ITEM 1A
PROPOSED MINUTES

COMMISSION ON STATE MANDATES

State Capitol, Room 126
Sacramento, California
May 26, 2005

Present: Chairperson Anne Sheehan
Representative of the Director of the Department of Finance
Member Nicholas Smith
Representative of the State Controller
Member Francisco Lujano
Representative of the State Treasurer
Member Jan Boel
Representative of the Director of the Office of Planning and Research

Vacant: Local Elected Officials (2)
Public Member

CALL TO ORDER AND ROLL CALL

Chairperson Sheehan called the meeting to order at 9:31 a.m. She noted that the Commission would be considering the Butte County application for finding of significant financial distress at 1:30 p.m. Also, she noted that items 7 and 8 would be moved to the end of the morning portion of the hearing because the members received new correspondence that they would like to review.

Paula Higashi, Executive Director, introduced the Commission's new student assistant, Alicia Estrada. She also congratulated two Commission employees who recently graduated from California State University, Sacramento – Victoria Soriano, who received her Bachelor's degree; and Cathy Cruz, who received her Master's Degree in Public Policy and Administration.

Paul Starkey, Chief Legal Counsel, also introduced the Commission's summer law clerks: Todd Ratshin, Charlotte Martinez, Leslie Walker, and Cliff Tong.

APPROVAL OF MINUTES

Item 1a March 30, 2005

Upon motion by Member Smith and second by Member Boel, the minutes were unanimously adopted.

PROPOSED CONSENT CALENDAR

HEARING TO SET ASIDE AND MODIFY COMMISSION DECISIONS PURSUANT TO COURT ORDERS (Gov. Code, § 17559, subd. (b).) (action)

Item 4 *Order to Partially Set Aside and Modify Statement of Decision*
Test Claim Decision*: Pupil Expulsions*, CSM-4455
San Diego Unified School District, Claimant
Education Code Sections 48900, 48900.2, 48900.3, 48900.4, 48915, 48915.1, 48915.2, 48915.7, 48916, 48918, as added and amended by Statutes 1975, Chapter 1253 (AB 1770); Statutes 1977, Chapter 965 (AB 530); Statutes 1978, Chapter 668 (AB 2191); Statutes 1982, Chapter 318 (SB 1385); Statutes 1983, Chapter 498 (SB 813); Statutes 1984, Chapters 23, 536, and 622 (AB 1619, AB 3151, and SB 1685); Statutes 1985, Chapter 318 (AB 343); Statutes 1986, Chapter 1136 (AB 4085); Statutes 1987, Chapters 383 and 942 (AB 56 and AB 2590); Statutes 1989, Chapter 1306 (SB 142); Statutes 1990, Chapter 1231 (AB 3794); Statutes 1992, Chapter 909 (SB 1930); Statutes 1993, Chapters 1255, 1256, and 1257 (AB 342, SB 1198, and SB 1130); Statutes 1994, Chapters 146, 1017, and 1198 (AB 3601, AB 2752, AB 2543).

(On Remand from the California Supreme Court, *San Diego Unified School District v. State of California* (2004) 33 Cal.4th 859); (Peremptory Writ of Mandamus from the Superior Court, *San Diego Unified School District v. Commission on State Mandates* (GIC 737638)

Item 5 Order to Partially Set Aside Portion of Statements of Decision on Incorrect Reduction Claims (IRCs) and Order to Direct State Controller to Set Aside Reduction of Reimbursement Claims for Teacher Salaries, to Reevaluate the Reimbursement Claims in Light of the Court's Ruling, and to Submit the Results of the Reevaluation to the Commission Within 60 Days

A. *San Diego Unified School District v. Commission on State Mandates, et al*., Case Number 03CS01401 in the Superior Court of the State of California, County of Sacramento. CSM Case No. 03-L-03 [*Graduation Requirements IRC Decision,* 4435-I-01 and 4435-I-37, Adopted September 28, 2001]
B. *San Jose Unified School District v. Commission on State Mandates, et al*., Case Number 03CS01569 in the Superior Court of the State of California, County of Sacramento. CSM Case No. 03-L-05 [*Graduation Requirements IRC Decision,* 4435-I-04, Adopted May 24, 2001]
C. *Sweetwater Union High School District v. Commission on State Mandates, et al*., Case Number 03CS01570 in the Superior Court of the State of California, County of Sacramento. CSM Case No. 03-L-06 [*Graduation Requirements IRC Decision,* 4435-I-05, Adopted June 28, 2001]
D. *Castro Valley Unified School District v. Commission on State Mandates, et al*., Case Number 03CS01568 in the Superior Court of the State of California, County of Sacramento. CSM Case No. 03-L-04 [*Graduation Requirements IRC Decision,* 4435-I-13 and 4435-I-39, Adopted August 23, 2001]

Item 6 Order to Partially Set Aside Part 2, Issue 3 of the Statements of Decision on Incorrect Reduction Claims (IRCs) and Order Directing the State Controller to Set Aside Reduction of Reimbursement Claims for Teacher Salary Costs, to Reevaluate the Reimbursement Claims in Light of the Court's Ruling, and to Submit the Results of the Reevaluation to the Commission Within 60 Days

A. *Clovis Unified School District v. Commission on State Mandates, et al*., Case Number 03CS01702 in the Superior Court of the State of California, County of Sacramento. CSM Case No. 03-L-09 [*Graduation Requirements IRC Decision*, 4435-I-35, Adopted January 24, 2002]

B. *Grossmont Union High School District v. Commission on State Mandates, et al*., Case Number 04CS00028 in the Superior Court of the State of California, County of Sacramento. CSM Case No. 03-L-10 [*Graduation Requirements IRC Decision*, 4435-I-06 and 4435-I-38, Adopted January 24, 2002]

INFORMATIONAL HEARING PURSUANT TO CALIFORNIA CODE OF REGULATIONS, TITLE 2, CHAPTER 2.5, ARTICLE 8 (action)

ADOPTION OF ORDER TO SET ASIDE PARAMETERS AND GUIDELINES

Item 15 *Regional Housing Needs Determination: Cities and Counties*
Statutes 1980, Chapter 1143 (AB 2853)
Directed by Statutes 2004, Chapter 227, Sections 109-110 (SB 1102)

ADOPTION OF ORDER TO INITIATE RULEMAKING PROCEEDING

Item 17 Appeal of Executive Director Decisions
Proposed Amendments to California Code of Regulations, Title 2, Chapter 2.5, Article 1. General, Section 1181

Member Boel moved for adoption of the consent calendar, which consisted of items 4, 5, 6, 15, and 17. With a second by Member Smith, the consent calendar was unanimously adopted.

APPEAL OF EXECUTIVE DIRECTOR DECISIONS PURSUANT TO CALIFORNIA CODE OF REGULATIONS, TITLE 2, SECTION 1181, SUBDIVISION (c)

Item 3 Staff Report

There were no appeals.

RECONSIDERATION OF PRIOR STATEMENTS OF DECISION AS DIRECTED BY THE LEGISLATURE IN STATUTES 2004, CHAPTERS 895, 227, and 493 (AB 2855, SB 1102 AND SB 1895)

Ms. Higashi swore in the parties and witnesses intending to testify before the Commission.

