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Soup to Nuts: An Analysis of Selected Recommendations of the California Performance Review

On Tuesday, August 3, the California Performance Review (CPR) presented its 2,500- plus page report to Governor Schwarzenegger. The report proposes more than 1,000 recommendations aimed at increasing the efficiency of government and restructuring state agencies and departments, as well as a variety of policy changes affecting a wide array of state programs.

The CPR's recommendations range from the specific, such as increasing the sale of surplus state property, to broad statements of vision, such as urging adoption of principles aimed at improving the relationship between the state and local governments. Overall, the report fails to prioritize its recommendations and fails to distinguish proposals that largely affect the structure of government from those that could be implemented independently.

The CPR recommends replacing the current organizational structure of state government, based on agency secretaries and departments, with 11 "mega-agencies," with assistant secretaries responsible for overseeing program and service delivery. A Governor's Office of Management and Budget would replace the current Department of Finance, Department of Personnel Administration, most of the Department of General Services, and a number of other offices and programs. The CPR also recommends shifting responsibility for determining eligibility for a number of health and human services programs from counties to the state and includes a sweeping realignment of responsibility for health and human services programs, including transfer of financial responsibility for indigent health care to the state.

Next Steps

A 21-member commission will hold five hearings, beginning later this month, to consider public comment on the recommendations. The first hearing, scheduled for August 13 on the campus of UC Riverside, will examine proposals in the areas of Infrastructure, Resource Conservation, and Environmental Protection. Commission members were not identified on the CPR's website (cpr.ca.gov).

Overview

Specifically, the CPR includes:

- A major centralization of responsibility for delivery of state services in 11 "mega-agencies" and a new Office of Management and Budget. While some aspects of this proposed reorganization may have merit, the report offers little evidence to support the premise that "bigger is always better."

- A number of relatively modest “good government” changes that could be implemented, after evaluation, with little controversy.
- Significant policy proposals that may or may not have merit. In many instances – such as the proposed realignment of health and human services programs between the state and county governments – the devil will be in the details of the implementation and funding strategies.
- Recycled budget reductions and policy proposals. These include eliminating the Homeowners and Renters Property Tax Assistance Program, weakening environmental regulations, and modifying the requirement that 75 percent of community college faculty should be full-time instructors.
- Repeated calls for privatization of public services. However, the report does not provide independent evidence that private contractors could provide services more efficiently or cost-effectively. In fact, the report notes in one instance that, “State entities can sometimes provide a lower cost for...services than private sector vendors.”
- Questionable claims of cost savings or added revenues, including claims of higher revenues from reinstating the Manufacturers’ Investment Tax Credit and reducing the share of lottery proceeds that go to education.

The recommendations of the CPR are too extensive to review in their entirety. This analysis examines examples of the range of recommendations contained in the report.

A Sweeping Reorganization of State Government

The report proposes eliminating departments and replacing them with “mega-agencies,” with divisions headed by assistant secretaries responsible for overseeing program and service delivery. Many boards and commissions would be eliminated. The proposed changes include:

- **Health and Human Services:** Creating a new Department of Health and Human Services.
- **K-12 and Higher Education:** Expanding the role of the appointed Secretary of Education, consolidate selected higher education entities into a new Higher Education Division (the University of California and the California State University would remain independent), and eliminate county boards of education and offices of education and create a regional K-12 governance structure instead.
- **Workforce and Economic Development:** Integrating the state’s workforce and economic development programs into a new Department of Labor and Economic Development.

- **Infrastructure:** Consolidating the infrastructure operations of more than two dozen state entities into a new Infrastructure Department with six divisions, including water, energy, transportation, and telecommunications.
- **Commerce and Consumer Protection:** Consolidating the state’s business licensing system and consumer protection activities into a new Department of Commerce and Consumer Protection.
- **Public Safety:** Reorganizing a number of entities that provide law enforcement, disaster relief, and victim compensation into a new Department of Public Safety and Homeland Security.
- **Environmental Protection and Natural Resources:** Creating a new Environmental Protection Department to focus on air and water quality and other issues, and a new Natural Resources Department to focus on parks, forestry and land management, and other issues.

