

December 13, 2017

Michael Cohen, Director
California Department of Finance
915 L Street
Sacramento, CA 95814

Dear Mr. Michael Cohen,

In accordance with the State Leadership Accountability Act (SLAA), the Commission on State Mandates submits this report on the review of our internal control and monitoring systems for the biennial period ending December 31, 2017.

Should you have any questions please contact Heidi Palchik, Assistant Executive Director, at (916) 323-3562, Heidi.Palchik@csm.ca.gov.

BACKGROUND

The Commission on State Mandates (Commission) is a quasi-judicial body whose statutory responsibilities are: To adjudicate test claims of local governments that allege the existence of reimbursable state-mandated programs and determine any costs required to be reimbursed; To hear and decide claims alleging that the State Controller's Office has incorrectly reduced payments to local governments for reimbursement claims; To hear and decide requests for mandate redetermination, alleging that the state's liability for a mandate has been modified based on a subsequent change in law; To determine the existence of significant financial distress for applicant counties seeking to reduce their General Assistance Aid payments.

The Commission is composed of seven members: The State Controller, State Treasurer, Director of the Department of Finance, Director of the Office of Planning and Research, a public member with experience in public finance, and two local elected officials.

Our Vision: The Commission on State Mandates timely renders sound quasi-judicial decisions, in compliance with article XIII B, section 6 of the California Constitution, resolving disputes regarding reimbursement for state-mandated local programs and relieving unnecessary congestion of the courts.

Our Mission: To fairly and impartially hear and determine matters filed by state and local government; resolve complex legal questions in a deliberative and timely manner; and produce clear, well-reasoned, and lawful decisions.

ONGOING MONITORING

As the head of Commission on State Mandates, Heather Halsey, Executive Director, is responsible for the overall establishment and maintenance of the internal control and monitoring systems.

EXECUTIVE MONITORING SPONSOR(S)

The executive monitoring sponsor responsibilities include facilitating and verifying that the Commission on State Mandates internal control monitoring practices are implemented and functioning as intended. The responsibilities as the executive monitoring sponsor(s) have been given to: Heather Halsey, Executive Director, and Heidi Palchik, Assistant Executive Director.

MONITORING ACTIVITIES

The Commission on State Mandates' (Commission's) management team, consisting of the executive director, assistant executive director, and chief legal counsel, meets weekly to discuss and identify agency risks. Once a risk is identified, management also collaborates with staff and Commission members to identify controls to mitigate the risk.

ADDRESSING VULNERABILITIES

Because there is a statutory duty to hear and decide test claims, adopt parameters and guidelines, and adopt a statewide cost estimate within 12-18 months of the filing of the test claim, these matters take priority over all other matters. The next priority for the Commission is resolution of amendments to parameters and guidelines and mandate redeterminations as these have a material effect on all eligible claimants for the program and for the state. Incorrect reduction claims have the lowest priority since they affect only one local agency and have no statutory deadline by which they must be heard. This creates a risk that incorrect reduction claims may not be timely heard and decided, due to the other matters with higher priority taking precedence. Hearing incorrect reduction claims with cross-cutting issues first is one way that the Commission has been helping spur informal resolution of these claims between the claimant and the State Controller's Office. To the extent that there are cross-cutting issues, staff analyzes and presents those claims together for hearing for purposes of efficiency and consistency. The 13 incorrect reduction claims are tentatively set for hearing through January 2019 and are expected to be completed by then, barring other mandate or litigation caseload that may take precedence over the incorrect reduction claim caseload. Commission management meets to identify deficiencies, sets reasonable timeframes to resolve deficiencies, and conducts thorough review to ensure proper and complete resolution.

COMMUNICATION

As the head of the Commission on State Mandates, Heather Halsey, Executive Director, has statutory authority over resource allocation and personnel, and delegated authority over policy matters, as prescribed in regulation. The Executive Director is appointed by and serves at the pleasure of the Commission on State Mandates and is responsible for the overall establishment and maintenance of the internal control system. Heid Palchik, Assistant Executive Director, under general direction of the Executive Director, has full management and supervisory responsibility for the administrative functions and day-to-day operations of the Commission and is the designated agency monitor. The Assistant Executive Director reports directly to the Executive Director. Commission staff continues to eliminate the currently pending backlog of 16 test claims and 13 incorrect reduction claims by adhering to several strategies discussed in the backlog reduction plan submitted to the Department of Finance on September 11, 2017. A copy of the updated plan is on the Commission's website. Specifically, Commission management meets weekly, conducts biweekly all-staff meetings, and continually communicates with staff and Commission members to discuss the possibility of risks and recognize unanticipated deficiencies. Commission management and staff utilize internal memos, email communications, policy and procedures, and a daily maillog to ensure the executive director is made aware of any deficiencies.

ONGOING MONITORING COMPLIANCE

The Commission on State Mandates has implemented and documented the ongoing monitoring processes as outlined in the monitoring requirements of California Government Code sections 13400-13407. These processes include reviews, evaluations, and improvements to the Commission on State Mandates systems of controls and monitoring.

RISK ASSESSMENT PROCESS

The following personnel were involved in the Commission on State Mandates risk assessment process: Executive Management, and Staff.

