher state reimbursement costs, based on a comparison between the cost of mental health services provided at residential facilities that are organized and operated for-profit versus those that are organized as nonprofit.⁴⁸

Claimant disagrees with the conclusions and recommendations in the Draft Proposed Decision and reasserts it is entitled to the full amount of costs claimed for the placement of pupils in out-of-state residential facilities that are organized and operated on a non-profit basis.⁴⁹ The claimant argues the following:

[T]he Proposed Decision disallows the costs associated with these vendors because of the corporate status of the companies they deal with, such as Charter Provo Canyon. Nothing in the Parameters and Guidelines references subcontractors, affiliates, or partners. Rather, it references “vendors” which the

⁴⁵ Exhibit A, Incorrect Reduction Claim 11-9705-I-02, pages 12-13; Exhibit B, Incorrect Reduction Claim 12-9705-I-03, pages 9-10.

⁴⁶ Exhibit A, Incorrect Reduction Claim 11-9705-I-02, pages 10-12, 14-16; Exhibit B, Incorrect Reduction Claim 12-9705-I-03, pages 12-13, 15-17.

⁴⁷ Exhibit A, Incorrect Reduction Claim 11-9705-I-02, page 13; Exhibit B, Incorrect Reduction Claim 12-9705-I-03, page 14.

⁴⁸ Exhibit A, Incorrect Reduction Claim 11-9705-I-02, page 14; Exhibit B, Incorrect Reduction Claim 12-9705-I-03, pages 14-15.

⁴⁹ Exhibit J, Claimant’s Comments on the Draft Proposed Decision.

Proposed Decision concedes in two instances the County's vendors were non-profit entities.⁵⁰

The claimant also asserts that the Proposed Decision adopts an inappropriate abuse of discretion standard of review of the Controller's audit decisions, and argues that the Commission must conduct an independent review of the matter and "make a determination that the Controller incorrectly reduced the County's claims for the reasons stated in the claims in this letter."⁵¹

B. State Controller's Office

It is the Controller's position that the audit adjustments are correct and that these IRCs should be denied. The Controller found 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.⁵² The Controller asserts that the unallowable treatment and board-and-care vendor payments claimed result from the claimant's placement of SED pupils in prohibited for-profit out-of-state residential facilities.⁵³ The Controller argues that the county did not support that costs claimed for eight out-of-state facilities were for placement in nonprofit residential facilities, and concludes that the county made placements in out-of-state facilities that are organized and operated for profit.⁵⁴

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

⁵⁰ Exhibit J, Claimant's Comments on the Draft Proposed Decision, pages 1 and 2.

⁵¹ Exhibit J, Claimant's Comments on the Draft Proposed Decision, page 2. The Commission need not make a determination with regard to claimant's assertion of the legal standard to apply to the Controller's auditing decisions generally, since the issue in this case is a pure issue of law and therefore the de novo standard of review applies.

⁵² Exhibit D, Controller's Late Comments on IRC 11-9705-I-02, page 15; Exhibit E, Controller's Late Comments on IRC 12-9705-I-03, page 19.

⁵³ Exhibit D, Controller's Late Comments on IRC 11-9705-I-02, page 14; Exhibit E, Controller's Late Comments on IRC 12-9705-I-03, page 18.

⁵⁴ Exhibit D, Controller's Late Comments on IRC 11-9705-I-02, page 14 (county did not support that costs claimed for eight out-of-state facilities were incurred for placement in non-profit residential facilities); Exhibit E, Controller's Late Comments on IRC 12-9705-I-03, page 18 (county did not support that costs claimed for six out-of-state facilities were incurred for placement in non-profit residential facilities).

maintains that under the mandated program, costs incurred at out-of-state for-profit residential programs are not reimbursable.⁵⁵

The Controller also distinguishes the OAH, U.S. District Court, Central District of California Court, and U.S. Supreme Court cases cited by the claimant. In the OAH case and related appeal to the U.S. District Court, 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.⁵⁶ In the U.S. Supreme Court case, *Florence County Sch. Dist. Four v. Carter by & Through Carter* (1993) 510 U.S. 7, the court ruled that parents who unilaterally withdrew their child from an inappropriate placement must be reimbursed even if the parents' school placement does not meet state educational standards and is not state approved, which the Controller distinguishes for the same reason as the OAH and U.S. District Court cases. 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 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.⁵⁷

The Controller filed comments in support of the Draft Proposed Decision.⁵⁸

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.

⁵⁵ Exhibit D, Controller's Late Comments on IRC 11-9705-I-02, pages 15-16; Exhibit E, Controller's Late Comments on IRC 12-9705-I-03, page 20.

⁵⁶ Exhibit D, Controller's Late Comments on IRC 11-9705-I-02, pages 16-17; Exhibit E, Controller's Late Comments on IRC 12-9705-I-03, page 21.

⁵⁷ Exhibit D, Controller's Late Comments on IRC 11-9705-I-02, page 16 (citing OAH case Nos. N 2007090403 and 2005070683, available at Exhibit D, Tabs 9 and 10, pages 67-84); Exhibit E, Controller's Late Comments on IRC 12-9705-I-03, page 21 (citing OAH case Nos. 2007090403 and 2005070683, available at Exhibit E, Tabs 11 and 12, pages 205-222).

⁵⁸ Exhibit I, Controller's Comments on the Draft Proposed Decision, filed May 17, 2016.

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 6.⁵⁹ 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.”⁶⁰

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.⁶¹ Under this standard, the courts have found that:

When reviewing the exercise of discretion, “[t]he scope of review is limited, out of deference to the agency’s authority and presumed expertise: ‘The court may not reweigh the evidence or substitute its judgment for that of the agency. [Citation.]’”...“In general...the inquiry is limited to whether the decision was arbitrary, capricious, or entirely lacking in evidentiary support...” [Citations.] When making that inquiry, the “ ‘court must ensure that an agency has adequately considered all relevant factors, and has demonstrated a rational connection between those factors, the choice made, and the purposes of the enabling statute.’ ”⁶²

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.⁶³ 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.⁶⁴

⁵⁹ *Kinlaw v. State of California* (1991) 54 Cal.3d 326, 331-334; Government Code sections 17551, 17552.

⁶⁰ *County of Sonoma v. Commission on State Mandates* (2000) 84 Cal.App.4th 1264, 1280, citing *City of San Jose v. State of California* (1996) 45 Cal.App.4th 1802, 1817.

⁶¹ *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.

⁶² *American Bd. of Cosmetic Surgery, Inc., v. Medical Bd. of California* (2008) 162 Cal.App.4th 534, 547-548.

⁶³ *Gilbert v. City of Sunnyvale* (2005) 130 Cal.App.4th 1264, 1274-1275.

⁶⁴ 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

The Controller's Reduction of Costs Is Correct as a Matter of Law.

Reimbursement claims filed with the Controller are required as a matter of law to be filed in accordance with the parameters and guidelines adopted by the Commission.⁶⁵ Parameters and guidelines provide instructions for eligible claimants to prepare reimbursement claims for direct and indirect costs of a state-mandated program.⁶⁶

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.

- A. 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 out-of-state service vendors that are organized and operated on a for-profit basis are beyond the scope of the mandate and not reimbursable as a matter of law.

As indicated above, the original Parameters and Guidelines for the *SED* program governs the 2000-2001 through 2005-2006 reimbursement claims and authorizes reimbursement for payments to service vendors providing mental health services to SED pupils placed in out-of-state residential facilities, as specified in California Code of Regulations, title 2, section 60100. Section 60100 of the regulations implements the requirements of former Welfare and Institutions Code section 18350, which was enacted to govern the payments for 24 hour out-of-home care provided on behalf of SED pupils who are placed out-of-home pursuant to an IEP. Former 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. Section 11640(c)(3) specifies that SED pupils shall only be placed in out-of-state facilities organized and operated on a nonprofit basis. Consistent with these statutes, section 60100(h) of the regulations states that out-of-state residential programs shall meet the requirements in Welfare and Institutions Code section 11640(c)(2) through (3). The July 21, 2006 correction to the Parameters and Guidelines clarifies that "mental health services" includes residential board and care.

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.

⁶⁵ 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.

⁶⁶ Government Code section 17557; California Code of Regulations, title 2, section 1183.7.

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 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.⁶⁷

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.” 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.”⁶⁸

When the Parameters and Guidelines for the *SED* program were consolidated with *Handicapped and Disabled Students* and the *Handicapped and Disabled Students II* programs for costs incurred beginning July 1, 2006, reimbursement continued to be authorized for the payments to out-of-state residential facilities based on rates established in accordance with Welfare and Institutions Code sections 18350 and 18356. Although the consolidated Parameters and Guidelines do not quote the language in section 60100(h) in full, they plainly state that counties are required to determine that the residential placement “meets all the criteria established in Welfare and Institutions Code sections 18350 through 18356 before authorizing payment,” which as described above includes ensuring that the facility providing the out-of-state services operates on a nonprofit basis pursuant to Welfare and Institutions Code section 11460. Thus, the

⁶⁷ Exhibit K, Final Statement of Reasons for Joint Regulations for Pupils with Disabilities, page 127 (emphasis added).

⁶⁸ Exhibit K, Final Statement of Reasons for Joint Regulations for Pupils with Disabilities, page 128.

requirement that the out-of-state residential facility be operated on a nonprofit basis remained the same when the Parameters and Guidelines were consolidated.

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.⁶⁹ 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 non-profit basis under this program.

Moreover, legislation was later 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 a non-profit 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 Senate Bill 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 non-profits 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 government eliminated the requirement that a facility be operated as a non-profit in order to receive federal funding in 1996.⁷⁰ However, the bill did not pass the assembly.⁷¹

⁶⁹ Exhibit A, Incorrect Reduction Claim IRC 11-9705-I-02, page 13; Exhibit B, Incorrect Reduction Claim 12-9705-I-03, page 14.

⁷⁰ Exhibit K, Assembly Committee on Human Services, analysis of Senate Bill No. 292 (2007-2008 Reg. Sess.), June 17, 2009, page 2.

⁷¹ Exhibit K, Complete Bill History, Senate Bill No. 292 (2007-2008 Reg. Sess.).

In 2008, AB 1805, a budget trailer bill, containing identical language to SB 292 was vetoed by the governor.⁷² 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."⁷³

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.⁷⁴ 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.⁷⁵ 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.⁷⁶ 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.⁷⁷ The author notes the discrepancy between California law and federal law, which allows federal funding of for-profit group home placements.⁷⁸ However, the bill did not pass the Assembly and therefore did not move forward.⁷⁹

⁷² Exhibit K, Assembly Committee on Appropriations, analysis of Assembly Bill No. 421 (Reg. Sess. 2009-2010), May 20, 2009, page 3.

⁷³ Exhibit K, Governor's Veto Message, Assembly Bill 1885 (Reg. Sess. 2007-2008), September 30, 2008.

⁷⁴ Exhibit K, Assembly Committee on Appropriations, analysis of Assembly Bill No. 421 (Reg. Sess. 2009-2010), May 20, 2009, page 2.

⁷⁵ Exhibit K, Assembly Committee on Appropriations, analysis of Assembly Bill No. 421 (Reg. Sess. 2009-2010), May 20, 2009, page 1.

⁷⁶ Exhibit K, Assembly Committee on Appropriations, analysis of Assembly Bill No. 421 (Reg. Sess. 2009-2010), May 20, 2009, page 2.

⁷⁷ Exhibit K, Assembly Committee on Appropriations, analysis of Assembly Bill No. 421 (Reg. Sess. 2009-2010), May 20, 2009, page 2.

⁷⁸ Exhibit K, Assembly Committee on Appropriations, analysis of Assembly Bill No. 421 (Reg. Sess. 2009-2010), May 20, 2009.

⁷⁹ Exhibit K, Complete Bill History, Assembly Bill No. 421 (Reg. Sess. 2009-2010).

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, 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.⁸⁰

Accordingly, pursuant to the law and the Parameters and Guidelines, reimbursement is required only if the out-of-state service vendor that provides board and care and treatment services to SED pupils operates on a nonprofit basis. 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 and are not eligible for reimbursement as a matter of law.

B. The Controller's reduction of costs claimed for vendor service payments is consistent with the Parameters and Guidelines and is correct as a matter of law.

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 on a for-profit basis are beyond the scope of the mandate and are not eligible for reimbursement as a matter of law. The Parameters and Guidelines also require that the claimant provide documentation in support of the costs claimed for contract services, including the name of the contractor and the services performed to implement the reimbursable activities.

In this case, the Controller concluded that the vendor payments made by the claimant to eight out-of-state facilities were not allowable because the documentation provided by the county did not support that the costs were incurred for services provided by nonprofit residential facilities. Since the facilities providing the treatment and board and care are for-profit facilities, the Controller found that the costs were not eligible for reimbursement under the Parameters and Guidelines.⁸¹

1. The documentation in the record supports the Controller's findings.

The claimant makes no argument disputing the Controller's findings that the facilities providing treatment and board and care services for its SED pupils are for-profit. Claimant contends, however, that reimbursement is required because "it contracted with nonprofit facilities to provide all program services." Specifically the county asserts that it

...contracted for out-of-state residential services with Mental Health Systems, Inc. (whose facilities include: Provo Canyon School and Logan River Academy), Aspen Solutions, Inc. (whose facilities include: Island View, Aspen Ranch, Youth Care of Utah, and SunHawk Academy), and Kids Behavioral Health of Alaska, Inc. (whose facilities

⁸⁰ California Constitution, article III, section 3.5; *Robin J. v. Superior Court* (2004) 124 Cal.App.4th 414, 425.

⁸¹ Exhibit D, Controller's Late Comments on IRC 11-9705-I-02, page 14; Exhibit E, Controller's Late Comments on IRC 12-9705-I-03, page 18.

includes Copper Hills Youth Center). Each of the entities that the County contracted with are organized as nonprofit organizations...the County contracted with these providers in a manner consistent with the requirements of the California Code of Regulations and Welfare and Institutions Code reference above.⁸²

The County also provided copies of the Articles of Incorporation, an IRS verification of tax exempt status letter, and Certificate of Good Standing, as verification that Mental Health Systems, Inc., Aspen Solutions, Inc., and Kids Behavioral Health of Alaska, Inc., are nonprofit entities.⁸³ Claimant further argues that

Neither the federal nor the state government has provided procedures or guidelines to specify if and/or exactly how counties should determine for-profit or nonprofit status. Although counties have used many of these out-of-state facilities for SED student placement for years, the State only recently has begun to question their nonprofit status. Nor has the State ever provided the County with a list of facilities that it deems to be nonprofit, and therefore acceptable to the State. The State's history of paying these costs without question encouraged the County to rely upon the State's acceptance of prior claims for the very same facilities now characterized as for-profit.⁸⁴

Although the claimant may have contracted with nonprofit entities, the evidence in the record supports the Controller's findings that the board and care and treatment services for the SED pupils were provided by out-of-state, *for-profit* entities.

The Controller found that the county claimed vendor costs for Aspen Solutions, Inc., and Mental Health Systems, Inc., California nonprofit entities. However, these nonprofit entities contracted with for-profit facilities where the out-of-state placements occurred (Youth Care of Utah and Charter Provo Canyon Schools) to provide the services. Copies of the contracts for the provision of mental health services to SED pupils between Aspen Solutions, Inc., and Youth Care of Utah, Inc. (Youth Care contract),⁸⁵ Mental Health Services, Inc. (MHS), and Charter Provo Canyon School, LLC (Provo Canyon contract),⁸⁶ and MHS, Inc., and UHS of Provo Canyon (Provo

⁸² Exhibit A, Incorrect Reduction Claim 11-9705-I-02, page 12; see also, Exhibit J, Claimant's Comments on the Draft Proposed Decision, pages 1-2.

⁸³ Exhibit A, Incorrect Reduction Claim 11-9705-I-02, pages 21, 24, and 26.

⁸⁴ Exhibit A, Incorrect Reduction Claim 11-9705-I-02, pages 12-13; Exhibit B, Incorrect Reduction Claim 12-9705-I-03, page 10.

⁸⁵ Exhibit D, Controller's Late Comments on IRC 11-9705-I-02, pages 100-108 (Tab 12, Contract between Aspen Solutions, Inc., and Youth Care of Utah, Inc.); Exhibit E, Controller's Late Comments on IRC 12-9705-I-03, pages 238-246 (Tab 14, Contract between Aspen Solutions, Inc., and Youth Care of Utah, Inc.).

⁸⁶ Exhibit D, Controller's Late Comments on IRC 11-9705-I-02, pages 110-120 (Tab 13, Contract between Mental Health Services, Inc. (MHS), and Charter Provo Canyon School, LLC); Exhibit E, Controller's Late Comments on IRC 12-9705-I-03, pages 248-258 (Tab 15, Contract between Mental Health Systems, Inc., and Charter Provo Canyon School, LLC).

Canyon II contract),⁸⁷ are in the record. These agreements demonstrate that the vendor payments to the nonprofit entities were for services provided by for-profit facilities. In the Youth Care contract, Youth Care of Utah, Inc., is described as a Delaware corporation and the contract states:

Youth has the sole responsibility for provision of therapeutic services.
ASI...shall not exercise control over or interfere in any way with the exercise of professional judgment by Youth or Youth's employees in connection with Youth's therapeutic services.⁸⁸

In the Provo Canyon contract, Charter Provo Canyon School, LLC is described as a Delaware for-profit limited liability contract and the contract states "Provo Canyon has agreed to provide the services of qualified professionals to provide care to those persons authorized to receive mental health services."⁸⁹

In the Provo Canyon II contract, UHS of Provo Canyon, Inc., is described as a Delaware for-profit limited liability company and the contract states "Provo Canyon has agreed to provide the services of qualified professionals to provide care to those persons authorized to receive mental health services."⁹⁰

The claimant similarly claimed that it had contractual agreements with Aspen Solutions, Inc., and Mental Health Systems, Inc., for placement of SED pupils in four other facilities: Aspen Ranch, Island View, SunHawk Academy, and Logan River, LLC. However, the claimant did not provide any documentation to support the nonprofit status of the facilities that provided the services, or show the business relationship between the facilities and the California nonprofits.⁹¹ Instead, claimant provided documentation titled "List of Providers for the Provision of Mental Health Outpatient Services for Fiscal Years 2002-03, 2003-04, and 2004-05" which lists: Aspen Ranch (For-Profit), Island View, and SunHawk under a bullet for Aspen Solutions, Inc., and

⁸⁷ Exhibit D, Controller's Late Comments on IRC 11-9705-I-02, pages 124-135 (Tab 14, Contract between MHS, Inc., and UHS of Provo Canyon, Inc.); Exhibit E, Controller's Late Comments on IRC 12-9705-I-03, pages 260-271 (Tab 16, Contract between MHS, Inc., and UHS of Provo Canyon, Inc.).

⁸⁸ Exhibit D, Controller's Late Comments on IRC 11-9705-I-01, page 100; Exhibit E, Controller's Late Comments on IRC 12-9705-I-03, page 238.

⁸⁹ Exhibit D, Controller's Late Comments on IRC 11-9705-I-02, page 110; Exhibit E, Controller's Late Comments on IRC 12-9705-I-03, page 248.

⁹⁰ Exhibit D, Controller's Late Comments on IRC 11-9705-I-02, page 124; Exhibit E, Controller's Late Comments on IRC 12-9705-I-03, page 260.

⁹¹ Exhibit D, Controller's Late Comments on IRC 11-9705-I-02, page 17; Exhibit E, Controller's Late Comments on IRC 12-9705-I-03, page 20.

Logan River in parenthesis next to Mental Health Systems, Inc.⁹² This documentation does not support the nonprofit status of the facilities providing the services.

The claimant also contracted with Kids Behavioral Health of Alaska, Inc., for placement of SED pupils in Copper Hills Youth Center in fiscal years 2005-2006 through 2008-2009. With respect to Kids Behavioral Health of Alaska, the claimant provided a Certificate of Good Standing from the State of Alaska and Certificate of Registration of a foreign nonprofit from the State of Utah.⁹³ However, the Certificate of Registration for nonprofit status was not approved until December 7, 2007. Moreover, no documentation has been provided by the claimant showing that Copper Hills Youth Center was organized and operated on a nonprofit basis.

And for one of the vendors claimed in fiscal years 2003-2004 and 2004-2005, National Deaf Academy, the Controller states that the claimant acknowledged that the facility is for-profit and did not provide any evidence in support of its nonprofit status.⁹⁴

Therefore 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.

2. Claimant's reliance on the decisions issued by OAH and the federal courts is misplaced.

The claimant further argues that decisions issued by the OAH and the United States District Court in *Riverside County Department of Mental Health v. Sullivan* support the position that reimbursement is required if a SED pupil is placed in a for-profit facility that complies with federal IDEA law.⁹⁵ These decisions involve 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

⁹² Exhibit D, Controller's Late Comments on IRC 11-9705-I-02, page 137 (Tab 15, "Exhibit A, List of Providers for the Provision of Mental Health Outpatient Services for Fiscal Years 2002-03, 2003-04, and 2004-05"); Exhibit E, Controller's Late Comments on IRC 12-9705-I-03, page 278 (Tab 18, "Exhibit A, List of Providers for the Provision of Mental Health Outpatient Services for Fiscal Years 2002-03, 2003-04, and 2004-05").

⁹³ Exhibit D, Controller's Late Comments on IRC 11-9705-I-02, pages 139 (Tab 16, Certificate of Good Standing from the State of Alaska) and 141 (Tab 17, Certificate of Registration, Corporation- Foreign- Non-Profit, State of Utah); Exhibit E, Controller's Late Comments on IRC 12-9705-I-03, pages 278 (Tab 19, Certificate of Good Standing from the State of Alaska) and 282 (Tab 20, Certificate of Registration, Corporation- Foreign- Non-Profit, State of Utah).

⁹⁴ Exhibit D, Controller's Late Comments on IRC 11-9705-I-02, page 17. The for-profit status of National Deaf Academy is confirmed in the OAH case relied on by claimant and submitted for decision in 2007 (Exhibit A, Incorrect Reduction Claim 11-9705-I-02, pages 29-38).

⁹⁵ Exhibit A, Incorrect Reduction Claim 11-9705-I-02, pages 10-11; Exhibit B, Incorrect Reduction Claim 12-9705-I-03, pages 12-13.

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. Both OAH and the federal District Court 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.⁹⁶ The 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.⁹⁷

Although the District Court's decision in *Riverside County* is binding with respect to the placement of that student,⁹⁸ the court did not address state-mandated reimbursement under article XIII B, section 6. Moreover, the claimant has provided no documentation or evidence that the costs claimed in these 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. Thus, the Commission does not need to reach the issue whether reimbursement under article XIII B, section 6 would be required in such a case.

The claimant also relies on the U.S. Supreme Court decision in *Florence County School District Four v. Carter*,⁹⁹ for the proposition that local government will be subject to increased litigation with the Controller's interpretation.¹⁰⁰ In the *Florence* case, the court held that parents can be reimbursed under the 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

⁹⁶ Exhibit A, Incorrect Reduction Claim 11-9705-I-02, pages 29-38, 40-52; Exhibit B, Incorrect Reduction Claim 12-9705-I-03, pages 27-36, 38-50.

⁹⁷ Exhibit A, Incorrect Reduction Claim 11-9705-I-02, pages 40-52; Exhibit B, Incorrect Reduction Claim 12-9705-I-03, pages 38-50.

⁹⁸ Absent "unusual circumstances," or an intervening change in the law, the decision of the reviewing court establishes the law of the case and binds the agency and the parties to the action in all further proceedings addressing the particular claim. (*George Arakelian Farms, Inc., v. Agricultural Labor Relations Board* (1989) 49 Cal.3d 1279, 1291.)

⁹⁹ *Florence County School District v. Carter* (1993) 510 U.S. 7.

¹⁰⁰ Exhibit A, Incorrect Reduction Claim 11-9705-I-02, page 13; Exhibit B, Incorrect Reduction Claim 12-9705-I-03, pages 13-14.

placement, rather than a proposed IEP, is proper under the Act.”¹⁰¹ Unlike the court’s equitable powers under IDEA, the reimbursement requirements of article XIII B, section 6, must be strictly construed and not applied as an “equitable remedy to cure the perceived unfairness resulting from political decisions on funding priorities.”¹⁰²

Therefore, these decisions do not support the claimant’s asserted 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 facilities organized and operated for-profit, is consistent with the Commission’s Parameters and Guidelines and is correct as a matter of law.

V. Conclusion

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

¹⁰¹ *Florence County School District, supra*, 510 U.S. 5, 12 (citing its prior decision in *School Comm. of Burlington v. Department of Ed. of Mass.* (1985) 471 U.S. 359, 369.)

¹⁰² *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).



RE: **Decision**

Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services,
11-9705-I-02

Government Code Section 7576, as amended by Statutes 1996, Chapter 654 (AB 2726);
California Code of Regulations, Title 2, Division 9, Chapter 1, Sections 60100 and 60110
Fiscal Years: 2001-2002, 2002-2003, 2003-2004, 2004-2005, and 2005-2006

And

Handicapped and Disabled Students; Handicapped and Disabled Students II; and
Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services,
12-9705-I-03

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 Orange, Claimant

On September 23, 2016, the foregoing Decision of the Commission on State Mandates was
adopted on the above-entitled matters.



Heather Halsey, Executive Director

Dated: September 28, 2016

BEFORE THE
COMMISSION ON STATE MANDATES
STATE OF CALIFORNIA

IN RE INCORRECT REDUCTION CLAIM
ON:

Former Education Code Section 72246
(Renumbered as 76355)¹

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, and 2005-2006

Foothill-DeAnza Community College District,
Claimant

Case No.: 09-4206-I-24 and 10-4206-I-34

Health Fee Elimination

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

(Adopted May 26, 2016)

(Served June 1, 2016)

DECISION

The Commission on State Mandates (Commission) heard and decided these consolidated incorrect reduction claims (IRCs) during a regularly scheduled hearing on May 26, 2016. Keith Petersen appeared on behalf of the Foothill-DeAnza Community College District. Jim Spano and Jim Venneman appeared on behalf of the State Controller's Office (Controller).

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

The Commission adopted the proposed decision to deny the IRC by a vote of five to zero, as follows:

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

¹ Statutes 1993, chapter 8.

Summary of the Findings

This analysis addresses these consolidated IRCs filed by Foothill-DeAnza 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 2005-2006 under the *Health Fee Elimination* program. Over the four fiscal years in question, reductions totaling \$284,615 were made based on understated offsetting health fees authorized to be collected and disallowed indirect costs.

The Commission finds that the audit was both timely initiated and timely completed in accordance with Government Code section 17558.5. Additionally, the Commission concludes that it does not have jurisdiction to consider the adjustments to indirect costs for fiscal year 2004-2005 that resulted in an increase to the reimbursement claim; and does not have jurisdiction to consider the 2005-2006 reimbursement claim in its entirety, because there is no reduction for that fiscal year. Furthermore, the Commission finds that reductions of indirect costs claimed for fiscal years 2002-2003 and 2003-2004, based on the claimant's failure to obtain federal approval for its indirect cost rate calculated pursuant to the federal OMB Circular A-21 method, and the Controller's recalculation of indirect costs using another method authorized by the parameters and guidelines and claiming instructions, were correct as a matter of law, and not arbitrary, capricious, or entirely lacking in evidentiary support. The Commission further finds that the reduction of costs based on understated offsetting health fee authority was correct as a matter of law, and not arbitrary, capricious, or entirely lacking in evidentiary support.²

Accordingly, the Commission denies these IRCs.

COMMISSION FINDINGS

I. Chronology

- | | |
|------------|---------------------------------------------------------------------------------------------|
| 09/11/2008 | The entrance conference for the audit of fiscal years 2002-2003 through 2005-2006 was held. |
| 02/06/2009 | Controller issued the draft audit report. ³ |
| 02/23/2009 | Claimant responded by letter to the draft audit report. ⁴ |
| 05/20/2009 | Controller issued the final audit report. ⁵ |
| 10/05/2009 | Claimant filed IRC 09-4206-I-24. ⁶ |

² The total net reduction for the audit period is only \$284,615, because understated indirect costs for fiscal years 2004-2005 and 2005-2006, as well as understated student insurance costs and understated salaries and benefits, were offset against the overstated indirect costs for fiscal years 2002-2003 and 2003-2004 and understated health fees for all four years.

³ Exhibit A, IRC 09-4206-I-24, page 75.

⁴ Exhibit A, IRC 09-4206-I-24, page 75.

⁵ Exhibit A, IRC 09-4206-I-24, page 52.

⁶ Exhibit A, IRC 09-4206-I-24, page 1.

08/18/2010 Controller issued the revised final audit report.⁷
11/22/2010 Claimant filed IRC 10-4206-I-34.⁸
12/02/2010 Commission staff issued a notice of complete filing, consolidation of 09-4206-I-24 and 10-4206-I-34, and request for comments.
12/02/2014 Controller filed late comments on the consolidated IRCs.⁹
02/10/2016 Commission staff issued the Draft Proposed Decision.¹⁰
02/12/2016 Controller filed comments on the Draft Proposed Decision.¹¹
03/01/2016 Claimant filed comments on the Draft Proposed Decision.¹²

II. Background

Health Fee Elimination Program

Prior to 1984, former Education Code section 72246 authorized community college districts that voluntarily provided health supervision and services, direct and indirect medical and hospitalization services, or operation of student health centers to charge almost all students a health service fee not to exceed \$7.50 for each semester or \$5 for each quarter or summer session, to fund these services.¹³ In 1984, the Legislature repealed the community colleges' fee authority for health services.¹⁴ However, the Legislature also reenacted section 72246, to become operative on January 1, 1988, in order to reauthorize the fee, at \$7.50 for each semester (or \$5 per quarter or summer session).¹⁵

In addition to temporarily repealing community college districts' authority to levy a health services fee, the 1984 enactment required any district that provided health services during the 1983-1984 fiscal year, for which districts were previously authorized to charge a fee, to maintain health services at the level provided during the 1983-1984 fiscal year for every subsequent fiscal year until January 1, 1988.¹⁶ As a result, community college districts were required to maintain

⁷ Exhibit B, IRC 10-4206-I-34, page 21.

⁸ Exhibit B, IRC 10-4206-I-34, page 1.

⁹ Exhibit C, Controller's Late Comments on IRC.

¹⁰ Exhibit D, Draft Proposed Decision.

¹¹ Exhibit E, Controller's Comments on the Draft Proposed Decision.

¹² Exhibit F, Claimant's Comments on the Draft Proposed Decision.

¹³ Former Education Code section 72246 (Stats. 1981, ch. 763) [Low-income students, students that depend upon prayer for healing, and students attending a college under an approved apprenticeship training program, were exempt from the fee.].

¹⁴ Statutes 1984, 2nd Extraordinary Session, chapter 1, section 4 [repealing Education Code section 72246].

¹⁵ Statutes 1984, 2nd Extraordinary Session, chapter 1, section 4.5.

¹⁶ Education Code section 72246.5 (Stats. 1984, 2d. Ex. Sess., ch. 1, § 4.7).

health services provided in the 1983-1984 fiscal year without any fee authority for this purpose until January 1, 1988.

In 1987, the Legislature amended former Education Code section 72246, operative January 1, 1988, to incorporate and extend the maintenance of effort provisions of former Education Code section 72246.5, which became inoperative by its own terms as of January 1, 1988.¹⁷ In addition, Statutes 1987, chapter 1118 restated that the fee would be reestablished at not more than \$7.50 for each semester, or \$5 for each quarter or summer session.¹⁸ As a result, beginning January 1, 1988 all community college districts were required to maintain the same level of health services they provided in the 1986-1987 fiscal year each year thereafter, with limited fee authority to offset the costs of those services. In 1992, section 72246 was amended to provide that the health fee could be increased by the same percentage as the Implicit Price Deflator whenever that calculation would produce an increase of one dollar.¹⁹

On November 20, 1986, the Commission determined that Statutes 1984, chapter 1 imposed a reimbursable state-mandated new program upon community college districts. On August 27, 1987, the Commission adopted parameters and guidelines for the *Health Fee Elimination* program. On May 25, 1989, the Commission amended the parameters and guidelines to reflect amendments made by Statutes 1987, chapter 1118.

The parameters and guidelines generally provide that eligible community college districts shall be reimbursed for the costs of providing a health services program, and that only services specified in the parameters and guidelines and provided by the community college in the 1986-1987 fiscal year may be claimed.

Controller's Audit and Summary of the Issues

These consolidated IRCs address two audit reports, the latter of which is stated by the Controller to supersede the former. The Commission finds that the revised audit was completed within the period of limitation and therefore may take jurisdiction over it.

The Controller's revised audit determined that the claimant understated direct costs for counseling-related services for the audit period in the amount of \$545,467, and related indirect cost of \$171,659 (Finding 1). The claimant does not dispute this finding.²⁰ In Finding 2, the Controller determined that the claimant understated student insurance premiums for the audit period by \$143,415, along with related indirect costs of \$43,881. The claimant does not dispute this finding.²¹ In Finding 3, the Controller determined that the claimant overstated its indirect costs for fiscal years 2002-2003 and 2003-2004, by a total of \$436,827. The Controller determined that the claimant applied the OMB methodology for calculating indirect costs but

¹⁷ Education Code section 72246 (as amended, Stats. 1987, ch. 1118). See also former Education Code section 72246.5 (Stats. 1984, 2d Ex. Sess., ch. 1, § 4.7).

¹⁸ Education Code section 72246 (as amended, Stats. 1987, ch. 1118).

¹⁹ Education Code section 72246 (as amended, Stats. 1992, ch. 753). In 1993, former Education Code section 72246, was renumbered as Education Code section 76355. (Stats. 1993, ch. 8.)

²⁰ Exhibit B, IRC 10-4206-I-34, page 30.

²¹ Exhibit B, IRC 10-4206-I-34, page 31.

failed to obtain federal approval for its calculated rates.²² For fiscal years 2004-2005 and 2005-2006, the Controller determined that the claimant used the state methodology (FAM 29-C), but did not correctly allocate direct and indirect costs, resulting in an understatement of \$195,796.²³ The claimant challenged the Controller's methodology for recalculating indirect costs generally, but later stated that it does not dispute the findings for fiscal years 2004-2005 and 2005-2006.²⁴ In Finding 4, the Controller found that the claimant understated offsetting health service fee authority, resulting in a reduction of \$716,795 for the audit period.²⁵ In Finding 5, the Controller found that the claimant understated offsetting savings or reimbursements by \$116,597 for the audit period.²⁶

The Controller reduced the costs claimed for fiscal years 2002-2003 through 2005-2006 under the *Health Fee Elimination* program, totaling \$284,615, based on the net of overstatements and understatements. The following issues are in dispute:

- The period of limitation applicable to audits by the Controller.
- The Controller's determination not to reimburse costs recalculated in the claimant's favor because the increase exceeded the amount claimed for that fiscal year;
- Reduction of indirect costs based on asserted faults in the development and application of indirect cost rates; and
- The amount of offsetting revenue to be applied from health service fee authority.

III. Positions of the Parties

Foothill-DeAnza Community College District

The claimant does not dispute the Controller's findings that the claimant understated counseling-related salaries and benefits, and student insurance costs for the audit period, resulting in a net increase in reimbursement of \$688,882 plus \$215,540 in related indirect costs (Findings 1 and 2).²⁷ However, the claimant disputes the Controller's reduction of \$511,782 in indirect costs (reduced in the revised audit report to \$241,031), on the ground that indirect costs were not correctly calculated consistently with the claiming instructions. The claimant argues that the claiming instructions are not enforceable, and that federal approval for the OMB-developed rates for fiscal years 2002-2003 and 2003-2004 is therefore not required.²⁸ With respect to the *understated* indirect cost rates in fiscal years 2004-2005 and 2005-2006, the claimant states that

²² Exhibit B, IRC 10-4206-I-34, page 32.

²³ Exhibit B, IRC 10-4206-I-34, page 32.

²⁴ Exhibit F, Claimant's Comments on the Draft Proposed Decision, page 4.

²⁵ Exhibit B, IRC 10-4206-I-34, page 35.

²⁶ Exhibit B, IRC 10-4206-I-34, page 40.

²⁷ Exhibit A, IRC 09-4206-I-24, pages 10; 60-61.

²⁸ Exhibit A, IRC 09-4206-I-24, pages 11-14; Exhibit F, Claimant's Comments on the Draft Proposed Decision, pages 4-8.

the Controller's method is reasonable, and it no longer disputes the audited rates.²⁹ However, the claimant argues that for fiscal year 2005-2006, in which the total of all adjustments resulted in a *net increase* in allowable costs, but which the Controller reimbursed only to the extent of the total claim, and no further, the Controller was required to reimburse the "\$114,614 disallowed as excess."³⁰ The claimant argues that "[t]o not reimburse the excess is to not reimburse the sum total of the audit and Commission findings."³¹ And, in the claimant's response to the Draft Proposed Decision, the claimant no longer disputes the Controller's finding that the claimant understated authorized offsetting health fee authority, required to be deducted, by \$716,795 for the audit period.³²

Finally, the claimant argues that the Controller's audit of reimbursement claims for fiscal years 2002-2003 and 2003-2004 was not timely; that the period of limitation for these claims expired on January 12, 2008, based on the filing date of January 12, 2005,³³ but the audit entrance conference did not occur until September 11, 2008.³⁴ Although the audit report states that the audit was timely because initial payment on the claims did not occur until October 25, 2006, the claimant argues that this alternative time period, as authorized in Government Code section 17558.5, is impermissibly vague, and is contrary to the purpose of a statute of limitations.³⁵

State Controller's Office

The Controller determined that the claimant understated counseling-related salaries and benefits for the audit period, plus related indirect costs, resulting in a net increase of \$717,126.³⁶ In addition, the Controller determined that the claimant understated allowable student insurance costs, plus related indirect costs, totaling \$187,296 for the audit period.³⁷ The Controller offset these increases in direct costs against authorized health fee revenues that were greater than what was claimed, except in the 2005-2006 fiscal year, in which the total of all adjustments resulted in a net increase in allowable costs, which the Controller reimbursed only to the extent of the total amount claimed for that year. The Controller denied reimbursement for \$114,614 in calculated allowable costs for fiscal year 2005-2006 because that amount exceeded the amount claimed.³⁸

²⁹ Exhibit F, Claimant's Comments on the Draft Proposed Decision, page 4.

³⁰ Exhibit F, Claimant's Comments on the Draft Proposed Decision, pages 10-11.

³¹ Exhibit F, Claimant's Comments on the Draft Proposed Decision, pages 10-11.

³² See Exhibit A, IRC 09-4206-I-24, pages 10-18; 63-70; Exhibit F, Claimant's Comments on the Draft Proposed Decision, page 10.

³³ Exhibit A, IRC 09-4206-I-24, pages 18-19 (Note that the 2002-2003 and 2003-2004 claims were filed at the same time).

³⁴ Exhibit A, IRC 09-4206-I-24, page 18.

³⁵ Exhibit A, IRC 09-4206-I-24, pages 18-21; Exhibit F, Claimant's Comments on the Draft Proposed Decision, page 2.

³⁶ Exhibit A, IRC 09-4206-I-24, page 61.

³⁷ Exhibit A, IRC 09-4206-I-24, page 62.

³⁸ Exhibit B, IRC 10-4206-I-34, page 28.

The Controller further asserted that the claimant overstated its indirect costs for fiscal years 2002-2003 and 2003-2004, finding that the claimant did not obtain federal approval for its indirect cost rate developed pursuant to OMB Circular A-21 guidelines, totaling \$436,827. And, the Controller found that the claimant understated its indirect costs for fiscal years 2004-2005 and 2005-2006, based on recalculation pursuant to the Controller's FAM-29C method, including allowable depreciation expenses that were excluded in the prior years. This resulted in an increase of \$195,796.³⁹

The Controller also found that the claimant understated its authorized health service fees for the audit period by \$716,795. Using enrollment and exemption data obtained from the California Community Colleges Chancellor's Office, the Controller recalculated the health fees that the claimant was authorized to collect, and reduced the claim by the amount not stated as offsetting revenues.⁴⁰ The Controller states: "We agree that community college districts may choose not to levy a health service fee or to levy a fee less than the authorized amount...[but] Education Code section 76355, subdivision (a) provides districts the *authority* to levy the fee."⁴¹ The Controller concludes that: "To the extent that districts have authority to charge a fee, they are not required to incur a cost."⁴² This finding is unchanged in the revised audit report.⁴³

The Controller stated in comments on the Draft Proposed Decision that it supports the Commission's decision with respect to the timeliness of the audit of the 2002-2003 and 2003-2004 reimbursement claims. The Controller also agrees with the proposed findings on the substantive issues.⁴⁴

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 the local agency or school district. If the Commission determines that a reimbursement claim has been incorrectly reduced, section 1185.9 of the Commission's regulations requires the Commission to send the decision to the Controller and request that the costs that were incorrectly reduced 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

³⁹ Exhibit B, IRC 10-4206-I-34, page 32.

⁴⁰ Exhibit A, IRC 09-4206-I-24, page 66.

⁴¹ Exhibit A, IRC 09-4206-I-24, page 69.

⁴² Exhibit A, IRC 09-4206-I-24, page 70.

⁴³ Exhibit B, IRC 10-4206-I-34, pages 35-39.

⁴⁴ Exhibit E, Controller's Comments on the Draft Proposed Decision.

over the existence of state-mandated programs within the meaning of article XIII B, section 6.⁴⁵ 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.”⁴⁶

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.⁴⁷ Under this standard, the courts have found that:

When reviewing the exercise of discretion, “[t]he scope of review is limited, out of deference to the agency’s authority and presumed expertise: ‘The court may not reweigh the evidence or substitute its judgment for that of the agency. [Citation.]’” ... “In general ... the inquiry is limited to whether the decision was arbitrary, capricious, or entirely lacking in evidentiary support. . . .” [Citations.] When making that inquiry, the “ ‘court must ensure that an agency has adequately considered all relevant factors, and has demonstrated a rational connection between those factors, the choice made, and the purposes of the enabling statute.’” [Citation.]”⁴⁸

The Commission must review the Controller’s audit in light of the fact that the initial burden of providing evidence for a claim of reimbursement lies with the claimant.⁴⁹ In addition, sections 1185.1(f)(3) and 1185.2(c) of the Commission’s regulations require that any assertions of fact by the parties to an IRC must be supported by documentary evidence. The Commission’s ultimate findings of fact must be supported by substantial evidence in the record.⁵⁰

A. The Audit Was Timely Initiated and Timely Completed Pursuant to Government Code Section 17558.5.

⁴⁵ *Kinlaw v. State of California* (1991) 54 Cal.3d 326, 331-334; Government Code sections 17551, 17552.

⁴⁶ *County of Sonoma v. Commission on State Mandates* (2000) 84 Cal.App.4th 1264, 1280, citing *City of San Jose v. State of California* (1996) 45 Cal.App.4th 1802, 1817.

⁴⁷ *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.

⁴⁸ *American Bd. of Cosmetic Surgery, Inc. v. Medical Bd. of California* (2008) 162 Cal.App.4th 534, 547-548.

⁴⁹ *Gilbert v. City of Sunnyvale* (2005) 130 Cal.App.4th 1264, 1274-1275.

⁵⁰ 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 claimant argues that the Controller did not timely conduct the audit pursuant to Government Code section 17558.5. Section 17558.5, as applicable to the claim years here at issue, requires a valid audit to be initiated no later than three years after the date that the reimbursement claim is filed or last amended. However, the section also provides that *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 time for the Controller to initiate an audit shall commence to run from the date of initial payment of the claim.”⁵¹ “In any case,” section 17558.5 requires the audit to be completed no later than two years after it is commenced.⁵²

1. The Audit Was Timely Initiated Pursuant to Government Code Section 17558.5.

The claimant asserts that the audit of the 2002-2003 and 2003-2004 claim years was not timely initiated, based on the date that the claims were “filed or last amended” (January 12, 2005), and the date that the audit entrance conference took place (September 11, 2008). However, the Controller points out that the fiscal year 2002-2003 claim was not paid until October 25, 2006, and that therefore section 17558.5 provides for a timely audit to be initiated as late as October 25, 2009.⁵³

Government Code section 17558.5 states that “[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” However, if funds are not appropriated or no payment is made to the claimant for a given year, section 17558.5 states the “time for the Controller to initiate an audit shall commence to run from the date of initial payment of the claim.”⁵⁴

The claimant argues that this provision “is void because it is impermissibly vague,”⁵⁵ and that “the only specific and enforceable time limitation to commence an audit is three years from the

⁵¹ Government Code section 17558.5 (as amended, Stats. 2002, ch. 1128 (AB 2834)).

⁵² Government Code section 17558.5 (as amended, Stats. 2004, ch. 890 (AB 2856)).

⁵³ Government Code section 17558.5 (as amended, Statutes 2004, ch. 890 (AB 2856)). Neither the filing date of the subject reimbursement claims, nor the date the audit was commenced, controls whether the later-amended version(s) of section 17558.5 are applicable. See *Scheas v. Robertson* (1951) 38 Cal.2d 119, 126 [“It is settled that the Legislature may enact a statute of limitations ‘applicable to existing causes of action or shorten a former limitation period...’”]; *California Employment Stabilization Commission v. Payne* (1947) 31 Cal.2d 210, 215 [“...the power of the Legislature to lessen a statute of limitations is subject to the restriction that an existing right cannot be cut off summarily without giving a reasonable time after the act becomes effective to exercise such right. [citation] This principle, however, does not apply where the state gives up a right previously possessed by it or by one of its agencies. Except where such an agency is given powers by the Constitution, it derives its authority from the Legislature, which may add to or take away from those powers and therefore a statute which adversely affects only the right of the state is not invalid merely because it operates to cut off an existing remedy of an agency of the state.”].

⁵⁴ Government Code section 17558.5 (as amended, Stats. 2002, ch. 1128 (AB 2834)).

⁵⁵ Exhibit A, IRC 09-4206-I-24, page 21.

date the claim was filed.” The claimant argues that “the annual reimbursement claims for FY 2002-03 and FY 2003-04 were past this time period when the audit was commenced on September 11, 2008.”⁵⁶

But article III, section 3.5 of the California Constitution states that an administrative agency has no power “[t]o declare a statute unenforceable, or refuse to enforce a statute, on the basis of it being unconstitutional unless an appellate court has made a determination that such statute is unconstitutional...”⁵⁷ Here, the fiscal year 2002-2003 reimbursement claim was amended on or about January 12, 2004,⁵⁸ but was not paid, based on the evidence in the record, until October 25, 2006.⁵⁹ Therefore, the time to initiate an audit, in this case, commenced to run from October 25, 2006, and an audit initiated before October 25, 2009 would be timely.

Based on the evidence in the record, the Commission finds that the audit in issue was initiated no later than September 11, 2008, the date of the entrance conference, and the audit was therefore timely initiated.

