

COMMISSION ON STATE MANDATES

980 NINTH STREET, SUITE 300
SACRAMENTO, CA 95814
PHONE: (916) 323-3562
FAX: (916) 445-0278
E-mail: csminfo@csm.ca.gov



January 9, 2015

Mr. Keith Petersen
SixTen & Associates
P.O. Box 340430
Sacramento, CA 95834-0430

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

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

Re: **Draft Proposed Decision, Schedule for Comments, and Notice of Hearing**
Health Fee Elimination, 06-4206-I-13
Education Code Section 76355
Statutes 1984, Chapter 1, 2nd E.S.; Statutes 1987, Chapter 1118
Fiscal Years 1999-2000, 2000-2001, and 2001-2002
Pasadena Area Community College District, Claimant

Dear Mr. Petersen and Ms. Kanemasu:

The draft proposed decision for the above-named matter is enclosed for your review and comment.

Written Comments

Written comments may be filed on the draft proposed decision by **January 30, 2015**. You are advised that comments filed with the Commission are required to be simultaneously served on the other interested parties on the mailing list, and to be accompanied by a proof of service. However, this requirement may also be satisfied by electronically filing your documents. Please see <http://www.csm.ca.gov/dropbox.shtml> on the Commission's website for instructions on electronic filing. (Cal. Code Regs., tit. 2, § 1181.3.)

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

Hearing

This matter is set for hearing on **Friday, March 27, 2015**, at 10:00 a.m., State Capitol, Room 447, Sacramento, California. The proposed decision will be issued on or about March 13, 2015. Please let us know in advance if you or a representative of your agency will testify at the hearing, and if other witnesses will appear. If you would like to request postponement of the hearing, please refer to section 1187.9(b) of the Commission's regulations.

Sincerely,

A handwritten signature in black ink, appearing to read "Heather Halsey".

Heather Halsey
Executive Director

ITEM __
INCORRECT REDUCTION CLAIM
DRAFT PROPOSED DECISION

Former Education Code section 72246 (Renumbered as 76355)¹,
Statutes 1984, Chapter 1 (1983-1984 2nd Ex. Sess.); Statutes 1987, Chapter 1118

Health Fee Elimination

Fiscal Years 1999-2000, 2000-2001 and 2001-2002

06-4206-I-13

Pasadena Area Community College District, Claimant

EXECUTIVE SUMMARY

Overview

This analysis addresses reductions made by the State Controller's Office (Controller) to Pasadena Area Community College District's (claimant's) reimbursement claims for fiscal years 1999-2000, 2000-2001, and 2001-2002 under the *Health Fee Elimination* program. Over the three fiscal years in question, the Controller reduced claimed costs by a total of \$375,941. The following issues are in dispute in this IRC:

- The statutory deadlines applicable to the audit of the 1999-2000 and 2000-2001 reimbursement claims;
- Reduction of costs claimed in fiscal years 2000-2001 and 2001-2002 based on claimant's development and application of indirect cost rates.
- The amount of offsetting revenue to be applied from health service fee revenue.
- Adjustment made based on prior payments to the claimant for the program.

Health Fee Elimination Program

Prior to 1984, former Education Code section 72246 authorized community college districts to charge almost all students a general fee (health service fee) for the purpose of voluntarily providing health supervision and services, direct and indirect medical and hospitalization services, and operation of student health centers.² In 1984, the Legislature repealed the

¹ Statutes 1993, chapter 8.

² 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.]

community colleges' fee authority for health services.³ 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 for quarter or summer semester).⁴

In addition to temporarily repealing community college district's 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 the district was previously authorized to charge a fee, to maintain the health services at the level provided during the 1983-1984 fiscal year for every subsequent fiscal year until January 1, 1988. As a result, community college districts were required to maintain 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, 1988.⁵ 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 semester.⁶ 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 a limited fee authority to offset the costs of those services. In 1992, section 72246 was amended to provide that the health services fee could be increased by the same percentage as the Implicit Price Deflator whenever that calculation would produce an increase of one dollar.⁷

Procedural History

Claimant's 1999-2000 fiscal year claim was filed with the Controller on January 10, 2001. Claimant's 2000-2001 fiscal year claim was filed with the Controller on December 20, 2001. Claimant's 2001-2002 fiscal year claim was dated January 10, 2003. The Controller conducted an entrance conference on May 21, 2003, to initiate an audit of the claims. On March 17, 2004, the Controller issued its final audit report, concluding that claimant had overstated its indirect costs for the program and had inaccurately reported offsetting revenue collected. Claimant filed this IRC with the Commission on State Mandates (Commission) on July 3, 2006.⁸

On, January 8, 2008, the Controller submitted comments on the IRC.⁹

³ Statutes 1984, 2nd Extraordinary Session, chapter 1, section 4 [repealing Education Code section 72246].

⁴ Statutes 1984, 2nd Extraordinary session, chapter 1, section 4.5.

⁵ 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).

⁶ 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).

⁷ 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.

⁸ Exhibit A, Glendale Community College District IRC.

⁹ Exhibit B.

On January 9, 2015, a draft proposed decision on the IRC was issued for comment.

Commission Responsibilities

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 decision to the Controller and request that the costs in the claim be reinstated.

The Commission must review questions of law, including interpretation of parameters and guidelines, de novo, without consideration of 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 6.¹⁰ 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."¹¹

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.¹²

The Commission must also 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.¹³ In addition, section 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.¹⁴

¹⁰ *Kinlaw v. State of California* (1991) 54 Cal.3d 326, 331-334; Government Code sections 17551, 17552.

¹¹ *County of Sonoma*, supra, 84 Cal.App.4th 1264, 1280, citing *City of San Jose v. State of California* (1996) 45 Cal.App.4th 1802, 1817.

¹² *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.

¹³ *Gilbert v. City of Sunnyvale* (2005) 130 Cal.App.4th 1264, 1274-1275.

¹⁴ 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 Commission must also 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.¹⁵ In addition, section 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.¹⁶

Claims

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

Subject	Description	Staff Recommendation
Statutory deadlines applicable to the audit of claimant’s 1999-2000 and 2000-2001 annual reimbursement claims.	At the time costs were incurred and the 1999-2000 and 2000-2001 reimbursement claims were filed, Government Code section 17558.5 stated: “A reimbursement claim for actual costs filed by a local agency or school district pursuant to this chapter is subject to 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.” Claimant asserts that the claim was no longer subject to audit at the time the final audit report was issued.	<i>The audit was not time-barred by any statutory or common law limitation - Staff finds that the plain language of section 17558.5, at the time the reimbursement claims were filed, did not require the Controller to complete an audit within any specified period of time, and that a subsequent amendment to the statute demonstrates that “subject to audit” means “subject to the initiation of an audit.” Additionally, the audit was completed within a reasonable time and so is not barred by common law principles of laches.</i>
Reduction based on asserted flaws in the development of indirect cost rates.	Claimant asserts that the Controller incorrectly reduced indirect costs claimed for fiscal years 2000-2001 and 2001-2002,	<i>Correct as a matter of law and not arbitrary, capricious or entirely lacking in evidentiary support- Claimant did not comply with the</i>

¹⁵ *Gilbert v. City of Sunnyvale* (2005) 130 Cal.App.4th 1264, 1274-1275.

¹⁶ 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.