Item 9 *Standardized Testing and Reporting (STAR)*, 04-RL-9723-01
Education Code Sections 60607, subdivision (a), 60609, 60615, 60630, 60640, 60641, and 60643, as amended by Statutes 1997, Chapter 828 (SB 376); Title 5, California Code of Regulations, Sections 850-874, 97-TC-23
Directed by Statutes 2004, Chapter 895, Section 19 (AB 2855)

Eric Feller, Commission Counsel, introduced this item. Staff found that the prior Commission decision on the Standardized Testing and Reporting program, or STAR, was correct, except for the activities required under federal law, which Mr. Feller outlined as follows:

- Activities required under the Individuals with Disabilities Education Act.
    1. exemption from testing for pupils, if the pupil's individualized education program has an exemption provision;
    2. determination of the appropriate grade-level test for each pupil in a special education program; and
    3. provision of appropriate testing adaptation or accommodations to pupils in special education programs.
- Activity required under the Equal Education Opportunity Education Act.
    1. administering an additional test to limited-English proficiency pupils enrolled in grades 2 through 11.

Mr. Feller stated San Diego Unified School District's position that the additional test for limited-English proficiency pupils should continue to be reimbursable. He noted that the Legislative Analyst's Office and the Department of Finance disagreed because the STAR program implements a federal mandate known as the No Child Left Behind Act, and its predecessor, the Improving America's School Act.

According to Mr. Feller, the issue was whether these acts are federal mandates under California's mandate reimbursement laws. He indicated that the California Supreme Court has held that the existence of a federal mandate depends on various aspects of the federal program, such as the certainty and severity of penalties on the state for not participating in the program. Because of the lack of evidence as to the certainty or severity of the penalty in this case, staff found that the No Child Left Behind Act and the Improving America's School Act are not federal mandates.

Moreover, Mr. Feller stated that the Legislative Analyst's Office and the Department of Finance also argue that the reconsideration decisions should be retroactive. Staff found that there was no evidence in the record or in the reconsideration statutes to support retroactivity. He noted that the statute states that it implements the 2004-2005 budget. Therefore, staff found that the reconsideration should be effective July 1, 2004.

Mr. Feller indicated that in the event the Commission finds a reimbursable mandate, the Legislative Analyst's Office and the Department of Finance assert that federal Title 1 funds should be used to offset the costs of the mandate. However, staff found no legal requirement for school districts to use federal funds to offset costs. Staff agreed that any state funds for the program should be used to offset costs.

Staff recommended that the Commission adopt the staff analysis, which partially approved the prior Commission decision.

Parties were represented as follows: Art Palkowitz and Robert Raines, on behalf of San Diego City Schools; Gerry Shelton, with the Department of Education; Paul Warren, with the Legislative Analyst's Office; and Pete Cervinka and Lenin Del Castillo, with the Department of Finance.

Mr. Palkowitz disagreed with staff's conclusion related to the testing of English learners. He argued that the staff analysis failed to mention any federal statute requiring English learners to be tested. Without identifying such a statute, he disagreed with staff's basis for denying reimbursement, which is that federal law preempts California state law. He also disagreed with staff's reliance on the *Castaneda* case because he felt that at no point did the case hold that local education authorities of any local agency must test English learners. Mr. Palkowitz asserted that the Spanish Assessment of Basic Education should remain a reimbursable mandate.

Mr. Raines described some of the activities related to the Spanish Assessment of Basic Education because they were parallel to the activities required for the STAR program.

Mr. Shelton submitted that the issue before the Commission was whether the No Child Left Behind Act and its predecessors constitute a federal mandate that places requirements in the area of assessment and accountability, or whether the state has a choice in meeting the No Child Left Behind Act requirements. His answer was a resounding "no" because he felt that the state did not have a choice in whether or not to meet the requirements of the No Child Left Behind Act.

Mr. Shelton argued that as the STAR program evolved, additional activities and tests were added that resulted in additional costs to the locals. Speaking for the Superintendent and State Board of Education, Mr. Shelton felt that the testing system evolved to the point where the state was now effectively meeting the minimum requirements of the No Child Left Behind Act. Moreover, Mr. Shelton disagreed with staff's reference to the *Hayes* decision, where the court said that the test of whether or not a federal mandate was where the requirement was derived should be at the local level. He believed that the test should be at the level of the department responsible for administering and implementing the program.

Furthermore, Mr. Shelton explained that the state operated under an environment of compulsion and coercion from the federal government, and stated that recently, the Department of Education had discussions with the federal government over definitional issues related to categorizing schools as program-improvement schools under the No Child Left Behind Act. He said that the federal government threatened that if the department does not change the definition, it would lose 25 percent of the administrative funds received under the No Child Left Behind Act and could lose the entire federal grant, a total of about $3 billion, or eight percent of the total educational funding in California. Mr. Shelton maintained that this was an unreasonable level of coercion and compulsion placed on the state, and because the state has no choice in the matter, the activities imposed on local education agencies derive from federal requirements. Thus, the costs are not reimbursable by the state.

Mr. Del Castillo stated his belief that the No Child Left Behind Act is a federal mandate, and that the STAR program allows California to implement and satisfy the federal assessment requirements in the No Child Left Behind Act. Without the program, he argued that the state's eligibility to receive federal funds would be jeopardized. Also, Mr. Del Castillo asserted that the Legislature intended to apply the reconsideration decision retroactively. He noted that the Legislature had not budgeted any funds for the mandate, meaning that they have never formally approved the

Commission's decision. Therefore, the Department of Finance believed that any changes to the findings of the STAR mandate should be applicable to all district claims regardless of timing.

Mr. Del Castillo urged the Commission to consider offsetting funds, savings, and revenue if it disagreed that STAR is a federal mandate. He also concurred with the Legislative Analyst's comments.

Addressing Mr. Palkowitz's arguments, Mr. Feller quoted the federal statute, which effectively stated that educational agencies must take appropriate action to overcome language barriers that impede equal participation in instructional programs. He explained that the statute does not say "bilingual education," and for many years, the courts struggled to interpret the meaning of "appropriate action." He noted that the *Castaneda* court established a three-part test to determine the sufficiency of the appropriate action: 1) whether the program is based on an educational theory recognized as sound, 2) whether the program is reasonably calculated to implement that theory, and 3) whether the program produced satisfactory results after being used for a time sufficient to afford a legitimate trial. He stated that testing of pupils was the only way to determine whether appropriate action was taken and whether the three-part test was met. Therefore, he maintained that the *Castaneda* case interpreted the federal statute, which he believed controlled in this case.

Regarding the Department of Finance's issue regarding retroactivity of the reconsideration statute, Mr. Feller reiterated that there was no evidence to support retroactive application before fiscal year 2004-2005. Additionally, he stated that there was no legal requirement for school districts to offset the STAR test with federal funds.

With regard to the Department of Education's comments that the No Child Left Behind Act is a federal mandate, Mr. Feller maintained that there was insufficient evidence that the penalties for non-participation are certain and severe. He noted that the new testimony provided by Mr. Shelton is not reflected in the staff analysis before the Commission. Therefore, he recommended that the Commission continue the item so that the Department of Education could submit more evidence as to coercion from the U.S. Department of Education.

Chairperson Sheehan asked Mr. Shelton to submit comments in writing in terms of his testimony about the potential sanctions from the federal government under the No Child Left Behind Act. Mr. Shelton agreed.

Mr. Feller further disagreed with Mr. Shelton that the STAR program meets the minimum requirements under the No Child Left Behind Act. He noted that the STAR program goes beyond the federal requirements. Mr. Shelton responded that there were requirements in the federal No Child Left Behind Act related to the assessment system beyond testing requirements. Chairperson Sheehan commented that she saw two issues: 1) the grade levels required for testing, and 2) the actual substance of the assessments.