2. The Audit Was Timely Completed.

Government Code section 17558.5 also prescribes the time in which an audit must be completed: “In any case, an audit shall be completed not later than two years after the date that the audit is commenced.”⁶⁰ Based on the evidence in the record, the audit in issue was initiated no later than September 11, 2008, the date of the entrance conference.⁶¹ And here, there are two final audit reports in the record that identify and explain the adjustments in accordance with Government Code section 17558.5(c).⁶² The first audit report was issued May 20, 2009, well within two

⁵⁶ Exhibit A, IRC 09-4206-I-24, page 21; Exhibit F, Claimant’s Comments on the Draft Proposed Decision, pages 2-3.

⁵⁷ California Constitution, article III, section 3.5 (added June 6, 1978, by Proposition 5).

⁵⁸ The Controller’s final audit report states that the amended claim was received on January 13, 2004, but the claimant states that it was mailed on January 12, 2004. Whether the filing date for purposes of annual reimbursement claims is measured upon receipt or upon dispatch is not necessary to resolve the period of limitation issue in this claim. (Exhibit A, IRC 09-4206-I-24, page 72.)

⁵⁹ Exhibit A, IRC 09-4206-I-24, pages 19; 72.

⁶⁰ Government Code section 17558.5 (Stats. 2004, ch. 890).

⁶¹ Exhibit A, IRC 09-4206-I-24, pages 18; 72.

⁶² Government Code section 17558.5(c) states the following:

The Controller shall notify the claimant in writing within 30 days after issuance of a remittance advice 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 or school district, and the reason for the adjustment. Remittance advices and other notices of payment actions shall not constitute notice of adjustment from an audit or review.

years of the entrance conference;⁶³ the second was issued August 18, 2010, also prior to the expiration of the two year period beginning September 11, 2008.

Based on the foregoing, the Commission finds that both the first final audit report and the revised final audit report were timely completed in accordance with Government Code section 17558.5.

B. The Commission Does Not Have Jurisdiction Over the Indirect Cost Rates Calculated by the Controller for Fiscal Year 2004-2005 and the Adjustments of Direct and Indirect Costs for Fiscal Year 2005-2006 Because There Has Been No Reduction of Costs.

1. There Is No Reduction of Indirect Costs Claimed for Fiscal Year 2004-2005, and the Claimant No Longer Disputes the Audited Rate Calculated by the Controller for This Fiscal Year.

For fiscal year 2004-2005, the Controller's revised audit recalculated indirect costs including allowable depreciation expenses in accordance with the claiming instructions, resulting in an adjustment of \$92,881 in the claimant's favor.⁶⁴

The claimant generally challenges the enforceability of the Controller's claiming instructions with respect to indirect cost claiming in both its response to the draft audit report and its IRC narrative, and with respect to all years of the audit period. However, for fiscal year 2004-2005, the revised audit found a net increase, rather than a reduction, in indirect costs.⁶⁵ More importantly, the claimant no longer disputes the audited rate.⁶⁶ Accordingly, the Commission does not have jurisdiction and makes no findings with respect to the indirect cost rate for fiscal year 2004-2005.

2. There Is No Reduction of Direct and Related Indirect Costs Claimed for Fiscal Year 2005-2006.

The Controller found understated direct and indirect costs throughout the audit period, and adjusted the costs claimed in the claimant's favor, as appropriate. However, for fiscal year 2005-2006, the total amount adjusted in the claimant's favor exceeded the amount originally claimed, even after applying offsetting health service fees and offsetting savings or reimbursements.⁶⁷ Therefore, for fiscal year 2005-2006, the Controller adjusted direct and indirect costs in the claimant's favor to the full extent of the amount claimed, but no further.

The claimant, however, seeks reimbursement for the understated direct and related indirect costs determined by the Controller that exceed the amounts claimed. In this respect, the claimant asserts the Controller "incorrectly reduced allowable costs by \$114,614 for FY 2005-06 by reducing the 'total program costs' by this amount because it is in 'excess' of the total amount

⁶³ Exhibit A, IRC 09-4206-I-24, page 52.

⁶⁴ Exhibit B, IRC 10-4206-I-34, page 32.

⁶⁵ Exhibit B, IRC 10-4206-I-34, page 32.

⁶⁶ Exhibit B, IRC 10-4206-I-34, page 9; Exhibit F, Claimant's Comments on the Draft Proposed Decision, page 4.

⁶⁷ Exhibit B, IRC 10-4206-I-34, page 28.

claimed.”⁶⁸ The claimant states “[t]his reduction was not an audit ‘finding’ by the Controller, it is just a mathematical computation that is a result of other audit findings.” The claimant states that the audit report relies on Government Code section 17568, which provides “[i]n no case shall a reimbursement claim be paid that is submitted more than one year after the deadline specified in Section 17560.” The claimant continues:

The State did not pay these claims in full or in part within one year of the filing deadline, and rarely does so, so that citation does not appear relevant. Section 17568 pertains to the timely filing of an annual claim in order to be eligible for payment, not to the amount of ultimate payment or the contents of the claim itself.⁶⁹

The claimant reasons that “[t]he issue to be adjudicated is that the FY 2005-06 claim has been reduced by \$114,614 without a legal basis...” and that “[t]o not reimburse the excess is to not reimburse the sum total of the audit and Commission findings.”⁷⁰ Finally, the claimant concludes that Government Code section 17561 requires the Controller to adjust both underpayments and overpayments, and “the Controller does not have discretion to unilaterally determine that it will require reimbursement for audit adjustments in favor of the State and simply ignore audit adjustments in favor of the claimants.”⁷¹

However, the Controller adjusted the claim for fiscal year 2005-2006 *in the claimant’s favor*, and to the full extent of the total claim for the fiscal year. Thus, there is no reduction of costs claimed for fiscal year 2005-2006. Government Code sections 17551(d) and 17558.7 only authorize the Commission to hear and decide incorrect *reduction* claims. The Commission does not have jurisdiction over a reimbursement claim that results in no reduction of costs. Thus, the Commission does not have jurisdiction and makes no findings with respect to the 2005-2006 reimbursement claim.

C. The Controller’s Reduction of Indirect Costs Claimed for Fiscal Years 2002-2003 and 2003-2004 Is Correct as a Matter of Law, and Not Arbitrary, Capricious, or Entirely Lacking in Evidentiary Support.

For fiscal years 2002-2003 and 2003-2004, the claimant claimed indirect costs based on a rate calculated pursuant to the OMB Circular A-21 method, which was authorized under the claiming instructions at that time. However, the Controller found that the claimant did not obtain federal approval for its claimed rate, which is required by the OMB Circular. The Controller therefore reduced the indirect costs and recalculated the rate based on the state FAM-29C method, using data available from the claimant’s annual financial and budget reporting to the Chancellor’s Office on the CCFS-311.

The claimant disputes the enforceability of the claiming instructions as a whole, arguing that “[n]either state law nor the parameters and guidelines make compliance with the Controller’s

⁶⁸ Exhibit B, IRC 10-4206-I-34, page 7.

⁶⁹ Exhibit F, Claimant’s Comments on the Draft Proposed Decision, page 10.

⁷⁰ Exhibit F, Claimant’s Comments on the Draft Proposed Decision, pages 10-11.

⁷¹ Exhibit F, Claimant’s Comments on the Draft Proposed Decision, page 12.

claiming instructions a condition of reimbursement.”⁷² And, the claimant asserts that the Controller has not made a determination that the claimed indirect cost rates were either excessive or unreasonable, and that the only available audit standard requires such a determination.⁷³ The claimant further argues that “there is no reason to obtain federal approval [of claimed indirect cost rates] if the claiming instructions are not enforceable.”⁷⁴

Based on the analysis herein, the Commission finds that the Controller’s reduction of indirect costs for fiscal years 2002-2003 and 2003-2004 on the basis of the claimant’s failure to obtain federal approval for indirect cost rates developed in accordance with the OMB Circular A-21 method is correct as a matter of law, and recalculation in accordance with the FAM-29C methodology described in the claiming instructions was not arbitrary, capricious, or entirely lacking in evidentiary support.

1. If a Claimant Chooses to Claim Indirect Costs Using the Federal OMB Circular A-21 Method, the Claimant Must Obtain Federal Approval for the Claimed Indirect Cost Rates.

The parameters and guidelines adopted for this program, in addition to identifying the reimbursable activities, provide instructions for eligible claimants to prepare reimbursement claims for the direct and indirect costs of the program.⁷⁵ The Commission’s adoption of parameters and guidelines is quasi-judicial and, therefore, the parameters and guidelines are final and binding on the parties unless set aside by a court pursuant to Government Code section 17559 or amended by the filing of a request pursuant to Government Code section 17557.⁷⁶ In this case, the parameters and guidelines for the *Health Fee Elimination* program have not been challenged, and no party has requested they be amended. The parameters and guidelines are therefore binding and must be applied to the reimbursement claims here.

Section VI. of the parameters and guidelines provide that “*indirect costs may be claimed in the manner described by the State Controller in his claiming instructions.*”⁷⁷ Claimant argues that the word “may” in the indirect cost language of the parameters and guidelines is permissive, and that therefore the parameters and guidelines do not require that indirect costs be claimed in the manner described by the Controller.⁷⁸

⁷² Exhibit A, IRC 09-4206-I-24, page 14.

⁷³ *Ibid.*

⁷⁴ Exhibit F, Claimant’s Comments on the Draft Proposed Decision, page 8.

⁷⁵ Government Code section 17557; California Code of Regulations, title 2, section 1183.7.

⁷⁶ *California School Boards Assoc. v. State of California* (2009) 171 Cal.App.4th 1183, 1200, which stated the following: “[U]nless a party to a quasi-judicial proceeding challenges the agency’s adverse findings made in that proceeding, by means of a mandate action in superior court, those findings are binding in later civil actions.” [Citation omitted.] See also, Government Code section 17557.

⁷⁷ Exhibit A, IRC 09-4206-I-24, page 35.

⁷⁸ Exhibit A, IRC 09-4206-I-24, page 11.

Claimant's argument is unsound: the parameters and guidelines plainly state that "indirect costs may be claimed in the manner described by the State Controller in his claiming instructions." The interpretation that is consistent with the plain language of the parameters and guidelines is that "indirect costs may be claimed," or may not, but if a claimant chooses to claim indirect costs, the claimant must adhere to the parameters and guidelines and claim indirect costs in the manner described in the Controller's claiming instructions.

The claiming instructions specific to the *Health Fee Elimination* mandate, are found in the Controller's Mandated Cost Manual which is revised each year and contains claiming instructions applicable to all community college mandated programs. The cost manual issued by the Controller's Office in September 2003 governs the reimbursement claim filed for fiscal year 2002-2003.⁷⁹ This cost manual provides two options for claiming indirect costs:

A college has the option of using a federally approved rate, utilizing the cost accounting principles from *Office of Management and Budget Circular A-21* "Cost Principles for Educational Institutions," or the Controller's methodology outlined in the following paragraphs. If the federal rate is used, it must be from the same fiscal year in which the costs were incurred.

The Controller allows the following methodology for use by community colleges in computing an indirect cost rate for state mandates. The objective of this computation is to determine an equitable rate for use in allocating administrative support to personnel that performed the mandated cost activities claimed by the community college. This methodology assumes that administrative services are provided to all activities of the institution in relation to the direct costs incurred in the performance of those activities. *Form FAM-29C* has been developed to assist the community college in computing an indirect cost rate for state mandates. . . .

[¶]

The [FAM-29C] computation is based on total expenditures as reported in "California Community Colleges Annual Financial and Budget Report, Expenditures by Activity (CCFS-311)." Expenditures classified by activity are segregated by the function they serve. Each function may include expenses for salaries, fringe benefits, supplies, and capital outlay. OMB Circular A-21 requires expenditures for capital outlays to be excluded from the indirect cost rate computation.

Generally, a direct cost is one incurred specifically for one activity, while indirect costs are of a more general nature and are incurred for the benefit of several activities. As previously noted, the objective of this computation is to equitably allocate administrative support costs to personnel that perform mandated cost activities claimed by the college. For the purpose of this computation we have defined indirect costs to be those costs which provide administrative support to personnel who perform mandated cost activities. We have defined direct costs to be those indirect costs that do not provide administrative support to personnel who perform mandated costs activities and those costs that are directly related to

⁷⁹ Exhibit G, School Mandated Cost Manual excerpt, 2002-2003.

instructional activities of the college. Accounts that should be classified as indirect costs are: Planning and Policy Making, Fiscal Operations, General Administrative Services, and Logistical Services. If any costs included in these accounts are claimed as a mandated cost, i.e., salaries of employee performing mandated cost activities, the cost should be reclassified as a direct cost. Accounts in the following groups of accounts should be classified as direct costs: Instruction, Instructional Administration, Instructional Support Services, Admissions and Records, Counseling and Guidance, Other Student Services, Operation and Maintenance of Plant, Community Relations, Staff Services, Non-instructional Staff-Retirees' Benefits and Retirement Incentives, Community Services, Ancillary Services and Auxiliary Operations. A college may classify a portion of the expenses reported in the account Operation and Maintenance of Plant as indirect. The claimant has the option of using a 7% or a higher expense percentage is allowable if the college can support its allocation basis.

The rate, derived by determining the ratio of total indirect expenses and total direct expenses when applied to the direct costs claimed, will result in an equitable distribution of the college's mandate related indirect costs. . . .⁸⁰

The claiming instructions for fiscal year 2003-2004 were substantially similar.⁸¹

If a claimant chooses to use the OMB Circular A-21 methodology, claimant must obtain federal approval for the rate calculated through formal negotiation, an informal correspondence process or a simplified method which sets the indirect cost rate using a salaries and wage base.⁸² The end result of the negotiation process is a sponsored agreement in which final approval lies with the federal government negotiating the rate and must be supported by "adequate documentation to support costs charged to sponsored agreements."⁸³ The OMB Circular A-21 establishes principles for determining costs applicable to grants, contracts, and other agreements between the federal government and educational institutions. Section G(11) of the OMB Circular A-21 governs the determination of indirect cost rates and requires the federal approval of a proposed rate by the "cognizant federal agency," which is normally either the federal Department of Health and Human Services or the Department of Defense's Office of Naval Research.⁸⁴ Thus, a claimant that has received federal approval for their indirect cost rate has negotiated specific direct costs with the relevant federal approving agency.

Here, claimant did not negotiate a particular rate, but applied the general principles of the OMB Circular A-21 to direct costs it determined to be applicable. Claimant used the methodology in the OMB Circular A-21 for fiscal years 2002-2003 and 2003-2004, and asserts that its indirect cost rates are more consistent from year to year, and that the Controller has the burden to show that the rates were excessive or unreasonable, "not to recalculate the rate according to its

⁸⁰ Exhibit G, Community Colleges Mandated Cost Manual, issued September 2003.

⁸¹ Exhibit G, Community Colleges Mandated Cost Manual, issued February 2005.

⁸² Exhibit G, OMB Circular A-21, pages 37-39.

⁸³ Exhibit G, OMB Circular A-21, page 6.

⁸⁴ Exhibit G, OMB Circular A-21.

unenforceable ministerial preferences.”⁸⁵ That assertion is in essence a challenge to the Controller’s entire claiming instructions as an underground regulation adopted without complying with the APA.

However, the Commission does not need to reach the alleged underground regulation issue for the use of the FAM-29C because the claimant failed to obtain federal approval for its use of the OMB Circular A-21 methodology as required by the OMB Circular A-21 itself.

As claimant did not negotiate with a federal agency to determine appropriate direct costs used to calculate the indirect costs rate, it cannot be determined whether the claimed rates would have received federal approval. Moreover, federal approval is clearly required by both the claiming instructions and the OMB methodology itself, but the Controller has no power to grant federal approval for an OMB-calculated rate.

The claimant asserts that this reasoning is “circular and outcome-driven,” and that “there is no reason to obtain federal approval if the claiming instructions are not enforceable.”⁸⁶ However, as the above discussion illustrates, the OMB method requires federal approval by its own terms. Thus, the claimant has not complied with the terms of the OMB methodology itself, and therefore the reduction of costs for failure to obtain federal approval is correct as a matter of law, and not arbitrary, capricious, or entirely lacking in evidentiary support.

2. The Controller’s Recalculation of Indirect Costs Is Not Arbitrary, Capricious, or Entirely Lacking in Evidentiary Support.

Here, instead of reducing indirect costs to \$0, the Controller recalculated claimant’s indirect cost rate by using its own Form FAM-29C, a method of calculating indirect costs that the Controller has included in its claiming instructions for many years, and which has been incorporated into parameters and guidelines for several state-mandated programs.

The claiming instructions provide:

Form FAM-29C has been developed to assist the community college in computing an indirect cost rate for state mandates. Completion of this form consists of three main steps:

1. The elimination of unallowable costs from the expenses reported on the financial statements.
2. The segregation of the adjusted expenses between those incurred for direct and indirect activities.
3. The development of a ratio between the total indirect expenses and the total direct expenses incurred by the community college.

The computation is based on total expenditures as reported in "California Community Colleges Annual Financial and Budget Report, Expenditures by Activity (CCFS-311)." Expenditures classified by activity are segregated by the function they serve. Each function may include expenses for salaries, fringe

⁸⁵ Exhibit B, IRC 10-4206-I-34, page 8; Exhibit A, IRC 09-4206-I-24, page 12.

⁸⁶ Exhibit F, Claimant’s Comments on the Draft Proposed Decision, page 8.

benefits, supplies, and capital outlay. OMB Circular A-21 requires expenditures for capital outlays to be excluded from the indirect cost rate computation.

Generally, a direct cost is one incurred specifically for one activity, while indirect costs are of a more general nature and are incurred for the benefit of several activities. As previously noted, the objective of this computation is to equitably allocate administrative support costs to personnel that perform mandated cost activities claimed by the college. For the purpose of this computation we have defined indirect costs to be those costs which provide administrative support to personnel who perform mandated cost activities. We have defined direct costs to be those costs that do not provide administrative support to personnel who perform mandated cost activities and those costs that are directly related to instructional activities of the college.⁸⁷

Thus, the calculation of indirect costs under Form FAM-29C are similar to the calculation under OMB Circular A-21, but not identical. However, because the OMB method is intended to be negotiated with and approved by either the federal Department of Health and Human Services or the Department of Defense's Office of Naval Research,⁸⁸ the Controller is not in a position to unilaterally recalculate and approve indirect costs under the OMB Circular A-21 method.

As previously stated, the standard of review which the Commission employs to review the Controller's audit provides that the Commission may "not reweigh the evidence or substitute its judgment for that of the agency."⁸⁹ Thus, the Commission cannot compel the Controller to use other auditing procedures in place of the Form FAM-29C and there is no evidence that the Controller's recalculation of indirect costs was arbitrary, capricious, or entirely lacking in evidentiary support.

Accordingly, the Commission finds the reduction of indirect costs for fiscal years 2002-2003 and 2003-2004, and recalculation by the FAM-29C method, is correct as a matter of law, and not arbitrary, capricious, or entirely lacking in evidentiary support.

D. The Controller's Reduction for Understated Offsetting Revenues Is Correct as a Matter of Law.

The Controller determined that the claimant understated its authorized health fee revenues by \$716,795 over the four fiscal years at issue.⁹⁰ These reductions were made on the basis of the fee authority available to claimant, multiplied by the number of students subject to the fee, less the amount of offsetting revenue claimed. The plain language of Education Code section 76355 provides authority to collect health fees for all students except those who depend exclusively on prayer for healing, those attending a community college under an approved apprenticeship

⁸⁷ Exhibit G, Excerpt from Community Colleges Mandated Cost Manual, issued September, 2003.

⁸⁸ Exhibit G, OMB Circular A-21.

⁸⁹ *American Bd. of Cosmetic Surgery, Inc. v. Medical Board of California* (2008) 162 Cal.App.4th 534, 547-548.

⁹⁰ Exhibit A, IRC 09-4206-I-24, page 66.

training program, or those who demonstrate financial need.⁹¹ For the audit period, the authorized fee amounts identified by the Chancellor ranged from \$9 per student to \$11 per student. The Controller states that it “obtained student enrollment and Board of Governors Grant (BOGG) recipient data from the CCCCCO” and identified exempt students based on the information available, and multiplied those enrollment data by the authorized fee amounts for each semester during the audit period.⁹²

Claimant disputes the reduction, arguing that the relevant Education Code provisions permit, but do not require, a community college district to levy a health services fee, and that the parameters and guidelines require a community college district to deduct from its reimbursement claims “[a]ny offsetting savings that the claimant *experiences* as a direct result of this statute...” Claimant argues that “[s]tudent fees *actually collected* must be used to offset costs, but not student fees that could have been collected and were not...”⁹³

The Commission finds that the correct calculation and application of offsetting revenue from student health fees has been resolved by the *Clovis Unified* decision,⁹⁴ and that a reduction to the extent of fee revenue *authorized*, rather than fee revenue collectible as a practical matter, is correct as a matter of law.

After the claimant filed IRC 09-4206-I-24, the Third District Court of Appeal issued its opinion in *Clovis Unified*, which specifically addressed the Controller’s practice of reducing claims of community college districts by the maximum fee amount that districts are statutorily authorized to charge students, whether or not a district chooses to charge its students those fees. As cited by the court, the Health Fee Rule states in pertinent part:

Eligible claimants will be reimbursed for health service costs at the level of service provided in the 1986/87 fiscal year. The reimbursement will be reduced by the amount of student health fees authorized per the Education Code [section] 76355.⁹⁵ (Underline in original.)

The Health Fee Rule relies on Education Code section 76355(a), which provides in relevant part:

(a)(1) The governing board of a district maintaining a community college may require community college students to pay a fee in the total amount of not more than ten dollars (\$10) for each semester, seven dollars (\$7) for summer school, seven dollars (\$7) for each intersession of at least four weeks, or seven dollars (\$7) for each quarter for health supervision and services, including direct or indirect medical and hospitalization services, or the operation of a student health center or centers, or both.

(a)(2) The governing board of each community college district may increase [the health service fee] by the same percentage increase as the Implicit Price Deflator

⁹¹ Education Code section 76355.

⁹² Exhibit A, IRC 09-4206-I-24, page 66.

⁹³ Exhibit A, IRC 09-4206-I-24, pages 67-68.

⁹⁴ *Clovis Unified School Dist. v. Chiang* (2010) 188 Cal.App.4th 794.

⁹⁵ *Clovis Unified School Dist., supra*, 188 Cal.App.4th 794, 811.

for State and Local Government Purchase of Goods and Services. Whenever that calculation produces an increase of one dollar (\$1) above the existing fee, the fee may be increased by one dollar (\$1).⁹⁶

Pursuant to the plain language of Education Code section 76355(a)(2), the fee authority given to districts automatically increases at the same rate as the Implicit Price Deflator; when that calculation produces an increase of one dollar above the existing fee, the fee may be increased by one dollar.⁹⁷ The Chancellor of the California Community Colleges issues a notice to the governing boards of all community colleges when a fee increase is triggered.⁹⁸ Therefore the *authority* to impose the health service fees increases automatically with the Implicit Price Deflator, as noticed by the Chancellor. Accordingly, the court in *Clovis Unified* upheld the Controller’s use of the Health Fee Rule to reduce reimbursement claims based on the fees districts are *authorized* to charge. In making its decision the court noted that the concept underlying the state mandates process that Government Code sections 17514 and 17556(d) embody is:

To the extent a local agency or school 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.⁹⁹

The court also noted that, “this basic principle flows from common sense as well. As the Controller succinctly puts it, ‘Claimants can choose not to require these fees, but not at the state’s expense.’”¹⁰⁰ Additionally, in responding to claimant’s argument that, “since the Health Fee Rule is a claiming instruction, its validity must be determined *solely* through the Commission’s P&G’s,”¹⁰¹ the court held:

To accept this argument, though, we would have to ignore, and so would the Controller, the fundamental legal principles underlying state-mandated costs. We conclude *the Health Fee Rule is valid*.¹⁰² (Italics added.)

Thus, pursuant to the court’s decision in *Clovis Unified*, the Health Fee Rule used by the Controller to adjust reimbursement claims filed by claimant for the *Health Fee Elimination*

⁹⁶ Education Code section 76355(d)(2) (Stats. 1993, ch. 8 (AB 46); Stats. 1993, ch. 1132 (AB 39); Stats. 1994, ch. 422 (AB 2589); Stats. 1995, ch. 758 (AB 446); Stats. 2005, ch. 320 (AB 982)) [Formerly Education Code section 72246(e) (Stats. 1987, ch. 118)].

⁹⁷ See Education Code section 76355 (Stats. 1995, ch. 758 (AB 446)). The Implicit Price Deflator for State and Local Purchase of Goods and Services is a number computed annually (and quarterly) by the United States Department of Commerce as part of its statistical series on measuring national income and product, and is used to adjust government expenditure data for the effect of inflation.

⁹⁸ See, e.g., Exhibit G, Memorandum from Chancellor.

⁹⁹ *Clovis Unified School Dist.*, *supra*, 188 Cal.App.4th 794, 812.

¹⁰⁰ *Ibid.*

¹⁰¹ *Ibid.* (Original italics.)

¹⁰² *Clovis Unified School Dist.*, *supra*, 188 Cal.App.4th 794, 812.

program is valid. Since the *Clovis* case is a final decision of the court addressing the merits of the issue presented here, the Commission, under principles of stare decisis, is required to apply the rule set forth by the court.¹⁰³ In addition, the *Clovis* decision is binding on the claimant under principles of collateral estoppel.¹⁰⁴ Collateral estoppel applies when (1) the issue necessarily decided in the previous proceeding is identical to the one that is currently being decided; (2) the previous proceeding terminated with a final judgment on the merits; (3) the party against whom collateral estoppel is asserted is a party to or in privity with a party in the previous proceeding; and (4) the party against whom the earlier decision is asserted had a full and fair opportunity to litigate the issue.¹⁰⁵ Although the claimant in this IRC was not a party to the *Clovis* action, the claimant is in privity with the petitioners in *Clovis*. “A party is adequately represented for purposes of the privity rule if his or her interests are so similar to a party’s interest that the latter was the former’s virtual representative in the earlier action.”¹⁰⁶

With respect to the Chancellor’s opinion of the scope of districts’ fee authority, the Commission finds that as the agency responsible for overseeing the community college system, the interpretation of the Chancellor of the California Community Colleges office is entitled to great weight; the courts have long held that “[a]n agency interpretation of the meaning and legal effect of a statute is entitled to consideration and respect by the courts.”¹⁰⁷ While the Commission has exclusive jurisdiction to determine the existence of a state mandate, and by extension to consider whether fee authority is sufficient under Government Code section 17556 to reduce or eliminate reimbursement of a mandate, the Commission is, like a court, expected to give deference to an agency with expertise in a particular matter.

Based on the foregoing the Commission finds that the Controller’s reduction of reimbursement to the extent of the fee authority found in Education Code section 76355, and as applied to all students, not just those from whom the claimant collects, is correct as a matter of law. The claimant states in comments on the Draft Proposed Decision that it “agrees that claimants and state agencies are bound to apply the Health Fee Rule as decided law” and therefore claimants no longer dispute this audit finding.¹⁰⁸

V. Conclusion

The Commission finds that both the original and the revised audit report were timely initiated and timely completed. The Commission further finds that it does not have jurisdiction to consider the adjustments to indirect costs for fiscal year 2004-2005 that resulted in an increase to

¹⁰³ *Fenske v. Board of Administration* (1980) 103 Cal.App.3d 590, 596.

¹⁰⁴ The petitioners in the *Clovis* case included Clovis Unified School District, El Camino Community College District, Fremont Unified School District, Newport-Mesa Unified School District, Norwalk-La Mirada Unified School District, Riverside Unified School District, San Mateo Community College District, Santa Monica Community College District, State Center Community College District, and Sweetwater Union High School District.

¹⁰⁵ *Roos v. Red* (2006) 130 Cal.App.4th 870, 879-880.

¹⁰⁶ *Rodgers v. Sargent Controls & Aerospace* (2006) 136 Cal.App.4th 82, 91.

¹⁰⁷ *Yamaha Corp. of America v. State Bd. of Equalization*, (1998) 19 Cal.4th 1.

¹⁰⁸ Exhibit F, Claimant’s Comments on the Draft Proposed Decision, page 10.

the reimbursement claim; and it does not have jurisdiction to consider the 2005-2006 reimbursement claim in its entirety, because there is no reduction for that fiscal year. The Commission concludes that reductions of indirect costs for fiscal years 2002-2003 and 2003-2004, based on the claimant's failure to obtain federal approval for the development of its indirect cost rate, and the Controller's recalculation of indirect costs using the method described in the claiming instructions, were correct as a matter of law, and not arbitrary, capricious, or entirely lacking in evidentiary support. And finally, the Commission finds that the reduction of costs over the audit period based on understated offsetting health fee authority was correct as a matter of law, and not arbitrary, capricious, or entirely lacking in evidentiary support.

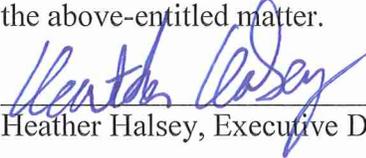
Based on the foregoing, the Commission denies these IRCs.



RE: **Decision**

Health Fee Elimination, 09-4206-I-24 and 10-4206-I-34
Former Education Code Section 72246 (Renumbered as 76355)
Statutes 1984, Chapter 1 (1983-1984 2nd Ex. Sess.) (AB2X 1);
Statutes 1987, Chapter 1118 (AB 2336)
Fiscal Years: 2002-2003, 2003-2004, 2004-2005, and 2005-2006
Foothill-DeAnza Community College District, Claimant

On May 26, 2016, the foregoing decision of the Commission on State Mandates was adopted on the above-entitled matter.



Heather Halsey, Executive Director

Dated: June 1, 2016

BEFORE THE
COMMISSION ON STATE MANDATES
STATE OF CALIFORNIA

IN RE INCORRECT REDUCTION CLAIM
ON:

Education Code Section 48260.5

Statutes 1983, Chapter 498

Fiscal Years 2007-2008, 2008-2009, and
2009-2010

Riverside Unified School District, Claimant

Case No.: 13-904133-I-13

Notification of Truancy

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

(Adopted January 22, 2016)

(Served January 27, 2016)

DECISION

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

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

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

Summary of the Findings

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

At issue in this IRC is whether the Controller may:

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

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

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

COMMISSION FINDINGS

I. Chronology

- 02/16/2010 Claimant signed the reimbursement claim for fiscal year 2007-2008.¹
- 02/16/2010 Claimant signed the reimbursement claim for fiscal year 2008-2009.²
- 02/15/2011 Claimant signed the reimbursement claim for fiscal year 2009-2010.³
- 12/19/2012 Controller issued the draft audit report.⁴
- 01/18/2013 Claimant submitted comments on the draft audit report.⁵
- 02/22/2013 Controller issued the final audit report.⁶
- 11/15/2013 Claimant filed this IRC.⁷
- 10/03/2014 Controller filed late comments on the IRC.⁸
- 10/28/2015 Commission staff issued the draft proposed decision.⁹
- 10/30/2015 The Controller filed comments on the draft proposed decision.¹⁰
- 11/03/2015 The claimant filed comments on the draft proposed decision.¹¹

¹ Exhibit A, Incorrect Reduction Claim, page 269.

² Exhibit A, Incorrect Reduction Claim, page 271.

³ Exhibit A, Incorrect Reduction Claim, page 273.

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

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

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

⁷ Exhibit A, Incorrect Reduction Claim.

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

⁹ Exhibit C, Draft Proposed Decision.

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

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

II. Background

The Notification of Truancy Program

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

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

(a) Upon a pupil's initial classification as a truant, the school district shall notify the pupil's parent or guardian, by first-class mail or other reasonable means, of the following:

(1) That the pupil is truant.

(2) That the parent or guardian is obligated to compel the attendance of the pupil at school.

(3) That parents or guardians who fail to meet this obligation may be guilty of an infraction and subject to prosecution pursuant to Article 6 (commencing with Section 48290) of Chapter 2 of Part 27.

(b) The district also shall inform parents or guardians of the following:

(1) Alternative educational programs available in the district.

(2) The right to meet with appropriate school personnel to discuss solutions to the pupil's truancy.

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

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

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

¹² Education Code section 48200.

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

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

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

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

The Legislature enacted Statutes 2007, chapter 69, effective January 1, 2008, which was sponsored by the Controller’s Office to require the Commission to amend the parameters and guidelines, effective July 1, 2006, to modify the definition of a truant and the required elements to be included in the initial truancy notifications in accordance with Statutes 1994, chapter 1023, and Statutes 1995, chapter 19.¹⁶ These statutes required school districts to add the following information to the truancy notification: that the pupil may be subject to prosecution under Section 48264, that the pupil may be subject to suspension, restriction, or delay of the pupil’s driving privilege pursuant to Section 13202.7 of the Vehicle Code, and that it is recommended that the parent or guardian accompany the pupil to school and attend classes with the pupil for one day. The definition of truant was also changed from a pupil with unexcused instances of absence or tardiness for “more than three days” to a pupil “who is absent from school without valid excuse three full days in one school year or tardy or absent for more than any 30 minute period during the schoolday without a valid excuse on three occasions in one school year, or any combination thereof.”¹⁷ In 2008, the Commission amended the parameters and guidelines, for costs incurred beginning July 1, 2006, as directed by the Legislature.¹⁸ However, reimbursement for the program under the amended parameters and guidelines remained fixed at a unit cost of \$10.21, adjusted annually by the Implicit Price Deflator (\$19.63 for fiscal year 2013-14). These are the parameters and guidelines applicable to this claim.

The Controller’s Audit and Summary of the Issues

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

¹⁵ Exhibit A, Incorrect Reduction Claim, page 69.

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

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

¹⁸ Statutes 2007, chapter 69 (AB 1698).

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

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

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

III. Positions of the Parties

A. Riverside Unified School District

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

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

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

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

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

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

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

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

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

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

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

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

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

B. State Controller’s Office

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

²⁴ Exhibit A, Incorrect Reduction Claim, page 14.

²⁵ Exhibit A, Incorrect Reduction Claim, page 15.

²⁶ Exhibit A, Incorrect Reduction Claim, page 16.

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

²⁸ Exhibit E, Claimant’s Comments on the Draft Proposed Decision, page 3.

²⁹ *Ibid.*

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

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

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

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

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

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

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

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

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

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

IV. Discussion

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

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

The Commission must review questions of law, including interpretation of the parameters and guidelines, de novo, without consideration of legal conclusions made by the Controller in the context of an audit. The Commission is vested with exclusive authority to adjudicate disputes over the existence of state-mandated programs within the meaning of article XIII B, section 6.³⁶ The Commission must also interpret the Government Code and implementing regulations in accordance with the broader constitutional and statutory scheme. In making its decisions, the Commission must strictly construe article XIII B, section 6 and not apply it as an "equitable remedy to cure the perceived unfairness resulting from political decisions on funding priorities."³⁷

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

⁴⁴ *Ibid.*

as well as special education pupils through age 21.⁴⁵ Specifically, claimant argues that although Education Code sections 48200 and 48400 establish the legal attendance requirements for pupils aged six through 18, there is an entitlement to attend kindergarten pursuant to section 48000, and to attend first grade pursuant to sections 48010 and 48011. Attendance cannot be denied by a school district. And special education pupils are statutorily entitled to education services from ages 3 to 22 pursuant to section 56026.⁴⁶ Section 46000 requires the district to keep attendance and record absences for all pupils for purposes of apportionment and compliance with the compulsory education law, subject to regulations by the State Board of Education. Claimant states: “the initial notification of truancy is a product of the attendance accounting process and promotes compliance of the compulsory education law and *every pupil’s* duty to attend school regularly.”⁴⁷ In comments on the draft proposed decision, the claimant states that it no longer disputes this issue.⁴⁸

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

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

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

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

⁴⁵ Exhibit A, Incorrect Reduction Claim, page 251.

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

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

⁴⁸ Exhibit E, Claimant’s Comments on the Draft Proposed Decision, page 2.

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

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

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

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

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

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

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

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

Education Code Section 48260⁵² defines a truant as a pupil who is absent from or tardy to school without valid excuse “on three occasions in one school year.” The Commission amended the parameters and guidelines effective for costs incurred beginning July 1, 2006, to reflect that the mandate to provide a truancy notification is triggered by a pupil who is absent from or tardy to school without valid excuse on three occasions in one school year and these parameters and guidelines apply to this IRC.⁵³ If a pupil cannot be initially classified as a truant, as defined in section 48260, a notification is not required, and any notification sent to that pupil’s parent or guardian is not reimbursable.

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

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

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

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

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

⁵⁵ Exhibit E, Claimant’s Comments on the Draft Proposed Decision, page 3.

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

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

In its audit, the Controller examined a random sample of initial truancy notices distributed by the claimant for each year to determine the proportion of notifications that were unallowable for the Controller's asserted legal reasons. The sample for all fiscal years totaled 883 notifications distributed by elementary and secondary schools, out of a total of 45,091 claimed for the audit period. The Controller selected its sample "based on a 95% confidence level, a precision rate of $\pm 8\%$, and an expected error rate of 50%."⁵⁶ The number of unallowable notifications within the sample for each fiscal year was then calculated as an annual error percentage, and extrapolated to the total number of notifications issued by the claimant in each fiscal year to approximate the total number of unallowable notifications for elementary and secondary schools. The number of unallowable notices was then multiplied by the unit cost for each fiscal year to calculate the total reduction for the audit period at \$68,410.⁵⁷

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

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

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

⁵⁶ Exhibit A, Incorrect Reduction Claim, page 241.

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

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

⁵⁹ Exhibit A, Incorrect Reduction Claim, page 14.

⁶⁰ Exhibit A, Incorrect Reduction Claim, page 15.

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

The Controller explains, in response, that the district incorrectly identifies the population sample size for secondary schools as 296 truancy notifications, thus incorrectly identifying the total sample size at 736 truancy notifications for elementary and secondary schools. The correct number of period attendance truancy notifications sampled by the Controller for secondary schools was 443, rather than 296 as alleged by the claimant, bringing the total notifications sampled to 883.⁶² The Controller explains that:

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

The Controller also states as follows:

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

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

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

⁶¹ Exhibit A, Incorrect Reduction Claim, page 16.

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

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

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

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

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

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

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

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

Section 11340.5 of the APA states in pertinent part:

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

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

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

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

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

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

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

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

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

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

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

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

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

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

⁷³ *Id.*, page 562.

⁷⁴ *Ibid.*

⁷⁵ *Ibid.*

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

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

11346.8, subd. (a), 11346.9); and forward a file of all materials on which the agency relied in the regulatory process to the Office of Administrative Law (Gov. Code, § 11347.3, subd. (b)), which reviews the regulation for consistency with the law, clarity, and necessity (Gov. Code, §§ 11349.1, 11349.3).

One purpose of the APA is to ensure that those persons or entities whom a regulation will affect have a voice in its creation (*Armistead v. State Personnel Board* (1978) 22 Cal.3d 198, 204-205 (Armistead)), as well as notice of the law's requirements so that they can conform their conduct accordingly (*Ligon v. State Personnel Bd.* (1981) 123 Cal.App.3d 583, 588 (Ligon)). The Legislature wisely perceived that the party subject to regulation is often in the best position, and has the greatest incentive, to inform the agency about possible unintended consequences of a proposed regulation. Moreover, public participation in the regulatory process directs the attention of agency policymakers to the public they serve, thus providing some security against bureaucratic tyranny. (See *San Diego Nursery Co. v. Agricultural Labor Relations Bd.* (1979) 100 Cal.App.3d 128, 142-143.)⁷⁸

The Court in *Tidewater Marine Western* found that the APA “defines ‘regulation’ very broadly” and explained that a regulation has two principal characteristics:

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

⁹² *Id.*, pages 438-439.

⁹³ *Id.*, pages 438-439.

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

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

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

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

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

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

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

⁹⁷ *Id.*, page 1344.

⁹⁸ *Id.*, page 1345 [emphasis added].

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

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

¹⁰¹ *Id.*, pages 803-805.

interpreted, or made specific...” the parameters and guidelines and the Controller’s audit authority and was, therefore, an underground regulation.¹⁰²

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

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

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

¹⁰² *Id.*, page 805.

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

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

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

¹⁰⁶ *Id.*, pages 803-805.

¹⁰⁷ *Id.*, page 805.

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

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

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

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

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

¹¹⁰ *Id.*, page 495.

¹¹¹ *Id.*, page 435.

¹¹² *Id.*, pages 438-439.

¹¹³ *Ibid.*

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

¹²⁶ Exhibit A, Incorrect Reduction Claim, page 11.

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

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

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

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

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

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

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

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

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

¹³⁰ Statutes 1968, chapter 449.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

¹³⁹ Exhibit A, Incorrect Reduction Claim, page 12.

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

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

¹⁴² *Id.*, page 495.

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

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

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

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

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

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

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

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

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

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

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

¹⁴⁸ Government Code section 12410.

¹⁴⁹ Exhibit A, Incorrect Reduction Claim, page 15.

¹⁵⁰ Exhibit A, Incorrect Reduction Claim, page 16.

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

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

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

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

n = sample size
p = percent of occurrence in population (expected error rate)
SE = desired sample precision
t = confidence level factor
N = population size¹⁵⁴

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

¹⁵² *Ibid.*

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

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

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

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

In addition, the adjustment range for the population’s true error rate within the 95 percent confidence interval is between \$30,986 to \$30,990, added or subtracted from the point estimate of \$68,410.¹⁵⁷ For the claimed costs reduced, this adjustment range represents less than four percent (3.8%) plus or minus of the total amount claimed in fiscal years 2007-2008, 2008-2009, and 2009-2010 (\$796,110).¹⁵⁸ Although there is a possibility that the \$68,410 reduction may result in more or less reimbursement to the claimant than the actual costs correctly claimed,

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

V. Conclusion

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

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

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

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

¹⁵⁸ Exhibit A, Incorrect Reduction Claim, page 236.

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

Accordingly, the Commission denies this IRC.

COMMISSION ON STATE MANDATES

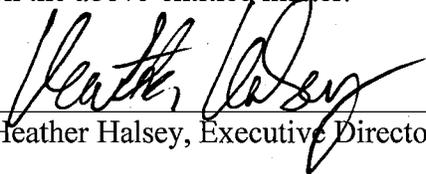
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RE: Decision

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

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



Heather Halsey, Executive Director

Dated: January 27, 2016

BEFORE THE
COMMISSION ON STATE MANDATES
STATE OF CALIFORNIA

**IN RE INCORRECT REDUCTION CLAIM
ON:**

Government Code Sections 3301, 3303, 3304, 3305, and 3306

Statutes 1976, Chapter 465; Statutes 1978, Chapters 775, 1173, 1174, and 1178; Statutes 1979, Chapter 405; Statutes 1980, Chapter 1367; Statutes 1982, Chapter 994; Statutes 1983, Chapter 964; Statutes 1989, Chapter 1165; Statutes 1990, Chapter 675

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

County of Santa Clara, Claimant

Case No.: 10-4499-I-01

Peace Officers Procedural Bill of Rights

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

(Adopted March 25, 2016)

(Served March 30, 2016)

DECISION

The Commission on State Mandates (Commission) heard and decided this incorrect reduction claim (IRC) during a regularly scheduled hearing on March 25, 2016. Jim Spano, Chris Ryan, and Masha Vorobyova appeared on behalf of the Controller. The County of Santa Clara did not appear, but filed a letter indicating that it was standing on the record submitted.

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

The Commission adopted the proposed decision to deny the IRC by a vote of 6 to 0, as follows:

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

Summary of the Findings

This analysis addresses the IRC filed by the County of Santa Clara (claimant) regarding reductions made by the State Controller's Office (Controller) to reimbursement claims for costs incurred during fiscal years 2003-2004 through 2005-2006 under the *Peace Officers Procedural Bill of Rights (POBOR)* program. Over the three fiscal years in question, reductions totaling \$526,802 were made based on alleged unallowable services claimed.

The Commission finds that the Controller properly reduced costs claimed for activities that go beyond the scope of the mandate. The Commission, therefore denies this IRC, finding that the Controller's reductions are correct as a matter of law.

COMMISSION FINDINGS

I. Chronology

- | | |
|------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 09/16/2010 | Claimant filed the IRC. ¹ |
| 12/02/2014 | Controller filed late comments on the IRC. ² |
| 12/05/2014 | Claimant filed a request for an extension of time to rebut which was granted for good cause. |
| 12/18/2014 | Controller filed additional late comments on the IRC. ³ |
| 03/05/2015 | Claimant filed rebuttal comments. ⁴ |
| 01/14/2016 | Commission staff issued the draft proposed decision. ⁵ |
| 01/15/2016 | Controller filed comments on the draft proposed decision. ⁶ |
| 03/22/2016 | Claimant filed a letter with the Commission indicating that a representative of the county would not be present at the hearing and that it stands on the record submitted. |

II. Background

The Peace Officers' Procedural Bill of Rights Program

The Peace Officers' Procedural Bill of Rights (POBOR)⁷ provides a series of rights and procedural safeguards to peace officers when the officer is subject to investigation or discipline

¹ Exhibit A, IRC 10-4499-I-01, page 1.

² Exhibit B, Controller's Late Comments on IRC.

³ Exhibit B, Controller's Additional Late Comments on IRC. Note that the Additional Late Comments relate to the initial comments, correcting page references in that document. Therefore they are included in one exhibit.

⁴ Exhibit C, Claimant's Rebuttal Comments.

⁵ Exhibit D, Draft Proposed Decision.

⁶ Exhibit E, Controller's Comments on Draft Proposed Decision.

⁷ The Peace Officers' Procedural Bill of Rights has been abbreviated "POBRA," by the courts (See *Department of Finance v. Commission* (2009) 170 Cal.App.4th 1355); and as "POBAR," by

by their employer. On November 30, 1999, the Commission adopted the *Peace Officers Procedural Bill of Rights (POBOR)* Statement of Decision, CSM 4499, approving the claim for those activities that exceeded the requirements of the due process clauses of the United States and California Constitutions.⁸ On July 27, 2000, the Commission adopted parameters and guidelines that authorized reimbursement, beginning July 1, 1994, for the ongoing activities summarized below:

- Developing or updating policies and procedures.
- Training for human resources, law enforcement, and legal counsel.
- Updating the status of POBOR cases.
- Providing the opportunity for an administrative appeal for permanent, at-will, and probationary employees that were subject to certain disciplinary actions that were not covered by the due process clause of state and federal law.
- When a peace officer is under investigation, or becomes a witness to an incident under investigation, and is subjected to an interrogation by the employer that could lead to certain disciplinary actions, the following costs and activities are eligible for reimbursement: compensation to the peace officer for interrogations occurring during off-duty time; providing prior notice to the peace officer regarding the nature of the interrogation and identification of investigating officers; tape recording the interrogation; providing the peace officer employee with access to the tape prior to any further interrogation at a subsequent time or if any further specified proceedings are contemplated; and producing transcribed copies of any notes made by a stenographer at an interrogation, and copies of complaints or reports or complaints made by investigators.
- Performing certain activities, specified by the type of local agency or school district, upon the receipt of an adverse comment against a peace officer employee. These activities include providing notice to the officer, an opportunity for the officer to review and respond to the adverse comment, and obtaining the signature of the officer or noting the officer's refusal to sign the adverse comment.⁹

the Commission in parameters and guidelines (Exhibit F, Parameters and Guidelines, corrected August 17, 2000) and on many other occasions the Commission and others have employed the acronym "POBOR," and this decision will follow suit. The correct acronym is of course POPBOR (for Peace Officers' Procedural Bill of Rights) or PSOBOR (for Public Safety Officers Procedural Bill of Rights Act- which is in fact the title of the act), but no one likes the sound of those.