	<p>because the claimant used an indirect cost rate calculation that did not comply with its federally approved indirect cost rate or the state Form FAM-29C as required by the claiming instructions. Claimant asserts that the parameters and guidelines are permissive, allowing the claimant to calculate the indirect cost rate any way it chooses.</p>	<p>parameters and guidelines, which direct claimants to claim indirect costs consistently with the claiming instructions by using either the state’s FAM-29C method, or a federally approved OMB Circular A-21 method. Instead, claimant used an alternative method to claim indirect costs of 47.3% for fiscal year 2000-2001 and 47.8% in fiscal year 2001-2002. Thus, the reduction is correct as a matter of law. In addition, the Controller’s recalculation of indirect costs using a 30% federally approved rate under OMB A-21, which the claimant used in fiscal year 1999-2000, is not arbitrary, capricious, or entirely lacking in evidentiary support.</p>
<p>Reduction based on understated offsetting health service fee revenues.</p>	<p>Claimant asserts that the student enrollment information provided in the reimbursement claims is accurate. The Controller ‘s audit found claimant did not provide any documentation to support the enrollment data provided in the reimbursement claims and recalculated student enrollment and fees collected based upon data provided by claimant to the California Community Colleges Chancellor’s Office, increasing offsetting revenue.</p>	<p><i>Correct as a matter of law and not arbitrary, capricious, or entirely lacking in evidentiary support - Staff finds that claimant did not provide any documentation to support the enrollment data used to calculate offsetting revenue, as required by the parameters and guidelines, and, thus, the Controller’s reduction is correct as a matter of law. Staff further finds that the Controller’s recalculation of student enrollment using data provided by claimant to the Chancellor’s Office was not arbitrary, capricious, or entirely lacking in evidentiary support.</i></p>

Staff Analysis

A. The audit of the reimbursement claims for fiscal years 1999-2000 and 2000-2001 is not barred by the deadlines found in Government Code section 17558.5.

Government Code section 17558.5, as added by Statutes 1995, chapter 945 (operative July 1, 1996) provides that a reimbursement claim “is subject to audit by the Controller *no later than two years after the calendar year* in which the reimbursement claim is filed or last amended.”¹⁷

¹⁷ Government Code section 17558.5 (Stats. 1995, ch. 945 (SB 11) [emphasis added]).

The 1999-2000 reimbursement claim was filed on January 10, 2001 and the 2000-2001 reimbursement claim was filed on December 20, 2001. Thus, both claims were “subject to audit” by the plain language of section 17558.5 until December 31, 2003.

The Controller states that it met the December 31, 2003 deadline since it *initiated* the audit on May 21, 2003, when an entrance conference was held for this audit. The claimant does not dispute that the entrance conference initiated the audit. However, the claimant asserts that “subject to” requires the Controller to *complete* the audit no later than two years after the end of the calendar year that the reimbursement claim was filed. Applying claimant’s argument in this case would require the completion of the audit for the 1999-2000 and 2000-2001 reimbursement claims by December 31, 2003. The Controller did not complete its final audit of this claim until nearly three months later, on March 17, 2004, when the Controller issued the final audit report.

The plain language of the first sentence in Government Code section 17558.5, as added in 1995, does not require the Controller to “complete” the audit within any specified period of time. The plain language of the statute provides that reimbursement claims are “subject to audit” within 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, but sets a time during which a claimant is on notice that an audit of a claim may occur. This interpretation is consistent with the 2002 amendment to the first sentence of section 17558.5, which clarified that “subject to audit” means “subject to the initiation of an audit.” In this case, the audit of the reimbursement claims filed for fiscal years 1999-2000 and 2000-2001 had to be initiated by December 31, 2003. Since the audit began no later than May 21, 2003, when the entrance conference was conducted, the audit was timely initiated.

In addition, the 2002 amendment to section 17558.5 expanded the statutory period to *initiate an audit* to “three years after the date that the actual reimbursement claim is filed or last amended.”¹⁸ Pursuant to the *Douglas Aircraft* case, “[u]nless a statute expressly provides to the contrary, any enlargement of a statute of limitations provision applies to matters pending but not already barred.”¹⁹ Therefore, an expansion of a statute of limitations applies to matters pending but not already barred, based in part on the theory that a party has no vested right in the running of a statutory period prior to its expiration.²⁰ In this case, the 2002 amendment to section 17558.5 became effective on January 1, 2003, when the audit period for both reimbursement claims was still pending and not yet barred under the prior statute. The 2002 statute, which enlarged the time to initiate the audit to three years after the date the reimbursement claim is filed or last amended controls, and gives the Controller additional time to initiate the audit. The Controller therefore had until January 10, 2004, to initiate the audit of the 1999-2000 reimbursement claim, and had until December 20, 2004, to initiate the 2000-2001 reimbursement claim. Since the audit was initiated no later than May 21, 2003, when the entrance conference was held and before the 2004 deadlines, the audit was timely initiated under section 17558.5, as amended in 2002.

¹⁸ Statutes 2002, chapter 1128 (AB 2834) (effective January 1, 2003).

¹⁹ *Douglas Aircraft Co. v. Cranston* (1962) 58 Cal.2d 462, at p. 465.

²⁰ *Mudd v. McColgan* (1947) 30 Cal.2d 463, 468

Moreover, section 17558.5 was amended in 2004 to establish, for the first time, the requirement to “complete” the audit two years after the audit is commenced. The 2004 amendment became effective on January 1, 2005, *after* the completion of the audit of the reimbursement claims for fiscal years 1999-2000 and 2000-2001 and, thus, does not apply to the audit in this case. Nevertheless, the Controller was still required under common law to complete the audit within a reasonable period of time. Under appropriate circumstances, the defense of laches may operate to bar a claim by a public agency if there is evidence of unreasonable delay by the agency and resulting prejudice to the claimant.²¹ The audit was completed less than one year after it was initiated and, under the facts of this case, within a reasonable period of time. In addition, there is no evidence that the claimant was prejudiced by the audit process.

Based on the above analysis, staff finds that the audit of the 1999-2000 and 2000-2001 reimbursement claims was timely.

B. The Controller’s Recalculation and Reduction of Indirect Costs Claimed is Correct as a Matter of Law and Not Arbitrary, Capricious or Entirely Lacking in Evidentiary Support.

The Controller reduced indirect costs claimed for fiscal years 2000-2001 and 2001-2002 by \$157,273 because claimant did not use either a federally approved rate or the state’s Form FAM-29C. For fiscal year 1999-2000, claimant used an indirect cost rate of 30 percent that was federally approved and the Controller did not reduce any indirect costs claimed for that year. In 2000-2001 and 2001-2002, claimant used an outside consultant to prepare its indirect cost rate and that rate exceeded the federally approved rate by 17.3 percent in 2000-2001 and 17.8percent in 2001-2002.²² The Controller reduced the indirect cost rates for 2000-2001 and 2001-2002 to the federally approved rate of 30% concluding that the outside consultant’s rate exceeded the approved federal rate and therefore was not consistent with the parameters and guidelines and claiming instructions.

The parameters and guidelines expressly require claimants to claim indirect costs in the manner described in the Controller’s claiming instructions, which in turn provide that an indirect cost rate may be developed in accordance with federal OMB guidelines or by using the state Form FAM-29C.

Staff finds claimant did not comply with the requirements in the parameters and guidelines and claiming instructions in developing and applying its indirect cost rate for fiscal years 2000-2001 and 2001-2002 since it did not use its federally approved indirect cost rate or the state Form FAM-29C. Therefore, the reduction is correct as a matter of law. Staff further finds that the Controller’s recalculation of indirect costs using the

²¹ *Cedar-Sinai Medical Center v. Shewry* (2006) 137 Cal.App.4th 964, 985-986. In that case, the court determined that the hospital failed to establish an unreasonable delay in audits conduct by Department of Health Services, since the Department conducted audits two years or less after the end of the fiscal period that it was auditing, which was less than the three-year period permitted by statute. See also, *Steen v. City of Los Angeles* (1948) 31 Cal.2d 542, 546, where the court held that laches applies in quasi-adjudicative proceedings.

²² Exhibit A, IRC, Exhibit D, at p. 57.

federally approved rate of 30 percent is not arbitrary, capricious, or entirely lacking in evidentiary support.

C. The Controller's Reduction for Understated Offsetting Revenues is Correct as a Matter of Law and not Arbitrary, Capricious, or Lacking in Evidentiary Support.