Mr. Palkowitz asked why Mr. Shelton's comments were not presented before the hearing. Mr. Shelton stated that the interaction with the federal government was fairly recent and he included it in his testimony in contemporaneous fashion.

Mr. Palkowitz also requested clarification of the issue, which Chairperson Sheehan and Mr. Shelton provided.

Chairperson Sheehan asked Mr. Shelton if he knew of federal penalties on other states. Mr. Shelton did not testify to the matter. Mr. Feller stated that he did not find any state that was sanctioned, but Utah came close.

Mr. Cervinka noted that the absence of any sanctions on other states was not relevant to the issue before the Commission. Mr. Shelton pointed out that the absence of sanctions could be taken as evidence of the power of coercion of the federal government.

Mr. Starkey reiterated that the record lacked supporting evidence that there were certain and severe penalties on states for non-participation. He stated that any evidence submitted must be of a nature that can be evaluated so that an effective legal recommendation could be made. Mr. Feller added that the evidence must be particular to the testing requirements. There was further discussion about the necessary evidence that should be submitted by the Department of Education. Ms. Higashi noted that additional evidence submitted would be posted on the Commission's website to allow parties an opportunity to review and respond.

Mr. Cervinka stated his understanding that until the Legislature provides funding for a mandate, the Commission's decision is not considered approved. Mr. Feller responded that the California Supreme Court has found that " a statute may be applied retroactively only if it contains express language of retroactivity." He added that none of the committee analyses indicated the Legislature's intent for the decision to be retroactive. Mr. Feller maintained that many other mandates have not been funded, but it was not evidence of legislative intent. Mr. Palkowitz agreed with Mr. Feller while Mr. Cervinka continued to disagree.

Ms. Higashi confirmed that there was nothing in statute specifically stating that the Commission's decision is not approved until funding is provided in the Budget Act.

Chairperson Sheehan requested further discussion about the offsetting issue. Mr. Cervinka argued that federal funds provided under the No Child Left Behind Act are in some cases dedicated specifically for assessment and should be considered as offsetting revenue. Mr. Feller responded that given the provision in the Education Code that gives school districts broad authority to carry out activities determined by the school board to be necessary, there must be some intent on the part of the federal government or the Legislature to use federal funds to offset the costs of the STAR program. However, Mr. Feller stated that there was no legal requirement or evidence in the record indicating the amount specifically earmarked for testing that could be considered an offset.

Mr. Cervinka responded that the Department of Finance could work with the Department of Education to identify specific dollar amounts. Mr. Feller stated that clarification from the Department of Finance regarding evidence they had submitted into the record would be helpful.

Mr. Warren commented about the issue of offsetting revenues. He stated that there were two views: 1) the No Child Left Behind Act provides funding on a voluntary basis to school districts because nothing required school districts to participate, or 2) the act is a federal mandate because it requires the state to test all students in all schools in all public school districts to qualify for federal funding. In response to Chairperson Sheehan's question, Mr. Warren stated that federal funds should be used to implement activities required by federal law, and the cost of activities that go beyond federal requirements should be reimbursed by the state.

Mr. Feller stated that staff must follow the California Supreme Court's direction to look at all the gray areas between the two views to make a determination. Mr. Warren argued that it was an unreasonable position to expect the federal government to specify specific amounts to be put aside for local assessment.

Chairperson Sheehan asked about the offsetting evidence submitted by the Department of Finance for which staff needed clarification. Mr. Feller clarified the type of evidence staff needed and Mr. Del Castillo stated that the evidence could be provided.

Chairperson Sheehan clarified that in addition to the information that the Department of Education is submitting, the Department of Finance will also provide additional information about offsetting revenues. She noted that the comments would be posted on the Commission's website.

Regarding the issue of retroactivity, Mr. Warren provided comments supporting the Department of Finance's arguments. Chairperson Sheehan stated that it would have been beneficial if the Legislature were more explicit about what they wanted the Commission to do. Mr. Feller restated staff's position.

Member Smith asked about the timeline. Ms. Higashi responded that the next meeting was in July and suggested two weeks for submitting the additional comments.

Chairperson Sheehan stated that items 9 and 10 would be continued to the July hearing.
Ms. Higashi noted that a revised notice and schedule would be issued.

Item 10 Proposed Statement of Decision
Standardized Testing and Reporting (STAR), 04-RL-9723-01
See Above

Item 10 was postponed to the July 28, 2005 hearing.

[At this time, a short break was taken.]

Item 11 *Handicapped & Disabled Students*, 04-RL-4282-10
Statutes 1984, Chapter 1747 (AB 3632); Statutes 1985, Chapter 1274 (AB 1500); California Code of Regulations, Title 2, §§ 60000-60200 (Emergency Regulations adopted July 12, 1986), CSM 4282
Directed By Statutes 2004, Chapter 493, Section 7, (SB 1895)

Camille Shelton, Senior Commission Counsel, presented this item. She noted that the test claim legislation implements federal special education law that requires states to guarantee disabled students the right to receive a free and appropriate public education that includes special education and related services, such as mental health services designed to meet the students' unique educational needs. Before the test claim legislation, Ms. Shelton stated that local educational agencies were financially responsible for providing mental health services required by students' individualized education plans. In 1986, the test claim legislation shifted the responsibility and funding for providing mental health services to county mental health departments.

On reconsideration, staff found that the Commission's 1990 decision correctly determined that the test claim legislation imposes a reimbursable state-mandated program. Ms. Shelton noted that the Commission's finding is supported by three appellate court decisions, including *County of Santa Clara v. Commission on State Mandates, Hayes v. Commission on State Mandates,* and *TriCounty SELPA v. County of Tuolumne*. However, she indicated that the 1990 decision does not fully identify all of the activities expressly mandated by the test claim statutes and regulations, which were specifically pled by the original test claimant. She also indicated that the decision does not fully identify all of the offsetting revenue that must be identified and deducted from the program costs claimed.

Ms. Shelton noted that the staff analysis analyzes the intervening changes in the law relevant to the cost and funding of psychotherapy and residential care of seriously emotionally disturbed pupils. Staff recommended that the Commission adopt the staff analysis, which approves the test claim, with a reimbursement period beginning July 1, 2004.

Parties were represented as follows: Leonard Kaye and Paul McIver, with the County of Los Angeles; Pamela Stone and Linda Downs, with the County of Stanislaus; Patricia Ryan, with the California Mental Health Directors Association; John Polich, with the County of Ventura; and Jeannie Oropeza, Nicholas Schweitzer, and Dan Troy, with the Department of Finance.

Mr. Kaye concurred with the staff analysis and urged the Commission's adoption. He welcomed staff's suggestion for a pre-hearing conference to discuss the development of parameters and guidelines.

Mr. Kaye noted one point for clarification regarding staff's recommendation to reimburse 60 percent of the total residential and non-educational costs of a seriously emotionally disturbed child placed in an out-of-home residential facility. Because the federal government may change the cost-sharing formula, he suggested that the language be modified to the effect that counties be reimbursed 100 percent of costs.

Mr. McIver commented that clarification was necessary with regard to participation in due-process hearings. He suggested that the language be modified to state participation in all dispute-resolution procedures, which is required of county mental health offices if named as a party in the dispute.