⁸ Exhibit F, Adopted Test Claim Statement of Decision, November 30, 1999, page 10 [For example, the Commission found: "in some circumstances, the due process clause requires the same administrative hearing as the test claim legislation. However, as reflected by the table below, the Commission found that the test claim legislation is broader than the due process clause and applies to additional employer actions that have not previously enjoyed the protections of the due process clause."].

⁹ Exhibit F, Statement of Decision on Reconsideration, April 26, 2006, page 7.

The parameters and guidelines analysis adopted by the Commission on July 27, 2000, also clarified the scope of the mandate and the activities that are *not* eligible for reimbursement. For example, the Commission determined that “[b]efore the test claim legislation was enacted, local law enforcement agencies were conducting investigations, issuing disciplinary actions, and maintaining files for those cases” and, thus, those activities were not reimbursable.¹⁰ The Commission also found that defending a lawsuit attacking the validity of the final administrative decision went beyond the scope of the mandate and was not eligible for reimbursement.¹¹ The Commission further recognized that Government Code section 3303(a) addresses only the compensation and timing of an interrogation, and does not require local agencies to investigate an allegation, prepare for the interrogation, conduct the interrogation, or review the responses given by the officers and/or witnesses.¹² And the Commission found that compensating local agencies for the officer’s time in responding to an adverse comment is not mandated by the state and not eligible for reimbursement.¹³

Statutes 2005, chapter 72, section 6 added section 3313 to the Government Code to direct the Commission to “review” the *POBOR* test claim Statement of Decision to clarify whether the test claim statutes imposed a mandate consistent with California Supreme Court Decision in *San Diego Unified School Dist. v. Commission on State Mandates* (2004) 33 Cal.4th 859 and other applicable court decisions.

On April 26, 2006, the Commission reviewed its original findings and adopted a Statement of Decision on reconsideration, 05-RL-4499-01. On review of the claim, the Commission found that the *San Diego Unified* case did not alter the decision, which found that the test claim statutes imposed a partially reimbursable state-mandated program within the meaning of article XIII B, section 6 of the California Constitution and Government Code section 17514. The reconsideration decision did, however, clarify the scope of the mandate, making clear that the test claim statute does not require an employer to investigate an officer’s conduct, interrogate an officer, take punitive action against the officer, or place an adverse comment in an officer’s personnel file; the *POBOR* mandate is about new procedures governing peace officer labor relations, and investigations of misconduct or malfeasance are beyond the scope of the mandate.¹⁴ The Commission thereafter adopted amended parameters and guidelines for costs

¹⁰ Exhibit F, Final Staff Analysis on Parameters and Guidelines, July 27, 2000, page 5.

¹¹ *Id.*, page 7.

¹² *Id.*, page 16.

¹³ *Id.*, page 20.

¹⁴ Exhibit F, Statement of Decision on Reconsideration, April 26, 2006, pages 38-39; see also page 15, where the Commission found that:

The [POBOR] rights are not triggered, however, until the employing agency decides to interrogate an officer, take punitive action against the officer, or place an adverse comment in an officer’s personnel file. These initial decisions are not mandated by the state, but are governed by local policy, ordinance, city charter, or a memorandum of understanding.

incurred beginning July 1, 2006, for all activities previously approved by the Commission *except* the following:

- The activity of providing the opportunity for an administrative appeal to probationary and at-will peace officers (except when the chief of police is removed) pursuant to Government Code section 3304 is no longer a reimbursable state-mandated activity because the Legislature amended Government Code section 3304 in 1998. The amendment limited the right to an administrative appeal to only those peace officers “who successfully completed the probationary period that may be required” by the employing agency and to situations where the chief of police is removed. (Stats. 1998, ch. 786, § 1.)
- The activities of obtaining the signature of the peace officer on the adverse comment or noting the officer’s refusal to sign the adverse comment, pursuant to Government Code sections 3305 and 3306, when the adverse comment results in a punitive action protected by the due process clause does not constitute a new program or higher level of service and does not impose costs mandated by the state pursuant to Government Code section 17556, subdivision (c).¹⁵

The parameters and guidelines on reconsideration also restate and further clarify the activities that are eligible for reimbursement and those activities that are not eligible for reimbursement.¹⁶

The Controller’s Audit and Summary of the Issues

The May 14, 2008 final audit report for the County of Santa Clara’s annual reimbursement claims for fiscal years 2003-2004 through 2005-2006 allowed \$222,086, out of \$748,888 claimed over the audit period, resulting in a net reduction of \$526,802. These reductions are based on five findings made by the Controller. The claimant accepts Findings 3 and 4 in the audit report, regarding understatements in the claims.¹⁷ And in rebuttal comments, the claimant withdraws its challenge on Finding 2 regarding the inclusion of training hours and break time within the productive hourly rate calculation.¹⁸ The claimant continues to dispute Findings 1 and 5, pertaining to activities disallowed on the basis of the Controller’s interpretation of the scope of the mandate.

In Finding 1, the Controller disallowed \$324,521 in salaries and benefits based on activities that were beyond the scope of the mandate, including activities categorized by the claimant under the components of Administrative Activities, Administrative Appeals, Interrogation, and Adverse Comment. The majority of the denied activities, which are more specifically explained below, were related to the investigation of POBOR cases, or maintaining of files and records of POBOR

¹⁵ Exhibit F, Amended Statement of Decision on Reconsideration, Pursuant to *Department of Finance v. Commission on State Mandates* (2009) 170 Cal.App.4th 1355, amended July 31, 2009, page 5.

¹⁶ See Exhibit F, Parameters and Guidelines, corrected August 17, 2000, pages 3-8; Adopted Parameters and Guidelines Amendment, December 4, 2006, pages 5-11 [describing reimbursable activities in greater detail].

¹⁷ Exhibit A, IRC 10-4499-I-01, pages 60-61.

¹⁸ Exhibit C, Claimant’s Rebuttal Comments, pages 6-8.

cases, or procedural requirements that were required by existing due process protections. The Controller held these activities were not related to the procedural due process requirements approved in the parameters and guidelines and disallowed these costs. Related indirect costs for these disallowed activities totaled \$184,518.¹⁹

In Finding 5, the Controller disallowed travel and training costs not related to the mandate. Only *POBOR*-related training is reimbursable, and the Controller found that \$1,521 in travel and training costs claimed for fiscal year 2004-2005 was not related to the *POBOR* mandate activities.²⁰

III. Positions of the Parties

County of Santa Clara

The claimant continues to dispute the following reductions, alleging that they are incorrect:

Finding 1

- Unallowable salaries and benefits for the Sheriff's Department, under the category of administrative activities, totaling \$8,463, plus related indirect costs, for preparing the file, logging the initial case information, and interviewing the complainant.²¹
- Unallowable salaries and benefits for the Probation Department, under the category of administrative activities, totaling \$35,490, plus related indirect costs, for certain training of internal affairs staff that the Controller found was not mandate-related; and for reviewing investigation reports for approval or correction; visiting other IA offices during establishment of IA office at the department; conducting interviews for an open position; reviewing progress on the development of an IA database; reviewing complaints, response letters, Merit System Rules, and assigning cases; and reviewing training schedule for the unit.²²
- Unallowable salaries and benefits for the Sheriff's Department, under the category of administrative appeals, totaling \$1,388, plus related indirect costs, for ineligible activities related to due process.²³
- Unallowable salaries and benefits for the Probation Department, under the category of administrative appeals, totaling \$985, plus related indirect costs, for ineligible activities related to due process.²⁴
- Unallowable salaries and benefits for the Sheriff's Department, under the category of interrogations, totaling \$61,350 plus related indirect costs, for gathering reports and reviewing complaints; investigation time; preparing questions for interviews;

¹⁹ Exhibit A, IRC 10-4499-I-01, pages 37-54.

²⁰ Exhibit A, IRC 10-4499-I-01, page 61.

²¹ Exhibit A, IRC 10-4499-I-01, page 39.

²² Exhibit A, IRC 10-4499-I-01, pages 39-40.

²³ Exhibit A, IRC 10-4499-I-01, pages 40-42.

²⁴ Exhibit A, IRC 10-4499-I-01, pages 40-42.

interviewing witnesses during work hours; reviewing tape and transcribing statements; conducting pre-interrogation meetings; and interviewing accused officers during normal work hours.²⁵

- Unallowable salaries and benefits for the Probation Department, under the category of interrogations, totaling \$130,236 plus related indirect costs, for gathering reports, logs, and evidence; reviewing complaints, reports, and evidence; interviewing witnesses; traveling to interview witnesses; transcribing witness tapes; reviewing tapes and making corrections; preparing interview questions; conducting pre-interrogation meetings; and interviewing accused officers during normal working hours.²⁶
- Unallowable salaries and benefits for the District Attorney's Office, under the category of interrogations, totaling \$16,350 plus related indirect costs, for gathering reports, log sheets; reviewing complaints, reports, and evidence; preparing interview questions; interviewing witnesses during normal working hours; conducting pre-interrogation meetings; interviewing accused officers during normal working hours; preparing a summary report of the agency complaint as part of the case file preparation; and reviewing interview tapes.²⁷
- Unallowable salaries and benefits for the Sheriff's Department, under the category of adverse comment, totaling \$43,291 plus related indirect costs, for reviewing the circumstances of the complaint to determine the level of investigation; documenting the complaint or allegation and reviewing it for accuracy; summarizing the investigation in a case summary report; and preparing interview questions.²⁸
- Unallowable salaries and benefits for the Probation Department, under the category of adverse comment, totaling \$26,108 plus related indirect costs, for preparing the investigation summary and reviewing it with the supervisor; and preparing the final case report.²⁹
- Unallowable salaries and benefits for the District Attorney's Office, under the category of adverse comment, totaling \$860 plus related indirect costs, for preparing the case summary report.³⁰

With respect to these reductions, the claimant argues that the Controller is relying on the greater specificity of reimbursable activities provided by the amended parameters and guidelines, which were not effective until the 2006-2007 fiscal year.³¹ The claimant argues that it cannot be held to

²⁵ Exhibit A, IRC 10-4499-I-01, pages 42-43.

²⁶ Exhibit A, IRC 10-4499-I-01, pages 42-44.

²⁷ Exhibit A, IRC 10-4499-I-01, pages 42-44.

²⁸ Exhibit A, IRC 10-4499-I-01, pages 44-45.

²⁹ Exhibit A, IRC 10-4499-I-01, pages 44-46.

³⁰ Exhibit A, IRC 10-4499-I-01, pages 44-46.

³¹ Exhibit A, IRC 10-4499-I-01, page 14.

the later parameters and guidelines of which it had no notice.³² In addition, the claimant argues that the earlier parameters and guidelines are “sufficiently flexible as to allow local government to adapt them to its own method of implementing the mandate.”³³ Specifically, the claimant argues that costs claimed for visiting other internal affairs units while establishing its own was a reasonable method of compliance with the approved activity of developing or updating internal policies, procedures, manuals, and other materials. With respect to training costs that were disallowed, the claimant argues that “[f]or a mandate as complex and pervasive as *POBOR*, however, such limitations are not proper.” The claimant argues that the *POBOR* mandate “properly encompasses issues of labor relations, confidentiality issues, investigation errors, first amendment-related conduct, key mistakes in workplace investigations, and assessing credibility, to name a few.”³⁴ In addition, the claimant argues that costs claimed for conducting interrogations while the officer was on duty *and* those costs for compensating the officer when the interrogation was performed during off-duty hours are reimbursable based on the original test claim statement of decision.³⁵ And, with respect to activities pertaining to adverse comment, the claimant simply disagrees with the Controller’s interpretation of the parameters and guidelines.³⁶

Finding 5

- Travel and training costs totaling \$1,521 related to ineligible training activities that were not mandate-related.³⁷

With respect to travel and training costs disallowed under Finding 5, the claimant reiterates that the parameters and guidelines are worded broadly, and that the Controller “cannot use the audit process to place limitations on the program that the Commission did not see fit to include.”³⁸

State Controller’s Office

The Controller’s reductions are broadly based on activities that the Controller finds are beyond the scope of the mandate. For example, under the category of Administrative Activities, which includes developing or updating policies and procedures, attending “specific training for human resources, law enforcement, and legal counsel regarding the requirements of the mandate,” and updating the status of *POBOR* cases, the Controller allowed costs for updating *POBOR* case records and training for Internal Affairs staff. However, the Controller found that costs claimed for “[p]reparing the file,” “[l]ogging initial case information into the system and assign the case,” and interviewing the complainants, were beyond the scope of the mandate, as approved by the Commission and described in the parameters and guidelines.³⁹ Similarly, while the parameters

³² Exhibit A, IRC 10-4499-I-01, page 14.

³³ Exhibit A, IRC 10-4499-I-01, page 15.

³⁴ Exhibit A, IRC 10-4499-I-01, page 16.

³⁵ Exhibit A, IRC 10-4499-I-01, pages 17-19 [quoting at length from the test claim statement of decision CSM-4499].

³⁶ Exhibit A, IRC 10-4499-I-01, pages 19-20; 25.

³⁷ Exhibit A, IRC 10-4499-I-01, pages 61-62.

³⁸ Exhibit A, IRC 10-4499-I-01, page 25.

³⁹ Exhibit A, IRC 10-4499-I-01, page 39.

and guidelines provide for “specific training...regarding the requirements of the mandate,” the claimant’s Probation Department claimed costs for training hours that the Controller found were not related to the *POBOR* mandate, including, for example “Budgeting implications” and “Juvenile Justice Reforms.”⁴⁰ And finally, under Finding 5, the Controller disallowed travel and training costs attributed to training hours that the Controller found to be beyond the scope of the mandate, in accordance with Finding 1.⁴¹

With respect to costs disallowed under the category of Administrative Appeals, the Controller determined that the *POBOR* cases for which costs were claimed were unallowable because the disciplinary actions resulting therefrom implicated existing due process protections and therefore fell outside the scope of state-mandated reimbursement.⁴²

Addressing costs claimed under Interrogation, the Controller notes that the officer’s salary is reimbursable only when the interrogation is conducted during the officer’s off-duty time and results in overtime pay to the officer. In addition, the costs incurred to conduct interrogations were never included in the Interrogations cost component as a reimbursable activity.⁴³

Reimbursement is also authorized for providing notice of an interrogation, tape recording the interrogation, and providing certain documents to the employee. Consequently, the Controller disallowed costs claimed for the claimant’s Sheriff’s Department and Probation Department to gather reports and evidence, interview witnesses during normal working hours, transcribe witness tapes, and interrogate accused officers during normal working hours.⁴⁴

With respect to costs claimed under the category of Adverse Comment, the Controller notes that the parameters and guidelines provide only for notice of the adverse comment; opportunity to review and sign the adverse comment; opportunity to respond; and noting an officer’s refusal to sign. The Controller disallowed costs related to investigating a complaint, preparing interview questions, and preparing a case summary report.⁴⁵

Answering the claimant’s argument that the disputed reductions were based on the more specific amended parameters and guidelines, the Controller states:

The county's comment that the audit was based on the revised parameters and guidelines for the *POBOR* program (adopted by CSM on December 4, 2006) appears frequently in its response to the draft report. During the audit exit conference, the county's SB 90 coordinator asked us several times whether the audit was based on the original parameters and guidelines or on the revised parameters and guidelines adopted on December 4, 2006. On each occasion, We responded that the audit was based on our understanding of the original

⁴⁰ Exhibit A, IRC 10-4499-I-01, pages 39-40.

⁴¹ Exhibit A, IRC 10-4499-I-01, pages 61-62.

⁴² Exhibit A, IRC 10-4499-I-01, pages 40-42.

⁴³ Exhibit B, Controller’s Late Comments on IRC, page 18.

⁴⁴ Exhibit A, IRC 10-4499-I-01, pages 42-44.

⁴⁵ Exhibit A, IRC 10-4499-I-01, pages 44-46.

parameters and guidelines adopted by CSM and that the revised parameters and guidelines apply to claims filed for FY 2006-07 and subsequent years.

Any references to the revised parameters and guidelines adopted on December 4, 2006, made during the exit meeting or in any discussion during the audit process were made solely to point out that reimbursable and non-reimbursable activities of the mandated program are spelled out more clearly in the revised parameters and guidelines. Except for changes to allowable activities for the cost components of Administrative Appeal for probationary and at-will peace officers (pursuant to amended Government Code Section 3304) and Adverse Comment (for punitive actions protected by the due process clause), reimbursable activities did not change from the original parameters and guidelines. In addition, our understanding of allowable and unallowable activities per the original parameters and guidelines did not change as a result of the CSM amending them on December 4, 2006.

The draft audit report and this final report state that the audit was based on parameters and guidelines adopted by the CSM on July 27, 2000, and corrected on August 17, 2000. The language in the audit report and in the SCO response to the county's comments emanates either from the original parameters and guidelines, the original statement of decision, or from the CSM staff analysis of the originally proposed parameters and guidelines for this mandate program.⁴⁶

The Controller's comments on the draft proposed decision state that the Controller concurs with the conclusion and recommendations made.⁴⁷

IV. Discussion

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

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

The Commission must review questions of law, including interpretation of the parameters and guidelines, de novo, without consideration of legal conclusions made by the Controller in the context of an audit. The Commission is vested with exclusive authority to adjudicate disputes over the existence of state-mandated programs within the meaning of article XIII B, section 6.⁴⁸ 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

⁴⁶ Exhibit A, IRC 10-4499-I-01, pages 62-63.

⁴⁷ Exhibit E, Controller's Comments on Draft Proposed Decision.

⁴⁸ *Kinlaw v. State of California* (1991) 54 Cal.3d 326, 331-334; Government Code sections 17551, 17552.

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.”⁴⁹

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.⁵⁰ Under this standard, the courts have found that:

When reviewing the exercise of discretion, “[t]he scope of review is limited, out of deference to the agency’s authority and presumed expertise: ‘The court may not reweigh the evidence or substitute its judgment for that of the agency. [Citation.]’” ... “In general ... the inquiry is limited to whether the decision was arbitrary, capricious, or entirely lacking in evidentiary support. . . .” [Citations.] When making that inquiry, the “ ‘ ‘court must ensure that an agency has adequately considered all relevant factors, and has demonstrated a rational connection between those factors, the choice made, and the purposes of the enabling statute.’ ”⁵¹

The Commission must review the Controller’s audit in light of the fact that the initial burden of providing evidence for a claim of reimbursement lies with the claimant.⁵² In addition, section 1185.1(f)(3) and 1185.2(c) of the Commission’s regulations requires 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.⁵³

Reductions of Salary and Benefit Costs Under Finding 1 and Travel and Training Costs Under Finding 5, Are Correct as a Matter of Law.

The Commission first adopted parameters and guidelines for the *POBOR* mandate on July 27, 2000.⁵⁴ Those parameters and guidelines were amended pursuant to legislative direction following the Commission’s reconsideration of the program on December 4, 2006, with a period

⁴⁹ *County of Sonoma v. Commission on State Mandates* (2000) 84 Cal.App.4th 1264, 1280, citing *City of San Jose v. State of California* (1996) 45 Cal.App.4th 1802, 1817.

⁵⁰ *Johnston v. Sonoma County Agricultural* (2002) 100 Cal.App.4th 973, 983-984. See also *American Bd. of Cosmetic Surgery, Inc. v. Medical Bd. of California* (2008) 162 Cal.App.4th 534, 547.

⁵¹ *American Bd. of Cosmetic Surgery, Inc. v. Medical Board of California* (2008) 162 Cal.App.4th 534, 547-548.

⁵² *Gilbert v. City of Sunnyvale* (2005) 130 Cal.App.4th 1264, 1274-1275.

⁵³ 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.

⁵⁴ Exhibit F, Final Staff Analysis on Parameters and Guidelines, adopted July 27, 2000.

of reimbursement beginning July 1, 2006.⁵⁵ The audit at issue here governs earlier claim years 2003-2004 through 2005-2006, and therefore the prior parameters and guidelines, adopted July 27, 2000, are applicable.⁵⁶ The parties do not dispute this conclusion.

Pursuant to Government Code section 17557 and the Commission's regulations, parameters and guidelines are required to identify the activities the Commission finds to be mandated by the state, and those additional activities proposed by the claimant that the Commission finds and approves, based on substantial evidence in the record, to be reasonably necessary to comply with the state-mandated program.⁵⁷ Parameters and guidelines are regulatory in nature and are interpreted the same as regulations and statutes.⁵⁸ Interpretation of an administrative agency's rule, including those found in the Commission's parameters and guidelines, is a question of law.⁵⁹

Under the rules of interpretation, when the language of an administrative agency's rule, such as the parameters and guidelines, is plain, the provisions are required to be enforced according to the terms of the document. The California Supreme Court determined that:

In statutory construction cases, our fundamental task is to ascertain the intent of the lawmakers so as to effectuate the purpose of the statute. We begin by examining the statutory language, giving the words their usual and ordinary meaning. If the terms of the statute are unambiguous, we presume the lawmakers meant what they said, and the plain meaning of the language governs. [Citations omitted.]⁶⁰

The language of the parameters and guidelines must be construed in the context of the Commission's decisions and adopted analyses on the test claim and parameters and guidelines, so that every provision may be harmonized and have effect.⁶¹ Under these rules, plain

⁵⁵ Exhibit F, Adopted Parameters and Guidelines Amendment, December 4, 2006.

⁵⁶ These parameters and guidelines were in effect when the costs were incurred. (*Clovis Unified School Dist. v. Chiang* (2010) 188 Cal.App.4th 794, 809, fn. 5.)

⁵⁷ Government Code sections 17557 and 17559; California Code of Regulations, title 2, section 1183.7; Former California Code of Regulations, title 2, section 1183.1 (Register 96, No. 30).

⁵⁸ *Clovis Unified School Dist. v. Chiang* (2010) 188 Cal.App.4th 794, 799.

⁵⁹ *Culligan Water Conditioning v. State Board of Equalization* (1976) 17 Cal.3d 86, 93; see also, *County of San Diego v. State* (1997) 15 Cal.4th 68, 81; 109, where the court held that the determination whether reimbursement is required pursuant to article XIII B, section 6 is a question of law.

⁶⁰ *Estate of Griswold* (2001) 25 Cal.4th 904, 910-911.

⁶¹ *City of Merced v. State of California* (1984) 153 Cal.App.3d 777, 781-782; see also, Government Code sections 17514 (defining "costs mandated by the state"), 17550 (providing that "reimbursement ... for costs mandated by the state shall be provided pursuant to this chapter"), 17551 (requiring the Commission to hear and decide a claim that a local agency is entitled to be reimbursed by the state for costs mandated by the state as required by article XIII B, section 6 of the California Constitution), 17552 (providing that this chapter shall be the sole and exclusive procedure by which a local agency may claim reimbursement for costs

provisions of the administrative rule may not be disregarded or enlarged, nor may the interpretation go beyond the meaning of the words used when the words are clear and unambiguous. Thus, the parties are prohibited from writing into an administrative rule, by implication, express requirements that are not there.⁶² The Commission's decisions on test claims and parameters and guidelines are quasi-judicial decisions that are binding on the parties.⁶³

Moreover, later clarification of existing law, including the Commission's decision on reconsideration of this program, which clarified its original decision regarding the scope of the mandated activities, may be applied to reimbursement claims for costs that predate the 2006 parameters and guidelines amendment. Under these circumstances, the Commission's clarification is not considered a retroactive application of a new rule, but is merely a statement of what the law has always been from the time it was enacted.⁶⁴ Accordingly, the later decision adopted by the Commission on reconsideration may be used to aid in understanding the original parameters and guidelines.

Finding 1 of the audit report includes reductions in salaries and benefits for activities that the Controller determined were beyond the scope of the mandate. The reductions include unallowable activities, and related indirect costs, in the categories (as articulated in the parameters and guidelines) of Administrative Activities; Administrative Appeals; Interrogation; and Adverse Comment. Finding 5 of the audit report reduces travel and training costs on the basis that the purpose for the travel and training went beyond the scope of the mandate. The specific activities disallowed differ for each category and for each unit claiming costs within the county, and therefore reductions are analyzed as they were claimed, separated by the categories provided in the parameters and guidelines, and attributed to either the Sheriff's Department, Probation Department, or District Attorney's Office.

A. Salaries and Benefits Claimed for Administrative Activities Performed by Claimant's Sheriff's Department Are Beyond the Scope of the Mandate.

The Controller disallowed costs claimed under the category of Administrative Activities for the claimant's Sheriff's Department to prepare files; log initial case information into "the system"; assign the case; and interview complainants.⁶⁵ The claimant argues that the disallowance is

mandated by the state), 17557 (governing the adoption of parameters and guidelines after the Commission determines there are costs mandated by the state), and 17558 (providing that the Controller's claiming instructions must be derived from the Commission's test claim decision and adopted parameters and guidelines).

⁶² *Whitcomb v. California Employment Commission* (1944) 24 Cal.2d 753, 757.

⁶³ *California School Boards Assoc. v. State of California* (2009) 171 Cal.App.4th 1183, 1200, which stated the following: "[U]nless a party to a quasi-judicial proceeding challenges the agency's adverse findings made in that proceeding, by means of a mandate action in superior court, those findings are binding in later civil actions." [Citation omitted.]

⁶⁴ *McClung v. Employment Development Dept.* (2004) 34 Cal.4th 467, 471.

⁶⁵ Exhibit A, IRC 10-4499-I-01, page 39.

based on the amended parameters and guidelines, which do not apply to the audit years.⁶⁶ The Controller asserts that its audit finding is based on the original parameters and guidelines.⁶⁷ The Controller argues that preparing files, logging initial case information, and interviewing complainants are beyond the scope of the mandate.

The Commission finds that the reductions are correct as a matter of law. The parameters and guidelines in effect during the audit period provide for reimbursement only for “[u]pdating the status of the [POBOR] cases.” The activities claimed to prepare files, log initial case information, and interview complainants were not approved by the Commission for reimbursement. Only the activities approved by the Commission are eligible for reimbursement.⁶⁸

Moreover, the analysis for the parameters and guidelines adopted by the Commission on July 27, 2000, analyzed the proposed activity and determined that it was too broad, as follows:

The Department of Finance states that the component “maintenance of the systems to conduct the mandated activities” is too ambiguous. Staff agrees.

Before the test claim legislation was enacted, local law enforcement agencies were conducting investigations, issuing disciplinary actions, and maintaining files for those cases...Accordingly, staff has modified this component to provide that claimants are eligible for reimbursement for “updating the status report of the POBAR cases.”

Therefore, the Commission’s adopted decision on parameters and guidelines reflects its consideration that prior to the *POBOR* mandate, local agencies were already investigating complaints and maintaining case files.⁶⁹ The mandated program is limited to the new procedural requirements imposed by the state; investigation and discipline activities conducted by the internal affairs unit of a police department are not eligible for reimbursement. As the Commission clarified on reconsideration:

The [POBOR] rights are not triggered, however, until the employing agency decides to interrogate an officer, take punitive action against the officer, or place an adverse comment in an officer's personnel file. These initial decisions are not

⁶⁶ Exhibit A, IRC 10-4499-I-01, pages 14; 69.

⁶⁷ Exhibit A, IRC 10-4499-I-01, page 48.

⁶⁸ Government Code section 17557; Code of Regulations, title 2, section 1183.7 [Parameters and guidelines shall contain “[a] description of the specific costs and types of costs that are reimbursable, including one-time costs and ongoing costs, and reasonably necessary activities required to comply [with the mandated program.]” Former Code of Regulations, title 2, section 1183.1 (Register 96, No. 30).

⁶⁹ See Exhibit F, Final Staff Analysis on Parameters and Guidelines, adopted July 27, 2000, page 16 [“Government Code section 3303, subdivision (a), addresses only the compensation and timing of the interrogation. It does not require local agencies to investigate an allegation, prepare for the interrogation, conduct the interrogation, and review the responses given by the officers and/or witnesses, as implied by the claimant’s proposed language. Certainly, local agencies were performing these investigative activities before POBAR was enacted.”].

mandated by the state, but are governed by local policy, ordinance, city charter, or a memorandum of understanding.⁷⁰

Thus, the activity of “updating the status of POBOR cases” was intended to be interpreted narrowly. The Controller’s disallowance of preparing files and logging files into “the system,” and interviewing complainants, is consistent with a narrow interpretation of the parameters and guidelines.

Based on the foregoing, the Commission finds that the Controller’s reduction of costs claimed under Administrative Activities for claimant’s Sheriff’s Department to prepare files, log initial case files, and interview complainants, are correct as a matter of law.

B. Salaries and Benefits and Travel and Training Expenses Claimed for Training and Other Administrative Activities Performed by Claimant’s Probation Department Are Beyond the Scope of the Mandate.

The Controller disallowed costs claimed under the category of Administrative Activities for claimant’s Probation Department to review investigation reports to approve or make corrections; visit other Internal Affairs units during establishment of the unit; conduct interviews for an Internal Affairs Management Analyst position; review the progress of development of an Internal Affairs database; review complaints, response letters, Merit System Rules, and assign cases; and to review the training schedule for the unit. The Controller also partially adjusted the costs claimed for training activities not related to the mandate, and the associated costs relating to the unallowable training.⁷¹ Specifically, the Controller disallowed training and travel costs for training on the following topics:

- Labor relations
- Unionized vs. non-unionized employees
- Private and public employees
- Handling sexual harassment issues
- Confidentiality issues
- Investigation errors
- Ethical issues in probation
- Budgeting implications
- Juvenile Justice Reforms
- Discrimination issues
- Electronic research
- First Amendment related conduct
- Preparing investigation reports
- Key mistakes in workplace investigations
- Assessing credibility
- Types of lawsuits
- Representation and indemnification
- Supervisory liability of failure to train

⁷⁰ Exhibit F, Statement of Decision on Reconsideration, April 26, 2006, page 15.

⁷¹ Exhibit A, IRC 10-4499-I-01, pages 39-40.

Minimizing exposure to liability⁷²

The applicable parameters and guidelines, under the heading “Administrative Activities,” provide for reimbursement as follows:

1. Developing or updating internal policies, procedures, manuals and other materials pertaining to the conduct of the mandated activities.
2. Attendance at specific training for human resources, law enforcement and legal counsel regarding the requirements of the mandate.⁷³

The Commission finds that the activities of reviewing investigation reports to approve or make corrections; visiting other Internal Affairs units during establishment of the unit; conducting interviews for an Internal Affairs Management Analyst position; reviewing the progress of development of an Internal Affairs database; reviewing complaints, response letters, Merit System Rules, and assigning cases; and reviewing the training schedule for the unit, are not included as reimbursable activities in the parameters and guidelines.⁷⁴

The claimant asserts, however, that salaries and benefits claimed for visiting other internal affairs units while establishing its own constitutes “developing or updating internal policies, procedures, manuals and other materials...” as provided for in the parameters and guidelines. The claimant asserts that visiting other departments’ internal affairs units could save time and money by borrowing from other counties, rather than spending time developing new policies and procedures, and thus this activity constitutes “a reasonable method of compliance...” with the mandate.⁷⁵ However, the reimbursable activity of developing policies and procedures applies only to those policies and procedures that are necessary to implement the *POBOR* mandate. Developing policies and procedures for a new internal affairs unit or database might be appropriate or necessary to *establish and operate* an internal affairs office and to effectively perform investigations, but these activities go beyond the scope of the mandate and are not reimbursable. Only the activities specifically approved by the Commission are eligible for reimbursement.⁷⁶

The claimant also argues that training costs should not be adjusted proportionally, but rather allowed entirely if related to the mandate. The claimant argued in response to the draft audit report: “We cannot go through the training with a microscope on this issue and we disagree with

⁷² Exhibit A, IRC 10-4499-I-01, pages 39-40.

⁷³ Exhibit F, Parameters and Guidelines, corrected August 17, 2000.

⁷⁴ Exhibit A, IRC 10-4499-I-01, pages 39-40.

⁷⁵ Exhibit A, IRC 10-4499-I-01, page 15.

⁷⁶ Government Code section 17557; Code of Regulations, title 2, section 1183.7 [Parameters and guidelines shall contain “[a] description of the specific costs and types of costs that are reimbursable, including one-time costs and ongoing costs, and reasonably necessary activities required to comply [with the mandated program.]”; Former Code of Regulations, title 2, section 1183.1 (Register 96, No. 30).

the audit's negative approach to training."⁷⁷ In its IRC narrative, the claimant more clearly states:

The SCO pared the list of covered topics to those it believes relate to the mandate. For a mandate as complex and pervasive as POBOR, however, such limitations are not proper. Training on POBOR properly encompasses issues of labor relations, confidentiality issues, investigation errors, first amendment-related conduct, key mistakes in workplace investigations, and assessing credibility, to name a few. While the County appreciates the SCO's attempt to include some costs rather than give a full disallowance, the SCO did not allow for some legitimate costs.⁷⁸

As indicated above, the parameters and guidelines in effect during the audit period state that reimbursement is required for "[a]ttendance at specific training for human resources, law enforcement and legal counsel *regarding the requirements of the mandate.*"⁷⁹ The later-amended parameters and guidelines further emphasized that "training *must relate* to mandate-reimbursable activities."⁸⁰ The parameters and guidelines do not authorize reimbursement for issues of labor relations, confidentiality issues, investigation errors, first amendment-related conduct, key mistakes in workplace investigations, and assessing credibility. Such topics go beyond the scope of the mandate to comply with the new procedural requirements imposed by the test claim statutes. Thus, the reduction is correct as matter of law.

In addition, the Controller proportionally reduced training costs to the extent training time was spent on activities beyond the scope of the mandate. The claimant has not provided any evidence to rebut the Controller's pro rata findings; instead, the claimant argues that training costs should be allowed even if a training course includes other topics. The claimant states: "We cannot go through the training with a microscope on this issue and we disagree with the audit's negative approach to training." The burden is on the claimant to establish whether costs are mandate-related in the context of the IRC, and the titles of the training modules that the Controller cites are facially unrelated to the mandate.⁸¹ Thus, there is no evidence that the Controller's pro rata reduction of training costs is incorrect as a matter of law, or that the calculation of the proportion of allowable costs is arbitrary, capricious, or entirely lacking in evidentiary support.

Based on the foregoing, the Commission finds that the Controller's reductions for salaries and benefits, travel, training, and administrative expenses claimed by the Probation Department are correct as a matter of law.

C. Salaries and Benefits Claimed for Administrative Appeals for the Sheriff's Department and Probation Department Are Beyond the Scope of the Mandate.

⁷⁷ Exhibit A, IRC 10-4499-I-01, page 70.

⁷⁸ Exhibit A, IRC 10-4499-I-01, pages 15-16.

⁷⁹ Exhibit F, Parameters and Guidelines, corrected August 17, 2000, page 3 [Emphasis added].

⁸⁰ Exhibit F, Amended Parameters and Guidelines, December 4, 2006, page 5 [Emphasis added].

⁸¹ Government Code sections 17560, 17561(d); *Advanced Choices, Inc. v. Department of Health Services* (2010) 182 Cal.App.4th 1661, 1669.

The Controller reduced \$1,388 in salaries and benefits for the claimant's Sheriff's Department and \$985 in salaries and benefits for the claimant's Probation Department, plus related indirect costs, under the category of Administrative Appeals, finding that the costs claimed were for ineligible appeals which were part and parcel of pre-existing due process requirements and therefore outside the scope of *POBOR*.⁸² The claimant argues that the costs claimed represent *POBOR* administrative appeal hearings authorized for reimbursement in the parameters and guidelines under the "catch-all" category of "[o]ther actions against permanent employees or the Chief of Police that result in disadvantage, harm, loss or hardship and impact the career opportunities of the employee."⁸³ Therefore, the dispute between the claimant and Controller turns on whether the administrative appeals for which costs were claimed fall within the catch-all category.

The Commission, in its test claim decision, analyzed the scope of the administrative appeal mandate in depth, and with respect to all levels of peace officer employees entitled to *POBOR* protections. The Commission found that a public service employee's rights are protected by pre-existing procedural due process safeguards defined by case law, some of which were also provided in Government Code section 3304. To the extent an administrative appeal or hearing is required by pre-existing law, then providing such an appeal under *POBOR* does not constitute a reimbursable new program or higher level of service, since it is not new. Accordingly, the Commission recognized that "permanent" employees, who can only be dismissed or subjected to other disciplinary measures for "cause," have a legitimate claim of entitlement to their job and thus, possess a property interest in continued employment, which is protected by the pre-existing due process clauses of the United States Constitution and the California Constitution.⁸⁴ The Commission further found that California courts require employers to comply with due process when a permanent employee is dismissed,⁸⁵ demoted,⁸⁶ suspended,⁸⁷ receives a reduction in salary,⁸⁸ or receives a written reprimand.⁸⁹ However, the Commission found that an employee

⁸² Exhibit A, IRC 10-4499-I-01, pages 16; 40-41.

⁸³ Exhibit A, IRC 10-4499-I-01, pages 16-17 [citing Final Staff Analysis on Parameters and Guidelines, adopted July 27, 2000, pages 11-12 (located here within Exhibit F)].

⁸⁴ *Slochower v. Board of Education* (1956) 350 U.S. 551 [U.S. Supreme Court found that tenured college professor dismissed from employment had property interest in continued employment safeguarded by due process clause.]; *Gilbert v. Homar* (1997) 520 U.S. 924 [U.S. Supreme Court found that police officer employed as a permanent employee by a state university had property interest in continued employment and suspension without pay implicated due process protections.]; *Skelly v. State Personnel Board* (1975) 15 Cal.3d 194 [California Supreme Court held a permanent civil service employee of the state has a property interest in continued employment and cannot be dismissed without due process of law.].

⁸⁵ *Skelly v. State Personnel Board* (1975) 15 Cal.3d 194.

⁸⁶ *Ng. v. State Personnel Board* (1977) 68 Cal.App.3d 600.

⁸⁷ *Civil Service Assn. v. City and County of San Francisco* (1978) 22 Cal.3d 552, 558-560.

⁸⁸ *Ng, supra*, 68 Cal.App.3d 600, 605.

⁸⁹ *Stanton v. City of West Sacramento* (1991) 226 Cal.App.3d 1438.

does *not* enjoy the rights prescribed by the due process clause when the employee is transferred.⁹⁰ In addition, the Commission analyzed the rights of probationary and at-will employees, finding that although such employees can be dismissed without cause, and do not have a property interest in their employment, the employee may have a liberty interest affected by a dismissal and protected by existing due process laws, when the charges supporting the dismissal damage the employee's reputation and impair the employee's ability to find other employment. Accordingly, the Commission found that the due process clauses of the United States and California Constitutions, apply when the charges supporting the dismissal of a probationary or at-will employee damage the employee's reputation and impair the employee's ability to find other employment.⁹¹

The Commission concluded that the administrative appeal requirements of POBOR constitute a mandated new program or higher level of service, above and beyond that required by the United States and California Constitutions due process clauses, only in the following circumstances:

- Dismissal, demotion, suspension, salary reduction or written reprimand received by probationary and at-will employees whose liberty interest *are not* affected (i.e.; the charges do not harm the employee's reputation or ability to find future employment);
- Transfer of permanent, probationary and at-will employees for purposes of punishment;
- Denial of promotion for permanent, probationary and at-will employees for reasons other than merit; and
- Other actions against permanent, probationary and at-will employees that result in disadvantage, harm, loss or hardship and impact the career opportunities of the employee.⁹²

The Controller states that for the Sheriff's Department, "[o]ur review of claimed costs under this cost component revealed that no administrative hearings were held for the cases included in the claims." And, the Controller states "Even if the hearings had taken place for the two cases in question, they would have resulted from unallowable disciplinary actions (letter of reprimand and suspension) that fall under due process."⁹³ For the Probation Department, the Controller

⁹⁰ *Runyon v. Ellis* (1995) 40 Cal.App.4th 961 [The court found that the employee was entitled to an administrative hearing under the due process clause as a result of a transfer *and an accompanying reduction of pay*. The court did not address the situation where the employee receives a transfer alone.]; *Howell v. County of San Bernardino* (1983) 149 Cal.App.3d 200, 205 ["Although a permanent employee's right to continued employment is generally regarded as fundamental and vested, an employee enjoys no such right to continuation in a particular job assignment."].

⁹¹ Exhibit F, Adopted Test Claim Statement of Decision, CSM-4499, November 30, 1999, pages 7-8.

⁹² Exhibit F, Adopted Test Claim Statement of Decision, CSM-4499, November 30, 1999, pages 10-12.

⁹³ Exhibit A, IRC 10-4499-I-01, pages 41-42; Exhibit B, Controller's Late Comments on IRC, page 14.

found that the appeals in issue resulted from letters of reprimand and suspension actions, for permanent employees.⁹⁴

As indicated above, the Commission determined that due process requirements triggered by a written reprimand of a permanent employee are not new state-mandated activities and are not eligible for reimbursement.⁹⁵ The claimant does not dispute the type of disciplinary action taken, and does not directly answer whether appeals were taken in the case of the Sheriff's Department costs claimed. Instead claimant argues that the claimed costs fall within the catch-all category of "other actions against permanent employees..."⁹⁶ But a catch-all category does not undermine the other specific provisions and limitations of the parameters and guidelines and Commission decisions on this mandate; where a statute (or, as here, parameters and guidelines, which are regulatory)⁹⁷ contains both general and specific provisions, the more specific provisions control.⁹⁸ In addition, an interpretation of law that would render some parts of a statute or regulation surplusage should be avoided.⁹⁹ Here, the type of disciplinary actions at issue in the appeals claimed were found by the Commission to fall under pre-existing due process requirements, and thus were not reimbursable, since they were not new or were mandated by the federal government and not the state. Therefore, to interpret "other actions..." as broadly as the claimant suggests would be inconsistent with the limited nature of this mandated program, and would go beyond the scope of the mandate.

Therefore, the Commission finds that the Controller's reduction of salary and benefit costs for administrative appeals claimed for the Sheriff's Department and Probation Department is correct as a matter of law.

D. Salaries and Benefits Claimed for Activities Related to Interrogations Performed by Claimant's Sheriff's Department, Probation Department, and District Attorney's Office Are Beyond the Scope of the Mandate.

The Controller reduced \$61,350 in salaries and benefits for the claimant's Sheriff's Department, \$130,236 in salaries and benefits for the claimant's Probation Department, and \$16,350 in salaries and benefits for the claimant's District Attorney's Office, plus \$120,026 in related indirect costs, under the category of Interrogation, finding that the costs claimed were for ineligible investigation activities outside the scope of the mandate.¹⁰⁰ The claimant argues that the Controller interprets the reimbursement provisions of the parameters and guidelines

⁹⁴ Exhibit A, IRC 10-4499-I-01, pages 41-42; Exhibit B, Controller's Late Comments on IRC, page 14.

⁹⁵ Exhibit F, Adopted Test Claim Statement of Decision, CSM-4499, November 30, 1999, pages 4-7.

⁹⁶ Exhibit A, IRC 10-4499-I-01, page 17.

⁹⁷ *Clovis Unified School Dist. v. Chiang* (2010) 188 Cal.App.4th 794, 799.

⁹⁸ *People v. Ahmed* (2011) 53 Cal.4th 156, 163.

⁹⁹ *Lopez v. Superior Court* (2010) 50 Cal.4th 1055, 1066.

¹⁰⁰ Exhibit A, IRC 10-4499-I-01, page 42.

incorrectly, and that the activities claimed do not fall under existing due process requirements, and exceed the requirements of an investigation prior to POBOR.¹⁰¹

With regard to interrogations, the parameters and guidelines provide reimbursement for certain activities “only when a peace officer is under investigation, or becomes a witness to an incident under investigation, and is subjected to an interrogation...that could lead to dismissal, demotion, suspension, reduction in salary, written reprimand, or transfer for purposes of punishment.” In addition, the parameters and guidelines expressly state that reimbursement is not required “when an interrogation of a peace officer is in the normal course of duty, counseling, instruction, or informal verbal admonishment by, or other routine or unplanned contact with, a supervisor or any other public safety officer.” In addition, POBOR rights do not extend to civilian witnesses;¹⁰² POBOR does not require local agencies to investigate an allegation or prepare for or conduct an interrogation;¹⁰³ and providing the employee access to a tape or transcription of an interrogation is reimbursable only when not otherwise required by due process.¹⁰⁴ And, reimbursement is not required when the investigation is “concerned solely and directly with alleged criminal activities.”¹⁰⁵

The parameters and guidelines authorize reimbursement for only the following activities:

- Compensating a peace officer for interrogations occurring during off-duty time in accordance with regular department procedure, when required by the seriousness of the investigation. Preparation and review of the officer’s overtime compensation request made as a result of the off-duty interrogation is also reimbursable;
- Providing prior notice to the officer regarding the nature of the interrogation and identification of investigating officers (this includes reviewing a complaint to prepare the notice, and possibly redacting confidential information);
- Tape recording the interrogation when the employee records the interrogation, including transcribing the tape;
- Providing the employee access to the tape prior to any further interrogation, as specified;
- Producing transcribed copies of any notes made by a stenographer at an interrogation, and copies of reports or complaints made by investigators or other persons, except those that are deemed confidential.

The staff analysis on the parameters and guidelines that was adopted by the Commission clarifies that the costs of transcription and tape recording are only reimbursable where disciplinary action

¹⁰¹ Exhibit A, IRC 10-4499-I-01, pages 51-52.

¹⁰² Exhibit F, Final Staff Analysis on Parameters and Guidelines, adopted July 27, 2000, page 12.

¹⁰³ Exhibit F, Final Staff Analysis on Parameters and Guidelines, adopted July 27, 2000, pages 15-16.

¹⁰⁴ Exhibit F, Final Staff Analysis on Parameters and Guidelines, adopted July 27, 2000, page 18.

¹⁰⁵ Exhibit F, Parameters and Guidelines, corrected August 17, 2000.

results, and when that disciplinary action does not involve “a pre-existing due process right” to the tape or transcription.¹⁰⁶

Here, the disallowed activities and costs include gathering reports and reviewing complaints as part of investigating the allegations, investigation time, preparing questions for interviews, interviewing witnesses during normal working hours (claimed for investigators’ time), reviewing tape and summarizing/transcribing witnesses’ statements, conducting pre-interrogation meetings, interviewing accused officers during normal working hours (also claimed for investigators’ time), traveling to interview witnesses, preparing a summary report of the agency complaint, and reviewing interview tapes.¹⁰⁷

As noted throughout this analysis, the *POBOR* mandate does not provide reimbursement for investigative activities, or for due process protections arising from peace officer misconduct except those above and beyond the due process protections required by the state and federal constitutions. The activities described under the Interrogations component of the parameters and guidelines, like all other activities, must be read and interpreted narrowly and in context with the Commission’s decision.