RISK IDENTIFICATION

The Commission currently has an incorrect reduction claim backlog of 13 claims. Incorrect reduction claims are filed with the Commission based on reductions of reimbursement claims taken by the State Controller's Office. Unlike test claims, where one claimant represents all potential claimants statewide, individual claimants file incorrect reduction claims with the Commission based on alleged incorrect reductions to reimbursement claims filed by that claimant only. Though the Commission may consolidate claims on the same program and similar issues for the purposes of analysis, oftentimes incorrect reduction claims do not lend themselves to consolidation because issues unique to each claim and each particular claimant's methods of implementing the program and claiming reimbursement must be addressed. The process for resolving incorrect reduction claims can be complex. Commission staff prepares a detailed analysis of the legal and auditing issues. Then the Commission approves, partially approves, or denies the claim, and adopts a decision. Whether or not the issues are resolved at an informal conference between the claimant and the State Controller's Office, staff must spend time to prepare and review the record (including the records for the decisions on the test claim and parameters and guidelines, and the claiming instructions), review detailed reimbursement claims and any other evidence submitted by the parties, and determine the legal and audit issues. This process can be lengthy.

The Commission's first statutory priority is to hear and decide test claims, adopt parameters and guidelines, and adopt a statewide cost estimate within 12-18 months of the filing of the test claim. Since a test claim backlog of 16 test claims exists, the incorrect reduction claim backlog takes a lower priority. Nonetheless, Commission staff have worked to reduce the incorrect reduction claim backlog from 41 claims in June 2015 to the current 13 claims. Executive management identifies this risk by continually monitoring pending caseload of matters pending before the Commission. The executive director reports pending matters that are tentatively scheduled for the next two hearings at each Commission meeting and prepares an annual report, by September 15 of each year, to the Department of Finance on the Commission's workload and backlog reduction plan. Executive management also acknowledges that, should the test claim backlog increase significantly, staff focus will shift away from the incorrect reduction claim and concentrate on the statutory requirement to timely complete test claims.

RISK RANKING

Since the Commission submitted its State Leadership Accountability Act Report in December 2015, the Commission has held 12 Commission hearings and heard and decided four test claim, 27 incorrect reduction claims, two reconsiderations of adopted decisions, one appeal of executive director decision, two parameters and guidelines, three parameters and guidelines amendments, and five statewide cost estimates. The Commission also had nine cases pending in the courts during 2016-17, many of which required significant staff time to brief and argue. Many of the claims completed in the 2015-2017 reporting period addressed complex issues regarding constitutional law, federal law, and issues of procedure and many of these issues were issues of first impression. Incorrect reduction claims have the lowest priority since they affect only one local agency and have no statutory deadline by which they must be heard. Nonetheless, the 13 pending incorrect reduction claims are tentatively set for hearing

through January 2019 and are expected to be completed by then, barring other mandate or litigation caseload that may take precedence over the incorrect reduction claim caseload.

Incorrect reduction claims are based on reductions made by the State Controller's Office to reimbursement claims filed by local government on reimbursable activities as defined in the parameters and guidelines adopted by the Commission. Generally, more mandates are imposed and test claims filed during times of economic prosperity and fewer during recessions. This is because budget concerns are less restrictive during times of prosperity and more legislation imposing new programs is passed and resources are freed up for local governments to file claims with the Commission.

The 2009 Bureau of State Audits shed light on the negative impacts to both the State and local governments of an incorrect reduction claim backlog. Since that time, the Commission has utilized various approaches to address the backlog, as spelled out in its backlog reduction plan. The likelihood of the current incorrect reduction claim backlog growing is possible although the trend over the last few years has been an increase in claims completed and a reduction in claims filed. This is due in part to addressing claims with cross-cutting issues first and then encouraging negotiation between parties and the State Controller's Office to informally resolve other claims with the same issues.

Many of the same factors that can contribute to a test claim backlog also contribute to the incorrect reduction claim backlog, including the number and complexity of the filings, and other competing workload, such as litigation. The Commission generally has a first-in-time policy to hear matters in the order in which they were filed, prioritizing those matters with a statutory deadline. However, exceptions to this policy have been made in certain circumstances. For example, Commission executive management has taken matters out of order for staff development purposes or assigned a less-complicated matter, like an incorrect reduction claim, to a staff person who has just completed a particularly difficult test claim, to prevent staff burnout. Nonetheless, the Commission remains committed to hearing all matters, including incorrect reduction claims within a reasonable time.

RISKS AND CONTROLS

RISK: OPERATIONS -EXTERNAL-ECONOMIC VOLATILITY

Part of the Commission's vision and mission is to *timely* render sound quasi-judicial decisions and to resolve complex legal questions in a deliberative and *timely* manner. Incorrect reduction claims have the lowest priority and are often scheduled to be heard after the hearing of other matters of higher priority. As a result, they run the risk of not being timely heard and decided.

Incorrect reduction claims have no statutory deadline by which they must be heard and decided by the Commission and therefore have the lowest priority for scheduling for hearing.

As a result, the scheduling of the incorrect reduction claims may be pushed to later dates if other items, such as test claims with higher priority, are heard and decided ahead of the incorrect reduction claim caseload.

CONTROL A

The Commission's management team, consisting of the executive director, the assistant executive director, and the chief legal counsel, meets weekly to discuss the incorrect reduction claim caseload. Commission management collaborates with Commission staff and members to identify controls, sets reasonable timeframes, and conducts thorough review to ensure proper and complete resolution. The

Commission makes every effort to hear all matters within a reasonable time.

Accordingly, the 13 incorrect reduction claims are tentatively set for hearing through January 2019 and are expected to be completed by then, barring other mandate or litigation caseload that may take precedence over the incorrect reduction claim caseload.

CONCLUSION

The Commission on State Mandates strives to reduce the risks inherent in our work and accepts the responsibility to continuously improve by addressing newly recognized risks and revising controls to prevent those risks from happening. I certify our internal control and monitoring systems are adequate to identify and address current and potential risks facing the organization.

Heather Halsey, Executive Director

CC: California Legislature [Senate (2), Assembly (1)]
California State Auditor
California State Library
California State Controller
Director of California Department of Finance
Secretary of California Government Operations Agency