Mr. Polich urged the Commission to adopt the staff recommendation. He noted that a request to amend parameters and guidelines was filed in 2002 by the County of Los Angeles and the County of Stanislaus that involves the same concept and arguments as this matter because important activities were omitted from the adopted Statement of Decision. He stated that the Commission's decision would help clear up some of the existing uncertainty as to what activities are mandated and reimbursable under the program.

Ms. Stone requested one change for purposes of specificity with regard to Medi-Cal funds. Ms. Downs clarified that the staff analysis identified specific offsets but left out the use of local revenue funds as a share of Medi-Cal. She recommended that the language be clarified to state, "Medi-Cal funds obtained for the purposes of this mandated program, in accordance with federal law, except for any local match requirements."

Ms. Ryan urged the Commission to adopt the staff recommendation in order to update mandate reimbursement rules with current law.

Mr. Troy believed this program to be a federal mandate, and thus, not reimbursable by the state. He stated that changes to the Individuals with Disabilities Education Act since the *Hayes* decision make it less clear that the state's choice triggers reimbursement pursuant to Article XIII B, section 6 because the most recent version of the law is clear that the state had broad discretion to designate responsibility for Individuals with Disabilities Education Act services to any public agency.

Ms. Oropeza noted that the state would be in jeopardy of losing $1.2 billion if the services were not provided. Maintaining that the program is a federal mandate, she explained that the state chose to budget funds through school districts and allowed them to contract with counties to provide the services.

Ms. Shelton indicated that there was one Supreme Court case and one Third District Court of Appeal case that instructs the Commission to analyze federal mandate issues using a two-part test. She explained that the first test, addressed in the *City of Sacramento* case, is the issue of whether the federal legislation is a mandate on the state. In that case, the Individuals with Disabilities

Education Act is a federal mandate, as the *Hayes* court determined. She stated that the Commission is bound by that part of the decision. The second test, which she noted was lacking from the Department of Finance's argument, is whether the state freely chose to shift some responsibilities and funding to local agencies. She indicated that even if there was a federal mandate, it could still be a reimbursable state mandate on local agencies. Here, Ms. Shelton explained that the federal legislation does not require, but authorizes states to shift some services to non-educational agencies. Moreover, she stated that the *Hayes* case and the *TriCounty SELPA* case support the decision that the test claim legislation is a state-mandated program, and therefore, the program is a reimbursable state mandate.

Regarding Mr. Kaye's suggestion about the cost-sharing formula, Ms. Shelton stated that the problem was that the formula is provided by statute. In the event the statute changes, she stated that a new test claim would have to be filed. As to Mr. McIver's comments related to due-process hearings, she stated that the Education Code describes various activities, including mediation, all of which were included in the staff analysis. With regard to the Mr. Polich's comments about the pending parameters and guidelines amendment, she noted that the item may be before the Commission at the September hearing. Finally, with regard to the Medi-Cal issue raised by Ms. Stone and Ms. Downs, Ms. Shelton stated her belief that the concern was addressed in the staff recommendation.

Ms. Oropeza requested Ms. Shelton to restate her comments about the two-part test, which Ms. Shelton did. Ms. Oropeza continued to argue that federal law permits the state to choose who would provide the service, and thus, the state did not make the choice without authority; the choice is still within the federal mandate. Ms. Shelton noted that the state shifted the funding and activities to counties before the federal law was amended to authorize states to make the choice. She maintained that the law only authorizes; it does not require, and therefore, following the plain holding of the *Hayes* case, the state is left with true discretion, the policy choice of what entity would carry out the activities.

Ms. Oropeza raised the argument that the Laird bill says that it does not matter whether state law or federal law came first. Ms. Shelton responded that under the Laird bill, there still has to be a finding that a federal mandate on local agencies exists. In this case, she stated that there is no finding and no evidence to show that there is in fact a federal mandate on the counties.

In response to Ms. Oropeza's argument, Mr. Kaye submitted that based on Ms. Shelton's response to his earlier recommendation, the Commission cannot base its findings on a future law that takes effect July 1, 2005.

Mr. Troy responded that the argument may not apply to prior years. However, he did not believe that it was inappropriate for the Commission to consider the issue. He added that he did not see much of a distinction between schools and county offices of mental health being responsible for the activities.

Ms. Shelton explained that under the federal law, schools have requirements under the Individuals with Disabilities Education Act, whereas counties do not have requirements. She stated that there is a brand new program on counties that was shifted by the state through a policy decision.

Chairperson Sheehan asked questions to clarify the arguments, which Ms. Oropeza and Ms. Shelton responded.

Mr. Kaye noted that no one was disputing the state's unfettered discretion to assign the mandate to counties. However, he contended that for doing so, the *Hayes* case requires that counties be reimbursed under Article XIII B, section 6.

Ms. Oropeza submitted that counties were entitled to reimbursement through federal funds because they were implementing a federal mandate. Ms. Shelton responded that federal funds that are ultimately appropriated to counties must be identified and deducted from claims.

Regarding the Medi-Cal funds issue, Ms. Stone argued that the language should be more specific to avoid incorrect reduction claims. Ms. Shelton maintained that the issue was addressed.

Ms. Oropeza commented that the activities in staff's recommendation were overly broad. Ms. Shelton noted that the language came straight out of the statute and regulations before the Commission, but stated that there could be more discussion about them in the parameters and guidelines phase.

After further discussion about the issues, Member Smith made a motion to adopt the staff recommendation, which was seconded by Member Boel. The motion carried unanimously.

Item 12 Proposed Statement of Decision
Handicapped & Disabled Students, 04-RL-4282-10
See Above

Camille Shelton, Senior Commission Counsel, presented this item. She stated that the sole issue before the Commission was whether the proposed Statement of Decision accurately reflected the Commission's decision. Staff recommended that the Commission adopt the proposed Statement of Decision. Ms. Shelton indicated that she would make changes to reflect the witnesses' hearing testimony.

Member Smith made a motion to adopt the proposed Statement of Decision, which was seconded by Member Boel. The motion carried unanimously.

HEARINGS AND DECISIONS, PURSUANT TO CALIFORNIA CODE OF REGULATIONS, TITLE 2, CHAPTER 2.5, ARTICLE 7 (action)

Item 13 *Handicapped & Disabled Students II*, 02-TC-40/02-TC-49
Counties of Stanislaus and Los Angeles, Claimants
Government Code Sections 7570, 7571, 7572, 7572.5, 7572.55, 7573, 7576, 7579, 7582, 7584, 7585, 7586, 7586.6, 7586.7, 7587, 7588
Statutes 1984, Chapter 1747 (AB 3632); Statutes 1985, Chapter 107 (AB 1304); Statutes 1985, Chapter 759 (AB 1255); Statutes 1985, Chapter 1274 (AB 1500); Statutes 1986, Chapter 1133 (AB 3012); Statutes 1992, Chapter 759 (AB 1248); Statutes 1994, Chapter 1128 (AB 1892); Statutes 1996, Chapter 654 (AB 2726); Statutes 1998, Chapter 691(SB 1686); Statutes 2001, Chapter 745 (SB 1191); Statutes 2002, Chapter 585 (SB 2012); and Statutes 2002, Chapter 1167 (AB 2781)
California Code of Regulations, Title 2, Sections 60000-60610

Camille Shelton, Senior Commission Counsel, presented this item. She stated that pursuant to the court's ruling in *Hayes v. Commission on State Mandates* and *TriCounty SELPA v. County of Tuolumne*, staff found that the test claim legislation mandates a new program or higher level of service and imposes costs mandated by the state on counties for specific activities listed in the staff analysis, with a reimbursement period beginning July 1, 2004.