The parameters and guidelines do provide, under the activity of providing prior notice of the nature of the interrogation: “Included in the foregoing is the review of agency complaints or other documents to prepare the notice of interrogation, determination of the investigating officers, redaction of the agency complaint for names of the complainant or other accused parties or witnesses...” And, the parameters and guidelines provide for a similar review for redaction under the activity of “[p]roducing transcribed copies of any notes made...at an interrogation, and copies of reports or other complaints made by investigators or other persons, except those that are deemed confidential...” However, in both of these cases, the “gathering” of complaints is for review and redaction of confidential information, and not, as described by the claimant, for “gathering” or “reviewing” reports and complaints “as part of investigating the allegations.”

Similarly, the claimed activities of “[c]onducting pre-interrogation meetings” and “[p]reparing interview questions” are investigative activities that are not reimbursable under the *POBOR* mandate. And, interviewing witnesses and “traveling to interview witnesses” are clearly activities that benefit the investigation and are not eligible for reimbursement. These activities are beyond the scope of the *POBOR* mandate.

In addition, the claimant sought reimbursement for reviewing tape and transcribing or summarizing a witness or a witness officer’s statement, while the parameters and guidelines only provide reimbursement for the cost of tape recording an interrogation with an officer, and only because the officer has the right to record. Testimony at the hearing on the test claim indicated that the officer almost always will record the interrogation, and thus the Commission approved the cost incurred by the employer to tape record as a reasonably necessary cost.¹⁰⁸ There is no provision in the parameters and guidelines for reviewing tape and transcribing or summarizing a witness or a witness officer’s statement. Moreover, tape recording an interrogation or interview

¹⁰⁶ Exhibit F, Final Staff Analysis on Parameters and Guidelines, adopted July 27, 2000, page 18.

¹⁰⁷ Exhibit A, IRC 10-4499-I-01, pages 42-44.

¹⁰⁸ Exhibit F, Adopted Test Claim Statement of Decision, CSM-4499, November 30, 1999, pages 13-14.

with a witness, including an officer-witness, is not eligible for reimbursement unless that officer “becomes a witness to an incident under investigation, and is subjected to an interrogation by the commanding officer, or any other member of the employing public safety department, that could lead to dismissal, demotion, suspension, reduction in salary, written reprimand, or transfer for purposes of punishment.”¹⁰⁹

And finally, the claimant reported costs for interviewing witnesses and accused officers during normal working hours, for which the audit report indicates “investigators’ time” was claimed. The parameters and guidelines provide only for reimbursement as follows: “When required by the seriousness of the investigation, compensating *the peace officer* for interrogations occurring during off-duty time in accordance with regular department procedures.” The parameters and guidelines do not authorize reimbursement to interrogate and, thus, an investigator’s time is not reimbursable. The staff analysis adopted by the Commission for the parameters and guidelines expressly held that Government Code section 3303(a) addresses only the compensation and timing of an interrogation, and does not require local agencies to investigate an allegation, prepare for the interrogation, conduct the interrogation, or review the responses given by the officers and/or witnesses.^{110,111} These decisions of the Commission are binding on the parties.¹¹² Thus, the costs claimed for investigators’ time go beyond the scope of the mandate.

Based on the foregoing, the Controller’s reductions under the Interrogation component are correct as a matter of law.

E. Salaries and Benefits Claimed for Activities Related to an Adverse Comment Performed by Claimant’s Sheriff’s Department, Probation Department, and District Attorney’s Office Are Beyond the Scope of the Mandate.

The Controller reduced \$43,291 in salaries and benefits for the claimant’s Sheriff’s Department, \$26,108 in salaries and benefits for the claimant’s Probation Department, and \$860 for the claimant’s District Attorney’s Office, plus related indirect costs, under the category of Adverse Comment, finding that the costs claimed were for ineligible investigation activities outside the scope of the mandate.¹¹³

The parameters and guidelines, under the component Adverse Comment, state separately the reimbursable activities for school districts, counties, and cities and special districts, respectively. For purposes of this IRC, only the reimbursable activities provided for counties are relevant. The parameters and guidelines provide three conditional statements, pertaining to the potential consequences of the adverse comment, and provide for different reimbursable activities in each case, depending on the existing requirements of due process or other law that are not reimbursable under the test claim decision:

- If an adverse comment results in dismissal, suspension, demotion, reduction in pay, or written reprimand for a permanent employee peace officer, or harms the officer’s

¹⁰⁹ Exhibit F, Parameters and Guidelines, corrected August 17, 2000, page 4.

¹¹⁰ Exhibit F, Final Staff Analysis on Parameters and Guidelines, adopted July 27, 2000, page 16.

¹¹¹ Exhibit F, Parameters and Guidelines, corrected August 17, 2000, page 4.

¹¹² *California School Boards Assoc.*, *supra*, 171 Cal.App.4th 1183, 1200.

¹¹³ Exhibit A, IRC 10-4499-I-01, pages 45-46.

reputation and opportunity to find future employment, then a county is entitled to reimbursement for obtaining the officer's signature on the adverse comment, or noting the officer's refusal to sign the adverse comment and obtaining the signature or initials of the officer.

- If an adverse comment is related to a possible criminal offense, a county is entitled to reimbursement for providing notice of the adverse comment; providing an opportunity to review and sign the adverse comment; providing an opportunity to respond within 30 days; and noting an officer's refusal to sign and obtaining a signature or initials under such circumstances.
- If an adverse comment is not related to a possible criminal offense, a county is entitled to reimbursement for providing notice of the adverse comment; obtaining the signature of the officer; or noting the officer's refusal to sign and obtaining a signature or initials.

The parameters and guidelines also authorize reimbursement for the following activities found to be reasonably necessary to comply with the mandates associated with adverse comments:

Included in the foregoing are review of circumstances or documentation leading to adverse comment by supervisor, command staff, human resources staff or counsel, including determination of whether same constitutes an adverse comment; preparation of comment and review for accuracy; notification and presentation of adverse comment to officer and notification concerning rights regarding same; review of response to adverse comment, attaching same to adverse comment and filing.¹¹⁴

However, as discussed throughout this analysis, the reimbursable activities pertaining to an adverse comment do not include investigative activities, including reviewing a complaint to determine whether and to what extent to investigate.¹¹⁵

Accordingly, the Controller denied the following activities:

For the Sheriff's Department:

- Reviewing the circumstances of the complaint *to determine the level of investigation* prior to starting the case investigation process (to determine whether the case will be investigated at the Internal Affairs or division level).
- Documenting the complaint/allegation and reviewing it for accuracy during the initial complaint intake *prior to starting the investigation*.
- *Summarizing the investigation* in a case summary report and having Internal Affairs review the summary report to ensure proper procedures were followed.
- Preparing interview questions.

For the Probation Department:

¹¹⁴ See Exhibit F, Parameters and Guidelines, corrected August 17, 2000, pages 6-8.

¹¹⁵ Exhibit F, Final Staff Analysis, Parameters and Guidelines, adopted July 27, 2000, page 5.

- *Preparing the investigation summary and reviewing it* with the supervisor prior to closing the case.
- Preparing the final case report.

And for the District Attorney's Office:

- Preparing the case summary report.¹¹⁶

These activities are not reimbursable and go beyond the scope of the mandate. The plain language of the parameters and guidelines pertaining to adverse comment is focused almost entirely on obtaining the officer's signature for an adverse comment, or an acknowledgement of the officer's refusal to sign. Likewise, in the test claim statement of decision, the Commission found that if an adverse comment would result in dismissal, suspension, demotion, or other deprivation of employment, notice to the officer and the opportunity to review and respond to the adverse comment would already be required by existing due process law.¹¹⁷ Government Code sections 3305 and 3306 only constitute a new program or higher level of service only with respect to the requirements to obtain an officer's signature or note the officer's refusal to sign the adverse comment.¹¹⁸ The activity to review the circumstances or documentation was included in the parameters and guidelines because the Commission recognized that the adverse comment could be considered a written reprimand or could lead to other punitive actions taken by the employer, both of which are already protected by the due process clause.

The Controller has disallowed costs for activities that, by their own terms, pertain to the investigation surrounding an adverse comment, and not to obtaining a signature, or acknowledging a refusal to sign. As noted above, the parameters and guidelines do state that "review of circumstances or documentation...including determination of whether same constitutes an adverse comment,"¹¹⁹ is included within the activities stated. Under such circumstances, the Commission found that the notice requirements of Government Code sections 3305 and 3306 do not constitute a new program or higher level of service pursuant to article XI11 B, section 6 of the California Constitution.¹²⁰ Thus, the activity to review the circumstances or documentation cannot be read to include, as was claimed "reviewing the circumstances of the complaint to determine the level of investigation..." or "summarizing the investigation in a case summary report..."¹²¹ These activities clearly pertain to investigative activities, which, as has been stated throughout this analysis, are not a reimbursable activity under the *POBOR* mandate. And, the parameters and guidelines do provide for "preparation of

¹¹⁶ Exhibit A, IRC 10-4499-I-01, pages 45-46.

¹¹⁷ Exhibit F, Adopted Test Claim Statement of Decision, CSM-4499, November 30, 1999, page 19 [citing *Hopson v. City of Los Angeles* (1983) 139 Cal.App.3d 347, 354].

¹¹⁸ Exhibit F, Adopted Test Claim Statement of Decision, CSM-4499, November 30, 1999, page 19.

¹¹⁹ Exhibit F, Parameters and Guidelines, corrected August 17, 2000 page 8.

¹²⁰ Exhibit F, Adopted Test Claim Statement of Decision, CSM-4499, November 30, 1999, page 19.

¹²¹ Exhibit A, IRC 10-4499-I-01, page 45.

comment and review for accuracy,” but that activity is related to the notice and opportunity to respond, and to obtaining an officer’s signature, not to “the initial complaint intake prior to starting the investigation,” as was claimed.

The *POBOR* mandate is very narrow, and as determined by the Commission, local law enforcement agencies were conducting investigations and issuing disciplinary actions before the *POBOR* statutes were enacted and, thus, those activities were not reimbursable.¹²² The Commission’s decision on reconsideration further clarifies the intended scope of the mandate, including and especially making clear that the test claim statute does not require an employer to investigate an officer’s conduct or place an adverse comment in an officer’s personnel file; the *POBOR* mandate is about new procedures governing peace officer labor relations, and investigations of misconduct or malfeasance are beyond the scope of the mandate.¹²³ These decisions are binding on the parties.¹²⁴

Based on the foregoing, the Commission finds that the Controller’s reduction of costs claimed under the Adverse Comment component are correct as a matter of law.

V. Conclusion

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

¹²² Exhibit F, Final Staff Analysis on Parameters and Guidelines, July 27, 2000, page 5.

¹²³ Exhibit F, Statement of Decision on Reconsideration, April 26, 2006, pages 38-39; see also page 15, where the Commission found that:

The [POBOR] rights are not triggered, however, until the employing agency decides to interrogate an officer, take punitive action against the officer, or place an adverse comment in an officer’s personnel file. These initial decisions are not mandated by the state, but are governed by local policy, ordinance, city charter, or a memorandum of understanding.

¹²⁴ *California School Boards Assoc.*, *supra*, 171 Cal.App.4th 1183, 1200.

COMMISSION ON STATE MANDATES

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RE: **Decision**

Peace Officers Procedural Bill of Rights (POBOR), 10-4499-I-01
Government Code Sections 3301, 3303, 3304, 3305, and 3306
Statutes 1976, Chapter 465; Statutes 1978, Chapters 775, 1173, 1174, and 1178;
Statutes 1979, Chapter 405; Statutes 1980, Chapter 1367; Statutes 1982, Chapter 994;
Statutes 1983, Chapter 964; Statutes 1989, Chapter 1165; Statutes 1990, Chapter 675
Fiscal Years: 2003-2004, 2004-2005, and 2005-2006
County of Santa Clara, Claimant

On March 25, 2016, the foregoing decision of the Commission on State Mandates was adopted on the above-entitled matter.


Heather Halsey, Executive Director

Dated: March 30, 2016

BEFORE THE
 COMMISSION ON STATE MANDATES
 STATE OF CALIFORNIA

**IN RE INCORRECT REDUCTION CLAIM
 ON:**

Government Code Sections 3301, 3303, 3304, 3305, and 3306.

Statutes 1976, Chapter 465; Statutes 1978, Chapters 775, 1173, 1174, and 1178; Statutes 1979, Chapter 405; Statutes 1980, Chapter 1367; Statutes 1982, Chapter 994; Statutes 1983, Chapter 964; Statutes 1989, Chapter 1165; Statutes 1990, Chapter 675

Fiscal Years 2003-2004, 2004-2005, 2005-2006, 2006-2007, and 2007-2008

City of Los Angeles, Claimant

Case No.: 12-4499-I-02

Peace Officers Procedural Bill of Rights

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

(Adopted May 26, 2016)

(Served June 1, 2016)

DECISION

The Commission on State Mandates (Commission) heard and decided this incorrect reduction claim (IRC) during a regularly scheduled hearing on May 26, 2016. Jim Spano and Masha Vorobyova appeared on behalf of the State Controller’s Office (Controller). The City of Los Angeles did not appear.

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

The Commission adopted the proposed decision to deny the IRC by a vote of 5-0 as follows:

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

Summary of the Findings

This incorrect reduction claim (IRC) challenges the Controller's finding that the City of Los Angeles (claimant) claimed unallowable costs of \$21,464,469 (of \$35,648,462 claimed) for the *Peace Officers Procedural Bill of Rights (POBOR)* program for fiscal years 2003-2004 through 2007-2008. The sole issue is whether the claimed activities in finding 1 (unallowable salaries, benefits, and related indirect costs) are eligible for reimbursement in accordance with the parameters and guidelines and the Commission's *POBOR* decisions.

The Commission finds that the reduction of costs claimed for salaries, benefits, and related indirect costs in audit finding 1 is correct as a matter of law, and not arbitrary, capricious, or entirely lacking in evidentiary support. Accordingly, the Commission denies this IRC.

COMMISSION FINDINGS

I. Chronology

- 09/28/2012 Claimant filed the IRC.¹
- 12/22/2014 Controller filed late comments on the IRC.²
- 03/23/2016 Commission staff issued the Draft Proposed Decision.³
- 03/28/2016 Controller filed comments on the Draft Proposed Decision.⁴

II. Background

The Peace Officers' Procedural Bill of Rights Program

The Peace Officers' Procedural Bill of Rights Act (POBOR)⁵ provides a series of procedural rights and safeguards to peace officers who are subject to investigation or discipline by their local government employer. On November 30, 1999, the Commission adopted the *Peace Officers Procedural Bill of Rights (POBOR)* Statement of Decision, CSM 4499, approving the test claim for activities that exceeded the requirements of the due process clauses of the United

¹ Exhibit A, IRC.

² Exhibit B, Controller's Late Comments on the IRC. Note that as stated in Government Code section 17553(d) "the Controller shall have no more than 90 days after the claim is delivered or mailed to file any rebuttal to an incorrect reduction claim. The failure of the Controller to file a rebuttal to an incorrect reduction claim shall not serve to delay the consideration of the claim by the Commission." However, in this instance, due to the backlog of IRCs, these late comments have not delayed consideration of this item and so they have been included in the analysis and proposed decision.

³ Exhibit C, Draft Proposed Decision.

⁴ Exhibit D, Controller's Comments on the Draft Proposed Decision.

⁵ The Peace Officers' Procedural Bill of Rights has been abbreviated "POBRA," by the courts (See *Department of Finance v. Commission* (2009) 170 Cal.App.4th 1355); and as "POBAR," by the Commission in the parameters and guidelines (Exhibit A, IRC (parameters and guidelines), p. 12) and on many other occasions the Commission and others have employed the acronym "POBOR," and this decision will follow suit.

States and California Constitutions.⁶ On July 27, 2000, the Commission adopted parameters and guidelines that authorized reimbursement, beginning July 1, 1994, for the ongoing activities summarized below:

- Developing or updating policies and procedures;
- Training for human resources, law enforcement, and legal counsel;
- Updating the status of *POBOR* cases;
- Providing the opportunity for an administrative appeal for permanent, at-will, and probationary employees that were subject to certain disciplinary actions that were not covered by the due process clause of state and federal law;
- When a peace officer is under investigation, or becomes a witness to an incident under investigation, and is subjected to an interrogation by the employer that could lead to certain disciplinary actions, the following costs and activities are eligible for reimbursement: compensation to the peace officer for interrogations occurring during off-duty time; providing prior notice to the peace officer regarding the nature of the interrogation and identification of investigating officers; tape recording the interrogation; providing the peace officer employee with access to the tape prior to any further interrogation at a subsequent time or if any further specified proceedings are contemplated; and producing transcribed copies of any notes made by a stenographer at an interrogation, and copies of complaints of reports or complaints made by investigators;
- Performing certain activities, specified by the type of local agency or school district, upon the receipt of an adverse comment against a peace officer employee. These activities include providing notice to the officer, an opportunity for the officer to review and respond to the adverse comment, and obtaining the signature of the officer or noting the officer's refusal to sign the adverse comment.⁷

The parameters and guidelines analysis adopted by the Commission on July 27, 2000, also clarified the scope of the mandate and the activities that are *not* eligible for reimbursement. For example, the Commission determined that “[b]efore the test claim legislation was enacted, local law enforcement agencies were conducting investigations, issuing disciplinary actions, and

⁶ Exhibit B, Controller's Late Comments on the IRC, page 38 (Statement of Decision, CSM 4499, November 30, 1999, p. 11). For example, the Commission found: “in some circumstances, the due process clause requires the same administrative hearing as the test claim legislation. However, as reflected by the table below, the Commission found that the test claim legislation is broader than the due process clause and applies to additional employer actions that have not previously enjoyed the protections of the due process clause.”

⁷ Exhibit A, IRC, page 29 (Statement of Decision on Reconsideration, 05-RL-4499-01, April 26, 2006, p. 7). Exhibit B, Controller's Late Comments on the IRC, pages 60-65 (Parameters and Guidelines, corrected Aug. 17, 2000). These Parameters and Guidelines were adopted on July 27, 2000, but two non-substantive clerical errors were corrected and they were issued on August 17, 2000.

maintaining files for those cases,” so that those activities are not reimbursable.⁸ The Commission also found that defending a lawsuit attacking the validity of the final administrative decision went beyond the scope of the mandate and is not eligible for reimbursement.⁹ The Commission further recognized that Government Code section 3303(a) addresses only the compensation and timing of an interrogation and does not require local agencies to investigate an allegation, prepare for the interrogation, conduct the interrogation, or “review the responses given by the officers and/or witnesses.”¹⁰ And the Commission found that compensating local agencies for the officer’s time in responding to an adverse comment is not mandated by the state and not reimbursable.¹¹

Statutes 2005, chapter 72, section 6 added section 3313 to the Government Code that directed the Commission to “review” the *POBOR* test claim Statement of Decision to determine whether it was consistent with California Supreme Court Decision in *San Diego Unified School Dist. v. Commission on State Mandates* (2004) 33 Cal.4th 859, and other applicable court decisions.

On April 26, 2006, the Commission reviewed its original findings and adopted a *POBOR* Statement of Decision on Reconsideration, 05-RL-4499-01. On review, the Commission found that the *San Diego Unified* case supported the Commission’s 1999 Statement of Decision, which found that the test claim statutes imposed a partially reimbursable state-mandated program within the meaning of article XIII B, section 6 of the California Constitution and Government Code section 17514. The reconsideration decision clarified the scope of the mandate, making clear that the test claim statute does not require an employer to investigate an officer’s conduct, interrogate an officer, take punitive action against the officer, or place an adverse comment in an officer’s personnel file. The *POBOR* mandate is about new procedures governing peace officer labor relations, but investigations of misconduct or malfeasance are beyond the scope of the mandate.¹²

On December 4, 2006, the Commission adopted amended parameters and guidelines for costs incurred beginning July 1, 2006, based on the *POBOR* Statement of Decision on Reconsideration, a report issued by the Bureau of State Audits on the program recommending that the Commission clarify the activities that are reimbursable and those that are not, and based on several requests to amend the parameters and guidelines. These amended parameters and

⁸ Exhibit B, Controller’s Late Comments on the IRC, page 169 (Final Staff Analysis on the Proposed Parameters and Guidelines, July 27, 2000, p. 5).

⁹ *Id.*, page 171.

¹⁰ *Id.*, page 180.

¹¹ *Id.*, page 184.

¹² Exhibit A, IRC, pages 29, 64-65 (Statement of Decision on Reconsideration, 05-RL-4499-01, April 26, 2006); see also page 41, where the Commission found that:

The [POBOR] rights are not triggered, however, until the employing agency decides to interrogate an officer, take punitive action against the officer, or place an adverse comment in an officer’s personnel file. These initial decisions are not mandated by the state, but are governed by local policy, ordinance, city charter, or a memorandum of understanding.

guidelines authorize reimbursement for all activities previously approved by the Commission except the following that were no longer reimbursable:

- Providing the opportunity for an administrative appeal to probationary and at-will peace officers (except when the chief of police is removed) pursuant to Government Code section 3304 is no longer a reimbursable state-mandated activity because the Legislature amended Government Code section 3304 in 1998. The amendment limited the right to an administrative appeal to only those peace officers “who successfully completed the probationary period that may be required” by the employing agency and to situations where the chief of police is removed. (Stats. 1998, ch. 786, § 1.)
- Obtaining the signature of the peace officer on the adverse comment or noting the officer’s refusal to sign the adverse comment, pursuant to Government Code sections 3305 and 3306, when the adverse comment results in a punitive action protected by the due process clause does not constitute a new program or higher level of service and does not impose costs mandated by the state pursuant to Government Code section 17556, subdivision (c).¹³

On March 28, 2008, the Commission amended the parameters and guidelines again, following requests filed by the Department of Finance and the County of Los Angeles, to allow reimbursement based on either actual costs incurred or a unit-cost reasonable reimbursement methodology, beginning July 1, 2006.¹⁴

The Controller’s Audit and Summary of the Issues

The reimbursement claims were based on a time study the claimant conducted in May 2004, which was designed to keep track of *POBOR* related activities performed by the claimant. The claimant used this time study to claim costs of \$35,648,462 in salaries and benefits for fiscal years 2003-2004 through 2007-2008. In audit finding 1 (the only disputed finding in this IRC), the Controller determined that \$21,464,469 is unallowable because the activities claimed are not identified in the parameters and guidelines as reimbursable costs. The related unallowable indirect costs total \$8,307,090.¹⁵

Finding 1 was divided into three components that correspond to the categories in the parameters and guidelines: administrative activities, interrogations, and adverse comment. Since the reimbursement claims were based on a time study, the Controller was able to separate the time attributable to each claimed task and separate minute increments for individual activities in order to exclude time spent on unallowable activities.¹⁶

¹³ See Exhibit B, Controller’s Late Comments on the IRC, page 188 (Final Staff Analysis on Requests to Amend the Parameters and Guidelines, Adopted Dec. 4, 2006).

¹⁴ Exhibit B, Controller’s Late Comments on the IRC, pages 85-99 (Parameters and Guidelines, 06-PGA-06, amended March 28, 2008).

¹⁵ Exhibit A, IRC, pages 82-88 (final audit report); Exhibit B, Controller’s Late Comments on the IRC, pages 100-167 (tab 7, Analysis of Claimed Activities).

¹⁶ Exhibit A, IRC, page 88 (final audit report); Exhibit B, Controller’s Late Comments on the IRC, pages 100-167 (tab 7, Analysis of Claimed Activities).

Of the \$2,864,828 claimed for administrative activities, the Controller found \$2,746,417 was unallowable. Of the nine activities claimed in this category, the Controller found only two to be allowable: updating status changes in *POBOR* case files and updating the database and noting the case assignment to an investigator for adjudication.¹⁷ The seven disallowed activities include: (1) creating a file and case number when the complaint form is received; (2) reading the complaint form and determining the best entity to perform the investigation; (3) updating the database when the investigation is complete; (4) updating the database for Internal Affairs' review; (5) creating another file and entering it into the advocate database for cases in the appeal phase; (6) distributing copies of the face sheet to concerned parties; and (7) closing out the case file by updating the database.¹⁸

Of the \$12,505,118 claimed for interrogations, the Controller found \$11,289,312 to be unallowable. Claimant sought reimbursement for 15 activities, but did not provide a description of them. The Controller said "LAPD [Los Angeles Police Dept.] staff stated that these activities involved time for conducting investigations, collecting evidence, writing reports, and editing reports. We determined that these activities are unallowable because they relate to the investigation process."¹⁹

Of the \$20,278,116 claimed for adverse comment activities, the Controller found \$7,428,740 to be unallowable. Of the 16 activities claimed under this component, the audit found that the following 11 are reimbursable: (1) reviewing the complaint form and determining whether it warrants further investigation; (2) providing first notice of the adverse comment and of an investigation and providing an opportunity to the accused officer to respond within 30 days; (3) providing first notice of the adverse comment and that an investigation is taking place and providing the officer an opportunity to respond within 30 days; (4) the officer under investigation reviewing and signing the adverse comment or complaint fact sheet; (5) the time involved if the officer under investigation refuses to sign the face sheet or initial the adverse comment; (6) review by Internal Affairs Management of a completed case before sending it out for notification to the officer under investigation; (7) time spent by the Command Officer (accused officer's supervisor) of the Area to adjudicate the complaint, including reviewing the completed complaint and writing a Letter of Transmittal; (8) area commanding officer review of complaint and letter of transmittal; (9) preparing the charge sheet for the chief of police to sign; (10) ensuring the accused officer is served with the charge sheet and obtaining the officer's signature or noting the refusal to sign; and (11) reviewing the accused officer's response to the complaint.²⁰

The Controller also found that five of the activities claimed under the adverse comment component were not reimbursable because they are part of the investigation process: (1) investigating the circumstances surrounding the adverse comment; (2) preliminary investigation conducted by supervisors, detectives, and the command staff in the area where the complaint was taken and that can include report writing, interviews, or any activity where information is

¹⁷ Exhibit A, IRC, pages 4-5, also in Exhibit A, page 83 (final audit report).

¹⁸ Exhibit A, IRC, pages 4-5, also in Exhibit A, page 83 (final audit report).

¹⁹ Exhibit A, page 84 (final audit report).

²⁰ Exhibit A, pages 86-87 (final audit report).

gathered for the complaint form; (3) “time spent by an Area to investigate the complaint” after the preliminary investigation; (4) the assigned advocate reviews the investigation for status and thoroughness; and (5) the time needed to conduct any additional investigations.²¹

III. Positions of the Parties

A. City of Los Angeles

The claimant argues that audit finding 1 (unallowable salaries, benefits and related indirect costs) is incorrect because the Controller “erred by limiting the scope of the eligible interrogation, administrative, and adverse comment activities.”²² For the administrative activities (of which five were found not reimbursable) the claimant argues that “all seven activities are necessary for a local agency the size and complexity of the Los Angeles Police Department to carry out the administrative activities associated with the mandate.”²³ For the interrogation activities, claimant argues that the parameters and guidelines as amended March 28, 2008, do not reflect the original *POBOR* Statement of Decision that found eligible costs included: “Conducting the investigation when the peace officer is on duty, and compensating the peace officer for off-duty time in accordance with regular department procedures and new requirements not previously imposed on local agencies and school districts.” Noting that the Controller has limited reimbursement for officer overtime, claimant argues that the costs for conducting interrogations during regular work time, and preparing for those interrogations, is reimbursable.²⁴ As to the adverse comment activities, the claimant alleges that most of the claimed activities are necessary to comply with the adverse comment requirements and should be reimbursable because the parameters and guidelines are inconsistent with the mandate requirements and the original statement of decision.²⁵

The claimant did not file comments on the Draft Proposed Decision.

B. State Controller’s Office

The Controller maintains that the audit reductions are correct and that the IRC should be denied because the reduced salary and benefit costs claimed are not eligible for reimbursement.²⁶ For the administrative activities, the Controller disallowed activities relating to managing case files because according to the July 27, 2000 staff analysis adopted by the Commission for the proposed parameters and guidelines: “before the test claim legislation was enacted, local law enforcement agencies were conducting investigations, issuing disciplinary hearings, and maintaining files for those cases.”²⁷ The Controller argues that the parameters and guidelines are

²¹ Exhibit A, IRC, page 87 (final audit report).

²² Exhibit A, IRC, page 3.

²³ *Id.*, page 5.

²⁴ *Id.*, page 7.

²⁵ *Id.*, page 9.

²⁶ Exhibit B, Controller’s Late Comments on the IRC, pages 10-12.

²⁷ *Id.*, pages 14 and 169 (Final Staff Analysis on Proposed Parameters and Guidelines, adopted July 27, 2000).

limited to reimbursement for activities that relate to updating the status report of the mandate-related activities.²⁸

The Controller also disagrees with the claimant's argument that interrogations conducted during an officer's regular on-duty time are reimbursable, noting that the claimant takes a sentence from the *POBOR* Statement of Decision out of context. Claimant quotes language from the section of the Decision discussing "Compensation and Timing of an Interrogation," the purpose of which was to discuss the test claimant's assertion that Government Code section 3303(a) results in payment of overtime to the investigated employee.²⁹ Moreover, the claimant ignores other language in the decision that prefaces the analysis of this issue, such as: "The procedures and rights given to peace officers under section 3303 do *not* apply to any interrogation in the normal course of duty, counseling, instruction, or informal admonition by a supervisor."³⁰ The Controller also quotes language from the staff analysis adopted by the Commission on the proposed parameters and guidelines (adopted July 27, 2000) that states:

Government Code section 3303, subdivision (a), addresses only the compensation and timing of the interrogation. It does not require local agencies to investigate the allegation, prepare for the interrogation, conduct the interrogation, and review the responses given by the officers and/or witnesses as implied by the claimant's proposed language. Certainly, local agencies were performing these investigative activities before POBAR [sic] was enacted.

Based on the foregoing, staff has modified Section IV (C) as follows:

~~1. Conducting an interrogation of a peace officer while the officer is on duty or compensating~~

When required by the seriousness of investigation, compensating the peace officer for interrogations occurring during off-duty time in accordance with regular department procedures. (Gov. Code section 3303, subd. (a).)³¹

The Controller further notes that the Commission revisited this issue in its analysis of the request to amend the parameters and guidelines (amended Dec. 4, 2006). The Commission's final staff analysis states:

The County of San Bernardino, the City of Sacramento, and the City of Los Angeles contend that investigation costs and the cost to conduct the interrogation are reimbursable.

²⁸ *Id.*, page 12.

²⁹ Exhibit B, Controller's Late Comments on the IRC, page 18.

³⁰ *Id.* pages 18 and 39 (Statement of Decision CSM-4499, adopted Nov. 30, 1999, p. 12).

³¹ Exhibit B, Controller's Late Comments on the IRC, pages 19 and 180 (Final Staff Analysis on Proposed Parameters and Guidelines, adopted July 27, 2000).

However ... the Commission has already rejected the arguments raised by the County and Cities for reimbursement of investigation costs and the cost to conduct the interrogation.³²

The Controller concludes that to state interrogations conducted during an officer's regular on-duty time is reimbursable is "contrary to the preponderance of evidence found in the administrative record" for this mandated program.

The Controller also disagrees with the claimant's position that its "adverse comment" activities are reimbursable. The activities denied for reimbursement were part of the city's investigatory process. The Controller responds to the claimant's argument that the parameters and guidelines are not consistent with the original *POBOR* Statement of Decision by noting that:

This analysis was addressed above for costs claimed under the Interrogations cost component and was pled by the test claimant for activities appearing in Government Code section 3303, subdivision (a). The costs for Adverse Comment were pled by the test claimant for activities appearing in Government Code sections 3305 and 3306. Accordingly, costs claimed under the Adverse Comment cost component have no relevance to costs claimed under the Interrogations cost component. The city's position is an expanded interpretation of the language in the parameters and guidelines that is taken out of context. The costs for conducting investigations were never included in the Adverse Comment cost component as reimbursable activities.³³

The Controller filed comments concurring with the Draft Proposed Decision on March 28, 2016.³⁴

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 the local agency or school district. If the Commission determines that a reimbursement claim has been incorrectly reduced, section 1185.9 of the Commission's regulations requires the Commission to send the 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

³² Exhibit B, Controller's Late Comments on the IRC, pages 19 and 207 (Final Staff Analysis on Proposed Parameters and Guidelines, adopted Dec. 4, 2006, p. 22).

³³ Exhibit B, Controller's Late Comments on the IRC, pages 22-23.

³⁴ Exhibit D, Controller's Comments on the Draft Proposed Decision.

over the existence of state-mandated programs within the meaning of article XIII B, section 6.³⁵ 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.”³⁶

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.³⁷ Under this standard, the courts have found that:

When reviewing the exercise of discretion, “[t]he scope of review is limited, out of deference to the agency’s authority and presumed expertise: ‘The court may not reweigh the evidence or substitute its judgment for that of the agency. [Citation.]’” ... “In general ... the inquiry is limited to whether the decision was arbitrary, capricious, or entirely lacking in evidentiary support. . . .” [Citations.] When making that inquiry, the “ ‘court must ensure that an agency has adequately considered all relevant factors, and has demonstrated a rational connection between those factors, the choice made, and the purposes of the enabling statute.’” [Citation.]”³⁸

The Commission must review the Controller’s audit in light of the fact that the initial burden of providing evidence for a claim of reimbursement lies with the claimant.³⁹ In addition, sections 1185.1(f)(3) and 1185.2(c) of the Commission’s regulations require that any assertions of fact by the parties to an IRC must be supported by documentary evidence. The Commission’s ultimate findings of fact must be supported by substantial evidence in the record.⁴⁰

³⁵ Government Code sections 17551, 17552; *Kinlaw v. State of California* (1991) 54 Cal.3d 326, 331-334.

³⁶ *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.

³⁷ *Johnston v. Sonoma County Agricultural Preservation and Open Space District* (2002) 100 Cal.App.4th 973, 983-984; *American Bd. of Cosmetic Surgery, Inc. v. Medical Bd. of California* (2008) 162 Cal.App.4th 534, 547.

³⁸ *American Bd. of Cosmetic Surgery, Inc. v. Medical Bd. of California* (2008) 162 Cal.App.4th 534, 547-548.

³⁹ *Gilbert v. City of Sunnyvale* (2005) 130 Cal.App.4th 1264, 1274-1275.

⁴⁰ 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 Reduction of Costs Claimed for Salaries, Benefits, and Related Indirect Costs in Audit Finding 1 Are Correct as a Matter of Law, and Not Arbitrary, Capricious, or Entirely Lacking in Evidentiary Support.

The Commission first adopted parameters and guidelines for the *POBOR* mandate on July 27, 2000,⁴¹ which were amended in accordance with legislative direction following the Commission's reconsideration of the program on December 4, 2006, with reimbursement beginning July 1, 2006.⁴² The parameters and guidelines, adopted July 27, 2000, are applicable to the audit of the 2003-2004 through 2005-2006 reimbursement claims.⁴³ The parameters and guidelines as amended on December 4, 2006 (effective July 1, 2006) apply to the 2006-2007 and 2007-2008 reimbursement claims.

As defined by Government Code section 17557 and the Commission's regulations, the parameters and guidelines identify the activities the Commission finds to be mandated by the state, and additional activities proposed by the claimant that the Commission finds and approves, based on substantial evidence in the record, to be reasonably necessary to comply with the state-mandated program.⁴⁴ Parameters and guidelines are regulatory in nature and are interpreted the same as regulations and statutes.⁴⁵ Interpretation of an administrative agency's rule, including the Commission's parameters and guidelines, is a question of law.⁴⁶

Under the rules of interpretation, when the language of an administrative agency's rule, such as the parameters and guidelines, is plain, the provisions are required to be enforced according to the terms of the document. The California Supreme Court determined that:

In statutory construction cases, our fundamental task is to ascertain the intent of the lawmakers so as to effectuate the purpose of the statute. We begin by examining the statutory language, giving the words their usual and ordinary meaning. If the terms of the statute are unambiguous, we presume the lawmakers meant what they said, and the plain meaning of the language governs. [Citations omitted.]⁴⁷

⁴¹ Exhibit B, Controller's Late Comments on the IRC, page 169 (Final Staff Analysis on Proposed Parameters and Guidelines, adopted July 27, 2000).

⁴² *Id.*, pages 188, 236 (Final Staff Analysis on Requests to Amend Parameters and Guidelines, adopted December 4, 2006).

⁴³ These parameters and guidelines were in effect when the costs were incurred. (*Clovis Unified School Dist. v. Chiang* (2010) 188 Cal.App.4th 794, 809, fn. 5.)

⁴⁴ Government Code sections 17557 and 17559; California Code of Regulations, title 2, section 1183.7; Former California Code of Regulations, title 2, section 1183.1 (Register 96, No. 30).

⁴⁵ *Clovis Unified School Dist. v. Chiang* (2010) 188 Cal.App.4th 794, 799.

⁴⁶ *Culligan Water Conditioning v. State Board of Equalization* (1976) 17 Cal.3d 86, 93; see also, *County of San Diego v. State* (1997) 15 Cal.4th 68, 81; 109, where the court held that the determination whether reimbursement is required by article XIII B, section 6 is a question of law.

⁴⁷ *Estate of Griswold* (2001) 25 Cal.4th 904, 910-911.

The language of the parameters and guidelines must be construed in the context of the Commission's decisions and adopted analyses on the test claim and parameters and guidelines, so that every provision may be harmonized and have effect.⁴⁸ Under these rules, plain provisions of the administrative rule may not be disregarded or enlarged, nor may the interpretation go beyond the meaning of the words used when the words are clear and unambiguous. Thus, the parties are prohibited from writing into an administrative rule, by implication, express requirements that are not there.⁴⁹ The Commission's decisions on test claims and parameters and guidelines are quasi-judicial decisions that are binding on the parties.⁵⁰

Moreover, later clarification of existing law, including the Commission's decisions on reconsideration of this program, which clarified its original decision regarding the scope of the mandated activities, may be applied to reimbursement claims for costs that predate the 2006 parameters and guidelines amendment. This is because the Commission's clarification is not considered a retroactive application of a new rule, but is merely a statement of what the law has always been from the time it was enacted.⁵¹ Accordingly, the later decision adopted by the Commission on reconsideration may be used to aid in understanding the original parameters and guidelines.

Finding 1 of the audit report includes reductions in salaries and benefits for activities that the Controller determined were beyond the scope of the mandate. The reductions include activities and related indirect costs in the categories (as articulated in the parameters and guidelines) of administrative activities; interrogation; and adverse comment. The Commission finds that the audit reductions are correct as a matter of law, and not arbitrary, capricious, or entirely lacking in evidentiary support.

⁴⁸ *City of Merced v. State of California* (1984) 153 Cal.App.3d 777, 781-782; see also, Government Code sections 17514 (defining "costs mandated by the state"), 17550 (providing that "reimbursement ... for costs mandated by the state shall be provided pursuant to this chapter"), 17551 (requiring the Commission to hear and decide a claim that a local agency is entitled to be reimbursed by the state for costs mandated by the state as required by article XIII B, section 6 of the California Constitution), 17552 (providing that this chapter shall be the sole and exclusive procedure by which a local agency may claim reimbursement for costs mandated by the state), 17557 (governing the adoption of parameters and guidelines after the Commission determines there are costs mandated by the state), and 17558 (providing that the Controller's claiming instructions must be derived from the Commission's test claim decision and adopted parameters and guidelines).

⁴⁹ *Whitcomb v. California Employment Commission* (1944) 24 Cal.2d 753, 757.

⁵⁰ *California School Boards Assoc. v. State of California* (2009) 171 Cal.App.4th 1183, 1200, which states: "[U]nless a party to a quasi-judicial proceeding challenges the agency's adverse findings made in that proceeding, by means of a mandate action in superior court, those findings are binding in later civil actions." [Citation omitted.]

⁵¹ *McClung v. Employment Development Dept.* (2004) 34 Cal.4th 467, 471.

- A. The Controller's reduction of costs claimed for administrative expenses is correct as a matter of law, and not arbitrary, capricious, or entirely lacking in evidentiary support.

The city claimed \$2,864,828 for nine administrative activities, of which \$2,746,417 was found unallowable in the audit. Based on an examination of the claimant's time study conducted in 2003-2004,⁵² the Controller found only the following two of the nine administrative activities claimed to be reimbursable because they involve updating the status report of the mandate-related activities:

1. **Status:** This activity occurs in the Administrative Records Section (ARS) and involves the time needed to update status changes within POBOR case files. Per LAPD staff, the cases are updated for every activity and/or procedural change.
2. **Assign:** This activity consists solely of updating the database and noting the case assignment to an investigator for adjudication.⁵³

The Controller also found that the following seven claimed activities are not reimbursable because they involve managing case files for investigations and disciplinary cases:

3. **Comment:** The ARS section in Internal Affairs performs this task by creating a file and a case number when the Professional Standards Bureau receives a "1.28" complaint form. Per LAPD staff, this activity is an internal procedure created by LAPD to ensure compliance with the investigation time frame of one year.
4. **Locate:** This activity denotes the time required for the Classification Unit to read the "1.28" (complaint form) and determine the best entity to perform the investigation. After determining which entity will investigate, the form is sent to the ARS.
5. **Invest:** When the investigation is complete, the case file is sent to the Review and Evaluation Section. This activity consists of updating the database to note this information.
6. **IA Review:** This activity consists of the time it takes to update the database for Internal Affairs' (IAG) review. Per LAPD staff, this activity is similar to Invest, but one IAG section or division will review the investigation of another IAG investigation unit for thoroughness, facts, results, and conclusions. It is another type of review and another change in status.
7. **Appeal:** This activity takes place when the case is going to the Advocate Section, where another file is created and entered into the Advocate Database. Per LAPD staff, the case is in the appeal phase and is no longer being investigated or reviewed. This activity pertains to the procedural process of transferring a case in the Advocate Unit, tracking the appeal process, and tracking where the case is.
8. **Note:** This activity consists of distributing copies of the face sheet (which contains the summary of allegations and the names of the involved parties) to concerned parties. This

⁵² Exhibit B, Controller's Late Comments on the IRC, page 11.

⁵³ Exhibit A, IRC, pages 4-5, also in Exhibit A, IRC, page 83 (final audit report).

activity occurs in the ARS and is based on the time it takes to update the database for the activity.

9. **Close out:** The ARS closes out the case file and documents this activity. This activity is a database update function.⁵⁴

The Controller states that the parameters and guidelines do not authorize reimbursement for activities related to managing case files and that the denied activities listed above fall into that category. The Controller argues that the parameters and guidelines only allow reimbursement for those activities that relate to updating the status report of the mandate-related activities.⁵⁵

The claimant argues that the seven activities denied for reimbursement are necessary to carry out the administrative activities associated with the mandate:

The City finds the SCO has incorrectly interpreted the parameters and guidelines and statement of decision for the POBOR program. Their extremely narrow and limited interpretation has resulted in the disallowance of nearly 95% of the costs. The City does not agree with the SCO's interpretation of what is necessary to comply with the constitutional "due process" activities afforded all government employees and what additional activities are imposed on peace officers by the POBOR mandate. The City asserts that all seven [disallowed] activities are necessary for a local agency the size and complexity of the Los Angeles Police Department to carry out the administrative activities associated with the mandate.⁵⁶

As originally adopted in July 2000, section IV.A of the parameters and guidelines provides reimbursement for the following administrative activities:

A. Administrative Activities (On-going Activities)

1. Developing or updating internal policies, procedures, manuals and other materials pertaining to the conduct of the mandated activities
2. Attendance at specific training for human resources, law enforcement and legal counsel regarding the requirements of the mandate.
3. Updating the status of the POBAR cases.⁵⁷

The analysis for the parameters and guidelines adopted by the Commission on July 27, 2000, considered a request by the test claimant to authorize reimbursement for "maintenance of the systems to conduct the mandated activities" as a reasonably necessary activity. The Commission denied the request because the activity was too broad and local agencies were maintaining files

⁵⁴ Exhibit A, IRC, pages 4-5, also in Exhibit A, IRC, page 83 (final audit report); Exhibit B, Controller's Late Comments on the IRC, pages 100-167 (Tab 7 Analysis of Claimed Activities).

⁵⁵ Exhibit B, Controller's Late Comments on the IRC, page 12.

⁵⁶ Exhibit A, IRC, page 5.

⁵⁷ Exhibit B, Controller's Late Comments on the IRC, page 60 (Parameters and Guidelines, corrected Aug. 17, 2000).

on peace officer investigations and disciplinary actions before the enactment of the test claim statutes:

The Department of Finance states that the component “maintenance of the systems to conduct the mandated activities” is too ambiguous. Staff agrees.

Before the test claim legislation was enacted, local law enforcement agencies were conducting investigations, issuing disciplinary actions, and *maintaining* files for those cases Accordingly, staff has modified this component to provide that claimants are eligible for reimbursement for “updating the status report of the POBAR cases.”⁵⁸

The Commission’s adopted decision on the parameters and guidelines reflects its consideration that prior to the *POBOR* mandate, local agencies were already investigating complaints, disciplining peace officer employees, and maintaining case files for those investigations and disciplinary actions.⁵⁹ Thus, the reimbursable activity to update the status of the *POBOR* cases is limited to updating the status of the new procedural requirements mandated by the state.

This interpretation is reinforced by the Commission’s clarification of this activity when it amended the parameters and guidelines on December 4, 2006, as follows (with changes in strikeout and underline):

Updating the status report of mandate-reimbursable POBOR cases activities. “Updating the status report of mandate-reimbursable POBOR activities” means tracking the procedural status of the mandate-reimbursable activities only. Reimbursement is not required to maintain or update the cases, set up the cases, review the cases, evaluate the cases, or close the cases.⁶⁰

Section IV.C. of the parameters and guidelines, as amended on December 4, 2006, further provides:

The following activities are **not** reimbursable:

Activities occurring before the assignment of the case to an administrative investigator. These activities include taking an initial complaint, setting up the

⁵⁸ Exhibit B, Controller’s Late Comments on the IRC, page 169 (Final Staff Analysis on Proposed Parameters and Guidelines, adopted July 27, 2000, emphasis in original).

⁵⁹ See Exhibit B, Controller’s Late Comments on the IRC, page 180. (In the Final Staff Analysis on Proposed Parameters and Guidelines, adopted July 27, 2000, p. 16, it was noted that: “Government Code section 3303, subdivision (a), addresses only the compensation and timing of the interrogation. It does not require local agencies to investigate an allegation, prepare for the interrogation, conduct the interrogation, and review the responses given by the officers and/or witnesses, as implied by the claimant’s proposed language. Certainly, local agencies were performing these investigative activities before POBAR [sic] was enacted.”)