Proposals to Increase the Efficiency and/or “User Friendliness” of State Government

Many of the report’s proposals are modest improvements that make sense and could be implemented without restructuring state government or making major policy changes. These recommendations should be considered apart from the major policy proposals that demand more thorough evaluation and debate. Some of the modest proposals include:

- Redesigning the state’s home page to make it easier for users to locate programs and services.
- Increasing the number of tax auditors and collection staff to boost state revenues.

Restructuring Health and Human Services

The CPR recommends creating six divisions within a new Department of Health and Human Services:

- **Health Purchasing:** Includes fraud prevention; Medi-Cal; Early Periodic Screening, Diagnosis, and Treatment (EPSDT); California Children’s Services; Child Health and Disability Prevention; Genetically Handicapped Persons Program; In-Home Supportive Services; Access for Infants and Mothers Program; Healthy Families; and the County Medical Services Program.
- **Public Health:** Includes all public health activities, in addition to functions currently under the Office of Statewide Health Planning. The functions of the Office of Environmental Health Hazards Assessment would be transferred from the California Environmental Protection Agency.
- **Quality Assurance:** Includes all health and human services licensing and oversight activities for businesses and consumers. The authority of the health professions licensing boards would be transferred from the Department of Consumer Affairs. In addition, the programs under the Department of Managed Care would be transferred to this new division.
- **Behavioral Health:** Includes programs under the Department of Mental Health and the Department of Alcohol and Drug Programs.
- **Services to the Disabled:** Includes programs under the Department of Developmental Services and the Department of Rehabilitation.
- **Social Services:** Includes CalWORKs; child support; Food Stamps; Women, Infants and Children Supplemental Nutrition Program (WIC); Supplemental Security Income/State Supplementary Payment (SSI/SSP); and community services.

- Exempting federally-funded programs from state hiring freezes and staffing reductions.
- Allowing applicants for Medi-Cal, CalWORKs, and Food Stamps to “self-certify” their assets. Currently, applicants must provide documentation of their assets. Allowing applicants to self-certify their assets would simplify the application process and reduce administrative costs. The proposal would not allow applicants who are aged, blind, or disabled to self-certify their assets.
- Improving recruitment of prospective adoptive parents of foster children through a media campaign, including the use of public service announcements.
- Passing federal bonus payments through to county adoption programs. The federal government provides bonus funding to states that increase adoptions. In the past, California has used the funds to supplant, rather than supplement, state funds for county adoption programs. This proposal would allow counties to keep any future federal bonus funds without reducing state support in order to expand adoption services.
- Reducing the cost of K-12 and higher education textbooks through measures such as negotiating with publishers, asking instructors to consider the cost of a textbook when selecting books, and using e-books, where appropriate.
- Creating single points of contact for certain governmental functions. Examples include a one-stop business licensing center and a single point of contact for the California Environmental Protection Agency. Currently, licensing and consumer protection responsibilities are split among numerous independent departments, bureaus, and commissions.
- Establishing parameters for redirecting special funds. The state periodically borrows from “special funds” – such as the Traffic Congestion Relief Fund or the Employment Development Department Contingent Fund – to help balance the General Fund. The CPR recommends creating uniform procedures to ensure that loans from special funds to the General Fund include specific repayment requirements and are made easy to understand in the annual budget.
- Improving management of the state vehicle fleet. The CPR reports that the state cannot identify the agencies responsible for over 25 percent of the state’s vehicle fleet and does not have an accurate inventory of state vehicles. Also, the state does not maintain records on reports of abuse of state vehicles. The CPR recommends reducing the cost of new vehicle purchases through an inventory of all state vehicles and procedures for tracking public complaints, motor vehicle violations, accident reports, fuel card misuse, and home storage permits.
- Reducing state video production costs. The CPR suggests that the state’s video production costs could be reduced by making better use of state agencies that have video production capabilities, rather than the current practice of contracting with private vendors.