Staff recommended that the Commission adopt the staff analysis, which approves the test claim.

Parties were represented as follows: Leonard Kaye and Paul McIver, with the County of Los Angeles; Pamela Stone and Linda Downs, with the County of Stanislaus; and Nicholas Schweitzer and Jody McCoy, with the Department of Finance.

Mr. Kaye concurred with the staff analysis and recommendations.

Mr. McIver reiterated his concern from the previous item about the dispute resolution language. He added that the staff analysis only describes participation in due-process hearings, and based on experience with the State Controller's auditors, he just wanted to make sure that the language specifies that participation in all aspects of dispute resolution is also included.

Ms. Stone pointed out one issue for clarification. Staff allowed the one-time activity of revising the interagency agreement to include the new procedures, with a footnote stating that revisions could occur every three years in conjunction with the reconsideration decision. She stated her concern that an auditor may misinterpret the language and disallow reimbursement. Therefore, she just wanted to clarify that claimants would also be reimbursed for the new elements of the agreement when the revisions occur.

Ms. Downs raised the Medi-Cal issue discussed in the previous item. She clarified that the local funds received at one point come from the state as part of a realignment allocation, but once they become county local funds, she asserted that they are not subject to the offsetting provisions.

Mr. Schweitzer believed that the new activities identified by the claimant – the residential placement plan, authorization of payments for out-of-home care, and the medication monitoring – are not new activities.

Ms. Shelton explained that this test claim was filed on all the subsequent amendments to the *Handicapped and Disabled Students* program; therefore, the activities reflect a higher level of service rather than a new program. Regarding the dispute resolution and due process issues raised by Mr. McIver, staff found that there is no increase in the level of service on counties for purposes of this test claim. She stated that while the law requires counties to still participate in the hearings, the activity is included in a different set of parameters and guidelines. As for the interagency agreement issue raised by Ms. Stone, Ms. Shelton noted that for purposes of this analysis, the ongoing activity of revising the agreement does not constitute a new program or increase in the level of service. With regard to Ms. Downs comments related to the Medi-Cal issue, Ms. Shelton suggested that more discussions about specificity should take place during the parameters and guidelines phase.

Addressing the Department of Finance's allegations, Ms. Shelton explained that the test claim legislation increased the level of service for the individualized education plan team for which the county now participates. She noted that this was not required under prior law. Regarding the comments made about payments for out-of-home care, she stated that the regulations did change and that the Department of Finance's contentions were not supported by any legal document or declaration signed under penalty of perjury. She maintained that the regulations for medication monitoring also changed and that under the rules of statutory construction, it is presumed that when an administrative agency materially alters the language, they intended to change the law. She added that the regulations increased the level of service by requiring new activities.

Ms. McCoy stated her belief that there was no meaningful difference in what the counties were required to do.

Member Boel made a motion to adopt the staff analysis, which was seconded by Member Smith. The motion carried unanimously.

Item 14 Proposed Statement of Decision
Handicapped & Disabled Students II, 02-TC-40/02-TC-49
See Above

Camille Shelton, Senior Commission Counsel, presented this item. She stated that the sole issue before the Commission was whether the proposed Statement of Decision accurately reflected the Commission's decision. Ms. Shelton indicated that she would modify the witness list.

Member Boel made a motion to adopt the proposed Statement of Decision, which was seconded by Member Smith. The motion carried unanimously.

RECONSIDERATION OF PRIOR STATEMENTS OF DECISION AS DIRECTED BY THE LEGISLATURE IN STATUTES 2004, CHAPTERS 895, 227, and 493 (AB 2855, SB 1102 AND SB 1895)

Item 7 *School Accountability Report Cards I*, 04-RL-9721-11
Education Code Sections 33126, 35356, 35256.1, 35258, 41409 and 41409.3, Statutes 1989, Chapter 1463 (SB 280); Statutes 1992, Chapter 759 (AB 1248); Statutes 1993, Chapter 1031 (AB 198), Statutes 1994, Chapter 824 (SB 1665); Statutes 1997, Chapter 918 (AB 568), 97-TC-21
Directed by Statutes 2004, Chapter 895, Section 18 (AB 2855)

Katherine Tokarski, Commission Counsel, presented this item. She noted that the Commission approved the test claim on April 23, 1998. She also noted that while AB 2855 directs the Commission to reconsider the prior final decision, Statutes 1997, chapter 912 was not explicitly named in AB 2855. Therefore, staff found that the Commission does not have the authority to rehear that portion of the original decision.

Ms. Tokarski explained that in enacting Proposition 98, the voters amended the state Constitution to provide public schools with state-funding guarantees. The measure also requires schools to undergo an annual audit and to issue an annual school accountability report card. She indicated that the test claim was filed on statutory amendments to the Proposition 98 requirements for the school accountability report card. Staff found that the state has not shifted the burdens of state government to school districts by requiring new data elements and a new method for publicizing and distributing the existing school accountability report card. She explained that the directive could be complied with by a minimal reallocation of resources as described in the 2003 decision in the *County of Los Angeles v. Commission on State Mandates* case. Therefore, staff did not find that a new program or higher level of service was imposed.

As a second and independent ground for denying reimbursement, staff found that there were also no costs mandated by the state. Ms. Tokarski stated that the California Supreme Court found in the *Department of Finance v. Commission on State Mandates* case that the availability of state program funds precludes a finding of a reimbursable state mandate. Thus, because there is a unique relationship between the voter-enacted school accountability report card requirement and the Proposition 98 funding guarantee, she indicated that the funds received under Proposition 98 can be used to complete the annual school accountability report card.

Ms. Tokarski noted that no briefs were received on the issues under reconsideration. Written comments regarding the draft staff analysis were received from the Sweetwater Union High

School District in complete opposition to staff's findings, and the Department of Finance in support of the staff analysis. She also noted that the Education Management Group submitted a late filing the day before asserting that staff's analysis on costs mandated by the state was based on a new legal theory that requires school districts to prove that reimbursable state-mandated costs are paid from a property tax source. The Education Management Group argues that this would make it impossible for school districts to prove any past or future mandate claims due to an accounting burden that schools cannot meet.

Staff finds that these allegations take the property tax argument out of context. Ms. Tokarski indicated that districts receive over $31 billion a year through Proposition 98. Thus, staff found that districts have the burden to prove that they are required to exceed Proposition 98 funding in order to provide annual school accountability report cards. Ms. Tokarski explained that the argument that the decision in this matter would affect future claims is incorrect because each of the Commission's decisions is limited to the claim presented. Moreover, decisions are not precedential and must be supported by constitutional, statutory, and case law.

Ms. Tokarski noted that staff's analysis does not present a novel theory of law as the exact issue was presented and approved by the Commission in March 2004 on *School Accountability Report Cards II* and *III*. Staff recommended that the Commission adopt the staff analysis to deny the reconsidered portions of the original test claim decision.

Parties were represented as follows: Abe Hajela, with School Innovations and Advocacy; Jai Sookprasert, with the California School Employees Association; Robert Miyashiro, with the Education Mandated Cost Network; Brent McFadden, with the Education Coalition and the Association of California School Administrators; Richard Hamilton, with the California School Boards Association; Sandra Thornton, with the California Teachers Association; and Lenin Del Castillo and Pete Cervinka, with the Department of Finance.