⁶⁰ Exhibit B, Controller’s Late Comments on the IRC, page 72 (adopted Parameters and Guidelines Amendment, December 6, 2006, p. 4).

complaint file, interviewing parties, reviewing the file, and determining whether the complaint warrants an administrative investigation.⁶¹

As indicated above, the Commission's amendment to the parameters and guidelines is a clarification of what the law has always been from the time it was enacted.⁶²

In this case, the costs claimed include those to create a file when a complaint form is received, read the complaint and determine the best entity to investigate, update the file when the investigation is complete, update the file when the Internal Affairs Unit reviews the investigation, update the file when the matter is transferred to the Advocate Unit for disciplinary action, distribute copies of the summary of allegations and names of the parties involved, and close the file when the disciplinary action is complete. None of these activities are mandated by the state. Nor have these activities been approved by the Commission as eligible for reimbursement. As indicated above, the parties are prohibited from writing into the parameters and guidelines, by implication, express requirements that are not there.⁶³ In fact, the Commission specifically held that activities to take an initial complaint, set up a complaint file, interview and investigate the facts, and review the file are *not* reimbursable. The Commission's decisions on parameters and guidelines are quasi-judicial and are binding on the parties.⁶⁴

In addition, one of the activities denied in the audit was "**Comment:** . . . creating a file and a case number when the Professional Standards Bureau receives a "1.28" complaint form. Per LAPD staff, this activity is an internal procedure created by LAPD *to ensure compliance with the investigation time frame of one year.*"⁶⁵ Ensuring timely completion of the investigation, however, was considered by the Commission upon the request of a city when the parameters and guidelines were amended on December 4, 2006. The Commission expressly rejected this activity because the statute that imposes the time limit was not pled in the test claim. In dismissing the objections, the Commission said:

Staff finds that the City's comments go beyond the scope of the test claim statutes and are not consistent with the Commission's findings in the Statement of Decision on reconsideration. As indicated in footnote 5, page 6 of the Commission's Statement of Decision on reconsideration (05-RL-4499-01), the POBOR Act has been subsequently amended by the Legislature. One of those amendments imposed the time limitations described by the City. [Stats. 1997, ch. 148.] The subsequent amendments were not pled in this test claim and, thus, they were not analyzed to determine whether they impose reimbursable state-mandated activities within the meaning of article XIII B, section 6. The City's arguments relating to the time limitations imposed by subsequent legislation are outside the

⁶¹ Exhibit B, Controller's Late Comments on the IRC, page 76 (adopted Parameters and Guidelines Amendment, December 6, 2006, p. 8).

⁶² *McClung v. Employment Development Dept.* (2004) 34 Cal.4th 467, 471.

⁶³ *Whitcomb v. California Employment Commission* (1944) 24 Cal.2d 753, 757.

⁶⁴ *California School Boards Assoc. v. State of California* (2009) 171 Cal.App.4th 1183, 1200.

⁶⁵ Exhibit A, IRC, pages 4-5, also in Exhibit A, IRC, page 83 (final audit report, emphasis added).

scope of the Commission's decision in POBOR (CSM 4499). Thus, the City's rationale is not consistent with the Commission's findings.⁶⁶

Thus, the activities identified by the claimant to support its time study exceed the scope of the mandated program. Moreover, as indicated by the Controller, the claimant has not provided any information or evidence to show that these activities fall within the scope of the mandate to update the status report of the mandate-related activities only.⁶⁷ In addition, there is no evidence in the record that the Controller's calculation of the costs reduced from the claimant's time study is arbitrary, capricious, or entirely lacking in evidentiary support.

Therefore, the Commission finds that the Controller's reduction of costs for administrative expenses is correct as a matter of law and not arbitrary, capricious, or entirely lacking in evidentiary support.

B. The Controller's reduction of costs claimed for interrogation expenses is correct as a matter of law, and not arbitrary, capricious, or entirely lacking in evidentiary support.

The city claimed \$12,505,118 for interrogations, of which \$11,289,312 was found unallowable in the audit. The city claimed the following 15 activities under the interrogations category:

1. Admin task (Administrative Task)
2. Call out
3. CO Contact (Commanding Officer Contact)
4. Evidence Collect
5. Interview in person
6. Interview Telephone
7. Kickback Editing
8. Mcct/Brief/Notify
9. Non-Evidence Task
10. Paraphrasing
11. Prep for Interview
12. Report Formatting
13. Telephone Contact
14. Travel
15. VI Computer Task⁶⁸

According to the audit:

The city did not provide a formal description of these activities. LAPD staff stated that these activities involved time for conducting investigations, collecting

⁶⁶ Exhibit A, IRC, page 93 (final audit report). Exhibit B, Controller's Late Comments on the IRC, page 200 (Final Staff Analysis on Requests to Amend Parameters and Guidelines, adopted December 4, 2006, p. 15).

⁶⁷ Exhibit B, Controller's Late Comments on the IRC, page 13.

⁶⁸ Exhibit A, IRC, page 84 (final audit report).

evidence, writing reports, and editing reports. We determined that these activities are unallowable because they relate to the investigation process.⁶⁹

The Controller states, however, that these 15 activities were not included in the documents supporting the time study the claimant used to calculate costs. Instead, the claimant's time study was based on the following activities, none of which were actually included in the reimbursement claims: conducting the interrogations usually during normal working hours; providing notice to the officer regarding the nature of the interrogation and identification of the investigating officer; determining who the investigating officer will be; tape recording the interrogation; and booking the tape at the Scientific Investigations Division.⁷⁰ The Controller agrees that some of the unclaimed activities that supported the time study are eligible for reimbursement (i.e., notice and tape recording when the person being interrogated requests the recording, and booking or storing the tape),⁷¹ but it is not clear from the record how the Controller calculated the reduction of costs.⁷²

The claimant challenges neither the calculation of the partial reduction of costs claimed, nor the Controller's characterization that the 15 claimed activities consisting of conducting investigations, collecting evidence, writing reports, and editing reports. Instead, claimant argues that the entire reduction is incorrect because the Commission's original *POBOR* Statement of Decision on the test claim found that eligible costs included: "Conducting the investigation when the peace officer is on duty, *and* compensating the peace officer for off-duty overtime in accordance with regular department procedures are new requirements not previously imposed on local agencies or school districts." The claimant "believes the costs for conducting interrogations during regular work time is reimbursable, as is preparation for those interrogations" and argues that the Controller's interpretation of the parameters and guidelines is inconsistent with the statement of decision. According to the claimant, "the Statement of Decision is given deference when there is a discrepancy between the finding of a judicial body and the documents that arise from that finding."⁷³

The Commission finds that the claimant's interpretation of the test claim statement of decision and parameters and guidelines is wrong. The Commission did not approve for reimbursement the activities of conducting an investigation, collecting evidence, writing reports, editing reports, preparing for the interrogation, or conducting the interrogation. As shown below, these activities were expressly denied by the Commission.

In the statement of decision on the test claim, the Commission found that Government Code section 3303(a) establishes procedures for the timing and compensation of a peace officer subject

⁶⁹ *Ibid*; see also, Exhibit B, Controller's Late Comments on the IRC, pages 100-163 (Tab 7 Analysis of Claimed Activities).

⁷⁰ Exhibit A, IRC, page 85 (final audit report).

⁷¹ Exhibit B, Controller's Late Comments on the IRC, pages 61-62 (Parameters and Guidelines, corrected August 17, 2000).

⁷² Exhibit B, Controller's Late Comments on the IRC, pages 100-163 (Tab 7 Analysis of Claimed Activities).

⁷³ Exhibit A, IRC, page 7.

to interrogation by an employer. If the interrogation takes place during the officer's off-duty hours because of the seriousness of the investigation, then reimbursement was approved for compensating the officer for off-duty time in accordance with regular department procedures.⁷⁴ When adopting the parameters and guidelines in July 2000, the Commission adopted the following staff recommendation that Government Code section 3303 does not require local agencies to investigate, prepare for the interrogation, conduct the interrogation, or review the responses:

Staff finds that the activity to review the necessity for the questioning and responses given is too broad and goes beyond the scope of Government Code section 3303, subdivision (a), and the Commission's Statement of Decision.

Government Code section 3303, subdivision (a), addresses only the compensation and timing of the interrogation. It does not require local agencies to investigate the allegation, prepare for the interrogation, conduct the interrogation, and review the responses given by the officers and/or witnesses as implied by the claimant's proposed language. Certainly, local agencies were performing these investigative activities before POBAR [sic] was enacted.⁷⁵

There is no conflict between the analysis adopted by the Commission for the parameters and guidelines and the statement of decision adopted by the Commission on the test claim, as asserted by the claimant. Both clearly state that Government Code section 3303(a) only affects the timing of an interrogation and compensation required if the interrogation occurred during off-duty hours. Thus, the parameters and guidelines authorize reimbursement for "compensating a peace officer for interrogations occurring during off-duty time in accordance with regular department procedures" when required by the seriousness of the investigation.⁷⁶ The state, however, has not mandated local agencies to investigate, interrogate, or review interrogation responses. As explained by the courts, POBOR deals with labor relations. It does not interfere with the employer's existing right to manage and control its own police department.⁷⁷

When the Commission adopted the April 26, 2006 *POBOR* Statement of Decision on Reconsideration, it clarified its earlier findings that activities to investigate, prepare for the interrogation, conduct the interrogation, and "review responses given by officers and/or witnesses" to an investigation are not reimbursable:

In comments to the draft staff analysis, the Counties of Orange, Los Angeles, and Alameda, and the City of Sacramento contend that the interrogation of an officer pursuant to the test claim legislation is complicated and requires the employer to

⁷⁴ Exhibit B, Controller's Late Comments on the IRC, page 39 (Statement of Decision adopted November 30, 1999).

⁷⁵ Exhibit B, Controller's Late Comments on the IRC, page 180 (Final Staff Analysis on the Proposed Parameters and Guidelines, July 27, 2000).

⁷⁶ Exhibit B, Controller's Late Comments on the IRC, page 61 (Parameters and Guidelines, corrected Aug. 17, 2000).

⁷⁷ *Sulier v. State Personnel Bd.* (2004) 125 Cal.App.4th 21, 26; *Baggett v. Gates* (1982) 32 Cal.3d 128, 135.

fully investigate in order to prepare for the interrogation. The County of Orange further states that “[t]hese investigations can vary in scope and depth from abuses of authority, the use of deadly force, excessive force when injuries may be significant, serious property damage, and criminal behavior.” These local agencies are requesting reimbursement for the time to investigate.

The Commission disagrees and finds that investigation services are not reimbursable. First, investigation of criminal behavior is specifically excluded from the requirements of Government Code section 3303. Government Code section 3303, subdivision (i), states that the interrogation requirements do not apply to an investigation concerned solely and directly with alleged criminal activities. Moreover, article XIII B, section 6, subdivision (a)(2), and Government Code section 17556, subdivision (g), state that no reimbursement is required for the enforcement of a crime.

The County of Los Angeles supports the argument that reimbursement for investigative services is required by citing Penal Code section 832.5, which states that each department that employs peace officers shall establish a procedure to investigate complaints. Penal Code section 832.5, however, was not included in this test claim, and the Commission makes no findings on that statute. The County of Los Angeles also cites to the phrase in Government Code section 3303, subdivision (a), which states that “[t]he interrogation shall be conducted ...” to argue that investigation is required. The County takes the phrase out of context. Government Code section 3303, subdivision (a), states the following:

The interrogation shall be conducted at a reasonable hour, preferably at a time when the public safety officer is on duty, or during the normal waking hours for the public safety officer, unless the seriousness of the investigation requires otherwise. If the interrogation does occur during off-duty time of the public safety officer being interrogated, the public safety officer shall be compensated for any off-duty time in accordance with regular department procedures, and the public safety officer shall not be released from employment for any work missed.

Government Code section 3303, subdivision (a), establishes the timing of the interrogation, and requires the employer to compensate the interrogated officer if the interrogation takes place during off-duty time. In other words, the statute defines the process that is due the peace officer who is subject to an interrogation. This statute does not require the employer to investigate complaints. When adopting parameters and guidelines for this program, the Commission recognized that Government Code section 3303 does not impose new mandated requirements to investigate an allegation, prepare for the interrogation, conduct the interrogation, and review responses given by officers and/or witnesses to an investigation. [Citing to Analysis adopted by the Commission on Parameters and Guidelines, July 22, 2000.]

Thus, investigation services go beyond the scope of the test claim legislation and are *not* reimbursable. As explained by the courts, POBOR deals with labor

relations. [Citing *Sulier v. State Personnel Bd.* (2004) 125 Cal.App.4th 21, 26.] It does not interfere with the employer's right to manage and control its own police department. [Citing *Baggett v. Gates* (1982) 32 Cal.3d 12832 Cal.3d 128, 135.]⁷⁸

When the parameters and guidelines were amended in December 2006, the Commission again rejected reimbursement for investigatory costs:

The County of San Bernardino, the City of Sacramento, and the City of Los Angeles contend that investigation costs and the cost to conduct the interrogation are reimbursable.

However, . . . the Commission has already rejected the arguments raised by the County and Cities for reimbursement of investigation costs and the cost to conduct the interrogation.⁷⁹

The *POBOR* Parameters and Guidelines on Reconsideration clearly state these findings by clarifying the activities that are not reimbursable:

1. Activities occurring before the assignment of the case to an administrative investigator. These activities include taking an initial complaint, setting up the complaint file, interviewing parties, reviewing the file, and determining whether the complaint warrants an administrative investigation.
2. Investigation activities, including assigning an investigator to the case, reviewing the allegation, communicating with other departments, visiting the scene of the alleged incident, gathering evidence, identifying and contacting complainants and witnesses.
3. Preparing for the interrogation, reviewing and preparing interrogation questions, conducting the interrogation, and reviewing the responses given by the officer and/or witness during the interrogation.
4. Closing the file, including the preparation of a case summary disposition reports and attending executive review or committee hearings related to the investigation.⁸⁰

Therefore, the Controller's reduction of costs claimed to conduct investigations, conduct interrogations, collect evidence, write reports, and edit reports is correct as a matter of law. Moreover, there is no evidence in the record that the Controller's calculation of the costs reduced from the claimant's time study is arbitrary, capricious, or entirely lacking in evidentiary support.

Accordingly, the Controller's reduction of costs claimed for interrogations is correct as a matter of law and not arbitrary, capricious, or entirely lacking in evidentiary support.

⁷⁸ Exhibit A, IRC, pages 64-65 (Statement of Decision on Reconsideration, 05-RL-4499-01, April 26, 2006, emphasis in original).

⁷⁹ Exhibit B, Controller's Late Comments on the IRC, page 207 (Final Staff Analysis on Requests to Amend Parameters and Guidelines, adopted December 4, 2006).

⁸⁰ Exhibit B, Controller's Late Comments on the IRC, page 76 (Parameters and Guidelines, amended December 4, 2006).

C. The Controller's reduction of costs claimed for adverse comment expenses is correct as a matter of law, and not arbitrary, capricious, or entirely lacking in evidentiary support.

The city claimed \$20,278,116 in salaries and benefits for the adverse comment component during the audit period, of which \$7,428,740 (plus indirect costs) was found unallowable because the activities claimed were beyond the scope of the reimbursable mandate.⁸¹ Of the 16 activities claimed under this component, the Controller found that the following five are not reimbursable because they are part of the investigative process:

Preliminary: This activity involves investigating the circumstances surrounding the adverse comment.

Collect: This activity consists of the preliminary investigation conducted by supervisors, detectives, and the command staff in the area where the complaint was taken. This activity can include report writing, interviews, or any activity where information is gathered for the "1.28" (complaint form).

Area invest: This activity consists of the time spent by an Area to investigate the complaint or "1.28" (complaint form). This activity occurs after the preliminary investigation.

Inspect: This activity occurs when the assigned advocate reviews the investigation for status and thoroughness.

RE invest: This activity involves the time needed to conduct any additional investigations.⁸²

All versions of the parameters and guidelines, under the component of adverse comment, separately list the reimbursable activities for school districts, counties, and cities and special districts, respectively.⁸³ For purposes of this IRC, only the reimbursable activities provided for cities are relevant. The parameters and guidelines provide three conditional statements, pertaining to the potential consequences of the adverse comment, and provide for different reimbursable activities in each case, depending on the existing requirements of due process or other law that are not reimbursable under the test claim decision:

- If an adverse comment results in dismissal, suspension, demotion, reduction in pay, or written reprimand for a permanent employee peace officer, or harms the officer's reputation and opportunity to find future employment, then cities and special districts are entitled to reimbursement for obtaining the officer's signature on the adverse comment, or noting the officer's refusal to sign the adverse comment and obtaining the signature or initials of the officer.
- If an adverse comment is related to a possible criminal offense, cities are entitled to reimbursement for providing notice of the adverse comment; providing an opportunity to review and sign the adverse comment; providing an opportunity to respond within 30

⁸¹ Exhibit A, IRC, page 86 (final audit report).

⁸² Exhibit A, IRC, page 87 (final audit report).

⁸³ For example, see Exhibit B, Controller's Late Comments on the IRC, pages 76-77 (Parameters and Guidelines, amended December 4, 2006).

days; and noting an officer's refusal to sign and obtaining a signature or initials under such circumstances.

- If an adverse comment is not related to a possible criminal offense, cities are entitled to reimbursement for providing notice of the adverse comment; providing an opportunity to respond within 30 days; obtaining the signature of the officer; or noting the officer's refusal to sign and obtaining a signature or initials.⁸⁴

The parameters and guidelines also authorize reimbursement for the following activities found to be reasonably necessary to comply with the mandates associated with adverse comments:

Included in the foregoing are review of circumstances or documentation leading to adverse comment by supervisor, command staff, human resources staff or counsel, including determination of whether same constitutes an adverse comment; preparation of comment and review for accuracy; notification and presentation of adverse comment to officer and notification concerning rights regarding same; review of response to adverse comment, attaching same to adverse comment and filing.⁸⁵

However, as discussed throughout this analysis, the reimbursable activities pertaining to an adverse comment do not include investigative activities, including reviewing a complaint to determine whether and to what extent to investigate.⁸⁶

The Controller has disallowed costs for activities that involve the investigation surrounding an adverse comment, and not to obtaining a signature, or acknowledging a refusal to sign. As noted above, the parameters and guidelines do state that "review of circumstances or documentation ... including determination of whether same constitutes an adverse comment,"⁸⁷ is included within the activities stated. If the comment is an adverse comment, the Commission found that the notice requirements of Government Code sections 3305 and 3306 do not constitute a new program or higher level of service under article XIII B, section 6 of the California Constitution.⁸⁸ Thus, the activities to review the circumstances or documentation cannot be read to include the claimed activities of: (1) investigating the circumstances surrounding the adverse comment; (2) the preliminary investigation conducted by supervisors, detectives, and the command staff in the area where the complaint was taken; (3) report writing, interviews; or time spent by the areas to investigate the complaint or "1.28" (complaint form) after the preliminary investigation; (4) when the assigned advocate reviews the investigation for status and thoroughness; or (5) the time

⁸⁴ Exhibit B, Controller's Late Comments on the IRC, pages 64-65 (Parameters and Guidelines, corrected August 17, 2000).

⁸⁵ Exhibit B, Controller's Late Comments on the IRC, page 65 (Parameters and Guidelines, corrected August 17, 2000).

⁸⁶ Exhibit B, Controller's Late Comments on the IRC, page 180 (Final Staff Analysis on the Proposed Parameters and Guidelines, July 27, 2000).

⁸⁷ Exhibit B, Controller's Late Comments on the IRC, page 65 (Parameters and Guidelines, corrected August 17, 2000, pp. 3-8).

⁸⁸ Exhibit A, IRC, pages 46-47 (Statement of Decision, CSM-4499, Nov. 30, 1999, p. 19).

needed to conduct any additional investigation.⁸⁹ These disallowed activities clearly pertain to investigations, which, as stated throughout this analysis, are not a reimbursable activity under the *POBOR* mandate.

The *POBOR* mandate is very narrow, and as determined by the Commission, local law enforcement agencies were conducting investigations and issuing disciplinary actions before the *POBOR* statutes were enacted, so those activities are not reimbursable.⁹⁰ The Commission's *POBOR* Statement of Decision on Reconsideration further clarifies the intended scope of the mandate, especially making clear that the test claim statute does not require an employer to investigate an officer's conduct or place an adverse comment in an officer's personnel file. Because the *POBOR* mandate is about new procedures governing peace officer labor relations, any investigations of misconduct or malfeasance are beyond the scope of the mandate.⁹¹ These decisions are binding on the parties.⁹²

Based on the foregoing, the Commission finds that the Controller's reduction of costs claimed under the adverse comment component are correct as a matter of law because of the claimed investigative activities that are beyond the scope of the mandate. Moreover, there is no evidence in the record that the Controller's calculation of the costs reduced from the claimant's time study is arbitrary, capricious, or entirely lacking in evidentiary support.

V. Conclusion

Based on the foregoing analysis, the Commission finds that the Controller's reductions of costs claimed are correct as a matter of law and not arbitrary, capricious, or entirely lacking in evidentiary support. Therefore, the Commission denies this IRC.

⁸⁹ *Id.*, page 87 (final audit report).

⁹⁰ Exhibit B, Controller's Late Comments on the IRC, page 171 (Final Staff Analysis on Proposed Parameters and Guidelines, adopted July 27, 2000).

⁹¹ Exhibit A, IRC, pages 29, 64-65 (Statement of Decision on Reconsideration, 05-RL-4499-01, April 26, 2006); see also page 41, where the Commission found that:

The [POBOR] rights are not triggered, however, until the employing agency decides to interrogate an officer, take punitive action against the officer, or place an adverse comment in an officer's personnel file. These initial decisions are not mandated by the state, but are governed by local policy, ordinance, city charter, or a memorandum of understanding.

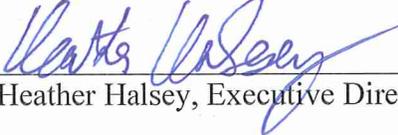
⁹² *California School Boards Assoc. v. State of California* (2009) 171 Cal.App.4th 1183, 1200.



RE: **Decision**

Peace Officers Procedural Bill of Rights, 12-4499-I-02
Government Code Sections 3301, 3303, 3304, 3305, and 3306;
Statutes 1976, Chapter 465; Statutes 1978, Chapters 775, 1173, 1174, and 1178;
Statutes 1979, Chapter 405; Statutes 1980, Chapter 1367; Statutes 1982, Chapter 994;
Statutes 1983, Chapter 964; Statutes 1989, Chapter 1165; Statutes 1990, Chapter 675
Fiscal Years: 2003-2004, 2004-2005, 2005-2006, 2006-2007, and 2007-2008
City of Los Angeles, Claimant

On May 26, 2016, the foregoing decision of the Commission on State Mandates was adopted on the above-entitled matter.



Heather Halsey, Executive Director

Dated: June 1, 2016

BEFORE THE
 COMMISSION ON STATE MANDATES
 STATE OF CALIFORNIA

IN RE INCORRECT REDUCTION CLAIM
 ON:
 Education Code Sections 48209.1, 48209.7,
 48209.9, 48209.10, 48209.13, 48209.14
 Statutes 1993, Chapter 160 (AB 19);
 Statutes 1994, Chapter 1262 (AB 2768)
 Fiscal Year 1997-1998
 Chula Vista Elementary School District,
 Claimant

Case No.: 11-4451-I-05
School District of Choice: Transfers and Appeals
 DECISION PURSUANT TO
 GOVERNMENT CODE SECTION 17500
 ET SEQ.; CALIFORNIA CODE OF
 REGULATIONS, TITLE 2, DIVISION 2,
 CHAPTER 2.5, ARTICLE 7
 (Adopted July 22, 2016)
 (Served July 26, 2016)

DECISION

The Commission on State Mandates (Commission) heard and decided this Incorrect Reduction Claim (IRC) during a regularly scheduled hearing on July 22, 2016. Jay Lal and Gwendolyn Carlos appeared on behalf of the State Controller’s Office. The Chula Vista Elementary School District did not appear, but filed a letter indicating that it would stand on its written submission for the record.

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

The Commission adopted the Proposed Decision to approve the IRC at the hearing by a vote of 6-0 as follows:

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

Summary of the Findings

This IRC challenges the State Controller's (Controller's) finding that the Chula Vista Elementary School District (claimant) claimed unallowable costs of \$25,081 for the *School District of Choice* program for fiscal year 1997-1998. The following issues are addressed:

- Whether the claimant filed the IRC in a timely manner; and
- Whether the Controller initiated the audit in a timely manner.

The Commission finds that the IRC was filed in a timely manner, but there is no evidence in the record that the Controller initiated the audit before the statutory deadline. Therefore, the Commission finds that the Controller's audit is void and the IRC is approved. The Controller is requested, in accordance with Government Code section 17551(d) and section 1185.9 of the Commission's regulations, to reinstate to the claimant all costs incorrectly reduced.

COMMISSION FINDINGS

I. Chronology

12/16/1999	Claimant signed its 1997-1998 reimbursement claim. ¹
01/06/2000	Controller received the 1997-1998 reimbursement claim. ²
04/29/2009	Controller sent claimant a letter with "results of [its] review" for the 1997-1998 reimbursement claim. ³
05/04/2009	Claimant sent an email requesting an explanation of the "Intradistrict Cost Adjustment of 23,884.00." ⁴
06/02/2009	Controller emailed claimant explaining reduction for 1997-1998. ⁵
07/29/2011	Claimant filed this IRC. ⁶
11/01/2011	Controller filed comments on the IRC. ⁷
03/18/2016	Commission staff issued the Draft Proposed Decision. ⁸

¹ Exhibit A, IRC, page 24.

² *Ibid.* This is based on a date-stamp in the upper right corner of the document.

³ Exhibit A, IRC, page 18. Note that Controller alleges that it first sent a letter to claimant on January 15, 2002, see Exhibit B, Controller's Comments on the IRC, page 2, but there is no evidence in the record to support a finding that the letter was received by claimant.

⁴ Exhibit A, IRC, pages 20-21.

⁵ Exhibit A, IRC, page 20.

⁶ Exhibit A, IRC.

⁷ Exhibit B, Controller's Comments on the IRC.

⁸ Exhibit C, Draft Proposed Decision.

- 04/08/2016 Controller requested an extension of time, until May 9, 2016, to file comments on the Draft Proposed Decision, and a postponement of the hearing.
- 04/12/2016 The executive director approved Controller’s request for an extension of time to file comments on the Draft Proposed Decision until April 29, 2016, and for postponement of the hearing from May 26, 2016 until July 22, 2016.
- 05/02/2016 Controller filed late comments on the Draft Proposed Decision.⁹

II. Background

Generally, under California law, each person between the ages of six and 18 years is required to attend school located in the district where the parent or guardian of the pupil resides.¹⁰ In 1993 and 1994, the Legislature enacted statutes authorizing school districts to accept and enroll pupils who do not reside in the district, upon request, to transfer to their “school district of choice.”¹¹ The “*interdistrict*” transfer of pupils is not allowed, however, if the transfer would negatively impact a court-ordered desegregation plan, a voluntary desegregation plan, or the racial and ethnic balance of the either the school district of residence or school district of choice.¹² The statutes also established the right of a parent or guardian of a pupil to appeal any transfer request denial to the county board of education.¹³

In 1995 and 1996, the Commission adopted decisions on two test claims, *School District of Choice* and *Choice Transfer Appeals*, finding that the test claim statutes imposed a partially reimbursable state-mandated program.¹⁴ The Parameters and Guidelines for the *School District of Choice* and *Choice Transfer Appeals* programs were consolidated in July 1996, and the consolidated program was renamed *School District of Choice: Transfers and Appeals*. The Parameters and Guidelines authorize reimbursement for the following activities beginning in 1994:

1) Information Requests

For all school districts to respond to telephone and written inquiries for information regarding alternative pupil attendance choices for its schools, programs, policies and procedures. These costs shall be offset to the extent that fees may be charged pursuant to the California Public Records Act (Government Code section 6250 et seq.).

2) Implementing Pupil Transfers

⁹ Exhibit D, Controller’s Late Comments on the Draft Proposed Decision.

¹⁰ Education Code section 48200.

¹¹ Statutes 1993, chapter 160, adding former Education Code section 48209 et seq., effective January 1, 1994.

¹² Former Education Code section 48209.1(b).

¹³ Former Education Code sections 48209.9(d) (Stats. 1994, ch. 1262, eff. Sept. 30, 1994).

¹⁴ Commission on State Mandates, *School District of Choice* Statement of Decision, CSM-4451, adopted April 28, 1995, and *Choice Transfer Appeals* Statement of Decision, CSM-4476, adopted May 6, 1996.

For school districts of residence to provide the district of choice information regarding the transferring pupil's completed coursework, attendance and other academic progress, and otherwise implement the transfer out of pupils, as well as the return transfer of a pupil whose choice transfer has been revoked by the district of choice as the result of a recommendation for expulsion.

3) Data Collection and Reporting

For school districts of residence to collect data on the number of transfers granted, denied, or withdrawn and annually report these statistics to the district governing board and Superintendent of Public Instruction.

4) Court-ordered Desegregation Plans

For school districts of residence with court-ordered desegregation plans to make a determination of whether the transfer to the school district of choice will negatively impact the plan; and to participate in and respond to a county board of education's appeal process, resulting only from a denied transfer based on the negative impact upon that district's court-ordered desegregation plan.

5) County Office Appeals

All county boards of education shall be reimbursed for the costs incurred to establish an appropriate, non-complex process to hear and decide appeals filed by the parent or guardian of any pupil who has been denied a choice transfer by a district of residence pursuant to section 48209.1 or 48209.7 and to respond to an appeal filed by the parent or guardian of any pupil who has been denied a choice transfer by a district of residence pursuant to section 48209.1 or 48209.7.¹⁵

On September 28, 2002, the Governor signed Statutes 2002, chapter 1032 (AB 3005), an urgency statute that amended the code sections approved in the Test Claim Statement of Decision and that made the program discretionary. On May 27, 2004, the Commission amended the Parameters and Guidelines to end reimbursement for the program, effective September 27, 2002.¹⁶

The Controller's Audit and Reduction of Costs

The Controller conducted a desk review of the claimant's reimbursement claim for costs incurred in fiscal year 1997-1998, and reduced costs claimed by \$25,081, the entire amount claimed. The Controller did not prepare an audit report explaining the reduction. However, the following facts are in the record.

The fiscal year 1997-1998 reimbursement claim was signed by the claimant on December 16, 1999, and claimant states that it submitted the claim to the Controller on or about

¹⁵ Exhibit A, IRC, pages 54-60.

¹⁶ Commission on State Mandates, Amendment to the Parameters and Guidelines, *School District of Choice: Transfers and Appeals*, 02-PGA-05, adopted May 27, 2004.

that date.¹⁷ The claim requested reimbursement of \$25,081, based only on the direct costs of \$23,884 for salaries and benefits of employees performing the first activity, “Information Requests,” and indirect costs of \$1,197.¹⁸ The description of the expenses claimed states:

COSTS OF RESPONDING TO INFORMATION REQUESTS (BOTH ORALLY AND PROVIDING WRITTEN MATERIAL) REGARDING SCHOOLS WITHIN THE DISTRICT, THESE REQUESTS ARE FROM PARENTS WHO ARE CONSIDERING WHETHER TO REQUEST A SCHOOL (OTHER THAN THEIR SCHOOL OF RESIDENCE) UNDER THE ALTERNATIVE ATTENDANCE OPTIONS OF OPEN ENROLLMENT, INTRA-DISTRICT TRANSFER OR INTERDISTRICT TRANSFER.¹⁹

The reimbursement claim is date-stamped January 6, 2000, which the claimant states is the date the Controller received the reimbursement claim.²⁰ The Controller has not disputed this fact.

The Controller states that an “adjustment letter” on letterhead of the State Controller was sent on January 15, 2002, addressed to the claimant at:

Bd of Trustees
Chula Vista Elementary SD
San Diego County
84 East J Street
Chula Vista, CA 91910-6199²¹

This letter states that the 1997-1998 reimbursement claim requesting reimbursement of \$25,081 was adjusted to \$0:

Amount Claimed		25,081.00
Adjustment to Claim:		
Indirect Costs Overstated	1,197.00	
Intradistrict Cost Adjustment	23,884.00	
Less: Total Adjustments		25,081.00
Claim Amount Approved		0.00
Amount Due Claimant		\$ 0.00. ²²

The letter also provides the claimant with the name of the contact person at the Controller’s Office for questions. No other information was provided.

¹⁷ Exhibit A, IRC, pages 5 and 24. The claim in the record appears to have been date-stamped by the Controller on January 6, 2000.

¹⁸ Exhibit A, IRC, pages 24, 26.

¹⁹ Exhibit A, IRC, page 27.

²⁰ Exhibit A, IRC, pages 5 and 24.

²¹ Exhibit B, Controller’s Comments on the IRC, page 2.

²² Exhibit B, Controller’s Comments on the IRC, page 2.

The claimant's IRC does not mention the January 15, 2002 letter. Instead, claimant acknowledges receipt of only one letter from the Controller's Office dated April 29, 2009, as follows:

The District received a 'results of review' letter dated April 29, 2009, reducing its claim as a result of the desk review. This letter constitutes a demand for repayment and adjudication of the claim.²³

The letter, dated April 29, 2009, is on the Controller's letterhead, contains the same address for the claimant as the letter dated January 15, 2002, and provides substantially the same information as the letter allegedly issued on January 15, 2002.²⁴ Unlike the January 15, 2002 letter provided by the Controller with its comments on the IRC, however, the April 29, 2009 letter is date-stamped by the claimant "RECEIVED May 04, 2009, CHULA VISTA ELEM SCH DIST ACCOUNTING DEPT."

On May 4, 2009, the claimant's representative (SixTen and Associates) sent an email to Kim Nguyen of the State Controller's Office asking for an explanation about the adjustment as follows:

Chula Vista Elementary (S37035) received an advisory dated April 29, 2009 regarding the Mandate Claim for Program 156, School District of Choice Chapter 1262/94 for fiscal year 1997/1998. The advisory states "Intradistrict Cost Adjustment" of \$23,884.00. The district has requested that we query the state regarding this adjustment and ask for an explanation. As you are listed as the "contact person" on this advisory, would you please provide us with an explanation of the adjustment?²⁵

Ms. Nguyen of the Controller's Office responded by email on May 4, 2009, advising the claimant's representative to contact Dennis Speciale of the Controller's Office "for assistance tomorrow."²⁶ The claimant's representative then forwarded the emails to Mr. Speciale that same day.²⁷

On June 2, 2009, Mr. Speciale of the Controller's Office emailed the claimant's representative at 11:48 a.m., explaining that the adjustment was based on cost items dealing with "Information Requests" for *intradistrict* transfers, or transfers within the district, which are not eligible for reimbursement under this program. Reimbursement is required only for information requests on *interdistrict* transfers. The email states in relevant part the following:

I will do the best I can to explain the adjustment below.

Referencing:

Chula Vista Elementary (S37035)

²³ Exhibit A, IRC, page 4.

²⁴ Exhibit A, IRC, page 18.

²⁵ Exhibit A, IRC, page 21.

²⁶ *Ibid.*

²⁷ Exhibit A, IRC, page 20.

Program 156, School District of Choice Chapter 1262/94
Fiscal Year: 1997/1998

An adjustment was made, “Intradistrict Cost Adjustment” for \$23,884.00. This adjustment was made specifically for cost items dealing with Information Request. The adjustments criteria are has [sic] follows:

- 1) If a group of cost fall under the description of providing “...information request...” relating to “...*interdistrict district transfer*...” then no adjustments are made to these costs. These are valid costs as they relate to providing interdistrict information requests.
- 2) If a group of cost falls under the description of providing “...information requests...” relating to “...*intradistrict*...” or “...*within the school district*...”, then we will need to remove these cost [sic]. Intradistrict-related cost [sic] are not reimbursable.²⁸

At 1:50 p.m. the same day, the claimant’s representative acknowledged receipt of the Controller’s email.²⁹

On December 15, 2009, claimant’s representative sent an email to Mr. Speciale of the Controller’s Office requesting a copy of the reimbursement claim and annual documents.³⁰ Claimant states that it received the documents on December 16, 2009.³¹

On July 29, 2011, claimant filed this IRC.

III. Positions of the Parties

A. Chula Vista Elementary School District

The claimant argues that the \$25,081 reduced is incorrect and should be reinstated. According to claimant, it received notice of the reduction on April 29, 2009 as a result of a Controller desk audit, but with no explanation of the reason for the reduction.³² The claimant argues that the Controller had two years to audit the reimbursement claim, measured from the date the claim was filed in January 2000, and that an adjustment made in 2009 is too late and beyond the “statute of limitation” provided in Government Code section 17558.5(a).

²⁸ Exhibit A, IRC, page 20. Intradistrict transfers are the subject of a separate mandated program called *Intradistrict Attendance*, CSM 4454, which required school districts to prepare and adopt rules establishing and implementing a policy of open enrollment within the district for residents of the district; establish and operate a random selection process in excess of schoolsite capacity; determine the attendance area capacity of the schools in the district; and evaluate each request for intradistrict attendance for its impact on district racial and ethnic balances.

²⁹ Exhibit A, IRC, pager 20.

³⁰ Exhibit A, IRC, page 22.

³¹ Exhibit A, IRC, page 6.

³² Exhibit A, IRC, page 18.

On the merits, claimant argues that the scope of the activity to provide information is broad, and is not limited to requests for information about interdistrict transfers only. Claimant bases its argument on the plain language of former Education Code section 48209.13, which states the following: “Each school district shall make information regarding its schools, programs, policies, and procedures available to any interested person upon request.” Thus, claimant argues that it properly claimed costs for providing information about intradistrict transfers.

The claimant did not file comments on the Draft Proposed Decision.

B. State Controller’s Office

The Controller argues that the IRC was not timely filed because an adjustment letter dated January 15, 2002, advised claimant of the reduction. Therefore, the IRC filed July 29, 2011, was not filed within the three-year deadline required by the Commission’s regulations.³³

The Controller filed late comments on May 2, 2016, disagreeing with the Draft Proposed Decision and stating that the adjustment letter was sent to the claimant on January 15, 2002. The Controller asserts that adjustment letters were also sent to 509 other school districts on that date for the same program in the same fiscal year. The district’s claim, along with claims of 42 other school districts, was reduced to zero due to adjustments for disallowed costs. The Controller further states that the April 29, 2009 letter was generated as a result of a system error while processing interest payments, and that the letter was sent to claimant and the other 42 districts that had their claims reduced to zero. According to the Controller, of the 43 districts that received the letter, only the claimant alleges that it did not receive the original, January 15, 2002, adjustment letter. The Controller further states that the process for sending adjustment letters non-certified and by U.S. mail has not changed for over a decade and has not resulted in any issues. Thus, the Controller argues that based on the first adjustment letter dated January 15, 2002, claimant should not be able to file an IRC after January 15, 2005.³⁴

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 the local agency or school district. If the Commission determines that a reimbursement claim has been incorrectly reduced, section 1185.9 of the Commission’s regulations requires the Commission to send the 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

³³ Exhibit B, Controller’s Comments on the IRC, pages 1-2.

³⁴ Exhibit D, Controller’s Late Comments on the Draft Proposed Decision.

over the existence of state-mandated programs within the meaning of article XIII B, section 6.³⁵ 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.”³⁶

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.³⁷ Under this standard, the courts have found that:

When reviewing the exercise of discretion, “[t]he scope of review is limited, out of deference to the agency’s authority and presumed expertise: ‘The court may not reweigh the evidence or substitute its judgment for that of the agency. [Citation.]’” ... “In general ... the inquiry is limited to whether the decision was arbitrary, capricious, or entirely lacking in evidentiary support. . . .” [Citations.] When making that inquiry, the “ ‘court must ensure that an agency has adequately considered all relevant factors, and has demonstrated a rational connection between those factors, the choice made, and the purposes of the enabling statute.’ ” [Citation.]”³⁸

The Commission must review the Controller’s audit in light of the fact that the initial burden of providing evidence for a claim of reimbursement lies with the claimant.³⁹ In addition, sections 1185.1(f)(3) and 1185.2(c) of the Commission’s regulations require that any assertions of fact by the parties to an IRC must be supported by documentary evidence. The Commission’s ultimate findings of fact must be supported by substantial evidence in the record.⁴⁰

³⁵ *Kinlaw v. State of California* (1991) 54 Cal.3d 326, 331-334; Government Code sections 17551, 17552.

³⁶ *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.

³⁷ *Johnston v. Sonoma County Agricultural Preservation and Open Space Dist.* (2002) 100 Cal.App.4th 973, 983-984. See also *American Bd. of Cosmetic Surgery, Inc. v. Medical Bd. of California* (supra.) 162 Cal.App.4th 534, 547.

³⁸ *American Bd. of Cosmetic Surgery, Inc. v. Medical Bd. of California* (2008) 162 Cal.App.4th 534, 547-548.

³⁹ *Gilbert v. City of Sunnyvale* (2005) 130 Cal.App.4th 1264, 1274-1275.

⁴⁰ 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.

A. The IRC Was Timely Filed.

The Controller argues that the IRC, filed July 29, 2011, was not filed within the three-year period of limitation in the Commission's regulations based on the adjustment letter dated January 15, 2002.⁴¹

The Commission finds, based on the evidence in the record, that the IRC was timely filed.

Under the statutory mandates scheme, a reimbursement claim filed by a local agency or school district is subject to the initiation of an audit by the Controller within the time periods specified in Government Code section 17558.5(a). 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, and the reason for the adjustment."⁴² 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.

Since 1999, the Commission's regulations have provided a period of limitation for filing an IRC. At the time the reimbursement claim in this case was filed in 2000, former section 1185(b) of the Commission's regulations required IRCs to be "submitted to the Commission no later than three (3) years following the date of the State Controller's remittance advice notifying the claimant of a reduction."⁴³ The period of limitation for filing an IRC is currently in section 1185.1(c), which similarly provides that "[a]ll incorrect reduction claims shall be filed with the Commission no later than three years following the date of the Office of State Controller's final state audit report, letter, remittance advice, or other written notice of adjustment to a reimbursement claim." An IRC is deemed incomplete by Commission staff and returned to the claimant if it is not timely filed.⁴⁴

"Critical to applying a statute of limitations is determining the point when the limitations period begins to run."⁴⁵ Thus, given the multiple documents issued by the Controller in this case, the threshold issue is when the right to file an IRC based on the Controller's reductions accrued, and consequently when the applicable period of limitations began to run against the claimant.

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.⁴⁶ The California Supreme Court has described statutes of limitations as follows:

⁴¹ Exhibit B, Controller's Comments on the IRC, page 1.

⁴² Former Government Code section 17558.5(b) (Stats. 1995, ch. 945, eff. July 1, 1996).

⁴³ Former California Code of Regulations, title 2, section 1185(b) (Register 1999, No. 38, eff. September 13, 1999).

⁴⁴ California Code of Regulations, title 2, sections 1181.2(e), 1185.2.

⁴⁵ *Poosh v. Phillip Morris USA, Inc.* (2011) 51 Cal.4th 788, 797.

⁴⁶ *Addison v. State of California* (1978) 21 Cal.3d 313, 317; *Jordach Enterprises, Inc. v. Brobeck, Phleger & Harrison* (1998) 18 Cal.4th 739, 761.

A statute of limitations strikes a balance among conflicting interests. If it is unfair to bar a plaintiff from recovering on a meritorious claim, it is also unfair to require a defendant to defend against possibly false allegations concerning long-forgotten events, when important evidence may no longer be available. Thus, statutes of limitations are not mere technical defenses, allowing wrongdoers to avoid accountability. Rather, they mark the point where, in the judgment of the legislature, the equities tip in favor of the defendant (who may be innocent of wrongdoing) and against the plaintiff (who failed to take prompt action): “[T]he period allowed for instituting suit inevitably reflects a value judgment concerning the point at which the interests in favor of protecting valid claims are outweighed by the interests in prohibiting the prosecution of stale ones.”⁴⁷

The general rule, supported by a long line of cases, holds that a statute of limitations attaches when a cause of action arises; when the action can be maintained.⁴⁸ Generally, the Court noted, “a plaintiff must file suit within a designated period after the cause of action accrues.”⁴⁹ The cause of action accrues, the Court said, “when [it] is complete with all of its elements.”⁵⁰ Put another way, the courts have held that “[a] cause of action accrues ‘upon the occurrence of the last element essential to the cause of action.’”⁵¹ Although the courts have carved out some exceptions to the statute of limitations, and have delayed or tolled the accrual of a cause of action when a plaintiff is justifiably unaware of facts essential to a claim or when latent additional injuries later become manifest,⁵² those exceptions are limited and do not apply when a plaintiff has sufficient facts to be on notice or constructive notice that a wrong has occurred and that he or

⁴⁷ *Poosh v. Phillip Morris USA, Inc.* (2011) 51 Cal.4th 788, 797.

⁴⁸ See, e.g., *Osborn v. Hopkins* (1911) 160 Cal. 501, 506 [“[F]or it is elementary law that the statute of limitations begins to run upon the accrual of the right of action, that is, when a suit may be maintained, and not until that time.”]; *Dillon v. Board of Pension Commissioners* (1941) 18 Cal.2d 427, 430 [“A cause of action accrues when a suit may be maintained thereon, and the statute of limitations therefore begins to run at that time.”].

⁴⁹ *Ibid.*

⁵⁰ *Ibid* [quoting *Norgart v. Upjohn Co.* (1999) 21 Cal.4th 383, 397].

⁵¹ *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].