The Controller reduced costs for the three fiscal years by \$287,865 because claimant understated its offsetting health fee revenues.²³ The reduction was made because claimant did not provide documentation to support the student enrollment data used to calculate the health fees revenues reported in its reimbursement claims. The Controller recalculated student enrollment using data claimant provided to the California Community Colleges Chancellor's Office. This enrollment data reflected more students paid health fees than claimant reported in its reimbursement claims.²⁴

The parameters and guidelines require claimants to demonstrate that "all costs claimed must be traceable to source documents and/or worksheets that show evidence of the validity of such costs."²⁵ As claimant did not provide adequate documentation to support its enrollment data, the Controller's reduction is correct as a matter of law. Staff further finds that the Controller's recalculation of student enrollment using data provided by claimant to the Chancellor's Office was not arbitrary, capricious, or entirely lacking in evidentiary support. The documents are public records provided by the claimant in the normal course of business, and the claimant has provided no other documents to support enrollment data.

D. The Controller's Adjustment Based on Payments Made to the Claimant is Supported by Evidence in the Record, and is not Arbitrary, Capricious, or Entirely Lacking in Evidentiary Support.

The claimant questions additional adjustments made by the Controller to the amounts owed based on two claim payments issued by the state to the claimant for fiscal years 1999-2000 and 2000-2001. The claimant contends that it cannot determine the propriety of these adjustments until the Controller states the reason for the change.²⁶

The Controller responds as follows:

As clearly stated in the audit report, and reconfirmed in the documentation in Tab 8, the District received two claim payments (\$57,365 issued on 8/1/2001 and \$26,099 issued on 3/9/2001) totaling \$83,464 for fiscal year 1999-2000, and one claim payment of \$19,270 issued on 3/8/2001 for fiscal year 2000-2001. The adjustments were made because of these reimbursement payments the District received.²⁷

²³ Exhibit B, Controller's Comments, Tab 1, at p. 7.

²⁴ Exhibit B, Controller's Comments, Tab 1, at pp. 7, 9.

²⁵ Exhibit X, Parameters and Guidelines, at p. 6.

²⁶ Exhibit A, IRC, pages 18-21.

²⁷ Exhibit B, Controller's comments on IRC, page 3.

Tab 8 of the Controller's comments contains copies of the warrants showing payments made to the claimant for the mandated program for \$83,464 and \$19,270.²⁸ These payments are reflected as adjustments in the final audit report for fiscal years 1999-2000 and 2000-2001.²⁹

Staff finds that the Controller's adjustment based on prior payments is supported by evidence in the record, and is not arbitrary, capricious, or entirely lacking in evidentiary support.

Conclusion

Pursuant to Government Code section 17551(d), staff concludes that the Controller's audit of the 1999-2000 and 2000-2001 reimbursement claims was timely, and that the reduction of the following costs is correct as a matter of law, and not arbitrary, capricious, or entirely lacking in evidentiary support:

- The reduction of indirect costs claimed for fiscal years 2000-2001 and 2001-2002, in the amount of \$157,273.
- The reduction of costs due to understated offsetting revenue in the amount of \$287,865.
- The adjustment based on prior payments made to the claimant.

Staff Recommendation

Staff recommends that the Commission adopt the proposed statement of decision to deny the IRC, and authorize staff to make any technical, non-substantive changes following the hearing.

²⁸ Exhibit B, Controller's comments on IRC, pages 102-103.

²⁹ Exhibit B, Controller's comments on IRC, page 164.

BEFORE THE
COMMISSION ON STATE MANDATES
STATE OF CALIFORNIA

IN RE INCORRECT REDUCTION CLAIM
ON:

Education Code Section 76355

Statutes 1984, Chapter 1 (1983-1984 2nd Ex.
Sess.) (AB 1) and Statutes 1987, Chapter 1118
(AB 2336)

Fiscal Years 1999-2000, 2000-2001, and 2001-
2002

Pasadena Area Community College District,
Claimant.

Case Nos.: 06-4206-I-13

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 March 27, 2015)

DECISION

The Commission on State Mandates (Commission) heard and decided this incorrect reduction claim (IRC) during a regularly scheduled hearing on March 27, 2015. [Witness list will be included in the adopted decision.]

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

The Commission [adopted/modified] the proposed decision to [approve/partially approve/deny] this IRC at the hearing by a vote of [vote count will be included in the adopted decision].

Summary of the Findings

This decision addresses reductions made by the State Controller's Office (Controller) to Pasadena Area Community College District's (claimant's) reimbursement claims for fiscal years 1999-2000, 2000-2001, and 2001-2002 under the *Health Fee Elimination* program. Over the three fiscal years in question, the Controller reduced costs totaling \$375,941, finding that (1) the claimant overstated indirect costs by not using either the OMB Circular A-21 or the Form FAM 29C methodologies, and (2) understated offsetting health fee revenues that were collected by the claimant, based on the Controller's review of documentation provided to the Chancellor's Office supporting enrollment data during the audit years. The claimant also questions adjustments made by the Controller based on prior payments on the program to the claimant.

The Commission finds that the Controller conducted the audit of the 1999-2000 and 2000-2001 reimbursement claims within the deadlines imposed by Government Code section 17558.5 and, therefore, the audit is not void with respect to these reimbursement claims.

The Commission further finds that the reduction of the following costs is correct as a matter of law, and not arbitrary, capricious, or entirely lacking in evidentiary support:

- The reduction of indirect costs claimed for 2000-2001 and 2001-2002 of \$157,273. Claimant did not comply with the parameters and guidelines and Controller's claiming instructions in preparing its indirect cost rate for 2000-2001 and 2001-2002 and, thus, the Controller's reduction of these costs is correct as a matter of law and not arbitrary, capricious, or entirely lacking in evidentiary support.
- The reduction of costs due to understated offsetting revenue of \$287,865. Claimant did not provide any documentation to support the enrollment data used to calculate offsetting revenue as required by the parameters and guidelines and, thus, the Controller's reduction is correct as a matter of law. The Commission further finds that the Controller's recalculation of student enrollment using data provided by claimant to the Chancellor's Office was not arbitrary, capricious, or entirely lacking in evidentiary support.

In addition, the adjustment based on prior payments to the claimant is supported by evidence in the record and is not arbitrary, capricious, or entirely lacking in evidentiary support.

Accordingly, the Commission denies this IRC.

COMMISSION FINDINGS

I. Chronology

- | | |
|----------|--|
| 01/10/01 | Claimant filed a reimbursement claim for fiscal year 1999-2000. ³⁰ |
| 12/20/01 | Claimant filed a reimbursement claim for fiscal year 2000-2001. ³¹ |
| 01/10/03 | Claimant submitted a reimbursement claim for fiscal year 2001-2002. ³² |
| 05/21/03 | The Controller conducted an entrance conference for the audits of the 1999-2000, 2000-2001 and 2001-2002 reimbursement claims. |
| 01/21/04 | The Controller issued a draft audit report. |
| 03/17/04 | The Controller issued a final audit report. ³³ |
| 07/03/06 | Claimant filed this IRC. ³⁴ |
| 07/13/06 | Commission staff issued a Notice of Complete Filing. |
| 01/07/08 | The Controller, Division of Audits filed comments on the IRC. ³⁵ |
| 01/09/15 | Commission staff issued the draft proposed decision for comment. |

³⁰ Exhibit A, IRC, Exhibit D, at pp. 64 *et seq.*.

³¹ Exhibit A, IRC, Exhibit D, at pp. 70 *et seq.*.

³² Exhibit A, IRC, Exhibit D, at pp.76 *et seq.* Reimbursement claim for FY 2001-2002.

³³ Exhibit A, IRC.

³⁴ Exhibit A, IRC.

³⁵ Exhibit B, Controller, Division of Audits, Comments.