Proposals That Deserve Consideration

The CPR also makes a number of significant policy proposals that appear to have merit, but which require evaluation and, potentially, modification before being implemented. These proposals deserve to be considered before the more problematic and controversial recommendations of the CPR. Examples include:

- Making it easier for students to transfer from community colleges to the University of California (UC) or the California State University (CSU) by developing lower division and major requirements that are recognized and accepted by all California public universities.
- Increasing college and university tuition for all non-resident students by 45 percent above 2003-04 rates. A 20 percent non-resident fee increase was included in the 2004-05 Budget. The CPR estimates an increase in revenues from the total fee hike of more than \$1 billion over five years.
- Providing fee waivers, rather than Cal Grant awards, for financially needy students at UC and CSU. Fee waivers are currently provided to financially needy students at the community colleges, for projected savings of \$32 million over five years.
- “Realigning” the funding and program responsibility for various health and human services programs. Specifically, the proposal would shift entire responsibility for the Medically Indigent Adult Program and the In-Home Supportive Services Program to the state. The proposal would also shift entire responsibility for Medi-Cal mental health services and Child Welfare Services to the counties. There may be some merit in realigning certain programs. However, key details, such as funding mechanisms and changes to service delivery, require careful evaluation.

Proposals That Require Careful Scrutiny

Most of the major policy proposals of the CPR demand considerable scrutiny. Many would significantly change the delivery of services and/or have a major impact on program beneficiaries. Examples include:

- Eliminating the 58 county boards of education, county offices of education, and county superintendents of education in favor of a regional governance structure for K-12. This proposal would consolidate the current 58 districts into 11 regions of similar size.
- Merging CalWORKs Stages 1 and 2 child care under county welfare departments. Currently, California administers a three-stage CalWORKs child care system. County welfare departments administer Stage 1 and the Department of Education administers Stages 2 and 3.
- Eliminating the requirement that the first \$50 of child support collected on behalf of CalWORKs families be passed through to the family. Instead, the state would retain the first \$50 currently directed to families, generating annual General Fund savings of \$29.5

million. This proposal would remove an incentive for non-custodial parents to pay child support and reduce financial support for low-income families.

- Changing the enrollment birth date for entering kindergarten from December 2 to September 1. The CPR argues that slightly older children perform more successfully both in kindergarten and in the future. However, a one-size-fits-all approach may not work for some children. In addition, increasing the age at which children can enter public kindergarten could raise the cost of child care for some working parents.
- Consolidating law enforcement into one agency. The CPR does not address the problem of parceling out pieces of an agency's mission. For example, park rangers have dual missions involving both law enforcement and non-law enforcement functions. Similarly, the CPR's recommendation fails to address the problem of melding together very different law enforcement functions.
- Transferring responsibility for 6,500 miles of state highway lanes to local government. This proposal would shift an estimated \$108 million in annual costs to local governments.

Recycled Budget Cuts and Policy Proposals

Other CPR proposals have been considered and rejected in prior budget and policy debates. Examples of recycled proposals include:

- Consolidating the Franchise Tax Board (FTB) and Board of Equalization (BOE) under the direction of the BOE. There may be merit in consolidating the functions of the two organizations, as well as the tax collector functions of the Employment Development Department. However, the proposal would dismantle the FTB, one of the state's most highly regarded departments, which is cited repeatedly in the CPR for innovative practices.
- Eliminating the Homeowners and Renters Property Tax Assistance Program, a program that provides tax relief to low-income seniors and people with disabilities, for savings of \$696.5 million over five years. At the same time, the CPR recommends new tax breaks for businesses.
- Reducing the reimbursement rates for child care providers who are exempt from state licensure from 90 percent to 50 percent of the regional market rate. The reimbursement rate would increase to 60 percent for providers who complete health and safety training. The Governor proposed to reduce the 2004-05 reimbursement rates to 40 percent of the regional market rate for license-exempt providers and to increase the rate to 50 percent if providers completed health and safety training. These proposals were rejected by the Legislature.
- Weakening California's environmental regulations, including: eliminating regulations that currently restrict unlimited oil refining; weakening California's pesticide regulation laws, which are stronger than federal law; and eliminating the permitting functions of the San Francisco Bay Conservation and Development Commission in areas such as sand mining, maintenance dredging, and routine repairs on docks.