⁵² *Royal Thrift and Loan Co. v. County Escrow, Inc.* (2004) 123 Cal.App.4th 24, 43 [“Generally, statutes of limitation are triggered on the date of injury, and the plaintiff’s ignorance of the injury does not toll the statute... [However,] California courts have long applied the delayed discovery rule to claims involving *difficult-to detect injuries or the breach of fiduciary relationship.*” (Emphasis added.); *Poosh v. Phillip Morris USA, Inc.* (2011) 51 Cal.4th 788, 802, where the court held that for statute of limitations purposes, a later physical injury caused by the same conduct “can, in some circumstances, be considered ‘qualitatively different’.” The court limited its holding to latent disease cases, and did not decide whether the same rule applied in other contexts. (*Id.* p. 792.)

she has been injured.⁵³ The courts do not toll a statute of limitations because the full extent of the claim, or its legal significance, or even the identity of a defendant, is not yet known at the time the cause of action accrues.⁵⁴

For IRCs, the “last element essential to the cause of action” that begins the running of the period of limitation under former section 1185(b) (now § 1185.1(c)) of the Commission’s regulations, is notice to the claimant of the adjustment that includes the claim components, amounts adjusted, and the reason for the adjustment. As enacted in 1995, Government Code section 17558.5(b) provided in pertinent part:

The Controller shall notify the claimant in writing within 30 days after issuance of a remittance advice 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, and the reason for the adjustment. Remittance advices and other notices of payment action shall not constitute notice of adjustment from an audit or review.⁵⁵

An IRC can be maintained and filed with the Commission to challenge the Controller’s findings in accordance with Government Code sections 17551 and 17558.7 as soon as the Controller issues a notice reducing a claim for reimbursement which specifies the claim components, amounts adjusted, and the reason for adjustment in accordance with Government Code section 17558.5. The Commission’s regulations give local government claimants three years following the notice of adjustment required by Government Code section 17558.5(c), in whatever written form provided by the Controller, to file an IRC with the Commission, or otherwise be barred from such action. The IRC must include a detailed narrative describing the alleged reductions

⁵³ *Jolly v. Eli Lilly & Co.* (1988) 44 Cal.3d 1103, 1110 [belief that a cause of action for injury from DES could not be maintained against multiple manufacturers when exact identity of defendant was unknown did not toll the statute]; *Goldrich v. Natural Y Surgical Specialties, Inc.* (1994) 25 Cal.App.4th 772, 780 [belief that patient’s body, and not medical devices implanted in it, was to blame for injuries did not toll the statute]; *Campanelli v. Allstate Life Insurance Co.* (9th Cir. 2003) 322 F.3d 1086, 1094 [Fraudulent engineering reports concealing the extent of damage did not toll the statute of limitations, nor provide equitable estoppel defense to the statute of limitations]; *Abari v. State Farm Fire & Casualty Co.* (1988) 205 Cal.App.3d 530, 534 [Absentee landlord’s belated discovery of that his homeowner’s policy might cover damage caused by subsidence was not sufficient reason to toll the statute]. See also *McGee v. Weinberg* (1979) 97 Cal.App.3d 798, 804 [“It is the occurrence of some ... cognizable event rather than knowledge of its legal significance that starts the running of the statute of limitations.”].

⁵⁴ *Scafidi v. Western Loan & Building Co.* (1946) 72 Cal.App.2d 550, 566 [“Our courts have repeatedly affirmed that mere ignorance, not induced by fraud, of the existence of the facts constituting a cause of action on the part of a plaintiff does not prevent the running of the statute of limitations.”]. See also, *Baker v. Beech Aircraft Corp.* (1974) 39 Cal.App.3d 315, 321 [“The general rule is that the applicable statute...begins to run when the cause of action accrues even though the plaintiff is ignorant of the cause of action or of the identity of the wrongdoer.”].

⁵⁵ See former Government Code section 17558.5(b) (Stats. 1995, ch. 945, eff. July 1, 1996).

and a copy of any “written notice of adjustment from the Office of the State Controller that explains the reason(s) for the reduction or disallowance.”^{56, 57}

In this case, the Controller alleges that it sent its first “adjustment letter” to the claimant on January 15, 2002 and contends that the statute of limitations began accruing against the claimant on that date.⁵⁸

However, the claimant does not mention this letter in its IRC, and instead contends that it first received a letter from the Controller on April 29, 2009, as follows:

This incorrect reduction claim is timely filed. Title 2, CCR, Section 1185(b), requires incorrect reduction claims to be filed no later than three years following the date of the Controller’s “written notice of adjustment notifying the claimant of a reduction.” The Controller conducted a desk review of the District’s FY 1997-98 annual claim. The District received a “results of review” letter dated April 29, 2009, reducing its claim as a result of the desk review. This letter constitutes a demand for repayment and adjudication of the claim.⁵⁹

In comments on the Draft Proposed Decision, the Controller states that the January 15, 2002 adjustment letter was also sent to 509 other school districts on that date for the same program in the same fiscal year. The district’s claim, along with claims of 42 other school districts, were reduced to zero due to adjustments for disallowed costs. The Controller further states that the April 29, 2009 letter was generated as a result of a system error while processing interest payments, and was sent to claimant and the other 42 districts that had their claims reduced to zero. According to the Controller, of the 43 districts that received the letter, only the claimant alleges that it did not receive the original, January 15, 2002, adjustment letter.⁶⁰

There is no evidence in the record, however, that the January 15, 2002 letter was ever sent to the claimant, or that the claimant received it. Unlike the letter dated April 29, 2009, the January 15, 2002 letter was *not* date-stamped “received” by the claimant. And as indicated above, a statute of limitations does not accrue until a claimant has sufficient facts to be on notice or constructive notice that a wrong has occurred. In this respect, Government Code section 17558.5 requires the Controller to “notify the claimant in writing within 30 days after issuance of a remittance advice of any adjustment to a claim for reimbursement that results from an audit or review” and the notice is required to specify the claim components, amounts adjusted, and the “the reason for the adjustment.” Evidence to support the Controller’s contention that the January 15, 2002 letter was served on the claimant could come, for example, from a declaration

⁵⁶ California Code of Regulations, title 2, section 1185.1(c) and (f)(4); See also, Former California Code of Regulations, title 2, section 1185(c) and (d)(4) (Register 2010, No. 44).

⁵⁷ This interpretation is consistent with previously adopted Commission decisions. See Commission on State Mandates, Decision, *Collective Bargaining*, 05-4425-I-11, adopted December 5, 2014, and Decision, *Handicapped and Disabled Students*, 05-4282-I-03 adopted September 25, 2015.

⁵⁸ Exhibit B, Controller’s Comments on the IRC, page 1.

⁵⁹ Exhibit A, IRC, page 4.

⁶⁰ Exhibit D, Controller’s Late Comments on the Draft Proposed Decision.

or proof of service by the Controller's Office setting forth the title of the document served, the name and business address of the person making the service, the date and place of deposit in the mail, the name and address of the person served as shown on the envelope, and that the envelope was sealed and deposited in the mail with the postage fully prepaid.⁶¹ The fact of service could also be supported by the filing of the return receipt for certified mail with a post office stamp.⁶² Evidence in the record that the January 15, 2002 letter was properly mailed or served is required before the Commission can presume under the law that the letter was received in the ordinary course of mail, absent evidence from the claimant to the contrary.⁶³ However, no such facts are contained in the record for this IRC.⁶⁴ Therefore, there is no evidence that the claimant received written notice of the adjustment on or about January 15, 2002, and thus, the Commission cannot find that the period of limitation began to accrue against the claimant with the January 15, 2002 letter. Even if evidence were filed to support a finding that the January 15, 2002 letter was mailed to and received by the claimant, additional analysis would still be required to determine whether the letter provided sufficient notice under Government Code section 17558.5 to trigger the accrual of the period of limitation to file an IRC.

The second letter dated April 29, 2009, which the claimant admits receiving on May 4, 2009, contains the same information as the January 15, 2002 letter. Both letters identify the amount adjusted, which was the full amount claimed for the one component of providing information to parents and guardians about alternative pupil attendance choices. However, the later letter prompted the claimant to contact the Controller's Office on May 4, 2009, to ask for an explanation of the adjustment. This raises the issue of whether the information contained in the letter of April 29, 2009, sufficiently specifies the reason for the adjustment as required by Government Code section 17558.5 to trigger accrual of the period of limitation.

Assuming for the purposes of argument that either the April 29, 2009 letter or the June 2, 2009 email, both of which were received by the claimant, complies with Government Code section 17558.5(c), the IRC was timely filed. Whether the beginning of the accrual period is measured from the April 29, 2009 adjustment letter or the June 2, 2009 email, the Commission finds that the IRC filed July 29, 2011 (less than three years after either of these notices) is timely because it complies with the three-year period of limitation in the Commission's regulations.

Accordingly, based on evidence in the record, the Commission finds that this IRC was timely filed.

B. There Is No Evidence in the Record that the Controller Timely Initiated the Audit and thus, the Audit Findings Are Void.

The claimant contends that the Controller did not audit its reimbursement claim in a timely manner. The claimant argues that the Controller had two years to audit the reimbursement claim,

⁶¹ See, e.g., Code of Civil Procedure section 1013a.

⁶² *Call v. Los Angeles County Gen. Hosp.* (1978) 77 Cal.App.3d 911, 916-917.

⁶³ Evidence Code section 641; *Bear Creek Master Ass'n. v. Edwards* (2005) 130 Cal.App.4th 1470, 1486.

⁶⁴ In addition, the Controller's allegation of fact (that the letter was sent) was not submitted under penalty of perjury as required by section 1187.5(b) of the Commission's regulations.

measured from the date the claim was filed in January 2000, and that an adjustment made in 2009 is too late and beyond the “statute of limitation” provided in Government Code section 17558.5(a).

At the time the reimbursement claim was filed in January 2000 (and as stated in Section VII. of the Parameters and Guidelines for this program),⁶⁵ Government Code section 17558.5(a), as added by Statutes 1995, chapter 945, provided that:

A reimbursement claim for actual costs filed by a local agency or school district pursuant to this chapter is subject to an audit by the Controller no later than two years after the end of the calendar year in which the reimbursement claim is filed or last amended. However, if no funds are appropriated for the program for the fiscal year for which the claim is made, the time for the Controller to initiate an audit shall commence to run from the date of initial payment of the claim.⁶⁶

The plain language of this section provides that reimbursement claims are “subject to audit” no later than two years after the end of the calendar year that the reimbursement claim was filed. The phrase “subject to audit” does not require the completion of the audit. Such a reading adds words to section 17558.5 that are not there. If the words of a statute are clear, the court should not add to or alter them to accomplish a purpose that does not appear on the face of the statute.⁶⁷ This section, however, sets a time during which a claimant is on notice that an audit may occur. This reading is consistent with the plain language of the second sentence, which provides that when no funds are appropriated for the program, “the time for the Controller to initiate an audit shall commence to run from the date of initial payment of the claim.”

This interpretation is also consistent with the Legislature’s 2002 amendment to Government Code section 17558.5, effective January 1, 2003, clarifying that “subject to audit” means “subject to the initiation of an audit,” as follows in underline and strikeout:

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

⁶⁵ Exhibit A, IRC, page 59. Section VII. of the Parameters and Guidelines describes the “Supporting Data” to claim reimbursement as follows:

For auditing purposes, all costs claimed must be traceable to source documents (e.g. employee time records, invoices, receipts, purchase orders, contracts, etc.) and/or worksheets that show evidence of and the validity of such claimed costs. Pursuant to Government Code section 17558.5, subdivision (a), a reimbursement claim for actual costs filed by a local agency or school district is subject to audit by the State Controller no later than two years after the end of the calendar year in which the reimbursement claim is filed or last amended. However, if no funds are appropriated for the program for the fiscal year for which the claim is made, the time for the Controller to initiate an audit shall commence to run from the date of initial payment of the claim.

⁶⁶ Government Code section 17558.5, as added by Statutes 1995, chapter 945, effective July 1, 1996.

⁶⁷ *Goodman v. Lozano* (2010) 47 Cal.4th 1327, 1332.

later than ~~two~~ three years after the ~~end of the calendar year in which the date that the actual~~ reimbursement claim is filed or last amended, ~~whichever is later.~~ However, 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 ~~made~~ filed, the time for the Controller to initiate an audit shall commence to run from the date of initial payment of the claim.^{68, 69}

Here, the claimant states that funds were appropriated for this program, and the Controller has not filed any evidence rebutting this assertion.⁷⁰ Thus, the first sentence in the 1995 version of section 17558.5(a) applies, specifying that the reimbursement claim is subject to the initiation of an audit “no later than two years after the end of the calendar year in which the reimbursement claim is filed.” Because the reimbursement claim was filed on January 6, 2000,⁷¹ as indicated by the claimant and the date stamp on the letter, the Controller had until December 31, 2002, to initiate the audit.

The Legislature did not specifically define the event that initiates the audit and, unlike other auditing agencies that have adopted formal regulations to clarify when the audit begins (which can be viewed as the controlling interpretation of a statute), the Controller has not adopted a regulation for the audits of state-mandate reimbursement claims.⁷² Since section 17558.5 is silent as to the act or event that initiates an audit, the Commission cannot, as a matter of law, state what the act or event is in all cases; but must determine when the audit commenced and whether it was timely initiated based on evidence in the record.

The requirement to initiate an audit no later than two years after the end of the calendar year in which the reimbursement claim is filed requires a unilateral act of the Controller. And failure to timely initiate the audit within the two-year deadline is a jurisdictional bar to any reductions made by the Controller of claimant’s reimbursement claims.⁷³ In this respect, the initiation provisions of Government Code section 17558.5 are better characterized as a statute of repose, rather than a statute of limitations. Section 17558.5 provides a period during which an audit or review may be initiated, and after which the claimant may enjoy repose, dispose of any evidence

⁶⁸ Statutes 2002, chapter 1128.

⁶⁹ This section was amended again (Stats. 2004, ch. 313, eff. Jan. 1, 2005) to require an audit to be completed not later than two years after it is commenced.

⁷⁰ Exhibit A, IRC, pages 14-15.

⁷¹ Exhibit A, IRC, page 24.

⁷² See, e.g., regulations adopted by the California Board of Equalization (title 18, section 1698.5, stating that an “audit engagement letter” is a letter “used by Board staff to confirm the start of an audit or establish contact with the taxpayer.”).

⁷³ 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. (*People v. McGee* (1977) 19 Cal.3d 948, 962, citing *Morris v. County of Marin* (18 Cal.3d 901, 909-910)). Because the deadlines in Government Code section 17558.5 are mandatory and not directory, the requirement to meet the statutory deadline is jurisdictional.

or documentation to support their claims, and assert a defense that the audit is not timely and therefore void.

The court in *Giest v. Sequoia Ventures, Inc.*, described a statute of repose as follows:

Unlike an ordinary statute of limitations which begins running upon accrual of the claim, [the] period contained in a statute of repose begins when a *specific event occurs*, regardless of whether a cause of action has accrued or whether any injury has resulted.” [citations] A statute of repose thus is harsher than a statute of limitations in that it cuts off a right of action after a specified period of time, irrespective of accrual or even notice that a legal right has been invaded.⁷⁴

Described by another court in *Inco Development Corp. v. Superior Court*,⁷⁵ the characteristics of a statute of repose include that it is “not dependent upon traditional concepts of accrual of a claim, but is tied to an independent, objectively determined and verifiable event...”

However, whether analyzed as a statute of repose, or a statute of limitations, the unilateral act that must occur before the expiration of the statutory period may be interpreted similarly. That is, the filing of a civil action may be interpreted analogously to the initiation of an audit, to the extent that the initiation of the audit, like the commencement of a civil action, terminates the running of the statutory period, and vests authority in the party to proceed.⁷⁶ However, unlike a plaintiff filing a complaint in court within a statutory time period to protect against a statute of limitations defense barring the matter, Government Code section 17558.5 does not require the Controller to lodge a document to *prove* it timely initiated an audit. Nevertheless, because it is the Controller’s authority to audit that must be exercised within a specified time, it must be within the Controller’s exclusive control to meet or fail to meet the deadline imposed. The Controller has the burden of proof on this issue and must show with evidence in the record that the claimant was notified that an audit was being initiated by the statutory deadline to ensure that the claimant not dispose of any evidence or documentation to support its claim for reimbursement. In this IRC, there is no evidence in the record to support a finding that the Controller initiated the audit by the December 31, 2002 deadline.

The Controller alleges that the claimant was notified of the audit reduction by the letter dated January 15, 2002.⁷⁷ Since the letter indicates that the Controller reduced costs to \$0, then it can logically be presumed, *if* this letter can be verified and shown that it was provided to the claimant, that the audit commenced some time before the January 15, 2002, date of the letter and thus, before the December 31, 2002 deadline.

⁷⁴ *Giest v. Sequoia Ventures, Inc.* (2000) 83 Cal.App.4th 300, 305.

⁷⁵ *Inco Development Corp. v. Superior Court* (2005), 131 Cal.App.4th 1014.

⁷⁶ *Liptak v. Diane Apartments, Inc.* (1980) 109 Cal.App.3d 762, 773 [“A party does not have a vested right in the time for the commencement of an action [and nor] does he have a vested right in the running of the statute of limitations prior to its expiration.” (citing *Kerchoff-Cuzner Mill and Lumber Company v. Olmstead* (1890) 85 Cal. 80; *Mudd v. McColgan* (1947) 30 Cal.2d 463, 468)].

⁷⁷ Exhibit B, Controller’s Comments on the IRC, pages 1-2.

However, the Controller's allegation that the letter was sent on January 15, 2002, was not submitted under penalty of perjury in compliance with the Commission's regulations.⁷⁸ The letter itself does not contain a proof of service, certificate of mailing, or an affidavit by the Controller's Office to verify the date of mailing. By itself, the letter is an out of court document being used for the truth of the matter asserted (i.e., that the claimant was notified of a reduction before the time expired to initiate an audit), and is unreliable hearsay evidence.⁷⁹ And, as explained in the section above, there is no evidence in the record that the claimant received this letter. Unlike the letter dated April 29, 2009, which the claimant states is the first notice received,⁸⁰ the January 15, 2002 letter is not date stamped "received" by the claimant. Moreover, the April 29, 2009 letter does not provide any information to indicate when the Controller initiated the audit.⁸¹ Thus, there is nothing in this record to verify when the Controller initiated the audit, or any evidence that the claimant was notified that it could not dispose of its supporting documents after the December 31, 2002 deadline.⁸²

Therefore, based on this record, the Commission finds that the Controller did not timely initiate the audit within the deadlines required by Government Code section 17558.5(a) and, therefore, the audit findings are void.

V. Conclusion

For the reasons discussed above, the Commission approves this IRC. The Commission requests, in accordance with Government Code section 17551(d) and section 1185.9 of the Commission's regulations, that the Controller reinstate to the claimant the \$25,081 incorrectly reduced, consistent with these findings.

⁷⁸ California Code of Regulations, title 2, section 1187.5(b).

⁷⁹ Evidence Code section 1200; *People v. Zunis* (2005) 134 Cal.App.4th Supp. 1, 5.

⁸⁰ Exhibit A, IRC, page 4.

⁸¹ Exhibit A, IRC, page 18.

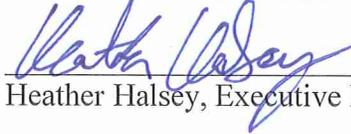
⁸² The facts in this case are unlike a previous IRC decided by the Commission (*Health Fee Elimination*, 05-4206-I-06, March 27, 2015) where the record contained declarations and admissions from the claimant showing that it received actual notice that an audit was being initiated before the deadline imposed by Government Code section 17558.5(a), which was sufficient to verify that finding.



RE: **Decision**

School District of Choice: Transfers and Appeals, 11-4451-I-05
Education Code Sections 48209.1, 48209.7, 48209.9, 48209.10, 48209.13, and 48209.14
Statutes 1993, Chapter 160 (AB 19), Statutes 1994, Chapter 1262 (AB 2768)
Fiscal Year 1997-1998
Chula Vista Elementary School District, Claimant

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



Heather Halsey, Executive Director

Dated: July 26, 2016

BEFORE THE
COMMISSION ON STATE MANDATES
STATE OF CALIFORNIA

**IN RE INCORRECT REDUCTION CLAIM
ON:**

Government Code Section 7576 as amended
by Statutes 1996, Chapter 654 (AB 2726);

California Code of Regulations, Title 2,
Division 9, Chapter 1, Sections 60100 and
60110¹

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

County of Los Angeles, Claimant

Case No.: 12-9705-I-04

*Seriously Emotionally Disturbed Pupils:
Out-of-State Mental Health Services*

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

(Adopted October 28, 2016)

(Served November 1, 2016)

DECISION

The Commission on State Mandates (Commission) heard and decided this Incorrect Reduction Claim (IRC) during a regularly scheduled hearing on October 28, 2016. Edward Jewik and Hasmik Yaghobyan appeared on behalf of the County of Los Angeles (claimant). Jim Spano and Chris Ryan appeared on behalf of the State Controller’s Office (Controller).

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

The Commission adopted the Proposed Decision to deny this IRC by a vote of 7-0 as follows:

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

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 specific sections of the statutes and executive orders that were approved in the test claim decision. However, that was an oversight in the Parameters and Guidelines at issue in this case.

Summary of the Findings

This IRC challenges the Controller's findings and reduction of direct and indirect costs totaling \$5,746,047 (Findings 1 and 3) claimed for fiscal years 2003-2004 through 2005-2006 by the claimant for the *Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services* program.

In Finding 1, costs relating to ineligible vendor payments for out-of-state residential placement of SED pupils in programs that are "owned and operated *for-profit*" were reduced. The claimant agrees with other counties that have filed IRCs contesting the disallowance of costs associated with out-of-state residential board and care costs. In this case, however, the claimant states that its focus is on the reductions to mental health treatment services. In this respect, claimant that the mental health treatment services were provided by for-profit companies, but argues that the law does not restrict the program selected to provide mental health treatment services and does not require that the program be organized on a nonprofit basis.

The Commission 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. The Parameters and Guidelines for this program track the regulatory language and state that reimbursement is authorized for payments to service vendors providing mental health services to SED pupils placed in out-of-state residential facilities, as specified in California Code of Regulations, title 2, section 60100. Section 60100(h) states that out-of-state residential programs shall meet the requirements in Welfare and Institutions Code section 11460(c)(2) through (3) and 11460(c)(3) specifies 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.*" The July 21, 2006 correction to the Parameters and Guidelines clarifies that "mental health services" provided to these students includes residential board and care. Thus, reimbursement for the mandated activity of "providing mental health services" in out-of-state facilities includes both treatment and board and care, which is conditioned on the providers meeting the requirements of Welfare and Institutions Code section 11460(c)(3), to be organized and operated on a nonprofit basis. The law does not support the claimant's position that the mental health treatment portion of the out-of-state "residential program" be excluded from the requirement that the "program" be organized and operated on a nonprofit basis.

In Finding 3, the Controller found that the claimant used an indirect cost rate methodology that is inconsistent with other related mandate programs. The Controller further found that the claimant, in some instances, applied a rate based on costs two years prior and, in other instances, applied a rate based on actual claim year costs. The disparate rates were applied to expenses in the same pool of costs, resulting in significant fluctuations in rates from year to year. The Controller recalculated indirect costs using actual rates applicable to the appropriate fiscal year and applied the rate to eligible costs. The claimant does not address the Controller's reductions relating to the indirect cost rate. Thus, there is no evidence in the record that the Controller's findings are incorrect as a matter of law, or are arbitrary, capricious, or entirely lacking in evidentiary support.

Therefore, the Commission denies this IRC.

I. Chronology

- 12/23/2009 Controller issued the Draft Audit Report dated December 23, 2009.²
- 01/13/2010 Claimant sent a letter to the Controller date January 13, 2010 in response to the Draft Audit Report.³
- 05/07/2010 Controller issued the Final Audit Report for fiscal years 2003-2004 through 2006-2006.⁴
- 05/07/2013 Claimant filed IRC 12-9705-I-04.⁵
- 10/03/2014 Controller filed late comments on IRC 12-9705-I-04.⁶
- 11/07/2014 Claimant filed request for an extension of time to file rebuttal comments, which was granted for good cause.
- 02/09/2015 Claimant filed late rebuttal comments.⁷
- 08/26/2016 Commission staff issued the Draft Proposed Decision.⁸
- 08/30/2016 Controller filed comments on the Draft Proposed Decision.⁹
- 09/15/2016 Claimant filed comments on the Draft Proposed Decision.¹⁰

II. Background

A. *Seriously Emotionally Disturbed 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.¹¹ The test claim statute and regulations were part of the state's response to the federal Individuals with Disabilities Education Act, or 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

² Exhibit A, IRC, page 51.

³ Exhibit A, IRC, pages 51-53 (Letter from Wendy L. Watanabe to Jeffrey V. Brownfield, dated January 13, 2010).

⁴ Exhibit A, IRC, page 37.

⁵ Exhibit A, IRC, page 1.

⁶ Exhibit B, Controller's Late Comments on the IRC, page 1.

⁷ Exhibit C, Claimant's Late Rebuttal Comments to the Controller's Late Comments on the IRC.

⁸ Exhibit D, Draft Proposed Decision.

⁹ Exhibit E, Controller's Comments on the Draft Proposed Decision.

¹⁰ Exhibit F, Claimant's Comments on the Draft Proposed Decision.

¹¹ Exhibit B, Controller's Late Comments on the IRC, pages 42-51.

unique educational needs.¹² 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 required that all services provided by the counties be provided *within* the State of California.¹³ 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.¹⁴ 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 needs. Section 60200 entitled “Financial Responsibilities” details county mental health and LEA financial responsibilities regarding the residential placements of SED pupils.

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

¹³ Former California Code of Regulations, title 2, section 60200.

¹⁴ Statutes 1996, chapter 654.

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.¹⁵

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.)¹⁶

Parameters and Guidelines for the *SED* program were adopted on October 26, 2000,¹⁷ and corrected on July 21, 2006,¹⁸ 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 60110.¹⁹

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, that the term “payments to service vendors providing mental health services to SED pupils in

¹⁵ Exhibit B, Controller’s Late Comments on the IRC, pages 44-45 (Test Claim Statement of Decision adopted May 25, 2000).

¹⁶ Exhibit B, Controller’s Late Comments on the IRC, page 51 (Test Claim Statement of Decision adopted May 25, 2000).

¹⁷ Exhibit B, Controller’s Late Comments on the IRC, page 54 (Parameters and Guidelines adopted October 26, 2000).

¹⁸ Exhibit B, Controller’s Late Comments on the IRC, page 67 (Parameters and Guidelines corrected July 21, 2006).

¹⁹ Exhibit B, Controller’s Late Comments on the IRC, page 56 (Parameters and Guidelines adopted October 26, 2000).

out-of-state residential placements” includes reimbursement for “residential costs” of out-of-state placements.²⁰

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.

The Parameters and Guidelines also contain instructions for claiming costs. Section V. of the Parameters and Guidelines require that claimed costs for fiscal years 2000-2001 through 2005-2006 “shall be supported by” cost element information, as specified. With respect to claims for contract services, claimants are required to:

Provide the name(s) of the contractor(s) who performed the services, including any fixed contract for services. Describe the reimbursable activity(ies) performed by each named contractor and give the number of actual hours spent on the activities, if applicable. Show the inclusive dates when services were performed and itemize all costs for those services.²¹

Section VI. of the Parameters and Guidelines requires documentation to support the costs claimed as follows:

For auditing purposes, all costs claimed shall be traceable to source documents (e.g., invoices, receipts, purchase orders, contracts, worksheets, calendars, declarations, etc.) that show the evidence and validity of such costs and their relationship to the state mandated program. All documentation in support of the claimed costs shall be made available to the State Controller’s Office, as may be requested...[T]hese documents must be kept on file by the agency submitting the claim for a period of no less than two years after the later of (1) the end of the calendar year in which the reimbursement claim is filed or last amended, or (2) if no funds are appropriated for the fiscal year for which the claim is made, the date of initial payment of the claim.²²

²⁰ Exhibit B, Controller’s Late Comments on the IRC, page 67 (Parameters and Guidelines corrected July 21, 2006).

²¹ Exhibit B, Controller’s Late Comments on the IRC, page 72 (Parameters and Guidelines corrected July 21, 2006).

²² Exhibit B, Controller’s Late Comments on the IRC, pages 72-73 (Parameters and Guidelines corrected July 21, 2006).

On October 26, 2006, the Commission consolidated the Parameters and Guidelines for *SED, Handicapped and Disabled Students*, CSM 4282 and 04-RL-4282-10, and *Handicapped and Disabled Students II*, 02-TC-40/02-TC-49, for costs incurred commencing with the 2006-2007 fiscal year.

Statutes 2011, chapter 43 (AB 114) eliminated the mandated programs for *Handicapped and Disabled Students*, CSM 4282 and 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, 2011.²³ 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 Controller issued the Draft Audit Report dated December 23, 2009, and provided a copy to the claimant for comment.²⁴

In a three-page letter dated January 13, 2010, the claimant responded directly to the Draft Audit Report, agreeing with its findings, and accepted its recommendations.²⁵ The first page of this three-page letter contains the following statement:

The County's response, which is attached hereto, indicated agreement with the audit findings and the actions that the County will take to implement policies and procedures to ensure that the costs claimed under SED are eligible, mandate related, and supported.²⁶

The letter also affirmatively agreed with each finding in the Draft Audit Report.²⁷

On May 7, 2010, the Controller issued the Final Audit Report.²⁸ The Controller audited and reduced the reimbursement claims for various reasons. The claimant disputes the reductions of direct and indirect costs totaling \$5,746,047 for all fiscal years in issue (Findings 1 and 3). In Finding 1, costs relating to ineligible vendor payments for out-of-state residential placement of SED pupils in programs that are "owned and operated *for-profit*" were reduced.²⁹ The Controller found unallowable costs claimed for ten residential facilities:

²³ Exhibit G, Assembly Bill No. 114 (2011-2012 Reg. Sess.), approved by the Governor, June 30, 2011.

²⁴ Exhibit A, IRC, page 51 (Final Audit Report).

²⁵ Exhibit A, IRC, pages 51-53 (Letter from Wendy L. Watanabe to Jeffrey V. Brownfield, dated January 13, 2010).

²⁶ Exhibit A, IRC, page 51 (Letter from Wendy L. Watanabe to Jeffrey V. Brownfield, dated January 13, 2010).

²⁷ Exhibit A, IRC, pages 53-54 (Letter from Wendy L. Watanabe to Jeffrey V. Brownfield, dated January 13, 2010).

²⁸ Exhibit A, IRC, page 37 (Final Audit Report).

²⁹ Exhibit A, IRC, page 45 (Final Audit Report).

- For three of the facilities (Youth Care of Utah, Logan River Academy, and Charter Provo Canyon School), the county claimed payments made to Mental Health Systems, Inc., and Aspen Solutions Inc., both California nonprofit corporations. However, the Controller found the costs not allowable because all three of these facilities that the nonprofit corporations contracted with to provide the out-of-state residential placement services are organized and operated as for-profit facilities.³⁰
- For three of the facilities (Aspen Ranch, New Leaf Academy and SunHawk Academy), the county asserted that the for-profit facilities has similar contractual arrangements with Aspen Solutions, Inc., (a nonprofit business incorporated in California). The county, however, did not provide any documentation to support the nonprofit status of the residential facilities providing the treatment services, or provide documentation illustrating a business relationship between the residential facilities and the California nonprofit entity.³¹
- For four of the facilities (Grove School, New Haven, Spring Creek Lodge, and Vista Adolescent Treatment Center), the county did not provide any documentation in support of their nonprofit status.³²

In Finding 3, the Controller found that the claimant used an indirect cost rate methodology that is inconsistent with other related mandate programs. The Controller further found that the claimant, in some instances, applied a rate based on costs two years prior and, in other instances, applied a rate based on actual claim year costs. The disparate rates were applied to expenses in the same pool of costs, resulting in significant fluctuations in rates from year to year.³³ In comments on the IRC, the Controller further explains the finding as follows:

The county's filing does not include the reimbursement claims filed with the SCO. The exhibit includes the claims prepared by the county's mental health department that were submitted to its auditor-controller (Exhibit D.) We have included the actual claim forms filed with the SCO as part of our response (Tabs 3, 4, and 5). These forms were signed by the county's auditor-controller and submitted to the SCO for reimbursement of state-mandated costs.

Concerning the indirect cost rates, the county claimed 7.7066% for FY 2003-04, 6.8276% for FY 2004-05, and 0.2227% for FY 2005-06 on its filed mandate claims. However, in its filed IRC, the county indicated that its indirect cost rates are 8.4749% ($\$120,853 \div \$1,426,010$) for FY 2003-04, 7.5079% ($\$144,629 \div \$1,926,362$) for FY 2004-05, and 7.864% ($\$155,159 \div \$1,973,033$) for FY 2005-06. Based on our audit of the claims, we found that actual indirect cost rates were

³⁰ Exhibit B, Controller's Late Comments on the IRC, page 13.

³¹ Exhibit B, Controller's Late Comments on the IRC, page 13.

³² Exhibit B, Controller's Late Comments on the IRC, page 13.

³³ Exhibit A, IRC, page 47.

4.8497% for FY 2003-04, 5.0543% for FY 2004-05, and 4.7072% for FY 2005-06.³⁴

III. Positions of the Parties

A. County of Los Angeles

Although the claimant agreed with the Draft Audit Report, the claimant now contends that the Controller's reductions are incorrect and that all costs should be reinstated.³⁵ The claimant states that payment for out-of-state residential placement consists of two components; care and supervision, and mental health treatment services. The Controller reduced costs for both components. The claimant agrees with the Counties of San Diego and Orange, who have also filed IRCs contesting the disallowance of costs associated with the first component.³⁶ In this case, however, the claimant states that its focus is on the reductions to the second component of mental health treatment services.

The claimant argues Welfare and Institutions Code section 11460 applies only to the AFDC-FC rate payment for care and supervision, and not to payments made for mental health treatment services. The claimant acknowledges that Code of Regulations, title 2, section 60100(h) requires that out-of-state placements be made only in residential programs that meet the requirements of Welfare and Institutions Code section 11460(c)(2) though (c)(3), and that subdivision (c)(3) provides that "State reimbursement for an AFDC-FC rate . . . shall be paid to a group home organized and operated on a nonprofit basis." However, the claimant asserts that the nonprofit limitation in section 11460(c)(3) does not apply to mental health treatment services. Rather, the AFDC-FC rate is defined in section 11460(b) to cover the costs for "care and supervision;" i.e., food, clothing, shelter, and like services and not mental health treatment services. The claimant also cites in rebuttal comments that the "Agency Plan for Title IV-E of the Social Security Act Foster Care and Adoption Assistance for the State of California," states that "California does not claim Title IV-E funds for administrative reimbursement for mental health or social work costs in the basic rate for FFAs or Group Homes."³⁷

The claimant asserts that the test claim statute (Statutes 1996, chapter 654) specifically stated the legislative intent to ensure that community mental health agencies would be responsible for the mental health services required under IEPs, no matter where the pupil is placed, and contained no limitation on the placement of pupils in out-of-state residential facilities. The Legislature is charged with knowledge of Welfare and Institutions Code section 11460 and had the Legislature intended to restrict the mental health services payment to nonprofit entities only, it could have done so in AB 2726. Following the enactment of AB 2726, the State Department of Mental Health (DMH) issued Information Notice No. 98-10 on July 9, 1998, which stated that "County

³⁴ Exhibit B, Controller's Late Comments on the IRC, page 15.

³⁵ Exhibit A, IRC; Exhibit C, Claimant's Late Rebuttal Comments to the Controller's Late Comments on the IRC.

³⁶ County of San Diego IRC, 10-9705-I-01 and 13-9705-I-05, decided May 26, 2016. County of Orange IRC, 11-9705-I-02 and 12-9705-I-03, scheduled for hearing on September 23, 2016.

³⁷ Exhibit C, Claimant's Late Rebuttal Comments to the Controller's Late Comments on the IRC, page 4.

mental health departments are also required by this legislation to pay mental health treatment costs which out-of-state providers now break out and bill separately from costs related to education and room and board.” The claimant states that the attachment to this notice identified the rates for mental health treatment and the residential daily rates. For Los Angeles County, the attachment lists various facilities, including Mental Health Services, Inc. (Provo Canyon School), which was disallowed by the Controller in this case.³⁸

Moreover, school districts had no restrictions on the use of for-profit placements when school districts were responsible for providing mental health treatment services under prior law. The Education Code was consistent with federal law, which currently contains no restriction.

The claimant states that section 60100(h) of the regulations as interpreted by the Controller, therefore, is inconsistent with federal law, the Government Code, and the Education Code, in that it unlawfully restricts the rights of pupils with serious emotional or mental illness to receive a free and appropriate public education. The courts and administrative bodies applying these provisions have consistently required counties to allow the placement of pupils in the exact facilities for which the Controller has disallowed costs. The claimant further asserts that the courts have consistently sided with the parents who unilaterally place a pupil in a for-profit facility.

The claimant does not address the Controller’s reductions relating to the indirect cost rate.

Claimant disagrees with the conclusions and recommendations in the Draft Proposed Decision and reasserts it is entitled to the full amount of costs claimed for the placement of pupils in out-of-state residential facilities that are owned and operated on a non-profit basis.³⁹

The claimant also asserts that the Proposed Decision adopts an inappropriate abuse of discretion standard of review of the Controller’s audit decisions, and argues that the Commission must “make an independent determination of the Controller’s actions in this matter.”⁴⁰

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 found 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.⁴¹ The Controller asserts that the unallowable direct and indirect costs for mental health services treatment payments claimed result from the claimant’s placement of SED pupils in prohibited for-profit out-of-state residential facilities.⁴²

The Controller does not dispute the assertion that Government Code section 7572 requires mental health services to be provided by qualified mental health professionals, that there is

³⁸ Exhibit A, IRC, page 24.

³⁹ Exhibit F, Claimant’s Comments on the Draft Proposed Decision, page 1.

⁴⁰ Exhibit F, Claimant’s Comments on the Draft Proposed Decision, pages 2-3.

⁴¹ Exhibit B, Controller’s Late Comments on the IRC, page 8.

⁴² Exhibit B, Controller’s Late Comments on the IRC, page 13.

inconsistency between the federal law and California law related to IDEA funds, or 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 the Education Code does not restrict local educational agencies 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.⁴³

The Controller also reduced indirect costs on the ground that the claimant overstated the indirect cost rate. The Controller found that the claimant used an indirect cost rate methodology that is inconsistent with other related mandate programs. The Controller further found that the claimant, in some instances, applied a rate based on costs two years prior and, in other instances, applied a rate based on actual claim year costs. The disparate rates were applied to expenses in the same pool of costs, resulting in significant fluctuations in rates from year to year.⁴⁴

The Controller filed comments in support of the Draft Proposed Decision.⁴⁵

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 6.⁴⁶ 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."⁴⁷

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

⁴³ Exhibit B, Controller's Late Comments on the IRC, page 16.

⁴⁴ Exhibit A, IRC, page 47 (Final Audit Report).

⁴⁵ Exhibit E, Controller's Comments on the Draft Proposed Decision.

⁴⁶ *Kinlaw v. State of California* (1991) 54 Cal.3d 326, 331-334; Government Code sections 17551, 17552.

⁴⁷ *County of Sonoma v. Commission on State Mandates* (2000) 84 Cal.App.4th 1264, 1280, citing *City of San Jose v. State of California* (1996) 45 Cal.App.4th 1802, 1817.

1. During all of the fiscal years at issue, the Parameters and Guidelines and state law required that SED pupils placed in out-of-state residential programs 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.

Reimbursement claims filed with the Controller are required as a matter of law to be filed in accordance with the parameters and guidelines adopted by the Commission.⁵³ Parameters and guidelines provide instructions for eligible claimants to prepare reimbursement claims for the direct and indirect costs of a state-mandated program.⁵⁴ Parameters and guidelines are regulatory in nature and “APA valid, and absent a court ruling setting them aside, are binding on the parties.”⁵⁵

As indicated above, the Parameters and Guidelines for this program track the regulatory language and state that reimbursement is authorized for payments to service vendors providing mental health services to SED pupils placed in out-of-state residential facilities, as specified in California Code of Regulations, title 2, section 60100. Section 60100(h) states that out-of-state residential programs shall meet the requirements in Welfare and Institutions Code section 11460(c)(2) through (3) and 11460(c)(3) specifies 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.*” The July 21, 2006 correction to the Parameters and Guidelines clarifies that “mental health services” provided to these students includes residential board and care. Thus, reimbursement for the mandated activity of “providing mental health services” in out-of-state facilities includes both treatment and board and care, and is conditioned on the providers meeting the requirements of Welfare and Institutions Code section 11460(c)(3), to be organized and operated on a nonprofit basis. In this case, costs were reduced because the Controller found that the out-of-state services for some students were provided by for-profit companies, and that the claimant did not provide documentation to verify that costs were incurred for services provided by nonprofit organizations for other students.

Claimant acknowledges that the services were provided by for-profit companies.⁵⁶ Claimant argues, however, that neither the test claim statute nor federal law contained a limitation on the placement of out-of-state SED pupils, and that the nonprofit limitation in Welfare and Institutions Code section 11460(c)(3) does not apply to mental health treatment services. Rather, the AFDC-FC rate is defined in section 11460(b) to cover only the costs for care and supervision (i.e., food, clothing, shelter, and like services). The claimant also relies on DMH Information

[Parameters and guidelines are regulatory in nature and “APA valid, and absent a court ruling setting them aside, are binding on the parties.”)].

⁵³ Government Code sections 17561(d)(1); 17564(b); and 17571.

⁵⁴ Government Code section 17557; California Code of Regulations, title 2, section 1183.7.

⁵⁵ *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.

⁵⁶ Exhibit C, Claimant’s Late Rebuttal Comments to the Controller’s Late Comments on the IRC, page 5.

Notice 98-10 issued to counties following the enactment of the test claim statute, which states in part that “[c]ounty mental health departments are also required by this legislation to pay mental health treatment costs which out-of-state providers now break out and bill for separately from costs related to education and room and board (see Attachment A [which identifies the “DMH Daily Rate” and “Residential Daily Rate” for out-of-state residential treatment agencies approved for Los Angeles County]).”⁵⁷

The Commission finds that the Controller’s reduction of costs is correct as a matter of law. As indicated above, the test claim statute was enacted to shift to counties the responsibility to ensure and fund mental health services required by a pupil’s IEP when a seriously emotionally disturbed pupil is placed in an out-of-state residential facility. Section 1 of the bill that enacted the statute states that the fiscal and program responsibilities of community mental health services shall be the same regardless of the location of placement of the pupil. The test claim statute added subdivision (g) to Government Code section 7576 to provide that the county of origin shall have “fiscal and programmatic responsibility for providing or arranging for provision of necessary services.”

Section 60100(d) of the regulations was amended to implement this change in law, and specifically required the IEP team to document the pupil’s educational and mental health treatment needs that support the recommendation for residential placement. Section 60100(d) further states that “this documentation shall identify the special education and mental health services *to be provided by a residential facility listed in Section 60025* that cannot be provided in a less restrictive environment pursuant to [federal law].” (Emphasis added.) Section 60110(b) states that the residential plan shall include provisions, as determined by the pupil’s IEP, for the care, supervision, mental health treatment, psychotropic medication monitoring, if required, and education of a SED pupil. Section 60100(e) states that the community mental health service case manager, in consultation with the IEP team’s administrative designee, shall identify a mutually satisfactory placement that is acceptable to the parent *and addresses the pupil’s education and mental health needs*. Section 60100(h) then states that residential placement may be made out of California only when no in-state facility can meet the pupil’s needs and only when the requirements of subdivisions (d) and (e) have been met [i.e., that the residential facility addresses and provides the pupil’s mental health needs]. Further, section 60100(h) expressly states that “[o]ut-of-state placements shall be made only in residential programs that meet the requirements of Welfare and Institutions Code Sections 11460(c)(2) through (c)(3).” As stated above, Welfare and Institutions Code section 11460(c)(3) specifies 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*.”

It is correct that the costs for care and supervision and mental health treatment services were billed separately, as asserted by the claimant and indicated in the DMH Information Notice 98-10. Payments to the facilities for board and care costs are based upon rates established by the Department of Social Services in accordance with sections 18350 through 18356 of the Welfare and Institutions Code.⁵⁸ And, pursuant to Welfare and Institutions Code section 18355, the home care payment and local administrative costs for out-of-state residential placements were

⁵⁷ Exhibit A, IRC, page 23.

⁵⁸ See also, former title 2, California Code of Regulations, section 60200(e).

funded from a *separate* appropriation in the budget of the Department of Social Services. The provision of mental health treatment services, on the other hand, was historically the responsibility of the Department of Mental Health, and appropriations for the program were made by the Legislature based on cost sharing formulas between state and counties under the California community mental health provisions of the Short-Doyle Act and the Bronzan-McCorquodale Act.⁵⁹ Thus, the services were billed separately because they were historically managed and funded under different parts of the State Budget.

However, nowhere in the law does it support the claimant's position that the mental health treatment portion of the out-of-state "residential program" be excluded from the requirement that the "program" be organized and operated on a nonprofit basis. The plain language of section 60100 of the regulations expressly requires that the "residential programs," which by law must include the provision of mental health services, shall meet the requirements in Welfare and Institutions Code section 11460(c)(3) and be organized and operated on a nonprofit basis.

Moreover, 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 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.⁶⁰

⁵⁹ The cost sharing formula for funding the provision of mental health services under the Short-Doyle Act was required by former Welfare and Institutions Code section 5651 (Statutes 1985, chapter 1274), and former California Code of Regulations, title 2, section 60200 (Register No. 87, No. 30). In 1991, the Legislature enacted realignment legislation that repealed the Short-Doyle Act and replaced the sections with the Bronzan-McCorquodale Act (Stats. 1991, chapter 89, §§ 63 and 173). Beginning in fiscal year 2001-2002, Statutes 2002, chapter 1167 and Statutes 2004, chapter 493, required the state to pay the full share of allowable mental health treatment costs for Handicapped and Disabled and SED pupils.

⁶⁰ Exhibit G, Final Statement of Reasons for Joint Regulations for Pupils with Disabilities, page 127 (emphasis added).

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.” 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.”⁶¹

Legislation was later 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 a non-profit in order to receive federal funding. However, as described below, the legislation was not enacted and the law applicable to the reimbursement claims at issue in this IRC remained unchanged.

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. The committee analysis for the bill explained that since 1985, California law has tied the requirement for 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 non-profits 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 government eliminated the requirement that a facility be operated as a nonprofit in order to receive federal funding in 1996.⁶² However, the bill did not pass the assembly.⁶³

In 2008, AB 1805, a budget trailer bill, containing identical language to SB 292 was vetoed by the Governor.⁶⁴ 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.”⁶⁵

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 placement of SED pupils in out-of-state, for-profit residential facilities. The analysis states that the purpose of the proposed

⁶¹ Exhibit G, Final Statement of Reasons for Joint Regulations for Pupils with Disabilities, page 128.

⁶² Exhibit G, Assembly Committee on Human Services, analysis of SB 292, June 17, 2009, page 2.

⁶³ Exhibit G, Complete Bill History, Senate Bill No. 292.

⁶⁴ Exhibit G, Assembly Committee on Appropriations, analysis of AB 421, May 20, 2009, page 3.

⁶⁵ Exhibit G, Governor’s Veto Message, AB 1885, September 30, 2008.

legislation was to incorporate the allowance made in federal law for reimbursement of costs of placement in for-profit group homes for SED pupils.⁶⁶ 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.⁶⁷ 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.⁶⁸ 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.⁶⁹ The author notes the discrepancy between California law and federal law, which allows federal funding of for-profit group home placements.⁷⁰ However, the bill did not pass the Assembly and therefore did not move forward.⁷¹

Thus, during the entire reimbursement period for this program, reimbursement was authorized only for out-of-state residential programs 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.⁷²

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.⁷³ Therefore, costs claimed for out-of-state service

⁶⁶ Exhibit G, Assembly Committee on Appropriations, analysis of AB 421, May 20, 2009, page 2.