II. Background

Health Fee Elimination Program

Prior to 1984, former Education Code section 72246 authorized community college districts to charge almost all students a general fee (health service fee) for the purpose of voluntarily providing health supervision and services, direct and indirect medical and hospitalization services, and operation of student health centers.³⁶ In 1984, the Legislature repealed the community colleges' fee authority for health services.³⁷ However, the Legislature also reenacted section 72246 in order to reauthorize the fee, at \$7.50 for each semester (or \$5 for quarter or summer semester), which was to become operative on January 1, 1988.³⁸

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 the health services at the level provided during the 1983-1984 fiscal year for every subsequent fiscal year until January 1, 1988.³⁹ As a result, community college districts were required to maintain health services provided in the 1983-1984 fiscal year without any fee authority for this purpose, until January 1, 1988.

In 1987,⁴⁰ the Legislature amended former Education Code section 72246, which was to become 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, 1988.⁴¹ 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 semester.⁴² 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 a limited fee authority to offset the costs of those services.⁴³

³⁶ Statutes 1981, chapter 763. Students with low-incomes, students that depend upon prayer for healing, and students attending a college under an approved apprenticeship training program, were exempt from the fee.

³⁷ Statutes 1984, 2nd Extraordinary Session 1984, chapter 1, section 4 [repealing Education Code section 72246].

³⁸ Statutes 1984, 2nd Extraordinary Session 1984, chapter 1, section 4.5.

³⁹ Education Code section 72246.5 (Stats. 1984, 2d. Ex. Sess., ch. 1, § 4.7).

⁴⁰ Statutes 1987, chapter 1118.

⁴¹ 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).

⁴² Education Code section 72246 (as amended, Stats. 1987, ch. 1118).

⁴³ 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. (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).

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 adopted amendments to the parameters and guidelines for the *Health Fee Elimination* program 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

The claimant submitted reimbursement claims for 1999-2000, 2000-2001, and 2001-2002, claiming costs totaling \$678,460. Following a field audit, the Controller reduced the costs claimed by \$375,941, based on the following audit findings:

- Overstated indirect costs claimed in fiscal years 2000-2001 and 2001-2002 by \$157,273. Indirect cost rates of 47.3% for fiscal year 2000-2001 and 47.8% in fiscal year 2001-2002 were used by the claimant in those years. The claimant, however, did not calculate the indirect cost rates in accordance with OMB Circular A-21 or the alternative methodology in Form FAM-29C. The Controller recalculated indirect costs using the claimant's federally approved rate of 30%, which was correctly used by the claimant in the fiscal year 1999-2000 reimbursement claim.⁴⁴
- Understated offsetting health fee revenue in all three fiscal years totaling \$287,865, based on an unsupported student attendance data used by the claimant to calculate the fees collected. This audit was one of the first performed on the *Health Fee Elimination* program and it occurred before the court's decision in *Clovis Unified School District v. Chiang*. Thus, in this case, the Controller did not consider the extent of the claimant's fee revenue *authorized* to be collected, but looked only at the revenue actually collected by the claimant. The Controller found that the claimant failed to provide the student attendance data it used to determine offsetting revenues received and, thus, the Controller recalculated offsetting revenues received by using attendance data the claimant reported to the Chancellor's Office in the normal course of business. The Controller's recalculation resulted in a finding that the claimant underreported fee revenue received during the audit period.⁴⁵

The claimant challenges these findings and also raises the following issues:

- The statute of limitations applicable to the Controller's audit of the fiscal year 1999-2000 and 2000-2001 reimbursement claims. The claimant contends that the audit findings for

⁴⁴ Exhibit B, Controller's comments on IRC, at pages 14 (Tab 2) and 166 (Finding 1, Final Audit Report).

⁴⁵ Exhibit B, Controller's comments on IRC, at pages 2 (letter from the Controller's Senior Staff Counsel) and 166 (Finding 2, Final Audit Report).

these two years are void since the audit was not completed by the deadline required by Government Code section 17558.5.

- Additional adjustments to the amounts owed based on two claim payments issued by the state to the claimant for fiscal years 1999-2000 and 2000-2001. The claimant contends that it cannot determine the propriety of these adjustments until the Controller states the reason for the change.⁴⁶

III. Positions of the Parties

Pasadena Community College District

Claimant asserts that the Controller incorrectly reduced costs claimed in fiscal years 1999-2000, 2000-2001, and 2001-2002 totaling \$375,941, and requests that the entire amount be reinstated. Specifically, claimant asserts that for fiscal years 1999-2000 and 2000-2001, the audit is barred by the statutory deadline of Government Code section 17558.5.⁴⁷ Claimant also argues that the Controller inappropriately reduced indirect costs claimed.⁴⁸ For fiscal years 2000-2001 and 2001-2002, claimant argues that the parameters and guidelines do not require claimant to use one of the two alternative formulas for computing indirect cost rates, specifically the federally approved rate that the claimant used for fiscal year 1999-2000.⁴⁹

Claimant further asserts that its reimbursement claims should not be reduced by the amount of fees authorized to be charged, but only by those actually collected.⁵⁰ In addition, claimant asserts that the Controller should not have adjusted student enrollment data, using data claimant provided to the California Community Colleges Chancellor's Office, instead of data used to file the reimbursement claims.⁵¹

Claimant also questions the adjustments made based on payments made by the state.

State Controller's Office

The Controller argues that, pursuant to Government Code section 17558.5, it timely conducted the audit of the fiscal year 1999-2000 and 2000-2001 reimbursement claims.⁵² The Controller also contends that the reductions are correct and supported by the record.⁵³

⁴⁶ Exhibit A, IRC, pages 18-21.

⁴⁷ Exhibit A, IRC, at pp. 16-19.

⁴⁸ Exhibit A, IRC, at pp. 9-10.

⁴⁹ Exhibit A, IRC, at, pp. 9-10.

⁵⁰ Exhibit A, IRC, at pp. 12-15. However, because the audit only addressed fees actually collected, this is not at issue in this IRC.

⁵¹ Exhibit A, IRC, at p. 15.

⁵² Exhibit B, Controller's Comments on IRC, Cover Letter, at pp. 3-4.

⁵³ Exhibit B, Controller's Comments on 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 6.⁵⁴ 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 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

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

⁵⁵ *County of Sonoma, supra*, 84 Cal.App.4th 1264, 1280, citing *City of San Jose v. State of California* (1996) 45 Cal.App.4th 1802, 1817.

⁵⁶ *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.

⁵⁷ *American Bd. of Cosmetic Surgery, Inc, supra*, 162 Cal.App.4th at pgs. 547-548.

The Commission must review also 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, section 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.⁵⁹

A. The Audit of the Reimbursement Claims for Fiscal Years 1999-2000 and 2000-2001 is Not Barred by the Deadlines Found in Government Code Section 17558.5.

Claimant asserts that the audit of the 1999-2000 and 2000-2001 reimbursement claims was not timely and, therefore, the audit is void with respect to those claims.

In 2001 when claimant filed these two reimbursement claims, Government Code section 17558.5, as added in 1995, stated the following:

A reimbursement claim for actual costs filed by a local agency or school district pursuant to this chapter is subject to 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.⁶⁰

Claimant contends that funds were appropriated for this program for the 1999-2000 and 2000-2001 claim years and, thus, the first sentence of section 17558.5 applies.⁶¹ Since the 1999-2000 reimbursement claim was filed on January 10, 2001 and the 2000-2001 reimbursement claim was filed on December 20, 2001, both claims were subject to audit by the plain language of section 17558.5 until December 31, 2003. The Controller states that it initiated the audit on May 21 2003, when an entrance conference was held for this audit and this fact is not in dispute. However, claimant asserts that "subject to audit" requires the Controller "to complete" the audit no later than two years after the end of the calendar year that the reimbursement claim was filed. Claimant further argues that if the "subject to audit" language is interpreted as requiring the Controller to simply begin the audit before the deadline, it would lead to uncertainty for the claimant in knowing when the statute of limitations would expire.⁶² Applying claimant's argument in this case would require the completion of the audit for the 1999-2000 and 2000-

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 Government Code section 17558.5 (Stats. 1995, ch. 945, (SB11)). Former Government Code section 17558.5 was originally added by the Legislature by Statutes 1993, chapter 906, effective January 1, 1994. The 1993 statute became inoperative on July 1, 1996, and was repealed on January 1, 1997 by its own terms.