- Transferring responsibility for assessing commercial aircraft for property tax purposes from county assessors to the Board of Equalization. This change was proposed in SB 593 (Ackerman), sponsored by the airline industry, and held in the Senate Appropriations Committee earlier this year. If enacted, this proposal would likely reduce local government property tax revenues and increase the state's costs for education.
- Modifying the requirement that 75 percent of community college faculty be full-time instructors. The CPR argues that this state requirement interferes with the colleges' ability to recruit appropriate instructors for technical courses. However, community colleges are currently allowed to fill 25 percent of their faculty positions with part-timers, who are generally paid less than full-timers and often lack employee benefits.
- Allowing name-based HIV reporting. California currently uses a code-based system for reporting HIV cases and a name-based system for reporting AIDS cases to encourage individuals to come forward for testing and treatment.

Proposals for the Privatization of State Services

The CPR report includes a number of proposals to permit the "contracting out" of state services and administrative activities, without providing evidence that private contractors would improve the efficiency or effectiveness of service delivery. These proposals include:

- Allowing public elementary and secondary schools to contract with independent, non-state vendors for transportation, construction, maintenance, and food services. SB 1419 (Alarcon), passed in 2003, restricted school districts' ability to contract out for non-academic services. The CPR recommends repealing these restrictions.
- Consolidating and contracting out the eligibility functions of the Medi-Cal, CalWORKs, and Food Stamps programs, for annual General Fund savings of \$453.1 million and a reduction of 16,921 county workers who currently perform the eligibility functions for these programs. The state would have to seek federal waivers to allow non-public employees to conduct the eligibility function in the Medi-Cal and Food Stamps Programs. The proposal provides no evidence that contracting out eligibility functions would generate the level of assumed savings.
The proposal compares the eligibility costs in the three programs to lower costs in the Healthy Families Program, which contracts out the eligibility function. However, this comparison is misleading because the Medi-Cal, CalWORKs, and Food Stamps programs have more complex eligibility rules than the Healthy Families Program. Medi-Cal, for instance, includes more than 100 eligibility categories. The proposal could also affect service delivery. In CalWORKs, for example, county welfare departments also provide case management and employment services for participants. Separating the eligibility function could affect how counties deliver CalWORKs services.
- Contracting out child support services at the local level, for annual General Fund savings of \$12.2 million. By 2002, all local child support programs were transferred from local district attorneys' offices to new county child support departments in order to improve child support collections and service delivery. The CPR would make significant changes to a new

system, even though child support collections have improved and new county offices have already been established.

- Requiring state departments to use “pay station” contractors to process certain transactions, including vehicle registration payments, at retail sites located primarily in low-income neighborhoods. Pay station sites could be selected through “demographic analysis revealing low-income, cash-based neighborhoods where residents are unlikely to have bank accounts or credit cards.” Customers would be charged a transaction fee to fund this service. In contrast, the CPR recommends waiving the \$4 credit card transaction fee for online payment of vehicle registration fees.
- Allowing state departments to choose their own real estate service providers. This proposal would remove real estate services, such as leasing and facility management, from the Department of General Services. These functions would be delegated to state departments, which would be allowed to contract with private sector firms that provide these services, such as “qualified brokerage and space planning firms.” Delegating real estate service functions could create a more complex system and would require additional state oversight to ensure compliance with statewide policies. In addition, this proposal appears to conflict with the CPR’s recommendation to centralize management of the state’s real property assets in a new public corporation.
- Developing guidelines to help state departments determine when and how to employ “competitive sourcing,” including paying private firms to provide public services and allowing private firms to finance and operate public infrastructure, such as airports and roads.