⁶⁷ Exhibit G, Assembly Committee on Appropriations, analysis of AB 421, May 20, 2009, page 1.

⁶⁸ Exhibit G, Assembly Committee on Appropriations, analysis of AB 421, May 20, 2009, page 2.

⁶⁹ Exhibit G, Assembly Committee on Appropriations, analysis of AB 421, May 20, 2009, page 2.

⁷⁰ Exhibit G, Assembly Committee on Appropriations, analysis of AB 421, May 20, 2009.

⁷¹ Exhibit G, Complete Bill History, AB 421.

⁷² California Constitution, article III, section 3.5; *Robin J. v. Superior Court* (2004) 124 Cal.App.4th 414, 425.

⁷³ *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.

vendors that are organized and operated on a for-profit basis are beyond the scope of the mandate.

2. Claimant's reference to decisions issued by the courts and administrative bodies allowing placement in for-profit residential programs is misplaced.

The claimant argues that:

[t]he courts and administrative bodies in applying these various provisions have consistently required public agencies, including the County of Los Angeles, in conjunction with the local education agency to allow the placement of pupils in the exact facilities for which the SCO is disallowing the costs and these courts and administrative bodies have consistently sided with the parents after the parents made unilateral placements of a pupil in a for-profit facility.⁷⁴

While the claimant does not specify which decisions it is referring to in its assertion, the Commission's recently adopted decisions for *SED* IRCs 10-9705-I-01 and 13-9705-I-05 addressed this issue and analyzed decisions issued by the Office of Administrative Hearings (OAH) and the United States Supreme Court raised by the claimants in those IRCs.

The OAH decision relied upon by claimants in those IRCs, 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.⁷⁵ 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.⁷⁶

The claimants in the other IRCs on this program also relied on the U.S. Supreme Court decision in *Florence County School District Four v. Carter*,⁷⁷ 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,

⁷⁴ Exhibit C, Claimant's Late Rebuttal Comments to the Controller's Late Comments on the IRC, page 4.

⁷⁵ Exhibit G, *Student v. Riverside Unified School District and Riverside County Department of Mental Health*, OAH Case No. 2007090403, dated January 15, 2008.

⁷⁶ Exhibit G, *Riverside County Department of Mental Health v. Sullivan* (E.D.Cal. 2009) EDCV 08-0503-SGL.

⁷⁷ *Florence County School District v. Carter* (1993) 510 U.S. 7.

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.'"⁷⁸ Unlike the court's equitable powers under IDEA, the reimbursement requirements of article XIII B, section 6, must be strictly construed and not applied as an "equitable remedy to cure the perceived unfairness resulting from political decisions on funding priorities."⁷⁹

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 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 the facilities providing treatment and board and care services for its SED pupils are for-profit. In fact, the claimant acknowledges that fact.⁸⁰

Specifically, the Controller found that the county claimed vendor costs for Aspen Solutions, Inc., and Mental Health Systems, Inc., California nonprofit entities but that these nonprofit entities contracted with for-profit facilities where the out-of-state placements occurred (Youth Care of Utah, Logan River Academy LLC, and Charter Provo Canyon Schools, LLC). Copies of the contracts for the provision of mental health services to SED pupils between Aspen Solutions Inc., and Youth Care of Utah Inc. (Youth Care contract),⁸¹ Mental Health Services, Inc. (MHS), and Logan River Academy, LLC (Logan River contract),⁸² and Mental Health Services, Inc., and

⁷⁸ *Florence County School District, supra*, 510 U.S. 5, 12 (citing its prior decision in *School Comm. of Burlington v. Department of Ed. of Mass.* (1985) 471 U.S. 359, 369.)

⁷⁹ *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).

⁸⁰ Exhibit C, Claimant's Late Rebuttal Comments to the Controller's Late Comments on the IRC, page 5.

⁸¹ Exhibit B, Controller's Late Comments on the IRC, page 88 (Tab 12, Contract between Aspen Solutions Inc., and Youth Care of Utah, Inc.).

⁸² Exhibit B, Controller's Late Comments on the IRC, pages 98-99 (Tab 13, Contract between Mental Health Services, Inc., and Logan River Academy, LLC).

Charter Provo Canyon School (Charter Canyon contract),⁸³ are in the record. These agreements demonstrate that the vendor payments to the nonprofit entities were for services provided by for-profit programs.

In the Youth Care contract, Youth Care of Utah, Inc., is described as a Delaware corporation and the contract states:

Youth has the sole responsibility for provision of therapeutic services. ASI...shall not exercise control over or interfere in any way with the exercise of professional judgment by Youth or Youth's employees in connection with Youth's therapeutic services.⁸⁴

In the Logan River contract, Logan River Academy is described as a Utah for-profit limited liability company providing mental health services "to children and adolescents residing in California and desires to contract with MHS for the purpose of obtaining certain funds distributed by California State Social Services and California County Mental Health Departments."⁸⁵

In the Provo Canyon contract, Charter Provo Canyon School, LLC is described as a Delaware for-profit limited liability company providing mental health services "to children and adolescents residing in California and desires to contract with MHS for the purpose of obtaining certain funds distributed by California State Social Services and California County Mental Health Departments."⁸⁶

Therefore, reimbursement is not required for the costs incurred for Youth Care of Utah, Logan River Academy, and Charter Provo Canyon School.

The claimant similarly claimed that it had contractual agreements with Aspen Solutions, Inc., for placement of SED pupils in three other facilities: Aspen Ranch, New Leaf Academy, and SunHawk Academy. However, the claimant did not provide any documentation to support the nonprofit status of the programs that provided the services, or show the business relationship between the programs and the California nonprofit organization.⁸⁷ In addition, the claimant did not provide any documentation in support of the programs' nonprofit status for Grove School, New Haven, Spring Creek Lodge, and

⁸³ Exhibit B, Controller's Late Comments on the IRC, page 111 (Tab 14, Contract between Mental Health Services, Inc. and Charter Provo Canyon School).

⁸⁴ Exhibit B, Controller's Late Comments on the IRC, page 88 (Tab 12, Contract between Aspen Solutions Inc., and Youth Care of Utah, Inc.).

⁸⁵ Exhibit B, Controller's Late Comments on the IRC, page 99 (Tab 13, Contract between Mental Health Services, Inc., and Logan River Academy, LLC).

⁸⁶ Exhibit B, Controller's Late Comments on the IRC, page 111 (Tab 14, Contract between Mental Health Services, Inc. and Charter Provo Canyon School).

⁸⁷ Exhibit B, Controller's Late Comments on the IRC, page 13.

Vista Adolescent Treatment Center.⁸⁸ Section VI. of the Parameters and Guidelines requires the claimant to provide documentation to support the costs claimed as follows:

For auditing purposes, all costs claimed shall be traceable to source documents (e.g., invoices, receipts, purchase orders, contracts, worksheets, calendars, declarations, etc.) that show the evidence and validity of such costs and their relationship to the state mandated program. All documentation in support of the claimed costs shall be made available to the State Controller's Office, as may be requested...[T]hese documents must be kept on file by the agency submitting the claim for a period of no less than two years after the later of (1) the end of the calendar year in which the reimbursement claim is filed or last amended, or (2) if no funds are appropriated for the fiscal year for which the claim is made, the date of initial payment of the claim.⁸⁹

Thus, the claimant did not comply with the documentation requirements of the Parameters and Guidelines, or meet its burden of proof to verify that the costs claimed for Aspen Ranch, New Leaf Academy, SunHawk Academy, Grove School, New Haven, Spring Creek Lodge, and Vista Adolescent Treatment Center were within the scope of the mandate.

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.

B. There No Evidence That the Controller's Reduction of Indirect Costs Based on the Indirect Cost Rate Applied by the Claimant Is Incorrect as a Matter of Law, or Is Arbitrary, Capricious, or Entirely Lacking in Evidentiary Support.

The Controller also reduced indirect costs on the ground that the claimant overstated the indirect cost rate. The Controller found that the claimant used an indirect cost rate methodology that is inconsistent with other related mandate programs. The Controller further found that the claimant, in some instances, applied a rate based on costs two years prior and, in other instances, applied a rate based on actual claim year costs. The disparate rates were applied to expenses in the same pool of costs, resulting in significant fluctuations in rates from year to year.⁹⁰ In comments on the IRC, the Controller explains the finding as follows:

Concerning the indirect cost rates, the county claimed 7.7066% for FY 2003-04, 6.8276% for FY 2004-05, and 0.2227% for FY 2005-06 on its filed mandate claims. However, in its filed IRC, the county indicated that its indirect cost rates are 8.4749% ($\$120,853 \div \$1,426,010$) for FY 2003-04, 7.5079% ($\$144,629 \div \$1,926,362$) for FY 2004-05, and 7.864% ($\$155,159 \div \$1,973,033$) for FY 2005-06. Based on our audit of the claims, we found that actual indirect cost rates were 4.8497% for FY 2003-04, 5.0543% for FY 2004-05, and 4.7072% for FY 2005-06.⁹¹

⁸⁸ Exhibit B, Controller's Late Comments on the IRC, page 13.

⁸⁹ Exhibit B, Controller's Late Comments on the IRC, pages 72-73.

⁹⁰ Exhibit A, IRC, page 47 (Final Audit Report).

⁹¹ Exhibit B, Controller's Late Comments on the IRC, page 15.

Thus, the Controller recalculated indirect costs using actual rates applicable to the appropriate fiscal year and applied the rate to eligible costs.

Although the claimant seeks reinstatement of all costs reduced in Findings 1 and 3, the claimant does not address the Controller's reductions relating to the indirect cost rate in its narrative.

Thus, there is no evidence in the record that the Controller's findings are incorrect as a matter of law, or are arbitrary, capricious, or entirely lacking in evidentiary support.

V. Conclusion

Based on the foregoing, the Commission denies this IRC.

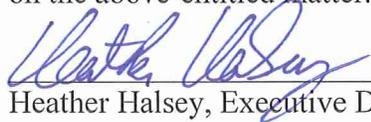


RE: **Decision**

Seriously Emotionally Disturbed Pupils: Out-of-State Mental Health Services,
12-9705-I-04

Government Code Section 7576 as amended by Statutes 1996, Chapter 654 (AB 2726);
California Code of Regulations, Title 2, Division 9, Chapter 1, Sections 60100 and 60110
Fiscal Years 2003-2004, 2004-2005, and 2005-2006
County of Los Angeles, Claimant

On October 28, 2016, the foregoing Decision of the Commission on State Mandates was adopted on the above-entitled matter.



Heather Halsey, Executive Director

Dated: November 1, 2016

BEFORE THE
 COMMISSION ON STATE MANDATES
 STATE OF CALIFORNIA

**IN RE INCORRECT REDUCTION CLAIM
 ON:**

Government Code Section 7576 as amended
 by Statutes 1996, Chapter 654 (AB 2726);

California Code of Regulations, Title 2,
 Division 9, Chapter 1, Sections 60100 and
 60110¹

Fiscal Years 2001-2002, 2002-2003,
 2003-2004, 2004-2005, and 2005-2006

County of San Diego, Claimant

Case Nos.: 10-9705-I-01 and 13-9705-I-05

*Seriously Emotionally Disturbed Pupils:
 Out-of-State Mental Health Services*

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

(Adopted May 26, 2016)

(Served June 1, 2016)

DECISION

The Commission on State Mandates (Commission) heard and decided these consolidated Incorrect Reduction Claims (IRCs) during a regularly scheduled hearing on May 26, 2016. Lisa Macchione and Kyle Sand appeared on behalf of the County of San Diego. Jim Spano and Chris Ryan appeared on behalf of the State Controller’s Office (Controller).

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

The Commission adopted the proposed decision to deny these IRCs by a vote of 5-0 as follows:

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

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 and 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.

Summary of the Findings

These consolidated IRCs challenge the State Controller's Office's (Controller's) reductions totaling \$2,626,697 claimed for fiscal years 2001-2002 through 2005-2006 by the County of San Diego (claimant) for the *Seriously Emotionally Disturbed (SED) Pupils: Out-of-State Mental Health Services* program. The Controller reduced vendor costs claimed for board and care and treatment services for out-of-state residential placement of SED pupils in facilities organized and operated for-profit. The parameters and guidelines and state law only allow vendor payments for SED pupils placed in an out-of-state group home organized and operated on a *nonprofit* basis.

The Commission finds that the Controller's reduction of costs claimed for fiscal years 2001-2002 through 2005-2006 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 meet the requirements of Welfare and Institutions Code section 11460(c)(2) through (3), which specified that reimbursement shall only be provided to facilities organized and operated on a nonprofit basis. 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 state statutes and regulations adopted in accordance with the Administrative Procedures Act, are valid.² Accordingly, pursuant to state law and the Commission's parameters and guidelines, reimbursement is required only if the out-of-state service vendor is organized and operated on a nonprofit basis. Costs claimed for out-of-state service vendors that operate on a for-profit basis are beyond the scope of the mandate and are not eligible for reimbursement.

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 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, 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 IDEA, the reimbursement requirements of article XIII B, section 6, must be strictly construed and not applied as an "equitable remedy to cure the perceived unfairness resulting from political decisions on funding priorities."

² California Constitution, article III, section 3.5; *Robin J. v. Superior Court* (2004) 124 Cal.App.4th 414, 425.

Therefore, the Commission denies these IRCs.

I. Chronology

- 11/14/2007 Controller issued the final audit report for fiscal years 2001-2002 through 2004-2005.³
- 09/10/2010 Controller issued the final audit report for fiscal year 2005-2006.⁴
- 11/10/2010 Claimant filed IRC 10-9705-I-01.⁵
- 09/09/2013 Claimant filed IRC 13-9705-I-05.⁶
- 10/03/2014 Controller filed late comments on IRC 10-9705-I-01.⁷
- 10/03/2014 Controller filed late comments on IRC 13-9705-I-05.⁸
- 11/05/2014 Claimant filed request for an extension of time to file rebuttal comments on both IRCs.⁹
- 02/04/2016 Commission staff issued the Notice of Proposed Consolidation of IRCs 10-9705-I-01 and 13-9705-I-05.
- 03/15/2016 Commission staff issued the Draft Proposed Decision.¹⁰
- 04/01/2016 Controller filed comments on the Draft Proposed Decision.¹¹
- 04/05/2016 Claimant filed request for an extension of time to file comments on the Draft Proposed Decision, which was approved for good cause.
- 04/15/2016 Claimant filed comments on the Draft Proposed Decision.¹²

II. Background

A. Seriously Emotionally Disturbed Pupils: Out-of-State Mental Health Services Program

³ Exhibit A, Incorrect Reduction Claim 10-9705-I-01, page 41. On October 25, 2013, in response to a Commission notice of incomplete filing, claimant resubmitted the claim form, specifying county as the claimant and providing an authorized signature of the county's Auditor-Controller on the claim certification. Exhibit A reflects the completed test claim filing.

⁴ Exhibit B, Incorrect Reduction Claim 13-9705-I-05, page 42.

⁵ Exhibit A, Incorrect Reduction Claim 10-9705-I-01, page 1

⁶ Exhibit B, Incorrect Reduction Claim 13-9705-I-05, page 1.

⁷ Exhibit C, Controller's Late Comments on IRC 10-9705-I-01, page 1.

⁸ Exhibit D, Controller's Late Comments on IRC 13-9705-I-05, page 1.

⁹ Exhibit E, Claimant's Request for Extension to file Rebuttal to Controller's Comments on IRCs, filed November 5, 2014.

¹⁰ Exhibit F, Draft Proposed Decision.

¹¹ Exhibit G, Controller's Comments on the Draft Proposed Decision, filed April 1, 2016.

¹² Exhibit H, Claimant's Comments on the Draft Proposed Decision, filed April 15, 2016.

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 (hereafter referred to as “SEDS”).¹³ The test claim statute and regulations were part of the state’s response to the federal Individuals with Disabilities Education Act, or 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. The test claim statute shifted to counties the responsibility and funding of mental health services required by a pupil’s individualized education plan (IEP). The test claim statute and regulations address the counties’ responsibilities for out-of-state placement of seriously emotionally disturbed pupils.

Parameters and guidelines for the SEDS program were adopted on October 26, 2000,¹⁴ and corrected on July 21, 2006,¹⁵ with a period of reimbursement beginning January 1, 1997. As relevant to these IRCs, the parameters and guidelines, as originally adopted, authorize reimbursement for the following cost:

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 60110.¹⁶

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, 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.¹⁷

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 which includes all of the fiscal years at issue in these IRCs. 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*

¹³ Exhibit C, Controller’s Late Comments on IRC 10-9705-I-01, pages 25-33.

¹⁴ Exhibit A, Incorrect Reduction Claim 10-9705-I-01, pages 28-32; Exhibit C, Controller’s Late Comments on IRC 10-9705-I-01, pages 37-41.

¹⁵ Exhibit C, Controller’s Late Comments on IRC 10-9705-I-01, pages 49-55.

¹⁶ Exhibit A, Incorrect Reduction Claim 10-9705-I-01, page 29; Exhibit B, Incorrect Reduction Claim 13-9705-I-05, page 30.

¹⁷ Exhibit I, Corrected Parameters and Guidelines, dated July 21, 2006.

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.

The Commission amended the parameters and guidelines on October 26, 2006 to consolidate the parameters and guidelines for SEDS with the parameters and guidelines for the Reconsideration of *Handicapped and Disabled Students*, 04-RL-4282-10, and *Handicapped and Disabled Students II*, 02-TC-40/02-TC-49, for costs incurred commencing with the 2006-2007 fiscal year.¹⁸ Reimbursement for the cost of out-of-state residential placement of seriously emotionally disturbed pupils remained the same when the program was consolidated with the *Handicapped and Disabled Students* program.¹⁹

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 *SED Pupils: Out-of-State Mental Health Services*, 97-TC-05; by transferring responsibility for seriously emotionally disturbed pupils to school districts, effective July 1, 2011.²⁰ Thus on September 28, 2012, the Commission adopted an amendment to the consolidated parameters and guidelines ending reimbursement effective July 1, 2011.

B. The Audit Findings of the Controller

The claimant submitted reimbursement claims for the SEDS program totaling \$12,396,610 for fiscal years 2001-2002, 2002-2003, 2003-2004, 2004-2005 (\$9,933,677) and 2005-2006 (\$2,462,933). The Controller audited the claims and reduced them by a total of \$2,953,833 for various reasons. The claimant only disputes the reduction in Finding 1 for \$1,979,388 for fiscal years 2001-2002 through 2004-2005, and \$647,309 for fiscal year 2005-2006, relating to ineligible vendor payments for board and care and treatment services for out-of-state residential placement of SED pupils in facilities that are “owned and operated *for-profit*.”²¹ 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 were not eligible for reimbursement under the parameters and guidelines.²²

¹⁸ Exhibit C, Controller’s Comments on IRC 10-9705-I-01, page 63; Exhibit I, Consolidated Parameters and Guidelines, adopted October 26, 2006.

¹⁹ Exhibit I, Consolidated Parameters and Guidelines, adopted October 26, 2006, page 8.

²⁰ Exhibit I, Assembly Bill No. 114 (2011-2012 Reg. Sess.), approved by Governor, June 30, 2011.

²¹ Exhibit A, Incorrect Reduction Claim 10-9705-I-01, page 9; Exhibit B, Incorrect Reduction Claim 13-9705-I-05, page 10. (Emphasis added.) Both the audit reports and IRCs use the terms “owned and operated for-profit.” However the statute states “organized and operated for-profit;” our analysis tracks the statutory language.

²² Exhibit C, Controller’s Late Comments on IRC 10-9705-I-01, pages 12, 15-16 (see also the contract between Mental Health Systems, Inc. and Charter Provo Canyon School, provided in

III. Positions of the Parties

A. County of San Diego

The claimant 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)).²³ 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 the 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.²⁴
- 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 their child 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.²⁵
- The County contracted with a nonprofit entity, Mental Health Services, Inc. to provide the out-of-state residential services subject to the disputed disallowances.²⁶
- 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.²⁷ 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

Tab 12, pages 94-104 of Exhibit C); Exhibit D, Controller's Late Comments on IRC 13-9705-I-05, pages 11, 13 (see also the contract between Mental Health Systems, Inc. and Charter Provo Canyon School, provided in Tab 11, pages 82-91 of Exhibit D).

²³ Exhibit A, Incorrect Reduction Claim 10-9705-I-01, page 10; Exhibit B, Incorrect Reduction Claim 13-9705-I-05, page 10.

²⁴ Exhibit A, Incorrect Reduction Claim 10-9705-I-01, pages 11-14; Exhibit B, Incorrect Reduction Claim 13-9705-I-05, pages 11-15.

²⁵ Exhibit A, Incorrect Reduction Claim 10-9705-I-01, pages 14-16; Exhibit B, Incorrect Reduction Claim 13-9705-I-05, pages 15-17.

²⁶ Exhibit A, Incorrect Reduction Claim 10-9705-I-01, pages 16-17; Exhibit B, Incorrect Reduction Claim 13-9705-I-05, page 17.

²⁷ Exhibit A, Incorrect Reduction Claim 10-9705-I-01, pages 17-18; Exhibit B, Incorrect Reduction Claim 13-9705-I-05, page 18.

these services to special education students, with no mention of the tax identification status of the services provider.²⁸

Claimant disagrees with the conclusions and recommendations in the Draft Proposed Decision and reasserts it is “entitled to the full amount of costs claimed for the placement of pupils in certain out-of-state residential facilities that are organized and operated on a non-profit basis for the reasons cited in the County’s incorrect reduction claim filing.”²⁹ The claimant also asserts that the Commission used the incorrect standard of review in making its decision on the incorrect reduction claim, and argues that the Commission must conduct an independent review of the matter and hear the claim de novo.³⁰

B. State Controller’s Office

It is the Controller’s position that the audit adjustments are correct and that these IRCs should be denied. The Controller found 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.³¹ The Controller asserts that the unallowable treatment and board-and-care vendor payments claimed result from the claimant’s placement of SED pupils in prohibited for-profit out-of-state residential facilities.³²

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.³³

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, because the decision does not address the issue of state mandated reimbursement for residential placements made outside of the regulations. The Controller also cites an OAH case where the administrative law

²⁸ Exhibit A, Incorrect Reduction Claim 10-9705-I-01, page 17; Exhibit B, Incorrect Reduction Claim 13-9705-I-05, page 18.

²⁹ Exhibit H, Claimant’s Comments on the Draft Proposed Decision, filed April 15, 2016, page 1.

³⁰ Exhibit H, Claimant’s Comments on the Draft Proposed Decision, filed April 15, 2016, page 1. The Commission need not make a determination with regard to Claimant’s assertion of the legal standard to apply to the Controller’s auditing decisions generally, since this issue in this claim is a pure issue of law and therefore the de novo standard applies in this case.

³¹ Exhibit C, Controller’s Late Comments on IRC 10-9705-I-01, page 12; Exhibit D, Controller’s Late Comments on IRC 13-9705-I-05, page 11.

³² Exhibit C, Controller’s Late Comments on IRC 10-9705-I-01, page 16; Exhibit D, Controller’s Late Comments on IRC 13-9705-I-05, page 13.

³³ Exhibit C, Controller’s Late Comments on IRC 10-9705-I-01, page 15; Exhibit D, Controller’s Late Comments on IRC 13-9705-I-05, page 12.

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 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.³⁴

The Controller filed comments in response to the Draft Proposed Decision, supporting the staff analysis and conclusion.³⁵

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 6.³⁶ The Commission must also interpret the Government Code and implementing regulations in accordance with the broader constitutional and statutory scheme. In making its decisions, the Commission must strictly construe article XIII B, section 6 and not apply it as an "equitable remedy to cure the perceived unfairness resulting from political decisions on funding priorities."³⁷

With regard to the Controller's audit decisions, the Commission must determine whether they were arbitrary, capricious, or entirely lacking in evidentiary support. This standard is similar to

³⁴ Exhibit C, Controller's Late Comments on IRC 10-9705-I-01, page 15 (citing OAH case Nos. N 2007090403 and 2005070683, available at Exhibit C, tabs 10 and 11, pages 75-92); Exhibit D, Controller's Late Comments on IRC 13-9705-I-05, pages 12-13 citing OAH case Nos. 2007090403 and 2005070683, available at Exhibit D, tabs 9 and 10, pages 62-79).

³⁵ Exhibit G, Controller's Comments on the Draft Proposed Decision, filed April 1, 2016.

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

³⁷ *County of Sonoma v. Commission on State Mandates* (2000) 84 Cal.App.4th 1264, 1280, citing *City of San Jose v. State of California* (1996) 45 Cal.App.4th 1802, 1817.

the standard used by the courts when reviewing an alleged abuse of discretion of a state agency.³⁸ Under this standard, the courts have found that:

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

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.⁴⁰ In addition, section 1185.1(f)(3) and 1185.2(c) of the Commission’s regulations requires that any assertions of fact by the parties to an IRC must be supported by documentary evidence. The Commission’s ultimate findings of fact must be supported by substantial evidence in the record.⁴¹

The Controller’s Reduction of Costs Is Correct as a Matter of Law.

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.

- A. During all of the fiscal years at issue in this claim, the parameters and guidelines and state law required that SED pupils be placed in out-of-state nonprofit facilities and thus, costs claimed for vendor services provided by out-of-state service vendors that are organized and operated on a for-profit basis are beyond the scope of the mandate and not reimbursable as a matter of law.

Reimbursement claims filed with the Controller are required as a matter of law to be filed in accordance with the parameters and guidelines adopted by the Commission.⁴² Parameters and

³⁸ *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.

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

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

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

⁴² 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

guidelines provide instructions for eligible claimants to prepare reimbursement claims for direct and indirect costs of a state-mandated program.⁴³

As indicated above, the parameters and guidelines track the regulatory language and state that reimbursement is authorized for payments to service vendors providing mental health services to SED pupils placed in out-of-state residential facilities, as specified in California Code of Regulations, title 2, section 60100. Section 60100 states that out-of-state residential programs shall meet the requirements in Welfare and Institutions Code section 11460(c)(2) through (3) and 11460(c)(3) specifies 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.*” The July 21, 2006 correction to the parameters and guidelines clarifies that “mental health services” includes residential board and care. Thus, reimbursement for the mandated activity of “providing mental health services” in out-of-state facilities includes both treatment and board and care, is conditioned on the providers meeting the requirements of Welfare and Institutions Code section 11460(c)(3), to be organized and operated on a nonprofit basis as explained above.

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 SEDs program, as well as who shall provide it, with no requirement regarding the provider’s tax identification status.⁴⁴ 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. Section 60100 of the regulations implements the requirements of former Welfare and Institutions Code section 18350, which was enacted to govern the payments for 24 hour out-of-home care provided on behalf of SED pupils who are placed out-of-home pursuant to an IEP developed pursuant to Government Code section 7572.5. Former Welfare and Institutions Code section 18350(c) requires 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. During the regulatory process for the adoption of section California Code of Regulations 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

found that the Commission’s quasi-judicial decisions are final and binding, just as judicial decisions.

⁴³ Government Code section 17557; California Code of Regulations, title 2, section 1183.7.

⁴⁴ Exhibit A, Incorrect Reduction Claim IRC 10-9705-I-01, page 17; Exhibit B, Incorrect Reduction Claim 13-9705-I-05, page 18.

residential placements is not an AFDC-Foster Care program.⁴⁵ 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 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.⁴⁶

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 nonprofit shell corporation.” 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.”⁴⁷

Subsequent to the adoption of the test claim decision and parameters and guidelines for this program, legislation was introduced to allow for state reimbursement for placement of SED pupils in out-of-state for-profit facilities. However, as described below, the legislation did not pass 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, as a reason the bill is necessary, that the federal government eliminated the requirement that a facility be

⁴⁵ Exhibit I, Final Statement of Reasons for Joint Regulations for Pupils with Disabilities, pages 127-128.

⁴⁶ Exhibit I, Final Statement of Reasons for Joint Regulations for Pupils with Disabilities, page 127 (emphasis added).

⁴⁷ Exhibit I, Final Statement of Reasons for Joint Regulations for Pupils with Disabilities, page 128.

operated as a nonprofit in order to receive federal funding in 1996.⁴⁸ However, SB 292 did not pass the assembly.⁴⁹

In 2008, AB 1805, a budget trailer bill, containing identical language to SB 292 was vetoed by the governor.⁵⁰ 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."⁵¹

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.⁵² 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.⁵³ 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.⁵⁴ 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.⁵⁵ The author notes the discrepancy between California law and federal law, which allows federal funding of

⁴⁸ Exhibit I, Assembly Committee on Human Services, analysis of Senate Bill No. 292 (2007-2008 Reg. Sess.), June 17, 2009, page 2.

⁴⁹ Exhibit I, Complete Bill History, Senate Bill No. 292 (2007-2008 Reg. Sess.).

⁵⁰ Exhibit I, Assembly Committee on Appropriations, analysis of Assembly Bill No. 421 (Reg. Sess. 2009-2010), May 20, 2009, page 3.

⁵¹ Exhibit I, Governor's Veto Message, Assembly Bill No. 1885 (Reg. Sess. 2007-2008), September 30, 2008.

⁵² Exhibit I, Assembly Committee on Appropriations, analysis of Assembly Bill No. 421 (Reg. Sess. 2009-2010), May 20, 2009, page 2.

⁵³ Exhibit I, Assembly Committee on Appropriations, analysis of Assembly Bill No. 421 (Reg. Sess. 2009-2010), May 20, 2009, page 1.

⁵⁴ Exhibit I, Assembly Committee on Appropriations, analysis of Assembly Bill No. 421 (Reg. Sess. 2009-2010), May 20, 2009, page 2.

⁵⁵ Exhibit I, Assembly Committee on Appropriations, analysis of Assembly Bill No. 421 (Reg. Sess. 2009-2010), May 20, 2009, page 2.

for-profit group home placements.⁵⁶ However the bill did not pass the Assembly and therefore did not move forward.⁵⁷

Thus, during the entire reimbursement period for this program, state law required that out-of-state residential programs shall meet the requirements of Welfare and Institutions Code section 11460(c)(2) through (3), which specified that reimbursement shall only be provided to facilities organized and operated on a nonprofit basis. Although the claimant contends that state law conflicted with federal law during this time period, absent a decision from the courts on this issue, the Commission is required by law to presume that the state statutes and regulations for this program, which were adopted in accordance with the Administrative Procedures Act, are valid.⁵⁸

Accordingly, pursuant to the law and the Commission's parameters and guidelines, reimbursement is required only if the out-of-state service vendor is organized and operated on a nonprofit basis. 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 and are not eligible for reimbursement as a matter of law.⁵⁹

B. The Controller's reduction of costs claimed for vendor service payments is consistent with the Commission's parameters and guidelines and is correct as a matter of law.

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

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.⁶⁰

⁵⁶ Exhibit I, Assembly Committee on Appropriations, analysis of Assembly Bill No. 421 (Reg. Sess. 2009-2010), May 20, 2009.

⁵⁷ Exhibit I, Complete Bill History, Assembly Bill No. 421 (Reg. Sess. 2009-2010).

⁵⁸ California Constitution, article III, section 3.5; *Robin J. v. Superior Court* (2004) 124 Cal.App.4th 414, 425.

⁵⁹ In this respect, the Commission agrees with the claimant's comments on the Draft Proposed Decision that the issue presented in this IRC is a question of law and, thus, the Commission reviews this matter de novo and determines whether the Controller's reduction of costs is correct as a matter of law.

⁶⁰ Exhibit C, Controller's Late Comments on IRC 10-9705-I-01, pages 12, 15-16 (see also the contract between Mental Health Systems, Inc. and Charter Provo Canyon School, provided in Tab 12, pages 94-104 of Exhibit C); Exhibit D, Controller's Late Comments on IRC 13-9705-I-

1. The documentation in the record supports the Controller's findings.

The claimant makes no argument disputing the Controller's findings that 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.⁶¹ 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.⁶²

The Commission finds that the evidence in the record supports the Controller's reduction of costs for vendor service payments and that, therefore, the reduction is correct as a matter of law.

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 on a for-profit basis are beyond the scope of the mandate and are not eligible for reimbursement as a matter of law. In response to the draft audit report, claimant provided a copy of the contract between Mental Health Systems, Inc. and Charter Provo Canyon School, LLC "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."⁶³ In addition, the reimbursement claims filed for 2004-2005 and 2005-2006 identify the vendor as "Mental Health Systems-Provo Canyon."⁶⁴

05, pages 11, 13 (see also the contract between Mental Health Systems, Inc. and Charter Provo Canyon School, provided in Tab 11, pages 82-91 of Exhibit D).

⁶¹ Exhibit A, Incorrect Reduction Claim 10-9705-I-01, page 23; Exhibit B, Incorrect Reduction Claim 13-9705-I-05, page 24.

⁶² Exhibit A, Incorrect Reduction Claim 10-9705-I-01, page 17.

⁶³ Exhibit C, Controller's Late Comments on IRC 10-9705-I-01, page 94 (Contract between Mental Health Services and Charter Provo Canyon School, LLC); Exhibit D, Controller's Late Comments on IRC 13-9705-I-05, page 81 (Contract between Mental Health Services and Charter Provo Canyon School, LLC).

⁶⁴ Exhibit A, Incorrect Reduction Claim 10-9705-I-01, page 98 (fiscal year 2004-2005); Exhibit B, Incorrect Reduction Claim 13-9705-I-05, page 81 (fiscal year 2005-2006).

Therefore, the evidence in the record supports the Controller's finding that the services were provided by a for-profit entity and are outside the scope of the mandate.

2. Claimant's reliance on decisions issued by OAH and the United States Supreme Court is misplaced.

The claimant further argues that a decision issued by OAH supports the position that reimbursement is required if a SED pupil is placed in a for-profit facility that complies with federal IDEA law.⁶⁵ The OAH decision relied upon by claimant involves 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.⁶⁶ 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.⁶⁷

Although the District Court's decision in *Riverside County* is binding with respect to the placement of that student,⁶⁸ the court did not address state-mandated reimbursement under article XIII B, section 6. Moreover, the claimant has provided no documentation or evidence that the costs claimed in these 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. Thus, the Commission does not need to reach the issue whether reimbursement under article XIII B, section 6 would be required in such a case.

The claimant also relies on the U.S. Supreme Court decision in *Florence County School District Four v. Carter*,⁶⁹ for the proposition that local government will be subject to increased litigation

⁶⁵ Exhibit A, Incorrect Reduction Claim 10-9705-I-01, pages 15-16; Exhibit B, Incorrect Reduction Claim 13-9705-I-05, pages 15-16.

⁶⁶ Exhibit B, Incorrect Reduction Claim 13-9705-I-05, pages 67-76.

⁶⁷ Exhibit I, *Riverside County Department of Mental Health v. Sullivan* (E.D.Cal. 2009) EDCV 08-0503-SGL.

⁶⁸ Absent "unusual circumstances," or an intervening change in the law, the decision of the reviewing court establishes the law of the case and binds the agency and the parties to the action in all further proceedings addressing the particular claim. (*George Arakelian Farms, Inc. v. Agricultural Labor Relations Board* (1989) 49 Cal.3d 1279, 1291.)

⁶⁹ *Florence County School District v. Carter* (1993) 510 U.S. 7.

with the Controller's interpretation.⁷⁰ In the *Florence* case, the court held that parents can be reimbursed under the 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.'"⁷¹ Unlike the court's equitable powers under IDEA, the reimbursement requirements of article XIII B, section 6, must be strictly construed and not applied as an "equitable remedy to cure the perceived unfairness resulting from political decisions on funding priorities."⁷²

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 facilities organized and operated for-profit, is consistent with the Commission's parameters and guidelines and is correct as a matter of law.

V. Conclusion

Based on the foregoing, the Commission finds that the Controller's reductions are correct as a matter of law.

Based on the foregoing, the Commission denies these IRCs.

⁷⁰ Exhibit A, Incorrect Reduction Claim 10-9705-I-01, pages 14-15; Exhibit B, Incorrect Reduction Claim 13-9705-I-05, page 15.

⁷¹ *Florence County School District, supra*, 510 U.S. 5, 12 (citing its prior decision in *School Comm. of Burlington v. Department of Ed. of Mass.* (1985) 471 U.S. 359, 369.)

⁷² *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).



RE: **Decision**

Seriously Emotionally Disturbed Pupils: Out-of-State Mental Health Services,
10-9705-I-01 and 13-9705-I-05
Government Code Section 7576, as amended by Statutes 1996, Chapter 654;
California Code of Regulations, Title 2, Division 9, Chapter 1, Sections 60100 and 60110
Fiscal Years: 2001-2002, 2002-2003, 2003-2004, 2004-2005, and 2005-2006
County of San Diego, Claimant

On May 26, 2016, the foregoing decision of the Commission on State Mandates was adopted on the above-entitled matter.



Heather Halsey, Executive Director

Dated: June 1, 2016

BEFORE THE
 COMMISSION ON STATE MANDATES
 STATE OF CALIFORNIA

**IN RE INCORRECT REDUCTION CLAIM
 ON:**

Education Code Sections 44660-44665

Statutes 1983, Chapter 498;

Statutes 1999, Chapter 4

Fiscal Years 1997-1998, 1998-1999, 1999-
 2000, 2000-2001, 2001-2002, 2002-2003,
 2003-2004, and 2004-2005

Oceanside Unified School District, Claimant

Case No.: 14-9825-I-01

The Stull Act

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

(Adopted September 23, 2016)

(Served September 28, 2016)

DECISION

The Commission on State Mandates (Commission) heard and decided this Incorrect Reduction Claim (IRC) during a regularly scheduled hearing on September 23, 2016. Arthur Palkowitz and Dr. Todd McAteer, Director of Human Resources for Oceanside Unified School District, appeared for the claimant. Jim Spano and Ken Howell appeared for the State Controller's Office.

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

The Commission adopted the Proposed Decision to partially approve the IRC by a vote of 6-0 as follows:

Member	Vote
Richard Chivaro, Representative of the State Controller	Yes
Mark Hariri, Representative of the State Treasurer, Vice Chairperson	Yes
Scott Morgan, Deputy Director of Administration and State Clearinghouse Director, Governor's Office of Planning and Research	Yes
Sarah Olsen, Public Member	Yes
Eraina Ortega, Representative of the Director of the Department of Finance, Chairperson	Yes
Carmen Ramirez, City Council Member	Absent
Don Saylor, County Supervisor	Yes

Summary of the Findings

This IRC addresses reductions made by the State Controller's Office (Controller) to reimbursement claims of the Oceanside Unified School District (claimant) for fiscal years 1997-

1998 through 2004-2005¹ under *The Stull Act* program. The Controller reduced the claims filed for these fiscal years to \$0 (an audit adjustment of \$1,270,420 in direct and indirect costs) due to lack of supporting documentation.

The Commission finds that:

- 1) The reduction of costs based on the number of employees evaluated under the mandate is correct as a matter of law and not arbitrary, capricious, or entirely lacking in evidentiary support.

The claimant did not provide any evidence of the employees evaluated during the audit. After the audit, however, the claimant provided the Controller with documentation showing that 1,698 employees were evaluated under the mandate during the audit period. The Controller found that of the 1,698 employees listed by the claimant that received evaluations for the audit period, 1,149 evaluations fell within the scope of the mandate. The claimant agrees with this finding, except for a small number of evaluations in fiscal year 1997-1998. The claimant, however, does not provide sufficient evidence to rebut the Controller's findings for that fiscal year.

- 2) Based on this record, the Controller's reduction of costs to \$0 is arbitrary, capricious, or entirely lacking in evidentiary support.

The Controller agrees that the claimant performed the required evaluations under the mandate and concluded that 1,149 evaluations were performed by the claimant during the audit period and, thus, a reduction of costs to \$0 is not supported by the record.

However, the parties dispute the time taken to perform the mandate. The claimant alleges that each evaluation took five to ten hours, and later asserted that each evaluation took 2.5 hours based on time studies conducted by other school districts. There is no evidence in the record to support the conclusion that it took the claimant's employees 2.5 hours, or five to ten hours, to conduct the evaluations under the mandate.

The Controller has offered to allow reimbursement at 30 minutes for each of the 1,149 employees evaluated (which results in reimbursement of \$35,967, which includes both direct and indirect costs), based on the claimant's time logs for fiscal year 2006-2007 that recorded the time spent on the mandate for all months in the fiscal year on one form; teacher evaluation forms provided by the claimant that disclosed 30 minutes of actual classroom observation; and the Controller's review of a sample of written evaluations for teachers for fiscal years 2006-2007 and 2007-2008. There is no evidence in the record that the Controller's findings are wrong, or that the Controller's offer to apply the 30 minutes to the evaluations conducted in fiscal years 1997-1998 through 2004-2005 is arbitrary, capricious, or entirely lacking in evidentiary support.

Accordingly, the Commission partially approves this IRC. Pursuant to Government Code section 17551(d) and section 1185.9 of the Commission's regulations, the Commission requests that the Controller reinstate \$35,967, which includes both direct and indirect costs, to the claimant.

¹ Fiscal years 2005-2006, 2006-2007, and 2007-2008 were also part of the audit, but were not included in this IRC.

COMMISSION FINDINGS

I. Chronology

- 08/24/2011 The Controller issued the Final Audit Report.²
- 08/20/2014 The claimant filed the IRC.³
- 11/26/2014 The Controller filed a request for extension of time to file comments on the IRC, which was granted for good cause.
- 02/02/2015 The Controller filed a second request for extension of time to file comments on the IRC, which was granted for good cause.
- 03/27/2015 The Controller filed comments on the IRC.⁴
- 05/04/2015 The Claimant filed late rebuttal comments on the IRC.⁵
- 06/17/2016 Commission staff issued the Draft Proposed Decision.⁶
- 06/29/2016 The Controller filed comments on the Draft Proposed Decision.⁷
- 07/08/2016 The claimant filed comments on the Draft Proposed Decision.⁸

II. Background

A. The Stull Act Program

The Stull Act was originally enacted in 1971 to establish a uniform system of evaluation and assessment of the performance of “certificated personnel” (including certificated non-instructional personnel) within each school district.⁹ As originally enacted, the Stull Act required the governing board of each school district to develop and adopt specific guidelines to evaluate and assess certificated personnel, and to avail itself of the advice of certificated instructional personnel before developing and adopting the guidelines. The evaluation and assessment of the certificated personnel had to be in writing, conducted once each school year for probationary employees and every other year for permanent employees, and a copy transmitted to the employee no later than sixty days before the end of the school year. If the employee was not performing in a satisfactory manner according to the standards, the “employing authority” was required to notify the employee in writing, describe the unsatisfactory performance, and confer with the employee in making specific recommendations

² Exhibit A, IRC, pages 80-98 (Final Audit Report).

³ Exhibit A, IRC.

⁴ Exhibit B, Controller’s Comments on the IRC.

⁵ Exhibit C, Claimant’s Late Rebuttal Comments.

⁶ Exhibit D, Draft Proposed Decision.

⁷ Exhibit E, Controller’s Comments on the Draft Proposed Decision.

⁸ Exhibit F, Claimant’s Comments on the Draft Proposed Decision.

⁹ Former Education Code sections 13485-13490.

as to areas of improvement and endeavor to assist in the improvement. The employee then had the right to initiate a written response to the evaluation, which became a permanent part of the employee's personnel file. The school district was also required to hold a meeting with the employee to discuss the evaluation.

The Stull Act was amended from 1975 through 1999, and a Test Claim was filed on these amendments. On May 27, 2004, the Commission partially approved the Test Claim and adopted the Statement of Decision, finding that Statutes 1983, chapter 498 and Statutes 1999, chapter 4, which amended Education Code sections 44660-44665, impose a reimbursable state-mandated higher level of service on school districts. The Commission also found that many activities in the Test Claim pertaining to certificated personnel were required under preexisting law and were therefore not reimbursable, such as developing and adopting specific evaluation and assessment guidelines for performance; evaluating and assessing them as it relates to the established standards; preparing and drafting a written evaluation, to include recommendations, if necessary, for areas of improvement; receiving and reviewing written responses to evaluations; and preparing for and holding a meeting with the evaluator to discuss the evaluation and assessment.¹⁰ The Parameters and Guidelines were adopted on consent on September 27, 2005, authorizing reimbursement for only the following activities:

A. Certificated Instructional Employees

1. Evaluate and assess the performance of certificated instructional employees that perform the requirements of educational programs mandated by state or federal law as it reasonably relates to the instructional techniques and strategies used by the employee and the employee's adherence to curricular objectives (Ed. Code, § 44662, subd. (b), as amended by Stats. 1983, ch. 498.). (*Reimbursement period begins July 1, 1997.*)

Reimbursement for this activity is limited to:

- a. reviewing the employee's instructional techniques and strategies and adherence to curricular objectives, and
- b. including in the written evaluation of the certificated instructional employees the assessment of these factors during the following evaluation periods:
 - o once each year for probationary certificated employees;
 - o every other year for permanent certificated employees; and
 - o beginning January 1, 2004, every five years for certificated employees with permanent status who have been employed at least ten years with the school district, are highly qualified (as defined in 20 U.S.C. § 7801), and whose previous evaluation

¹⁰ Exhibit A, IRC, pages 28 and 35 (Statement of Decision; page number citations refer to the PDF page numbers).

rated the employee as meeting or exceeding standards, if the evaluator and certificated employee being evaluated agree.

Note: For purposes of claiming reimbursement, eligible claimants must identify the state or federal law mandating the educational program being performed by the certificated instructional employees.