⁶¹ Exhibit A, IRC, at p. 18.

⁶² Exhibit A, IRC, at p. 19.

2001 reimbursement claims by December 31, 2003. The Controller did not complete its final audit of these claims until three months later, on March 17, 2004, when the Controller issued the final audit report.

The Controller argues that claimant's reading of Government Code section 17558.5 is based on an erroneous interpretation that attempts to rewrite that section, adding a deadline for completion of the audit where none exists. The Controller asserts that the "subject to audit" language in section 17558.5, as added in 1995, refers to the time the audit is initiated. In this case, the Controller states that the audit of both the 1999-2000 and 2000-2001 claims was initiated at the entrance conference conducted on May 21, 2003, and that this date is within the two years after the end of the calendar year in which the claims were filed pursuant to section 17558.5.

Alternatively, the Controller argues that a 2002 amendment to section 17558.5, which became effective on January 1, 2003, enlarges the statute of limitations to initiate an audit to three years, and that the later enacted statute applies here to give the Controller an additional year to initiate the audit since the audit period for the 1999-2000 and 2000-2001 was still open. In this regard, the Controller states the following:

"Moreover, Government Code section 17558.5 was subsequently amended while the District's claims were still subject to audit. The amended Government Code section 17558.5 that was operative in 2003⁶³ applies to these claims. Under this amended statute, claims are "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." It is well established that "...any legislative enlargement of the limitation period applies to pending matters not already barred." (43 Cal Jur 3d, Limitations of Actions, section 8.⁶⁴

The Commission finds that the audit of the 1999-2000 and 2000-2001 reimbursement claims was timely initiated and completed under Government Code section 17558.5.

The plain language of Government Code section 17558.5, as added in 1995, does not require the Controller to "complete" the audit within any specified period of time. The plain language of the statute provides that reimbursement claims are "subject to audit" within 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, but sets a time during which a claimant is on notice that an audit of a claim may occur. This reading is consistent with the plain language of the second sentence, which establishes a longer period of time to initiate the audit when no funds are appropriated for the program as follows:

...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 the initial payment of the claim.

While one rule of statutory construction states that the use of differing language in otherwise parallel statutory provisions (like the use of the word "initiate" in the second sentence, but not in the first sentence) supports an inference that a difference in meaning was intended by the Legislature, the Commission finds that inference is not supportable

⁶³ Stats. 2002, chapter 1128 (Assembly Bill 2834), section 14.5, operative January 1, 2003.

⁶⁴ Exhibit B, Controller's Comments, Cover Letter, at p. 3.

in this case.⁶⁵ Section 17558.5(a) is not a model of clarity. However, a careful reading of the language of the first and second sentences reveals that the primary difference between the two is whether an appropriation has been made for the program. The second sentence clearly refers to situations where funds are *not* appropriated. It can reasonably be inferred from the context that the first sentence, in contrast, refers to situations where funds *are* appropriated. The use of the word “however” to begin the second sentence, signals the contrast between these two situations (when funds are appropriated versus when they are not). There is nothing about the structure or language of the two sentences to suggest that the Legislature intended any other substantive differences between these two parallel sentences. In each situation, the Controller must perform some activity within a two-year period. The use in the second sentence of the phrase “the time for the Controller to initiate an audit” refers back to “the time” defined in the first sentence, namely two years. Similarly, the use of “initiate” in the second sentence refers to what the Controller is required to do within the two-year period. Read in this way, the two sentences are parallel. In the first sentence, when there is an appropriation, the time to initiate an audit is two years. In the second sentence, when there is no appropriation, the time to initiate an audit is also within two years of the first appropriation. The only difference between the two situations is the triggering event of an appropriation that determines when the two-year period to initiate an audit begins to run.

The Commission further finds this interpretation is consistent with the 2002 amendment to the first sentence of section 17558.5, which clarified that “subject to audit” means “subject to the initiation of an audit” 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 ~~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.⁶⁶

Therefore, in this case, the reimbursement claims filed for fiscal years 1999-2000 and 2000-2001 were subject to audit “no later than two years after the end of the calendar year in which the reimbursement claim is filed or last amended;” in this case, before December 31, 2003. Since the audit began no later than May 21, 2003, when the entrance conference was conducted, the audit was timely initiated.

The Controller also contends that the 2002 amendment to section 17558.5, which enlarged the period of time to initiate the audit to three years after the date the actual reimbursement claim is filed or last amended, applies in this case and gave the Controller additional time to initiate the audit in this case.⁶⁷ The Commission agrees. Pursuant to the *Douglas Aircraft* case, “[u]nless a

⁶⁵ *Fairbanks v. Superior Court* (2009) 46 Cal.4th 56, 62.

⁶⁶ Statutes 2002, chapter 1128.

⁶⁷ Statutes 2002, chapter 1128.

statute expressly provides to the contrary, any enlargement of a statute of limitations provision applies to matters pending but not already barred.”⁶⁸ The Court in *Douglas Aircraft* stated the general rule as follows:

The extension of the statutory period within which an action must be brought is generally held to be valid if made before the cause of action is barred. (*Weldon v. Rogers*, 151 Cal. 432.) The party claiming to be adversely affected is deemed to suffer no injury where he was under an obligation to pay before the period was lengthened. This is on the theory that the legislation affects only the remedy and not a right. (*Mudd v. McColgan*, 30 Cal.2d 463; *Davis & McMillan v. Industrial Acc. Com.*, 198 Cal. 631; 31 Cal.Jur.2d 434.) An enlargement of the limitation period by the Legislature has been held to be proper in cases where the period had not run against a corporation for additional franchise taxes (*Edison Calif. Stores, Inc. v. McColgan*, 30 Cal.2d 472), against an individual for personal income taxes (*Mudd v. McColgan, supra*, 30 Cal.2d 463), and against a judgment debtor (*Weldon v. Rogers, supra*, 151 Cal. 432). It has been held that unless the statute expressly provides to the contrary any such enlargement applies to matters pending but not already barred. (*Mudd v. McColgan, supra*, 30 Cal.2d 463.)⁶⁹

In *Mudd v. McColgan*, relied upon in *Douglas Aircraft*, the Court explained:

It is settled law of this state that an amendment which enlarges a period of limitation applies to pending matters where not otherwise expressly excepted. Such legislation affects the remedy and is applicable to matters not already barred, without retroactive effect. Because the operation is prospective rather than retrospective, there is no impairment of vested rights. [Citations.] Moreover, a party has *no vested right in the running of a statute of limitation prior to its expiration*. He is deemed to suffer no injury if, at the time of an amendment extending the period of limitation for recovery, he is under obligation to pay. In *Campbell v. Holt*, 115 U.S. 620, at page 628, it was said that statutes shortening the period or making it longer have always been held to be within the legislative power until the bar was complete.⁷⁰

And in *Liptak v. Diane Apartments, Inc.*, the Second District Court of Appeal, relying in part on *Mudd, supra*, reasoned:

A party does not have a vested right in the time for the commencement of an action. (*Mill and Lumber Co. v. Olmstead* (1890) 85 Cal. 80, 84-85.) Nor does he have a vested right in the running of the statute of limitations prior to its expiration. (*Mudd v. McColgan* (1947) 30 Cal.2d 463, 468; *Weldon v. Rogers* (1907) 151 Cal. 432, 434.) *A change in the statute of limitations merely effects a change in procedure and the Legislature may shorten the period, however, a reasonable time must be permitted for a party affected to avail himself of the remedy before the statute takes effect.* (*Rosefield Packing Co. v. Superior Court*

⁶⁸ *Douglas Aircraft Co. v. Cranston* (1962) 58 Cal.2d 462, at p. 465.