Mr. Hajela outlined two issues: 1) whether school districts must prove that they use property tax revenues, and 2) whether the new requirements of the school accountability report card are a higher level of service. Regarding the first issue, he argued that school districts cannot prove that local property tax revenues are used to comply with specific mandates because the funds are commingled with other funds received through Proposition 98. He added that school district accounting procedures are largely regulated by the state, and the state does not require that funds be segregated. Unlike the case cited in staff's analysis, he contended that in this case, there is no specific appropriation or funding stream for the program. He maintained that nothing new happened for the Commission to believe that a new interpretation of the law is necessary.

With regard to the second issue and staff's position that the new requirements are minimal, he asserted that there needs to be a dollar amount or percentage standard that provides guidance because the program could be further amended in the future.

Mr. Sookprasert associated himself with Mr. Hajela's comments. He disputed the argument that changes are minimal if school districts must break funds down to property tax revenues.

Mr. Miyashiro addressed the de minimis nature of the claim. He argued that while staff believes that incidental duties do not require reimbursement, staff did not establish a minimum dollar amount. He noted that the law specifies a thousand-dollar threshold for filing a reimbursement claim and that the Commission adopted a statewide cost estimate of $1.7 million for this program. He added that this estimate was the thirteenth largest of the 30 estimates adopted in 2002-2003.

Mr. Miyashiro clarified that Proposition 98 does not appropriate money for any program. Rather, it establishes a minimum funding guarantee level for which the Legislature then makes appropriations to specific programs. Thus, he asserted that it is not sufficient to reference the Proposition 98 guarantee and conclude that the minimum requirements fund a particular program because an appropriation must be made to fund the program. He argued that the language of Proposition 98 is not specifically intended for the *School Accountability Report Card* program and concluded that the staff analysis has not overcome the original findings of the Commission. He strongly urged the Commission to reject the staff analysis and to let the 1998 decision stand.

Mr. McFadden associated himself with the remarks made by the previous speakers.

Ms. Thornton agreed with all the previous comments. She also urged the Commission to oppose any recommendation that would affect the funding source or perpetuate the under funding of California's schools.

Mr. Hamilton concurred with the previous comments. He noted that the staff analysis does not address Government Code section 17556, subdivision (f), which speaks of imposing duties that are expressly included in a ballot measure.

Mr. Cervinka disagreed with the prior comments. He argued that Government Code section 17556, subdivision (f), specifically states that ballot measures adopted by the voters on a statewide initiative do not impose reimbursable mandates for duties expressly included in the ballot measure. He explained that the school accountability report card is not limited to the provisions originally set out in the Education Code because the electorate recognized that the details of the model report card are subject to change and districts are required to comply with those changes. Therefore, he asserted that this program is not reimbursable as it was a statewide ballot measure.

Mr. Hajela submitted that no one was claiming the voter-enacted portions as reimbursable. Mr. Cervinka responded that the proposition included the phrase "including but not limited to" and thus, required periodic updates to reflect changes made in the legislation. Mr. Hajela continued to disagree.

Regarding the property tax issue, Chairperson Sheehan commented that she did not feel that it was the justification for staff's recommendation. She noted that she was surprised by the comments in the late filing.

Ms. Tokarski indicated that when paying claims, the State Controller's Office does not require claimants to prove that the money came from their property tax source because it was sufficient to prove that they did not have the funds available from another source. However, she stated that there was no evidence that the $31 billion from the state was unavailable. She added that using the analysis in the *Kern School District* case, she could not find costs mandated by the state where districts had to go beyond the funds received under Proposition 98 to complete the additional requirements of the *School Accountability Report Card* program.

Member Lujano asked for clarification as to whether school districts have to prove that local property taxes received were used to comply with the mandated program. Mr. Starkey stated that the Proposition 98 funding is a quid pro quo: funding for accountability. He explained that case law has said that if there is a notion of a de minimis cost in a state mandate, the courts look at the imposition of taxes. Further, he stated that Article XIII B, section 6, is a tax limitation protection so that the state does not impose financial burdens on local governments. But the Legislature cannot frustrate the intent of the voters. Regarding the cases staff relied upon to

support its position, Mr. Starkey noted that they cannot be distinguished away just because they are not school district cases.

Mr. Starkey maintained his position that there is a de minimis element to mandates law, Proposition 98, and the *School Accountability Report Card* program. The policy rationale is that counties or local governments are not burdened within the meaning of a cost shift to the local governments.

Mr. Hajela requested clarification, which Mr. Starkey provided, as to what cases were being relied upon.

There was further discussion about the de minimis argument. Mr. Hajela expressed confusion about the need for the argument. Member Smith was also troubled by the argument.
Mr. Miyashiro stated that staff had not sufficiently provided the linkage between a court finding and its assertion that the additional requirements were in fact de minimis.

Chairperson Sheehan clarified the issue before the Commission.

Mr. Cervinka restated his position.

Mr. Hamilton stated that his trouble with the analysis is that there is a court case about de minimis requirements that was just being applied without quantification.

Ms. Higashi clarified that the statewide cost estimate numbers referenced by Mr. Miyashiro can be attributed to the State Controller's most recent deficiency letter. However, there was no detail in terms of what percentage of those costs or the exact amount that could be attributed to the activities that derive from statutes that are the subject of this test claim.

Mr. Miyashiro noted that the Department of Finance intends to seek legislation that would apply this decision to all of the *School Accountability Report Cards* programs. Thus, he felt it was relevant to recognize the cost of the entire mandate. Mr. Cervinka maintained his position.

Member Boel made a motion to adopt the staff analysis.

Member Lujano indicated that the Treasurer was concerned about this item. He stated his understanding that staff's position was that Proposition 98 actually funds this program.
Ms. Tokarski responded that the Proposition 98 funds should be used to pay for the costs of providing the school accountability report card.

Member Lujano stated that because Proposition 98 has been under funded for the past two years by about $3.1 billion, the Treasurer will be voting no.

Member Boel's motion to adopt the staff analysis was seconded by Chairperson Sheehan. The motion failed 2-2, with Member Smith and Member Lujano voting "No."

Ms. Higashi noted that the matter would be rescheduled after the Commission membership changes and at that time, the analysis will be updated to reflect the hearing testimony.

Item 8 Proposed Statement of Decision
School Accountability Report Cards I, 04-RL-9721-11
See Above

The Commission did not vote on this item.

[At 12:58 p.m., a midday recess was taken.]

INFORMATIONAL HEARING PURSUANT TO CALIFORNIA CODE OF REGULATIONS, TITLE 2, CHAPTER 2.5, ARTICLE 8 (action)

ADOPTION OF ORDER TO SET ASIDE PARAMETERS AND GUIDELINES

Item 16 *Regional Housing Needs Determination: Councils of Governments*, Statutes 1980, Chapter 1143 (AB 2853)
Directed by Statutes 2004, Chapter 227, Sections 109-110 (SB 1102)

Item 16 was postponed to the June 10, 2005 hearing.

SPECIAL ORDER OF BUSINESS – 1:30 P.M.

Chairperson Anne Sheehan reconvened the meeting at 1:36 p.m.

APPROVAL OF MINUTES

Item 1b May 12, 2005

Upon motion by Member Smith and second by Member Lujano, the minutes were adopted. Member Boel abstained.