2. Evaluate and assess the performance of certificated instructional employees that teach reading, writing, mathematics, history/social science, and science in grades 2 to 11 as it reasonably relates to the progress of pupils towards the state adopted academic content standards as measured by state adopted assessment tests (Ed. Code, § 44662, subd. (b), as amended by Stats. 1999, ch. 4.). (*Reimbursement period begins March 15, 1999.*)

Reimbursement for this activity is limited to:

- a. reviewing the results of the Standardized Testing and Reporting test as it reasonably relates to the performance of those certificated employees that teach reading, writing, mathematics, history/social science, and science in grades 2 to 11, and
 - b. including in the written evaluation of those certificated employees the assessment of the employee's performance based on the Standardized Testing and Reporting results for the pupils they teach during the evaluation periods specified in Education Code section 44664, and described below:
 - o once each year for probationary certificated employees;
 - o every other year for permanent certificated employees; and
 - o beginning January 1, 2004, every five years for certificated employees with permanent status who have been employed at least ten years with the school district, are highly qualified (as defined in 20 U.S.C. § 7801), and whose previous evaluation rated the employee as meeting or exceeding standards, if the evaluator and certificated employee being evaluated agree.
- B. Certificated (Instructional and Non-Instructional) Employees
1. Evaluate and assess permanent certificated, instructional and non-instructional, employees that perform the requirements of educational programs mandated by state or federal law and receive an unsatisfactory evaluation in the years in which the permanent certificated employee would not have otherwise been evaluated pursuant to Education Code section 44664 (i.e., every other year). The additional evaluations shall last until the employee achieves a positive evaluation, or is separated from the school district (Ed. Code, § 44664, as amended by Stats. 1983, ch. 498). (*Reimbursement period begins July 1, 1997.*)

This additional evaluation and assessment of the permanent certificated employee requires the school district to perform the following activities:

- a. evaluating and assessing the certificated employee performance as it reasonably relates to the following criteria: (1) the progress of pupils toward the standards established by the school district of expected pupil achievement at each grade level in each area of study, and, if applicable, the state adopted content standards as measured by state adopted criterion referenced assessments; (2) the instructional techniques and strategies used by the employee; (3) the employee's adherence to curricular objectives; (4) the establishment and maintenance of a suitable learning environment, within the scope of the employee's responsibilities; and, if applicable, (5) the fulfillment of other job responsibilities established by the school district for certificated non-instructional personnel (Ed. Code, § 44662, subs. (b) and (c));
- b. reducing the evaluation and assessment to writing (Ed. Code, § 44663, subd. (a)). The evaluation shall include recommendations, if necessary, as to areas of improvement in the performance of the employee. If the employee is not performing his or her duties in a satisfactory manner according to the standards prescribed by the governing board, the school district shall notify the employee in writing of that fact and describe the unsatisfactory performance (Ed. Code, § 44664, subd. (b));
- c. transmitting a copy of the written evaluation to the certificated employee (Ed. Code, § 44663, subd. (a));
- d. attaching any written reaction or response to the evaluation by the certificated employee to the employee's personnel file (Ed. Code, § 44663, subd. (a)); and
- e. conducting a meeting with the certificated employee to discuss the evaluation (Ed. Code, § 44553, subd. (a)).

Note: For purposes of claiming reimbursement, eligible claimants must identify the state or federal law mandating the educational program being performed by the certificated, instructional and non-instructional, employees.

C. Training

1. Train staff on implementing the reimbursable activities listed in Section IV of these parameters and guidelines. (One-time activity for each employee.) (*Reimbursement period begins July 1, 1997.*)¹¹

The Parameters and Guidelines, as originally proposed by the test claimant and adopted by the Commission, also require claimants to submit contemporaneous source documentation, such as time records or time logs, to verify their actual costs. Evidence to corroborate the source documents, such as declarations or worksheets, may also be submitted. However, corroborating documents cannot be substituted for the contemporaneous source documentation requirement. In this regard, the introductory paragraphs in Section IV. of the Parameters and Guidelines state the following:

To be eligible for mandated cost reimbursement for any fiscal year, only actual costs may be claimed. Actual costs are those costs actually incurred to implement the mandated activities. Actual costs must be traceable and supported by source documents that show the validity of such costs, when they were incurred, and their relationship to the reimbursable activities. A source document is a document created at or near the same time the actual cost was incurred for the event or activity in question. Source documents may include, but are not limited to, employee time records or time logs, sign-in sheets, invoices, and receipts.

Evidence corroborating the source documents may include, but is not limited to, worksheets, cost allocation reports (system generated), purchase orders, contracts, agendas, and declarations. Declarations must include a certification or declaration stating, "I certify (or declare) under penalty of perjury under the laws of the State of California that the foregoing is true and correct," and must further comply with the requirements of Code of Civil Procedure section 2015.5. Evidence corroborating the source documents may include data relevant to the reimbursable activities otherwise in compliance with local, state, and federal government requirements. However, corroborating documents cannot be substituted for source documents.¹²

Section V. of the Parameters and Guidelines authorizes reimbursement for employee salaries and benefits and directs claimants to:

Report each employee implementing the reimbursable activities by name, job classification, and productive hourly rate (total wages and related benefits divided by productive hours). Describe the specific reimbursable activities performed and the hours devoted to each reimbursable activity performed.

¹¹ Exhibit A, IRC, pages 54-56 (Parameters and Guidelines); Exhibit G, Item 2, Proposed Consent Calendar and 7, Final Staff Analysis and Proposed Parameters and Guidelines, *The Stull Act*, September 27, 2005, pages 10-11.

¹² Exhibit A, IRC, page 53 (Parameters and Guidelines).

And section VI. of the Parameters and Guidelines requires claimants to retain all documentation until the ultimate resolution of any audit findings:

All documentation used to support the reimbursable activities, as described in Section IV., must be retained during the period subject to audit. If an audit has been initiated by the Controller during the period subject to audit, the retention period is extended until the ultimate resolution of any audit findings.¹³

Claiming instructions dated December 12, 2005, were issued by the Controller for the filing of the initial reimbursements claims for *The Stull Act* program for costs incurred in fiscal years 1997-1998 through 2004-2005. The claiming instructions include the adopted Parameters and Guidelines and identify the reimbursable claim components and supporting documentation requirements consistent with the Parameters and Guidelines.¹⁴ The Controller states that the claiming instructions issued for subsequent claiming years during the audit period did not change.¹⁵

B. The Controller's Audit and Summary of the Issues

The Controller audited claimant's reimbursement claims for salary and benefit costs in fiscal years 1997-1998 through 2004-2005, and 2006-2007 through 2007-2008 (no claims were filed for 2005-2006). The Controller reduced the claims filed for fiscal years 1997-1998 through 2004-2005 to \$0 (an audit adjustment of \$1,270,420 in direct and indirect costs). No reductions were made to the reimbursement claims for fiscal years 2006-2007 and 2007-2008.¹⁶

For the 1997-1998 through 2004-2005 fiscal year claims, the claimant supported the time claimed for each employee with "Employee Average Time Records for Mandated Costs" forms prepared by the mandate consultant for purposes of claiming costs. The form asks each employee to "report below the *average* amount of time spent (in minutes) by you to implement each of the reimbursable activities for the mandated program" for each fiscal year at issue (fiscal years 1997-1998 through 2004-2005). In February or March 2006, 49 school principals and assistant principals completed and signed the forms under penalty of perjury that a "good faith estimate" of the average time performing the reimbursable activities for each evaluation during the audit period was being reported.¹⁷ For example, the first form provided shows an average time to prepare for the evaluation of 50 minutes, 45 minutes for a goals and objectives conference with the instructor, 20 minutes for a pre-observation conference with the instructor, 40 minutes for the classroom observation of the instructor, 30 minutes for the post-observation conference with the instructor, 40 minutes for the final conference with the instructor, and 80

¹³ Exhibit A, IRC, pages 57-58 (Parameters and Guidelines).

¹⁴ Exhibit A, IRC, pages 61, 75.

¹⁵ Exhibit B, Controller's Comments on the IRC, page 11.

¹⁶ Exhibit A, IRC, pages 80-99 (Final Audit Report), and 100-126 (reimbursement claims).

¹⁷ Exhibit A, IRC, pages 3 and 143-191.

minutes to complete a district report, which totals roughly five hours for one evaluation as follows:¹⁸

<u>Reimbursable Activities Codes:</u> Code 11 Preparing for the evaluation Code 12 Goals and objectives conference with instructor Code 13 Pre-observation conference with instructor Code 14 Classroom observation of instructor Code 15 Post-observation conference with instructor Code 16 Final conference with instructor Code 17 District reporting CLASSROOM TEACHER TIME IS NOT REIMBURSED	<u>Evaluation Criteria:</u> (A) district standards and test results (B) instructional techniques/strategies (C) adherence to curricular objectives (D) suitable learning environment																																
Allocate the average time spent on each criterion (A-D) for each of the following evaluation steps:	Average time in Minutes																																
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Code 11 Preparing for the evaluation	20	10	10	10																													
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Code 14 Classroom observation of instructor	10	10	10	10																													
Code 15 Post-observation conference with instructor	5	10	10	5																													
Code 16 Final conference with instructor	10	10	10	10																													
Code 17 District Reporting	20	20	20	20																													

Other “Employee Average Time Records for Mandated Costs” forms show estimates of five to ten hours per evaluation, for a mean time of about eight hours.¹⁹

The Controller reduced the reimbursement claims for fiscal years 1997-1998 through 2004-2005 to \$0 because the claimant did not support the time claimed with “source documents” in accordance with the Parameters and Guidelines, or provide the Controller access to the employee evaluations completed during the audit period to support the number of employees evaluated pursuant to the mandate.²⁰

The audit also included the reimbursement claims for fiscal years 2006-2007 and 2007-2008, for which there were no reductions made.

For these two years, the district provided a list of employees who evaluated teachers, their title, productive hourly rate detail, as well as contemporaneous time documentation that supported an average time of approximately 30 minutes per allowable evaluation. The district also provided a list of teachers who were

¹⁸ Exhibit A, IRC, page 143.

¹⁹ Exhibit A, IRC, pages 143-191 (Employee Average Time Record for Mandated Costs forms). The mean of the first ten forms (pp. 143-153) is 8.05 hours.

²⁰ Exhibit A, IRC, pages 84 and 91 (Final Audit Report); Exhibit B, Controller’s Comments on the IRC, page 12.

evaluated, which allowed the SCO auditors to determine which evaluations were reimbursable.²¹

The Final Audit Report more specifically states that the claimant provided time logs for fiscal year 2006-2007 that recorded the time spent on the mandate for all months in the fiscal year on one form. The time logs were not dated or signed by the employees, and “the district did not provide source documents supporting the time recorded in the annual forms.”²² So the Controller determined the allowable salaries and benefits by obtaining the district’s teacher evaluation procedures and forms, and interviewing administrators who performed the evaluation activities in these fiscal years. The district’s teacher evaluation forms disclosed 30 minutes of actual classroom observation. The claimant then requested that it be allowed to support its claims with “auditor verification of its written observations and final summary performance teacher evaluations from personnel records.”²³ The Controller also selected a ten percent random sample of 23 school sites in the claimant’s district. The claimant also provided copies of written evaluations and summative evaluations for teachers at El Camino High School, Jefferson Middle School, and Mission Elementary School for fiscal years 2006-2007 and 2007-2008. Actual pay, benefit information, and resource codes for employees claimed in these two fiscal years were also provided to the Controller.²⁴ Based on this information, the Controller determined that the costs claimed for fiscal years 2006-2007 and 2007-2008 were understated by \$4,834, and the Final Audit Report indicates that the claimant “agreed to our recommendation that it allow half an hour for each written observation and final teacher evaluation verified.”²⁵

In the response to the IRC, the Controller explained: “There is no reasonable means of applying the time allowance [from 2006-2008] to FY 1997-98 through FY 2004-05 without knowing the certificated instructional employees evaluated and the reimbursability of the evaluations.”²⁶

C. Post-IRC Negotiations

After the claimant filed the IRC, the Controller contacted the claimant and offered to adjust the audit findings if the claimant provided a list of every employee evaluated during those years.²⁷ The Controller was emailed the list from the claimant on December 19, 2014.²⁸ On December 24, 2014, the Controller emailed the claimant to request clarification because the provided information appeared to be incomplete.²⁹ On January 5, 2015, the claimant emailed the

²¹ Exhibit B, Controller’s Comments on the IRC, page 13.

²² Exhibit A, IRC, page 91.

²³ Exhibit A, IRC, page 91.

²⁴ Exhibit A, IRC, page 92. Exhibit B, Controller’s Comments on the IRC, page 13.

²⁵ Exhibit A, IRC, pages 91 and 92 (Final Audit Report).

²⁶ Exhibit B, Controller’s Comments on the IRC, page 14.

²⁷ Exhibit B, Controller’s Comments on the IRC, page 8.

²⁸ Exhibit B, Controller’s Comments on the IRC, pages 8, 67-97, 100.

²⁹ Exhibit B, Controller’s Comments on the IRC, pages 8, 99, 104-105, which seeks clarification as follows:

Controller to confirm that the information provided was complete.³⁰ On January 21, 2015, the Controller emailed the claimant to explain that of the 1,698 employees listed by the claimant that received evaluations during fiscal years 1997-1998 through 2004-2005, the Controller allowed 1,149 evaluations and excluded the rest because of duplicated evaluations for permanent employees performed in consecutive years, rather than every other year; duplicated evaluations performed in the same year; evaluations outside the audit period; and unallowable subjects or programs performed by certificated instructional employees.³¹ The email states in relevant part the following:

The district provided a listing of 1,698 employees that received evaluations for the audit period. We removed evaluations from the population for the following reasons:

- Duplicated evaluations for permanent employees performed in consecutive years, rather than every other year (51)
- Duplicated evaluations performed in the same year (10)
- Items outside the IRC period (472)
- Unallowable subjects/programs performed by certificated instructional employees (16)

The allowable population was 1,149 total evaluations for the IRC period. Here's a breakdown of allowable evaluations per year:

- FY 1997-98 – 4

Namely, does this list exclude certificated instructional and non-instructional employees that have less than 10 years tenure? If so, the list would not represent the complete listing of certificated instructional and non-instructional employees that received evaluations for FY 1997-98 through 2004-05.

Also, the list only mentions CIE (Certificated Instructional Employees) ... does this mean that certificated non-instructional employees are not included? Per the Ps and Gs, permanent certificated instructional and non-instructional employees that receive an unsatisfactory evaluation in the years in which they would not have otherwise been evaluated are considered reimbursable (along with various activities).

My overarching concern with this analysis is that [we] may be working with incomplete data, and I want to provide the district every opportunity to provide the full and complete listing for consideration.

³⁰ Exhibit B, Controller's Comments on the IRC, pages 8, 103-104, where the claimant responds as follows: "The list includes all certificated employees. The District does not [hire] employees that are certificated non-instructional employees. The list represents the complete listing of certificated instructional employees that received evaluations for FY 1997-98 through 2004-05."

³¹ Exhibit B, Controller's Comments on the IRC, pages 15, 108.

- FY 1998-99 – 55
- FY 1999-2000 – 96
- FY 2000-01 – 196
- FY 2001-02 – 249
- FY 2002-03 – 164
- FY 2003-04 – 220
- FY 2004-05 – 165³²

The Controller offered to revise the audit adjustment to reimburse 30 minutes for each of the 1,149 evaluations (the same average time allowed for the 2006-2007 and 2007-2008 claims), and to augment the audit findings for 1997-1998 to 2004-2005 by \$35,967 in allowable costs.

On January 29, 2015, the claimant’s representative sent an email refusing the Controller’s offer, arguing that five to six hours, rather than 30 minutes, is the average time to perform the mandated activities as follows:

As I initially expressed to you, we are not in agreement to the estimate of 30 minutes per evaluation. The reasonable period to conduct the informal classroom observations; formal classroom observations, writing the final evaluation reports and/or preparing the Teacher Evaluation Report is approximately five-six hours. This period of time has been accepted by the Controller in other Stull Act audits.³³

As a result of the impasse, the Controller said it “did not expand [its] audit procedures to test the validity of the FY 1997-98 through FY 2004-05 listing of evaluations the district provided.”³⁴ Therefore, the reimbursement claims at issue in this IRC all remain reduced to \$0.

III. Positions of the Parties

A. Oceanside Unified School District

The claimant argues that the Controller incorrectly reduced the costs claimed for fiscal years 1997-1998 through 2004-2005 and seeks reinstatement of \$1,270,420. The claimant argues that it provided a list of employees, title, and the employees’ hourly rates for each fiscal year that evaluations were performed. It also provided average time records, copies of its collective bargaining agreements containing evaluation requirements, and policies and procedures on evaluations, all of which confirm that the activities were performed during the audit period. The claimant states that “[t]here can be no doubt the District’s school site staff performed the reimbursable activities” and that “sufficient documentation” was provided to prove that each

³² Exhibit B, Controller’s Comments on the IRC, page 108.

³³ Exhibit B, Controller’s Comments on the IRC, pages 15, 118.

³⁴ Exhibit B, Controller’s Comments on the IRC, page 15.

school site performed the activities of assessing and evaluating certificated employees as required by the mandate.³⁵ The claimant also states:

Furthermore, the district complied fully with the requirements of the Stull Act during the claiming period and we feel that we submitted claims appropriate to the costs incurred. While we were able to supply supporting documentation, it was not accepted as sufficient by the audit team. The additional documentation requested was, and is, available but would be a significant drain on district resources, including staff and funds, to provide. Consequently, the district cannot expend any further time or resources to produce the requested records.³⁶

The claimant also relies on the Office of Management and Budget Circular A-87,³⁷ which establishes standards for state and local governments to determine administrative costs applicable to grants, contracts, and other agreements with state and local governments. According to the claimant: “Randomly sampling workers to find out what they are working on is one of the federally approved methods of identifying worker effort. Such method is reasonable and may be implemented rather than 100 percent time reporting method.”³⁸

In late rebuttal comments on the IRC submitted on May 4, 2015, the claimant states that “the time spent by District employees to conduct the reimbursable activities would average 6-7 hours per employee.”³⁹ The claimant further argues that the Controller’s audits on *The Stull Act* of other school district claims supports the average time claimed in this IRC. For example, the claimant refers to an audit finding of the average time spent for evaluations in the Poway Unified School District of 1.52 hours for permanent employees, 3.57 hours for non-permanent employees, and 12.93 hours for unsatisfactory evaluations. For the Norwalk-La Mirada Unified School District, the Controller allowed 1.89 hours for permanent employees, 3.07 hours for non-permanent employees, and 12.99 hours for unsatisfactory evaluations. And the claimant asserts that Long Beach Unified School District provided the same documentation to the Controller as the claimant, and was allowed an average of 2.14 hours for each evaluation for each fiscal year. The claimant argues that:

Documentation submitted by the claimant supports the reasonable time spent per evaluation of 6.40 hours [in] FY 1997-98 and 6.50 hours in FY 1998-99. For the claimant’s time to be limited by the Controller to 30 minutes is far below the other times accepted in School District audits and is inconsistent with the documentation submitted by the claimant. As a result [the] Controller’s decision to disallow the reimbursement claim is unreasonable, as well as arbitrary and capricious.⁴⁰

³⁵ Exhibit A, IRC, pages 6-7.

³⁶ Exhibit A, IRC, (claimant’s response to the Final Audit Report) page 98.

³⁷ Exhibit A, IRC, page 244.

³⁸ Exhibit A, IRC, page 7.

³⁹ Exhibit C, Claimant’s Late Rebuttal Comments, page 3.

⁴⁰ Exhibit C, Claimant’s Late Rebuttal Comments, page 4.

The claimant also argues that the Controller's offer to revise the audit findings for fiscal year 1997-1998 after the IRC was filed, by allowing only four evaluations instead of 67, is arbitrary and capricious. The claimant concludes by stating that the "District accepts the Controller's allowable total evaluations of 1,149 . . . adjusted for the evaluations for FY 1997-1998 for a total of 1,212. The Claimant's adjusted reimbursement claim for FY 1997-1998 to FY 2004-2005 in the amount of \$181,800.00 is based on an average hourly rate of \$60.00 per hour at 2.5 hours per evaluation."⁴¹

The claimant filed comments disagreeing with the Draft Proposed Decision, stating:

The guidelines for the Stull Act program were adopted September 27, 2005, by the Commission. The initial claim period, Fiscal Years 1997-1998, 1998-1999, 1999-2000, 2000-2001, 2001-2002, 2002-2003, 2003-2004, 2004-2005, predates the date of guideline adoption. Controller's application of an overly narrow interpretation of the supporting documentation guideline language to claims prior to the fiscal year 2005/06 violates the Clovis Unified School District appellate court decision dated September 21, 2010. This decision found Controller could not apply contemporaneous source documentation requirements (CSDR) prior to the date the CSDR language was actually approved by Commission on State Mandates and added to a program's guidelines.⁴²

Claimant further argues that 2.5 hours incurred for each evaluation is supported by the Controller's audit of a comparable neighboring K-12 school district, as well as other time studies accepted by the Controller for the audits of other school districts. Claimant asserts:

Effectively the time studies included in the Controller's audits created a Reasonable Reimbursement Methodology, a uniform cost allowance, in conformity with Government Code section 17518.5(b), as it is based on cost information from a representative sample of eligible claimants, information provided by association of local agencies and school districts, or other projections of local costs. The time study of 2.5 hours per evaluation is reliable since auditing of reimbursement claims is not a prerequisite for the development and approval of a reasonable reimbursement methodology. (Cal. Code Regs., §1183.12)

Time studies have been acceptable methodologies for reimbursement in lieu of or in support of contemporaneous records. To disregard its application, especially when the time studies have been approved by the Controller is an abuse of discretion. To conclude the reimbursable activities listed above were conducted in 30 minutes, allows less than 4 minutes for each activity to be completed. An analysis of each activity easily concludes otherwise. As such the record includes evidence, as required by the Commission's regulations, to justify reimbursement at 2.5 hours per evaluation.⁴³

⁴¹ Exhibit C, Claimant's Late Rebuttal Comments, page 7.

⁴² Exhibit F, Claimant's Comments on the Draft Proposed Decision, page 2.

⁴³ Exhibit F, Claimant's Comments on the Draft Proposed Decision, pages 2-3.

B. State Controller's Office

The Controller maintains that the reductions are correct and that the audit finding should be upheld because the district's claims do not comply with the documentation requirements in the Parameters and Guidelines. The Controller agrees that the claimant "(1) performed the required evaluations as contained in its Collective Bargaining Agreements, (2) confirmed that the activities were performed, and (3) provided the SCO auditors the district's procedure and forms."⁴⁴ However, the claimant did not provide sufficient source documentation supporting the costs claimed or identify a list of certificated instructional employees evaluated in fiscal years 1997-1998 through 2004-2005. The Controller states the following:

As noted previously, FY 2006-07 and FY 2007-08 were part of the audit period, but were not included in this IRC. For these two years, the district provided a list of employees who evaluated teachers, their title, productive hourly rate detail, as well as contemporaneous time documentation that supported an average time of approximately 30 minutes per allowable evaluation. The district also provided a list of teachers who were evaluated, which allowed the SCO auditors to determine which evaluations were reimbursable.

For FY 1997-98 through FY 2004-05, the district provided only annual certifications that estimated the time spent by evaluators on reimbursable activities. The district did not provide actual cost documentation supporting costs claimed or identify a list of certificated instructional employees evaluated during this period (Exhibit M). Such information is necessary to determine whether the evaluations are reimbursable. Therefore, none of the costs claimed for FY 1997-98 through FY 2004-05 are allowable⁴⁵

As to the claimant's reference to the Office of Management and Budget Circular A-87, the Controller notes that the "district did not provide the auditors with any reasonable sampling methodology to arrive at allowable costs."⁴⁶

The Controller states that after receiving the IRC, it agreed to reevaluate the adjustment if the claimant provided documentation supporting the number of employees evaluated in fiscal years 1997-1998 through 2004-2005. The claimant provided the information in December 2014, and the Controller recalculated allowable salary and benefit costs "based on the time allowance of approximately 30 minutes per evaluation that the district supported with contemporaneous documentation during FY 2006-07 and FY 2007-08." In response to the claimant's argument that the Controller authorized more time per evaluation in its other audits of *The Stull Act* program, the Controller states: "Time documentation supporting the reimbursable activities of the Stull Act Program for other audits is not relevant to this audit. The district's records supported approximately 30 minutes for the reimbursable activities of the Stull Act Program, not five to six hours, as requested by [the claimant]."⁴⁷ The Controller further states that "we

⁴⁴ Exhibit B, Controller's Comments on the IRC, page 14.

⁴⁵ Exhibit B, Controller's Comments on the IRC, page 13.

⁴⁶ Exhibit B, Controller's Comments on the IRC, page 14.

⁴⁷ Exhibit B, Controller's Comments on the IRC, page 14.

reached an impasse in reinstating any of the audit adjustments, and as such, we did not expand our audit procedures to test the validity of the FY 1997-98 through 2004-05 listing of evaluations the district provided.”⁴⁸

The Controller filed comments concurring with the Draft Proposed Decision to deny the IRC.⁴⁹

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 the local agency or school district. If the Commission determines that a reimbursement claim has been incorrectly reduced, section 1185.9 of the Commission’s regulations requires the Commission to send the 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 6.⁵⁰ 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.”⁵¹

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.⁵² Under this standard, the courts have found that:

When reviewing the exercise of discretion, “[t]he scope of review is limited, out of deference to the agency’s authority and presumed expertise: ‘The court may not reweigh the evidence or substitute its judgment for that of the agency. [Citation.]’” ... “In general ... the inquiry is limited to whether the decision was

⁴⁸ Exhibit B, Controller’s Comments on the IRC, page 14.

⁴⁹ Exhibit E, Controller’s Comments on the Draft Proposed Decision.

⁵⁰ Government Code sections 17551, 17552; *Kinlaw v. State of California* (1991) 54 Cal.3d 326, 331-334.

⁵¹ *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.

⁵² *Johnston v. Sonoma County Agricultural Preservation and Open Space District* (2002) 100 Cal.App.4th 973, 983-984; *American Bd. of Cosmetic Surgery, Inc. v. Medical Bd. of California* (2008) 162 Cal.App.4th 534, 547.

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.]’ ”⁵³

The Commission must review the Controller’s audit in light of the fact that the initial burden of providing evidence for a claim of reimbursement lies with the claimant.⁵⁴ In addition, sections 1185.1(f)(3) and 1185.2(c) of the Commission’s regulations require that any assertions of fact by the parties to an IRC must be supported by documentary evidence. The Commission’s ultimate findings of fact must be supported by substantial evidence in the record.⁵⁵

The Controller’s Reduction of Costs Due to Lack of Documentation Is Correct as a Matter of Law and Not Arbitrary, Capricious, or Entirely Lacking in Evidentiary Support. However, the Reduction to \$0 Is Not Supported by the Evidence in the Record.

After a test claim is approved, the Commission adopts parameters and guidelines to provide instructions for eligible claimants to prepare reimbursement claims for the direct and indirect costs incurred under a state-mandated program.⁵⁶ At the time the earlier reimbursement claims in this case were filed, the Government Code also stated “[c]laims for direct and indirect costs filed pursuant to Section 17561 shall be filed in the manner prescribed in the parameters and guidelines.”⁵⁷ The parameters and guidelines are regulatory, in that before their adoption, notice and an opportunity to comment on them are provided, and a full quasi-judicial hearing is held.⁵⁸ Once adopted, whether after judicial review or without it, the parameters and guidelines are final and binding on the parties. The parameters and guidelines may not be amended or set aside by the Commission absent a court order pursuant to Government Code section 17559, or a later request to amend the parameters and guidelines pursuant to section 17557 or request for the adoption of a new test claim decision pursuant to section 17570.⁵⁹ The Controller may audit the records of the claimant “to verify the actual amount of the mandated costs” claimed in a reimbursement claim, and reduce any claim that the Controller determines is excessive or

⁵³ *American Bd. of Cosmetic Surgery, Inc. v. Medical Bd. of California* (2008) 162 Cal.App.4th 534, 547-548.

⁵⁴ *Gilbert v. City of Sunnyvale* (2005) 130 Cal.App.4th 1264, 1274-1275.

⁵⁵ 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.

⁵⁶ Government Code section 17557; California Code of Regulations, title 2, section 1183.7(e).

⁵⁷ Government Code section 17564, as amended by Statutes 1999, chapter 643.

⁵⁸ *Clovis Unified School Dist. v. Chiang* (2010) 188 Cal.App.4th 794, 799, 805, and 808.

⁵⁹ *California School Boards Association v. State of California* (2009) 171 Cal.App.4th 1183, 1201.

unreasonable.⁶⁰

In this case, the Controller reduced the costs claimed in fiscal years 1997-1998 through 2004-2005 for salaries and benefits for two reasons: the documentation provided by the claimant during the audit did not identify the employees evaluated in these fiscal years; and the documentation provided by the claimant did not support reimbursement claimed at 5 to 10 hours per evaluation.

1. The reduction of costs based on the number of employees evaluated under the mandate is correct as a matter of law and not arbitrary, capricious, or entirely lacking in evidentiary support.

The Controller's reductions were based, in part, on the fact that the documentation provided by the claimant during the audit did not identify the employees evaluated in these fiscal years, which is necessary to determine whether the costs claimed were limited to the scope of the mandate. This program was approved only as a higher level of service and thus, not all activities required by the Education Code to evaluate employees are reimbursable. The Commission determined that the following activities were required by prior law and *not* eligible for reimbursement when evaluating a certificated instructional employee who did not have prior unsatisfactory evaluations: evaluating and assessing certificated employees as it relates to established standards; preparing and drafting a written evaluation, to include recommendations, if necessary, for areas of improvement; receiving and reviewing written responses to evaluations; and preparing for and holding a meeting with the evaluator to discuss the evaluation and assessment.⁶¹ Thus, the scope of the mandate to evaluate is limited to: (1) review a certificated instructional employee's instructional techniques and strategies and adherence to curricular objectives, and include in the written evaluation the assessment of these factors only during specified years; (2) for certificated instructional employees, review the results of the Standardized Testing and Reporting (STAR) test as it reasonably relates to the performance of those certificated instructional employees that teach reading, writing, mathematics, history/social science, and science in grades 2 to 11, and include the assessment of this information in the employee's written evaluation only during specified years; and (3) for those permanent certificated (instructional and non-instructional) employees who perform the requirements of educational programs mandated by state and federal law and receive an *unsatisfactory* evaluation in the years in which the employee would not have otherwise been evaluated (i.e., every other year), continue to evaluate and assess the employee as specified until the employee achieves a positive evaluation or is separated from the school district, reduce the evaluation to writing, transmit a copy of the written evaluation to the employee, attach any written response from the employee to the personnel file, and conduct a meeting with the employee to discuss the evaluation.⁶²

In this respect, after the audit was completed and the IRC filed, the claimant provided to the

⁶⁰ Government Code section 17561(d)(2)(A)(i) and (B).

⁶¹ Exhibit A, IRC, pages 28 and 35 (Statement of Decision; page number citations refer to the PDF page numbers).

⁶² Exhibit A, IRC, pages 54-56 (Parameters and Guidelines).

Controller a list of every employee evaluated during the audit years in question.⁶³ As part of its offer to revise the audit findings, the Controller found that of the 1,698 employees listed by the claimant that received evaluations for the audit period, the Controller would allow 1,149 evaluations. The Controller excluded the rest because the information the claimant provided indicated there were duplicated evaluations for permanent employees performed in consecutive years, rather than every other year; duplicated evaluations performed in the same year; evaluations made outside of the IRC period; and unallowable subjects or programs performed by certificated instructional employees.⁶⁴ Except for the adjustment allowing four evaluations in fiscal year 1997-1998 (the claimant alleges that 67 evaluations within the mandate occurred that year), the claimant accepted the Controller's findings and stated the following: "The District *accepts* the Controller's allowable total evaluations of 1,149 . . . adjusted for the evaluations for FY 1997-1998 for a total of 1,212 [evaluations]."⁶⁵

With respect to the four evaluations allowed by the Controller for fiscal year 1997-1998, the claimant asserts that the Controller accepted 67 evaluations for fiscal year 1998-1999 and should accept the same number for fiscal year 1997-1998. The claimant also includes a chart listing the names of the employees who conducted the asserted 67 evaluations in that fiscal year and refers the reader back to the average claim declarations for reference.⁶⁶ However, the claimant's chart does not address the Controller's findings of duplicated evaluations for permanent employees performed in consecutive years, rather than every other year; duplicated evaluations performed in the same year; evaluations made outside of the IRC period; and unallowable subjects or programs performed by certificated instructional employees. The claimant's chart simply lists the total number of evaluations performed. And there is no evidence in the record to support the assertion that 67 evaluations under the mandate, rather than four evaluations, were performed in fiscal year 1997-1998.

Accordingly, a reduction of costs based on the number of employees evaluated under the mandate (1,149) is correct as a matter of law and not arbitrary, capricious, or entirely lacking in evidentiary support.

2. The Controller's reduction of costs to \$0 is not supported by evidence in the record. However, the Controller's offer to allow reimbursement at 30 minutes for each of the 1,149 employees evaluated is supported by the record and is not arbitrary, capricious, or entirely lacking in evidentiary support.

The Controller's reduction of costs to \$0, when the Controller concluded that 1,149 of the evaluations were performed by the claimant and fall within the scope of the mandate, and agrees that the claimant "(1) performed the required evaluations as contained in its Collective Bargaining Agreements, (2) confirmed that the activities were performed, and (3) provided the SCO auditors the district's procedure and forms," is arbitrary and capricious and without

⁶³ Exhibit B, Controller's Comments on the IRC, page 14. The list is on pages 69-97 of Exhibit B.

⁶⁴ Exhibit B, Controller's Comments on the IRC, pages 15 and 108.

⁶⁵ Exhibit C, Claimant's Late Rebuttal Comments on the IRC, page 7.

⁶⁶ Exhibit C, Claimant's Late Rebuttal Comments on the IRC, page 5.

evidentiary support.⁶⁷ Thus, the claimant is entitled to some reimbursement for the time taken to perform the 1,149 evaluations under the mandate. The time taken by each employee to perform the mandate, however, is disputed by the parties.

The record indicates that the documentation provided to the Controller for fiscal years 1997-2005 to support the time taken on each evaluation consists of average time declarations signed by claimed staff in February or March of 2006. Each employee (evaluator) estimated the average minutes spent annually to perform evaluation activities for 1997-1998 through 2004-2005 on a single form, with estimates generally ranging from 5 to 10 hours per evaluation, and certified under penalty of perjury that a good faith estimate was reported. The “reimbursable activity codes” listed on the forms identify the following activities for which time was estimated: preparing for the evaluation, goals and objectives conference with instructor, pre-observation conference with instructor, classroom observation of instructor, post-observation conference with instructor, final conference with instructor, district reporting.⁶⁸ The claimant did not provide time logs or time sheets to verify the actual time taken to perform the mandate, or any contemporaneous documentation created at or near the same time the actual cost was incurred. The Controller disregarded these declarations, asserting that the declarations were not source documents that verified the actual time taken for each evaluation, as required by the Parameters and Guidelines.⁶⁹

The claimant contends that it has provided sufficient documentation to support the time claimed, and that the Controller’s imposition of the contemporaneous source document rule violates the *Clovis Unified School Dist. v. Chiang* decision, which “found [that the] Controller could not apply contemporaneous source documentation requirements (CSDR) prior to the date the CSDR language was actually approved by Commission on State Mandates and added to a program’s guidelines.”⁷⁰ The claimant is willing to agree to reimbursement based on 2.5 hours per evaluation, which it claims is supported by the Controller’s audit of a comparable neighboring K-12 school district, as well as other time studies accepted by the Controller for the audits of other school districts.⁷¹

The Parameters and Guidelines adopted for *The Stull Act* program authorize claimants to request reimbursement for actual costs incurred and require claimants and to keep contemporaneous source documentation (documentation created at or near the same time the actual costs was incurred) to support the actual costs incurred to implement the mandate:

To be eligible for mandated cost reimbursement for any fiscal year, only actual costs may be claimed. Actual costs are those costs actually incurred to implement the mandated activities. Actual costs must be traceable and supported by source documents that show the validity of such costs, when they were incurred, and

⁶⁷ Exhibit B, Controller’s Comments on the IRC, page 14.

⁶⁸ Exhibit A, IRC, pages 143-191 (Employee Average Time Record for Mandated Costs forms). The mean of the first ten forms (pp. 143-153) is 8.05 hours.

⁶⁹ Exhibit B, Controller’s Comments on the IRC, page 13.

⁷⁰ Exhibit F, Claimant’s Comments on the Draft Proposed Decision, page 2.

⁷¹ Exhibit F, Claimant’s Comments on the Draft Proposed Decision, pages 2-3.

their relationship to the reimbursable activities. A source document is a document created at or near the same time the actual cost was incurred for the event or activity in question. Source documents may include, but are not limited to, employee time records or time logs, sign-in sheets, invoices, and receipts.

Evidence corroborating the source documents may include, but is not limited to, worksheets, cost allocation reports (system generated), purchase orders, contracts, agendas, and declarations. Declarations must include a certification or declaration stating, "I certify (or declare) under penalty of perjury under the laws of the State of California that the foregoing is true and correct," and must further comply with the requirements of Code of Civil Procedure section 2015.5. Evidence corroborating the source documents may include data relevant to the reimbursable activities otherwise in compliance with local, state, and federal government requirements. However, corroborating documents cannot be substituted for source documents.⁷²

The claimant alleges that the Controller's use of the contemporaneous source document requirement is invalid based on *Clovis Unified School Dist. v. Chiang* (2010) 188 Cal.App.4th 794. While the *Clovis Unified* case is helpful in understanding the issues presented here, the case is distinguishable and does not directly apply to the issues here.

Unlike this case, the Commission had *not* adopted parameters and guidelines that contained the contemporaneous source document rule in the parameters and guidelines for the programs at issue in *Clovis*. Instead, the Controller enforced the contemporaneous source document rule through "non-regulatory" claiming instructions issued for three separate programs, without providing notice to school districts and an opportunity for school districts to comment on the rule. Thus, for example, in the *School District of Choice* program reviewed by the court in *Clovis*, the parameters and guidelines required the claimant to report the actual number of hours devoted to each function, supported by "source documents (e.g., employee time records, invoices, receipts, purchase orders, contracts, etc.) and/or worksheets that show evidence of and the validity of such claimed costs."⁷³ However, the Controller later issued amended claiming instructions to set forth, for the first time the contemporaneous source document rule.⁷⁴ The record showed that before the use of the contemporaneous source document rule, school districts obtained state-mandated reimbursement for employee salary and benefit costs based on "(1) declarations and certifications from the employees that set forth, after the fact, the time they had spent on SDC-mandated tasks; or (2) an annual accounting of time determined by the number of mandated activities and the average time for each activity."⁷⁵ After the Controller began using the contemporaneous source document rule in its audits, the Controller deemed the declarations, certifications, and average accounting methods insufficient and reduced the claims accordingly.⁷⁶

⁷² Exhibit A, IRC, page 53 (Parameters and Guidelines).

⁷³ *Clovis Unified School Dist. v. Chiang* (2010) 188 Cal.App.4th 794, 801-802.

⁷⁴ *Clovis Unified School Dist.*, *supra*, 188 Cal.App.4th 794, 802.

⁷⁵ *Clovis Unified School Dist.*, *supra*, 188 Cal.App.4th 794, 802.

⁷⁶ *Clovis Unified School Dist.*, *supra*, 188 Cal.App.4th 794, 802.

In addition, the rule, which requires contemporaneous time sheets and time logs, bars the use of employee time declarations and certifications as source documents. Instead, these documents are relegated to the “second-class status of ‘corroborating documents’ that can only serve as evidence that corroborates source documents.”⁷⁷ The school districts that used employee declarations and certifications and average time accountings to document time for reimbursement claims argued that the rule was an underground regulation and “it is *now* physically impossible to comply with the CSDR’s requirement of contemporaneousness that “a source document is a document *created at or near the same time the actual cost was incurred* for the event or activity in question.”⁷⁸ An underground regulation is a rule (which applies generally and implements, interprets, or makes specific the law enforced by the agency) that is not adopted in conformity with “basic procedural requirements that include public notice, opportunity for comment, agency response to comment, and review by the state Office of Administrative Law.”⁷⁹ The court concluded the Controller’s use of the contemporaneous source document rule imposed an invalid and unenforceable underground regulation.⁸⁰ The court authorized the Controller to re-audit the reimbursement claims based on the documentation requirements of the parameters and guidelines and claiming instructions that were in effect when the mandated costs were incurred.⁸¹

Here, the Parameters and Guidelines for *The Stull Act* have always contained the contemporaneous source document rule, and school districts had notice and a full opportunity to comment on the requirement (which was originally proposed by the test claimant) before the Parameters and Guidelines were adopted on consent. Nevertheless, because the Parameters and Guidelines were adopted in 2005, with a period of reimbursement going back to fiscal year 1997-1998, the claimant states that the “District started using File Maker in 2005. The information prior to that time, more than ten years ago, is currently inaccessible.”⁸² The Controller seems to acknowledge the problem since it offered to reimburse salary and benefit costs at 30 minutes for each of the 1,149 evaluations performed under the mandate, based on its findings for fiscal years 2006-2007 and 2007-2008.

Although the claimant accepted the 30 minute time per evaluation beginning in fiscal year 2006-2007, its rebuttal comments conclude that each evaluation conducted in fiscal years 1997-1998 through 2004-2005 should be reimbursed at 2.5 hours. However, the claimant does not explain why the evaluations conducted before fiscal year 2006-2007 took longer than 30 minutes. And there is no evidence in the record to support reimbursement at 2.5 hours, or five to ten hours per evaluation as originally asserted.

⁷⁷ *Clovis Unified School Dist.*, *supra*, 188 Cal.App.4th 794, 804.

⁷⁸ *Clovis Unified School Dist.*, *supra*, 188 Cal.App.4th 794, 804.

⁷⁹ *Clovis Unified School Dist.*, *supra*, 188 Cal.App.4th 794, 800, 803.

⁸⁰ *Clovis Unified School Dist.*, *supra*, 188 Cal.App.4th 794, 805 (where the court states that “the Commission submits regulatory P & Gs to the Controller, who in turn issues nonregulatory Claiming Instructions based thereon”) and pages 812-813.

⁸¹ *Clovis Unified School Dist.*, *supra*, 188 Cal.App.4th 794, 812-813.

⁸² Exhibit C, Claimant’s Late Rebuttal Comments on the IRC, page 5.

The declarations of estimated time to perform the mandate that were originally provided by the claimant to support reimbursement at five to ten hours per evaluation were based on activities that go beyond the scope of the mandate. The “reimbursable activity codes” listed on the declaration forms identify the full spectrum of evaluation activities for which time was estimated as follows: preparing for the evaluation, goals and objectives conference with instructor, pre-observation conference with instructor, classroom observation of instructor, post-observation conference with instructor, final conference with instructor, district reporting.⁸³ The Commission, however, denied reimbursement for evaluating and assessing certificated employees as it relates to established standards; preparing and drafting a written evaluation, to include recommendations, if necessary, for areas of improvement; receiving and reviewing written responses to evaluations; and preparing for and holding a meeting with the evaluator to discuss the evaluation and assessment.⁸⁴ The Commission limited the scope of the mandate for these employees to (1) review a certificated instructional employee’s instructional techniques and strategies and adherence to curricular objectives, and include in the written evaluation the assessment of these factors only during specified years; (2) review the results of the Standardized Testing and Reporting (STAR) test as it reasonably relates to the performance of those certificated instructional employees that teach reading, writing, mathematics, history/social science, and science in grades 2 to 11, and include the assessment of this information in the employee’s written evaluation only during specified years. Therefore, the declarations do not provide reliable evidence of the time it took to evaluate each employee under the limited scope of the mandate.

The claimant also argues that 2.5 hours for each evaluation is supported by the Controller’s audit of a comparable neighboring K-12 school district, as well as other time studies accepted by the Controller for the audits of other school districts for this program. Claimant further asserts:

Effectively the time studies included in the Controller's audits created a Reasonable Reimbursement Methodology, a uniform cost allowance, in conformity with Government Code section 17518.5(b), as it is based on cost information from a representative sample of eligible claimants, information provided by association of local agencies and school districts, or other projections of local costs. The time study of 2.5 hours per evaluation is reliable since auditing of reimbursement claims is not a prerequisite for the development and approval of a reasonable reimbursement methodology. (Cal. Code Regs., §1183.12).⁸⁵

However, the Controller’s audits of the records of other school districts are not relevant to the issue of the time it took the claimant to perform the mandated activities and, pursuant to section 1187.5(a) of the Commission’s regulations, and non-relevant evidence must be excluded as a

⁸³ Exhibit A, IRC, pages 143-191 (Employee Average Time Record for Mandated Costs forms). The mean of the first ten forms (pp. 143-153) is 8.05 hours.

⁸⁴ Exhibit A, IRC, pages 28 and 35 (Statement of Decision; page number citations refer to the PDF page numbers).

⁸⁵ Exhibit F, Claimant’s Comments on the Draft Proposed Decision, pages 2-3.

basis for the Commission's findings.⁸⁶ Nor is there any evidence that a time study based on the claimant's performance of the program was conducted to support reimbursement at 2.5 hours. And, finally, the Commission has not adopted a reasonable reimbursement methodology (RRM) or uniform cost allowance for this program that could be applied to all school districts. An RRM would have to be inserted into the Parameters and Guidelines in accordance with Commission regulations in order to be recognized.⁸⁷ Since no RRM for *The Stull Act* program has been adopted, any discussion of an RRM is not relevant.

Accordingly, there is no evidence to support the claimant's contention that reimbursement is required at least 2.5 hours, or between 5 and 10 hours per evaluation.

Rather, based on the evidence in the record, the Controller's finding that 30 minutes per evaluation in 2006 reasonably represents the time taken by the claimant to perform the mandate during the earlier audit period. The mandated program was not amended or increased, but remained the same. In addition, the Controller's finding of 30 minutes per evaluation was based on the claimant's time logs for fiscal year 2006-2007 that recorded the time spent on the mandate for all months in the fiscal year on one form; teacher evaluation forms provided by the claimant that disclosed 30 minutes of actual classroom observation; and the Controller's review of a sample of written evaluations for teachers at El Camino High School, Jefferson Middle School, and Mission Elementary School for fiscal years 2006-2007 and 2007-2008.⁸⁸ There is no evidence in the record that the Controller's findings are wrong, or that the Controller's offer to apply the 30 minutes to the evaluations conducted in fiscal years 1997-1998 through 2004-2005 is arbitrary, capricious, or entirely lacking in evidentiary support.

Accordingly, the Commission finds that the Controller's reduction of costs to \$0 is arbitrary, capricious, or entirely lacking in evidentiary support. However, the Controller's offer to allow reimbursement at 30 minutes for each of the 1,149 employees evaluated (which results in reimbursement of \$35,967, which includes both direct and indirect costs), is supported by the record and is not arbitrary, capricious, or entirely lacking in evidentiary support.

V. Conclusion

For the reasons discussed above, the Commission partially approves this IRC and pursuant to Government Code section 17551(d) and section 1185.9 of the Commission's regulations, requests that the Controller reinstate \$35,967, which includes both direct and indirect costs, to the claimant.

⁸⁶ California Code of Regulations, title 2, sections 1185.1 and 1187.5.

⁸⁷ See California Code of Regulations, title 2, sections 1183.7(e), 1183.10, 1183.11, 1183.12 and 1183.17(a)(3).

⁸⁸ Exhibit A, IRC, page 92. Exhibit B, Controller's Comments on the IRC, page 13.



RE: **Decision**

The Stull Act, 14-9825-I-01

Education Code Section 44660-44665

Statutes 1983, Chapter 498; Statutes 1999, Chapter 4

Fiscal Years: 1997-1998, 1998-1999, 1999-2000, 2000-2001, 2001-2002,
2002-2003, 2003-2004, and 2004-2005

Oceanside Unified School District, Claimant

On September 23, 2016, the foregoing Decision of the Commission on State Mandates was adopted on the above-entitled matter.



Heather Halsey, Executive Director

Dated: September 28, 2016