⁶⁹ *Id.*, at page 465.

⁷⁰ *Mudd v. McColgan* (1947) 30 Cal.2d 463, 468 [emphasis added].

(1935) 4 Cal.2d 120, 122; *Davis & McMillan v. Industrial Acc. Com.* (1926) 198 Cal. 631, 637; *Mill and Lumber Co. v. Olmstead, supra*, 85 Cal. at p. 84.)⁷¹

Therefore, an expansion of a statute of limitations applies to matters pending but not already barred, based in part on the theory that a party has no vested right in the running of a statutory period prior to its expiration.⁷² In this case, the 2002 amendment to section 17558.5 became effective on January 1, 2003, when the audit period for both reimbursement claims was still pending and not yet barred under the prior statute. The 2002 statute, which enlarged the time to initiate the audit to three years after the date the actual reimbursement claim is filed or last amended would control, and gives the Controller additional time to initiate the audit. The Controller therefore had until January 10, 2004, to initiate the audit of the 1999-2000 reimbursement claim, and had until December 20, 2004, to initiate the 2000-2001 reimbursement claim. Since the audit was initiated no later than May 21, 2003, when the entrance conference was held and before the 2004 deadline, the audit was timely initiated.

Moreover, section 17558.5 was amended in 2004 to establish, for the first time, the requirement to “complete” the audit two years after the audit is commenced. The 2004 amendment became effective *after* the completion of the audit of the reimbursement claims for fiscal years 1999-2000 and 2000-2001 and, thus, does not apply to the audit in this case.

Although the statute in effect at the time the reimbursement claims were filed did not expressly fix the time for which an audit must be completed, the Controller was still required under common law to complete the audit within a reasonable period of time. Under appropriate circumstances, the defense of laches may operate to bar a claim by a public agency if there is evidence of unreasonable delay by the agency and resulting prejudice to the claimant.⁷³ Claimant argues that it would be “impossible” to know when the statute of limitations would expire under the Controller’s interpretation.⁷⁴ However, the claimant was on notice of the audit when the entrance conference was conducted on May 21, 2003; the field audit was completed on November 21, 2003;⁷⁵ the draft audit report was issued on January 21, 2004; and the final audit report was issued March 10, 2004.⁷⁶ Moreover, there is no evidence that the claimant was prejudiced by the audit process. The audit was completed less than one year after it was started and, under the facts of this case, within a reasonable period of time.

⁷¹ (1980) 109 Cal.App.3d 762, 773.

⁷² *Mudd v. McColgan* (1947) 30 Cal.2d 463, 468

⁷³ *Cedar-Sinai Medical Center v. Shewry* (2006) 137 Cal.App.4th 964, 985-986. In that case, the court determined that the hospital failed to establish an unreasonable delay in audits conduct by Department of Health Services, since the Department conducted audits two years or less after the end of the fiscal period that it was auditing, which was less than the three-year period permitted by statute. See also, *Steen v. City of Los Angeles* (1948) 31 Cal.2d 542, 546, where the court held that laches applies in quasi-adjudicative proceedings.

⁷⁴ Exhibit A, IRC at pp.22-23.

⁷⁵ Exhibit A, IRC, Exhibit D, at. p. 52.

⁷⁶ See Exhibit A, IRC, Exhibit D, final audit report for the dates of the draft audit report.

Based on the foregoing, the Commission finds that the audit of claimant's reimbursement claims for fiscal years 1999-2000 and 2000-2001 was timely initiated and completed.

B. The Controller's Recalculation and Reduction of Claimed Indirect Costs is Correct as a Matter of Law and Not Arbitrary, Capricious, or Entirely Lacking in Evidentiary Support.

The Controller reduced indirect costs claimed by \$157,273 for fiscal years 2000-2001 and 2001-2002. Indirect cost rates of 47.3 percent for fiscal year 2000-2001 and 47.8 percent in fiscal year 2001-2002 were used by the claimant in those years. The Controller did not accept claimant's calculation of its indirect cost rate for these fiscal years as claimant failed to use one of the two options provided in the claiming instructions for calculating indirect costs; either the OMB Circular A-21 or the state's methodology in Form FAM-29C. The Controller recalculated indirect costs for these two fiscal years using the claimant's federally approved rate of 30percent, which was federally approved during the audit period and correctly used by the claimant in the fiscal year 1999-2000 reimbursement claim.⁷⁷

Claimant disputes the Controller's findings that the indirect cost rate proposal was incorrectly applied, charging that the Controller's conclusions were without basis in the law.

1. *The parameters and guidelines expressly require claimants to claim indirect costs in the manner described in the Controller's claiming instructions, which in turn provide for an indirect cost rate to be developed in accordance with federal OMB Circular A-21 guidelines or by using the state Form FAM-29C.*

Parameters and guidelines adopted by the Commission are required to provide instructions for eligible claimants to prepare reimbursement claims for the direct and indirect costs of a state-mandated program.⁷⁸ The reimbursement claims filed by the claimants are, likewise, required as a matter of law to be filed in accordance with the parameters and guidelines.⁷⁹ The parameters and guidelines for the *Health Fee Elimination* program provide that "*indirect costs may be claimed in the manner described by the State Controller in his claiming instructions.*"⁸⁰

Claimant argues that community college districts are not required to adhere to the claiming instructions.⁸¹ Claimant further 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.⁸²

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.*" The interpretation that is consistent with the plain language of the parameters and guidelines is that "indirect costs may be

⁷⁷ Exhibit B, Controller's comments on IRC, at pages 14 (Tab 2) and 166 (Finding 1, Final Audit Report).

⁷⁸ Government Code section 17557; California Code of Regulations, title 2, section 1183.7.

⁷⁹ Government Code sections 17561(d)(1); 17564(b); and 17571.

⁸⁰ Exhibit A, IRC, Exhibit C, at p. 40.

⁸¹ Exhibit A, IRC, at pp. 9-10.

⁸² Exhibit A, IRC, Exhibit C at p 10.

claimed,” or may not, but if a claimant chooses to claim indirect costs, the claimant must adhere to the Controller’s claiming instructions. This interpretation is urged by the Controller.⁸³

The claiming instructions specific to the *Health Fee Elimination* mandate, revised September 1997,⁸⁴ state that “college districts have the option of using a federally approved rate (i.e., utilizing the cost accounting principles from the Office of Management and Budget Circular A-21), or the State Controller’s methodology outlined in “Filing a Claim” of the Mandated Cost Manual for Schools.” In addition, the School Mandated Cost Manual, revised each year, and containing instructions applicable to all school and community college mandated programs,⁸⁵ provides as follows:

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.⁸⁶

The reference in the parameters and guidelines to the Controller’s claiming instructions necessarily includes the general provisions of the School Mandated Cost Manual (and later the Mandated Cost Manual for Community Colleges), and the manual provides ample notice to claimants as to how they may properly claim indirect costs. Claimant’s assertion that “[n]either State law or the parameters and guidelines made compliance with the SCO’s claiming

⁸³ Exhibit B, Controller’s Comments, Tab 1, at p 5.

⁸⁴ Exhibit B, Controller’s Comments on IRC, Tab 3 at p. 25-29 and Tab 4 at pp. 31-41.

⁸⁵ Exhibit B, Controller’s Comments, Tab 3 at pp. 25-29 and Tab 4 at pp. 31-41. School Mandated Cost Manual Excerpts for fiscal years 1999-2000 through 2001-2002.