HEARING AND DECISION PURSUANT TO CALIFORNIA CODE OF REGULATIONS, TITLE 2, CHAPTER 2.5, ARTICLE 6.5 (action)

Item 20 Adoption of Proposed Preliminary Decision: Butte County Application for Finding of Significant Financial Distress, Welfare & Institutions Code Section 17000.6

Shirley Opie, Project Manager, introduced this item. She explained that the county board of supervisors may adopt a general assistance standard of aid below the level established in Welfare and Institutions Code section 17000.5 if the Commission finds that meeting the general assistance standard of aid results in significant financial distress. On May 12, 2005, the Commission conducted a fact-finding hearing in Oroville to hear testimony from the County officials. No action was taken at that hearing.

Ms. Opie said that, based on the evidence and the testimony provided, staff recommends that the Commission find that the County's fiscal year 2004-2005 final budget totals $320.9 million, with a General Fund contingency appropriation of $5.6 million. While this represents increased financing requirements of approximately $2 million from the prior year, the General Fund contingency is expected to decrease by $400,000. The County's discretionary expenditure flexibility is constrained both by fund restrictions and by state and federal mandates, leaving $70.4 million of the $320.9 million in the final budget appropriations, as theoretically available for discretionary use. The full $70.4 million cannot be considered truly discretionary inasmuch as 35 percent, or $24.7 million, is directed towards state-mandated costs and state-established required maintenance of efforts. The County's total available discretionary resource for fiscal year 2004-2005 is projected to decline by $4 million, from $74.4 million in fiscal year 2004-2005. The County’s unmet needs in basic county services, including public safety, total $17,459,947. The County has total resource flexibility of $8,290,839, comprised of revenue and reserves, including appropriation of contingency of $5,616,078. Therefore, the County's unmet needs, offset by its resource flexibility, leaves the County with a net county cost of identified basic county services unmet need of $9,169,108. Ms. Opie also noted that demands outside of the County's growth, programs, and services, such as the increased cost of health care premiums for employees and California Department of Forestry contract costs, have increased.

Staff recommended that the Commission determine that Butte County has made a compelling case that meeting the general assistance standard of aid established in Welfare and Institutions Code section 17000.5 will result in significant financial distress to the County, and that absent this finding, basic county services, including public safety, cannot be maintained. Staff also recommended that the Commission make a finding of significant financial distress for a period of 12 months.

Parties were represented as follows: Paul McIntosh, Cathi Grams, Shari McCracken, Sean Farrell, and Greg Iturria, on behalf of Butte County; and Michael Herald, with the Western Center on Law and Poverty.

Mr. McIntosh thanked the Commission and staff for the time and resources invested in this process and endorsed the findings, with the exception of the 12-month finding. He asked the Commission to reconsider its decision and grant the finding for 36 months, as it did in 1996 and 1999. He submitted that, based upon the five-year fiscal forecast that was presented in the Application, the County's financial situation will not be improving anytime in the near future. Projections showed that the fund balance for 2008-2009 will drop to $283,704, nowhere near what is needed to begin meeting the $17.5 million in unmet needs. He said that any funds received from the state's repayment of the VLF gap will be one-time in nature, and will be used by the County as such. Upon receipt of any VLF gap loan repayment, his office will recommend to the Board of Supervisors that those funds be used to refund the Fire and Sheriff's Departments' Equipment Replacement Fund and that any remaining VLF gap loan repayment be used for other one-time costs that have been deferred over the past years, such as maintenance of existing capital assets. He said that what is key is that no one knows what the adopted State Budget will or will not include.

Mr. McIntosh pointed out that in the Commission's 1999 finding, it relied on the *Goff* case where the court agreed that the Commission must consider alternative revenue enhancements and expenditure reductions when determining if a county is in significant financial distress; but the alternatives must be viable and practical, not speculative. He said that the Commission also said in the 1999 finding that the court stated that alternatives are relevant only to the extent that they can cover the financial shortfall giving rise to the claim of significant financial distress.

Mr. McIntosh emphasized the speculative nature of these funds by noting that the Legislative Analyst's Office projections of revenues available to fund the 2005-2006 State Budget is about $600 million less than those used by the Governor's May Revision.

Also, Mr. McIntosh pointed out that the Governor's May Revision proposal to restore funding for the Small and Rural Sheriffs Program ($500,000 for Butte County) is also speculative, and is not large enough to impact the unmet needs of the Sheriff's Office. If the County does receive the funding, it will cover 6.9 percent of the $7.2 million of unmet needs in the Sheriff's Office. Therefore, he asserted that the recommendation for a 12-month finding does not meet the materiality of the *Goff* decision.

Moreover, Mr. McIntosh stated that Proposition 63 funds are for planning and future expansion of behavioral health services. Proposition 63 funds may only be used for new or expanded programs, not to supplant existing programs. Since the Commission did not recommend any of the unmet needs identified in the Behavioral Health Department, the County is unclear how Proposition 63 funds will help fund the unmet needs approved by the Commission.

To support a finding for 36 months, Mr. McIntosh referred to the Matrix A hand-out. He said that the Commission has consistently found that Butte County has a $17 million unmet need on an ongoing basis. In 1996, the Commission found Butte County had $17.6 million in unmet basic county services, and resource flexibility in the range of $5.4 to $6.8 million, netting to unmet needs in the range of $10.8 to $12.2 million. By 1999, the County had $17.3 million in the basic service unmet needs, and resource flexibility of $9.6 million, netting to unmet needs of $7.8 million. He argued that these findings reflect a decrease in County unmet needs and an increase in resource flexibility, and the Commission granted a 36-month finding. Now, the preliminary findings are that Butte County has a $17.5 million basic unmet need in county services, and $8.3 million in resource flexibility, netting to unmet needs of $9.2 million. Therefore, he argued that unmet needs have increased and resource flexibility has decreased since the 1999 decision.

Mr. McIntosh then referred to the Matrix B handout. Using public safety as an example, Butte County had and will have the same unmet needs over time. Since 1996, the District Attorney's Office has needed and will continue to need five attorneys. He indicated that the Sheriff's office had been understaffed for the past ten years.

Mr. McIntosh said that the five-year financial forecast for Butte County is based on current levels of service, does not restore the County's resources to previous levels, and does not meet the unmet needs identified by the Commission. It does take into account any increases in revenues that the County would anticipate from the passage of Proposition 1A.

Additionally, Mr. McIntosh contended that a 12-month finding would mean the County will be filing annual reapplications. Senate Bill 1033 was amended by the Legislature in light of the extreme administrative burden of gathering, producing and presenting the evidence necessary to convince the Commission of the County's significant financial distress. He stated that the fiscal reality is that the process only works to save the taxpayers money if a 36-month finding is made.

In summary, Mr. McIntosh said that Butte County must, again, request the Commission grant the finding of significant financial distress for a period of 36 months.

Member Boel asked Mr. McIntosh about the County's plans to spend the VLF gap loan repayment. She noted that the County previously indicated plans to spend it on a solar system. Mr. McIntosh replied that their first recommendation would be to restore the vehicle replacement funds that were stripped out in 2004-2005. If they get all $4 million, one option is to invest that one-time revenue source into a second phase of solar, which would then produce an ongoing General Fund savings of about $320,000 to $325,000 a year. In response to Member Boel's question, Mr. McIntosh said that the Board of Supervisors had not yet acted. However, the County awarded a contract for Phase 2 of the solar project contingent upon receiving about $4.2 million in grant funds from PG&E, and then requesting Board approval for financing of the second half of the project.

Member Boel requested confirmation of the number of people on general assistance and the amount of savings the County will realize with a finding of significant financial distress. Mr. McIntosh confirmed that there are about 300 people on assistance and the net annual savings would be about $176,000 to $180,000 a year.