Proposals That Contradict Prior Administration Policy

Some CPR proposals appear to contradict prior policy initiatives by the Schwarzenegger Administration. These proposals include:

- Requiring multi-county special districts to shift more of their property tax revenues to schools in order to reduce state costs for education. This proposal is inconsistent with the 2004-05 budget agreement between the Governor and local governments and would be prohibited by Proposition 1A, the constitutional amendment placed on the November 2004 ballot by the Legislature as part of the budget agreement.
- Requiring tribes entering into new gaming compacts with the state to negotiate judicially enforceable agreements with affected local governments to mitigate the impact of casinos on local communities. The Governor’s recent agreements with several tribes appear to contain no such requirement.
- Adopting principles to improve the partnership between state and local governments. The report offers seven principles for California governments: act as partners, communicate effectively, have predictable funding, be performance-based and accountable, have clear roles and responsibilities, be streamlined, and be flexible and innovative. The local government agreement contained in the 2004-05 budget agreement would limit the state's

ability to reform fiscal policies, make it more difficult to address future budget crises, and contribute to the state's structural deficit in 2006-07.

Questionable Revenue and Savings Assumptions

The CPR report claims state savings of \$32.2 billion over a five-year period from implementing the report's recommendations. However, evidence suggests that this estimate is substantially overstated. Moreover, not all of the estimated savings would accrue to the state budget.

Examples include:

- Assuming that the state will gain \$343.2 million from reinstating the Manufacturers' Investment Tax Credit (MIC). In fact, the MIC cost the state \$333.5 million in 2001. The MIC was allowed to sunset in 2003 for failure to achieve the performance target established at the time the credit was enacted.
- Assuming that schools will gain about \$1 billion from reducing the share of lottery proceeds allocated to education and increasing the amount allocated to prizes. The initiative authorizing the California State Lottery allocated a minimum of 34 percent of lottery proceeds to support public education. The CPR recommends reducing this share to boost lottery ticket sales. Whether the shift of lottery proceeds from schools to prizes will increase ticket sales is unknown. This change would, however, reduce the share of each lottery dollar that goes to education. A similar proposal, AB 2938 (Plescia), has not passed out of its first policy committee in the Legislature this year.
- Identifying \$317.1 million in five-year savings from increasing the State Compensation Insurance Fund's (SCIF) recoveries from other insurers. Increased recoveries would benefit employers that purchase workers' compensation coverage from the SCIF. While this recommendation may be worthy, cost savings would go to employers that purchase coverage from the SCIF, not the state budget.

Proposals That Have Already Been Implemented and/or Savings That Have Already Been Scored

The CPR report also contains proposals that have already been implemented, with savings or revenues already included in state budget estimates. For example, the CPR proposes:

- Increasing revenues by \$399.1 million by implementing a tax amnesty program. The 2004-05 Budget assumes \$333 million in additional revenues attributable to amnesty programs for personal income, corporate, and sales taxes.
- Using a portion of the Student Loan Operating Fund surplus to fund Cal Grant awards. The 2004-05 Budget uses \$146.5 million from the surplus to offset General Fund costs for the Cal Grant program. Thus, these funds are no longer available for transfer.
- Identifying permanent sources of revenue for local governments that are not subject to redirection to the state. The CPR recommends that the Governor and Legislature eliminate the uncertainty faced by local governments as a result of the allocation of local revenues.

The 2004-05 budget agreement places a constitutional amendment on the November 2004 ballot that prevents the state from reallocating certain local revenues and requires the state to reimburse counties and cities for revenues lost as a result of the 1998 Vehicle License Fee reduction.

Conclusion

The CPR's recommendations are too varied and broad to warrant action as a whole. Prior to seeking legislative review, the Administration should:

- Identify recommendations that would generate little, if any, controversy. These should be reviewed by the public and the Legislature and implemented as warranted.
- Separate major proposals that are primarily structural (e.g., reorganizing agencies and departments) from those that are primarily policy-related (e.g., reinstating the Manufacturers' Investment Tax Credit or changing the kindergarten start date) and submit proposals as individual bills for legislative consideration.
- Expand the number of public hearings on the CPR's recommendations and hold individual hearings on major policy proposals, allowing sufficient time for public review to promote informed debate.

The California Budget Project (CBP) was founded in 1994 to provide Californians with a source of timely, objective, and accessible expertise on state fiscal and economic policy issues. The CBP engages in independent fiscal and policy analysis and public education with the goal of improving public policies affecting the economic and social well-being of low- and middle-income Californians. Support for the CBP comes from foundation grants, publications, and individual contributions.