⁸⁶ *Ibid.* 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 and federal approval of indirect cost rates 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. The Form FAM 29C calculates indirect cost rates using total expenditures reported on the California Community Colleges Annual Financial and Budget Report, Expenditures by Activity (CCFS-311), and “eliminates unallowable expenses and segregates the adjusted expenses between those incurred for direct and indirect activities relative to the mandated cost program.” (Exhibit B, Controller’s response to IRC, page 7.)

instructions a condition of reimbursement”⁸⁷ is therefore not correct.⁸⁸ The parameters and guidelines, which were duly adopted at a Commission hearing, require compliance with the claiming instructions.

Claimant also argues that because the claiming instructions “were never adopted as law, or regulations pursuant to the Administrative Procedure Act, the claiming instructions are merely a statement of the ministerial interests of the SCO and not law.”⁸⁹ In the *Clovis Unified* case, the Controller’s contemporaneous source document rule, or CSDR, was held to be an unenforceable underground regulation because it was applied generally against school districts and had never been adopted as a regulation under the APA.⁹⁰ Here, claimant implies the same fault in the claiming instructions with respect to indirect cost rates. But the distinction is that here the parameters and guidelines, which were duly adopted at a Commission hearing, require compliance with the claiming instructions. Claimant had notice of the requirement in the parameters and guidelines to comply with the claiming instructions and notice of the claiming instructions’ requirements for claiming indirect costs, both prior to and during the claim years in issue and did not challenge the parameters and guidelines or the claiming instructions when they were adopted.

Therefore, the Commission finds that the parameters and guidelines expressly require claimants to claim indirect costs in the manner described in the Controller’s claiming instructions, which in turn provide that an indirect cost rate may be developed in accordance with federal OMB guidelines or by using the state Form FAM-29C; and that claimant had notice of the parameters and guidelines and the claiming instructions, and did not challenge them when they were adopted.

2. *Claimant did not comply with the requirements of the claiming instructions in developing and applying its indirect cost rates for 2000-2001 and 2001-2002. Therefore, the Controller’s reduction is correct as a matter of law and the recalculation of the indirect cost rate using claimant’s federally approved rate was not act arbitrary, capricious, or entirely lacking in evidentiary support.*

In its audit of claimant’s reimbursement claim for fiscal year 2000-2001 and 2001-2002, the Controller found that claimant “claimed indirect costs based upon an indirect cost rate of 47.3 percent and 47.8 percent respectively. The Controller found that this rate was prepared by an outside consultant allegedly “simplifying” OMB Circular A-21 methodology.”⁹¹

The claiming instructions specify that, to use the OMB Circular A-21 option, a claimant must obtain federal approval, which claimant received and used for fiscal year 1999-2000.⁹²

⁸⁷ Exhibit A, IRC, at p. 13.

⁸⁸ Government Code section 17564(b) was amended by Statutes 2004, chapter 890, to require: “Claims for direct and indirect costs filed pursuant to Section 17561 shall be filed in the manner prescribed in the parameters and guidelines and claiming instructions.”

⁸⁹ Exhibit A, IRC, p. 12.

⁹⁰ *Clovis Unified School Dist.*, *supra*, 188 Cal.App.4th at page 807.

⁹¹ Exhibit A, IRC, Exhibit D, at p.6; Exhibit B, Tab 1, at p. 4.

⁹² The Controller did not adjust indirect costs for fiscal year 1999-2000.

However, for fiscal years 2000-2001 and 2001-2002, claimant did not use its federally approved rate, or use the other authorized methodology provided in Form FAM 29C. Thus, since the claimant did not comply with the requirements of the parameters and guidelines and claiming instructions in developing and applying its indirect cost rate to the costs claimed in fiscal years 2000-2001 and 2001-2002, the reduction is correct as a matter of law.

The Controller recalculated claimant's indirect cost rate by using the federally approved rate of 30 percent that claimant used for fiscal year 1999-2000. This resulted in reduced indirect costs for both fiscal years. As claimant failed to follow the parameters and guidelines and claiming instructions in using either its federally approved rate of 30 percent or a rate prepared using the Form FAM-29C, the Controller's action to recalculate the rate using one of the options provided for in the claiming instructions is not arbitrary, capricious, or entirely lacking in evidentiary support.

C. The Controller's Reduction for Understated Offsetting Revenues is Correct as a Matter of Law, and Not Arbitrary, Capricious, or Entirely Lacking in Evidentiary Support.

The Controller reduced costs for the three fiscal years by \$287,865 based on unsupported student attendance data used by the claimant to calculate the fees collected. This audit was one of the first performed on the *Health Fee Elimination* program and it occurred before the court's decision in *Clovis Unified School District v. Chiang*. Thus, in this case, the Controller did not consider the extent of the claimant's fee revenue *authorized* to be collected, but looked only at the revenue actually collected by the claimant.⁹³ The Controller found that the claimant failed to provide the student attendance data it used to determine offsetting revenues received and, thus, the Controller recalculated offsetting revenues received by using attendance data the claimant reported to the Chancellor's Office (the claimant's GLD144-02 printouts).⁹⁴ The Controller's recalculation resulted in a finding that the claimant underreported fee revenue received during the audit period.⁹⁵

Claimant disputes the reduction, asserting that the student enrollment data provided in the reimbursement claims was accurate and the Controller should not have recalculated using the data claimant provided to the Chancellor's Office. The Controller states that, during the audit process, claimant was unable to provide documentation to support the enrollment data provided

⁹³ *Clovis Unified School Dist. v. Chiang, supra*, 188 Cal.App.4th 794, 812, where the court 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 notes that the concept underlying the state mandates process that Government Code sections 17514 and 17556(d) embody is as follows: "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."

⁹⁴ This documentation is in Tab 5 of Exhibit B, Controller's comments on IRC, at pages 42-74.

⁹⁵ Exhibit B, Controller's comments on IRC, at pages 2 (letter from the Controller's Senior Staff Counsel) and 166 (Finding 2, Final Audit Report).

in the reimbursement claims.⁹⁶ Claimant does not address the issue of documentation in its IRC. The parameters and guidelines require claimants to report:

VIII. OFFSETTING SAVINGS AND OTHER REIMBURSEMENTS

Any offsetting savings the claimant experiences as a direct result of this statute must be deducted from the costs claimed. In addition, reimbursement for this mandate received from any source, e.g., federal state, etc. shall be identified and deducted from this claim. This shall include the amount of \$7.50 per full-time student per semester, \$5.00 per full-time student for summer school, or \$5.00 per full-time student per quarter, as authorized by Education Code section 72246(a). This shall also include payments (fees) received from individuals other than students who are not covered by Education Code Section 72246 for health services.⁹⁷

Section VII also requires claimants to provide supporting data for auditing purposes as follows: “all costs claimed must be traceable to source documents and/or worksheets that show evidence of the validity of such costs.”⁹⁸

Thus, the parameters and guidelines expressly require claimants to identify offsetting revenue from health service fees for each full-time student enrolled, and further require documentation to support the costs claimed. Full documentation of increased costs, which by definition would include documentation of any offsets, is required.⁹⁹ As claimant did not provide any documentation to support its enrollment data, as required by the parameters and guidelines, the Controller’s reduction is correct as a matter of law.

The Commission further finds that the Controller’s recalculation of student enrollment using data provided by claimant to the Chancellor’s Office was not arbitrary, capricious, or entirely lacking in evidentiary support. The documents are public records provided by claimant in the normal course of business, and claimant has provided no other documents to support enrollment data.

Accordingly, the Commission finds that the Controller’s reduction for understated offsetting revenues is correct as a matter of law, and not arbitrary, capricious, or entirely lacking in evidentiary support.

D. The Controller’s Adjustment Based on Payments Made to the Claimant is Supported by Evidence in the Record, and is not Arbitrary, Capricious, or Entirely Lacking in Evidentiary Support.