Member Boel also asked Mr. McIntosh what the costs were to the County for presenting its case to the Commission. Mr. McIntosh replied that their actual out-of-pocket cost was virtually zero because the application was completed by salaried employees. They estimated that that cost well

exceeds $100,000. He noted that it is "an opportunity cost as opposed to a real cost."

Member Boel questioned staff about whether a finding or savings of about $200,000 is enough to impact public safety. Paul Starkey, Chief Legal Counsel, responded that under the statute, if the County cannot pay general assistance and still meet its basic needs, then the Legislature has made a policy decision that the County can, if they get the finding from the Commission, make the political decision about whether or not they should reduce general assistance. Under the Commission's regulations, basic county services means those services that are fundamental or essential. Such services shall include, but are not limited to, those services required by state or federal law, and may vary from county to county. The question about whether it is a good form of relief or whether it makes a lot of sense does not go into the equation.

Chairperson Sheehan commented that the relief under the statute is somewhat limited. The Commission only has the ability to make that finding. And, the Commission cannot opine on the wisdom of the net effect and the amount of savings, although it is difficult not to, having gone through the process.

Member Smith said that the problem the Controller has with this item is about the potential savings. A study shows that because people do not retire with adequate benefits, the costs resurface elsewhere, which has some net effect to the state. Similarly here, reducing a significant portion of the poorest of the poor's income means that the costs are going to resurface.
Mr. McIntosh responded that it was recognized at the May 12th hearing that the monetary savings provided in the statute is minimal. There may even be additional costs associated with achieving those savings. But the financially distressed designation offers the County other opportunities, such as grants. He cited to Opinion 5766 issued by the Attorney General on May 20 to support his arguments.

Ms. Opie responded that the staff analysis explains the reasoning for the 12-month finding. Part of the difficulty is the fact that the County provided information for the current year budget, rather than information for the proposed 2005-2006 budget. In addition, the County is carrying over into the next fiscal year $1,107,000 more in revenues than they carried over last year.
Ms. Opie noted that the last application expired in 2002, leaving a period of time when the County did not apply for a finding, and theoretically had the same needs.

Mr. McIntosh reiterated many of his previous arguments, and explained that the reason the County did not file in 2002 was because they thought they were pulling themselves up by the boot straps. They were faced with a 42 percent increase in the firefighters' salary and benefit package, a five or six million dollar increase in their CDF contract, and having to put additional funds in social service programs because realignment revenues were insufficient. He recalled that there was about $43 million over a three-year period of State Budget impacts on Butte County. He argued that it will take four to six years to recover from that, and thus, asked that the Commission grant a 36-month finding.

Paula Higashi, Executive Director, pointed out that in the last application process, Commission staff recommended a 12-month duration. She stated that it was the Commission itself that decided during the hearing, based on the evidence, to make the 36-month finding.

Mr. Herald disagreed with the staff recommendation, contending that Butte County failed to make a compelling case by clear and convincing evidence that they are in significant financial distress. Mr. Herald took issue that the staff analysis did not have more discussion about the impact of property tax revenue, in terms of the County's flexibility funding going forward. He

asserted that there was an increase in property taxes from $15 million to $24 million, and that resale home values in two proximate counties went up by 30 percent and 32 percent from 2003-2004 to 2004-2005, that will give Butte County more fiscal flexibility than the staff analysis suggested.

Mr. Herald agreed with Member Smith's comments about the increased costs due to the reduction taken for general-assistance recipients. As a prior staff member for Governor Davis' Homeless Task Force, he helped produce a series of reports that outlined the substantial state costs for allowing people to become homeless. There are many increased costs, including the use of 911 systems, mental health facilities, and public health systems. Allowing people to become homeless is counterproductive, and will cost the county more money than it will save. He said that the Institute on Law and Public Planning recently found that there is over-prosecution of minor offenses in Butte County. More money goes into public safety programs than what they see in other counties. For example, Butte County has three times the number of investigators as a comparable county, like Merced. Mr. Herald also said that the District Attorney's Office is using CalWORKS eligibility funds for fraud investigations, which are leading to increased convictions and increased costs for the county.

Chairperson Sheehan clarified that the Commission is not deciding to reduce general assistance and Mr. Herald agreed that it is the County's decision to do that.

Regarding property tax revenues, Chairperson Sheehan asked staff to provide the Commission's authority under current law, and asked Butte County representatives to provide estimates from the property tax assessor. Ms. Opie replied that staff's property tax analysis shows the actual and the estimate for 2004-2005. The estimate for 2004-2005 shows a significant increase over the prior years.

Mr. McIntosh confirmed that the information came from the County. He said that Mr. Herald failed to recognize the "triple-flip" funding mechanism that occurred. Property taxes increased from $16 million to $25 million, sales taxes dropped from $4 million to $3 million, and vehicle license fees dropped from $11 million to $5 million, with a net result in growth of $2 million. The change in the property tax revenue was taken into account in their five-year fiscal forecast.

Regarding other points that Mr. Herald made, Mr. McIntosh agreed that this is the wrong forum for discussion on what the impact of this decision is on low-income individuals, as it was before the Board of Supervisors. Regarding the Institute on Law and Public Planning finding, in their proposed budget, they recommended eliminating 9.5 investigators from the District Attorney's Welfare Fraud Program. He reiterated his May 12 testimony and again requested that the Commission make a 36-month finding.

Mr. Starkey emphasized that the statutory charge is to make the best possible decision. Regarding the three-year finding, the statute provides the Commission with the authority to make a three-year finding; it does not require it. At every stage, the Commission members have to keep in mind that this is a compelling case that has to be made for the first 12 months, the second 12 months and the third 12 months.

Chairperson Sheehan asked if there is a difference between a "reapplication" and a "new application." Mr. Starkey replied that there are additional factors required in the reapplication. Mr. Starkey stated that based on the regulations, the Commission has to be convinced that for the next three years, this is going to be the situation.

Ms. Higashi said that the Commission's next step is to adopt a preliminary decision. Once the Commission adopts that decision, the proposed Statement of Decision will be before the Commission for adoption on June 10th.

Member Boel made a motion to approve the application for Butte County with a finding of significant financial distress for 12 months.

In response to Chairperson Sheehan's question about when the 12 months would begin, Ms. Higashi replied that the County provides the actual date they want the finding to be effective. Mr. McIntosh requested an effective date of September 1, 2005.

Member Smith seconded Member Boel's motion. The motion carried unanimously.

STAFF REPORTS

Item 18 Chief Legal Counsel's Report (info)
Recent Decisions, Litigation Calendar

No report was made on item 18.

Item 19 Executive Director's Report (info/action)
Budget, Workload, Legislation, Next Hearing

Ms. Higashi reported that both subcommittees approved the Commission's budget. There is a conference item that is part of the Commission's budget item that relates to the test claim decision on the mandate reimbursement process. There is interest in both houses for the Commission to reconsider that decision. There are still open issues regarding which mandates are suspended, which ones are deferred, and which ones might be fully funded because of Proposition 1A.

CLOSED EXECUTIVE SESSION PURSUANT TO GOVERNMENT CODE SECTIONS 11126 and 17526.

Ms. Higashi indicated that there would be no closed session meeting.

ADJOURNMENT

Chairperson Sheehan adjourned the meeting at 2:39 p.m.

PAULA HIGASHI
Executive Director