Claimant questions adjustments made by the Controller in the audit to the amounts owed to claimant. The Controller represents that claimant did not acknowledge two warrants received from the state, one for \$26,099 for fiscal year 1999-2000 and one for \$19,270 for fiscal year 2000-2001 in its reimbursement claims. Claimant contends that it cannot

⁹⁶ Exhibit A, IRC, Exhibit D, final audit, at p. 57.

⁹⁷ Exhibit X, Parameters and Guidelines at p. 7.

⁹⁸ Exhibit X, Parameters and Guidelines, at p. 7.

⁹⁹ See Government Code sections 17514, 17557 and 17561(d)(C)(i).

determine the propriety of these adjustments until the Controller states the reason for the change.¹⁰⁰

The Controller responds as follows:

As clearly stated in the audit report, and reconfirmed in the documentation in Tab 8, the District received two claim payments (\$57,365 issued on 8/1/2001 and \$26,099 issued on 3/9/2001) totaling \$83,464 for fiscal year 1999-2000, and one claim payment of \$19,270 issued on 3/8/2001 for fiscal year 2000-2001. The adjustments were made because of these reimbursement payments the District received.¹⁰¹

Tab 8 of the Controller's comments contains copies of the warrants showing payments made to claimant for the mandated program for \$83,464 and \$19,270.¹⁰² These payments are reflected as adjustments in the final audit report for fiscal years 1999-2000 and 2000-2001.¹⁰³

The Commission therefore finds that the Controller's adjustment to claimant's reimbursement claims based on prior payments by the state to claimant is supported by evidence in the record, and is not arbitrary, capricious, or entirely lacking in evidentiary support.

Conclusion

Pursuant to Government Code section 17551(d), the Commission concludes that the Controller's audit of the 1999-2000 and 2000-2001 reimbursement claims was timely, and that the reduction of the following costs is correct as a matter of law, and not arbitrary, capricious, or entirely lacking in evidentiary support:

- The reduction of indirect costs claimed for fiscal years 2000-2001 and 2001-2002 of \$157,273.
- The reduction of costs due to understated offsetting revenue of \$287,865.
- The adjustment to claimant's reimbursement claims based on prior payments made to the claimant for fiscal years 1999-2000.

Accordingly, the Commission denies this IRC.

¹⁰⁰ Exhibit A, IRC, pages 18-21.

¹⁰¹ Exhibit B, Controller's comments on IRC, page 3.

¹⁰² Exhibit B, Controller's comments on IRC, pages 102-103.

¹⁰³ Exhibit B, Controller's comments on IRC, page 164.

DECLARATION OF SERVICE BY EMAIL

I, the undersigned, declare as follows:

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

On January 9, 2015, I served the:

Draft Proposed Decision, Schedule for Comments, and Notice of Hearing

Health Fee Elimination, 06-4206-I-13

Education Code Section 76355

Statutes 1984, Chapter 1, 2nd E.S.; Statutes 1987, Chapter 1118

Fiscal Years 1999-2000, 2000-2001, and 2001-2002

Pasadena Area Community College District, Claimant

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

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct, and that this declaration was executed on January 9, 2015 at Sacramento, California.



Heidi J. Palchik
Commission on State Mandates
980 Ninth Street, Suite 300
Sacramento, CA 95814
(916) 323-3562

COMMISSION ON STATE MANDATES

Mailing List

Last Updated: 7/1/14

Claim Number: 06-4206-I-13

Matter: Health Fee Elimination

Claimant: Pasadena Area Community College District

TO ALL PARTIES, INTERESTED PARTIES, AND INTERESTED PERSONS:

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

Socorro Aquino, *State Controller's Office*

Division of Audits, 3301 C Street, Suite 700, Sacramento, CA 95816

Phone: (916) 322-7522

SAquino@sco.ca.gov

Marieta Delfin, *State Controller's Office*

Division of Accounting and Reporting, 3301 C Street, Suite 700, Sacramento, CA 95816

Phone: (916) 322-4320

mdelfin@sco.ca.gov

Donna Ferebee, *Department of Finance*

915 L Street, Suite 1280, Sacramento, CA 95814

Phone: (916) 445-3274

donna.ferebee@dof.ca.gov

Susan Geanacou, *Department of Finance*

915 L Street, Suite 1280, Sacramento, CA 95814

Phone: (916) 445-3274

susan.geanacou@dof.ca.gov

Ed Hanson, *Department of Finance*

Education Systems Unit, 915 L Street, 7th Floor, 915 L Street, 7th Floor, Sacramento, CA 95814

Phone: (916) 445-0328

ed.hanson@dof.ca.gov

Cheryl Ide, Associate Finance Budget Analyst, *Department of Finance*

Education Systems Unit, 915 L Street, Sacramento, CA 95814

Phone: (916) 445-0328
Cheryl.ide@dof.ca.gov

Jill Kanemasu, *State Controller's Office*

Division of Accounting and Reporting, 3301 C Street, Suite 700, Sacramento, CA 95816
Phone: (916) 322-9891
jkanemasu@sco.ca.gov

Jay Lal, *State Controller's Office (B-08)*

Division of Accounting & Reporting, 3301 C Street, Suite 700, Sacramento, CA 95816
Phone: (916) 324-0256
JLal@sco.ca.gov

Kathleen Lynch, *Department of Finance (A-15)*

915 L Street, Suite 1280, 17th Floor, Sacramento, CA 95814
Phone: (916) 445-3274
kathleen.lynch@dof.ca.gov

Yazmin Meza, *Department of Finance*

915 L Street, Sacramento, CA 95814
Phone: (916) 445-0328
Yazmin.meza@dof.ca.gov

Robert Miyashiro, *Education Mandated Cost Network*

1121 L Street, Suite 1060, Sacramento, CA 95814
Phone: (916) 446-7517
robertm@sscal.com

Jameel Naqvi, *Analyst, Legislative Analysts' Office*

Education Section, 925 L Street, Suite 1000, Sacramento, CA 95814
Phone: (916) 319-8331
Jameel.naqvi@lao.ca.gov

Andy Nichols, *Nichols Consulting*

1857 44th Street, Sacramento, CA 95819
Phone: (916) 455-3939
andy@nichols-consulting.com

Christian Osmena, *Department of Finance*

915 L Street, Sacramento, CA 95814
Phone: (916) 445-0328
christian.osmena@dof.ca.gov

Arthur Palkowitz, *Stutz Artiano Shinoff & Holtz*

2488 Historic Decatur Road, Suite 200, San Diego, CA 92106
Phone: (619) 232-3122
apalkowitz@sashlaw.com

Keith Petersen, *SixTen & Associates*

Claimant Representative

P.O. Box 340430, Sacramento, CA 95834-0430
Phone: (916) 419-7093
kbsixten@aol.com

Sandra Reynolds, *Reynolds Consulting Group, Inc.*

P.O. Box 894059, Temecula, CA 92589

Phone: (951) 303-3034

sandrareynolds_30@msn.com

Kathy Rios, *State Controller's Office*

Division of Accounting and Reporting, 3301 C Street, Suite 700, Sacramento, CA 95816

Phone: (916) 324-5919

krios@sco.ca.gov

Nicolas Schweizer, *Department of Finance*

Education Systems Unit, 915 L Street, 7th Floor, 915 L Street, 7th Floor, Sacramento, CA 95814

Phone: (916) 445-0328

nicolas.schweizer@dof.ca.gov

David Scribner, *Max8550*

2200 Sunrise Boulevard, Suite 240, Gold River, CA 95670

Phone: (916) 852-8970

dscribner@max8550.com

Jim Spano, Chief, Mandated Cost Audits Bureau, *State Controller's Office*

Division of Audits, 3301 C Street, Suite 700, Sacramento, CA 95816

Phone: (916) 323-5849

jspano@sco.ca.gov

Dennis Speciale, *State Controller's Office*

Division of Accounting and Reporting, 3301 C Street, Suite 700, Sacramento, CA 95816

Phone: (916) 324-0254

DSpeciale@sco.ca.gov