



March 30, 2012

Mr. Daniel R. Levinson, Inspector General Department of Health and Human Services Room 5541, Cohen Building 330 Independence Avenue, S.W. Washington, D.C. 20201

Dear Mr. Levinson:

As the Governor's fiscal representative, I submit to you the State of California Single Audit Report for the fiscal year ended June 30, 2011. The report contains the Independent Auditor's Reports on the state's general-purpose financial statements, compliance and internal control over financial reporting, compliance and internal control related to federal grants, and schedule of federal assistance. Although the Independent Auditor identified four significant deficiencies related to internal control over financial reporting and two instances of noncompliance or other matters, the conditions do not adversely affect the state's general-purpose financial statements. The Independent Auditor also identified significant deficiencies related to internal control over compliance with major federal program requirements and identified several instances of noncompliance that were considered material. We recognize that there are areas where internal controls and administration of federal awards need to be improved, and we are taking steps to address these issues.

California provides its citizens with numerous state and federal programs. The mix of programs provided makes us larger and more complex than most economic entities in the world. Such complexity, along with ever-present budget constraints, challenges us to meet the requirements of those programs and activities efficiently and effectively. Moreover, such operations must exist within a system of internal and administrative control that safeguards assets and resources, and produces reliable financial information. Attaining these objectives and overseeing the financial and business practices of the state continues to be an important part of the Department of Finance's (Finance) leadership.

In meeting our responsibility for financial leadership and oversight, Finance provides internal audit related education and training to departments as well as oversight of departmental internal audit units by issuing audit guidelines and conducting quality assurance reviews. Further, we have an ongoing process of issuing audit directives to departments that establish statewide policy and provide technical advice on various audit-related areas.

Mr. Daniel R. Levinson March 30, 2012 Page 2

The state is committed to sound and effective fiscal oversight. The head of each state department is responsible for establishing and maintaining a system of internal accounting and administrative control within their department. This responsibility includes documenting the system, communicating system requirements to employees, and assuring that the system is functioning as prescribed, and is modified for changing conditions. Moreover, all levels of state management must be involved in assessing and strengthening their systems of internal accounting and administrative controls to minimize fraud, errors, abuse, and waste of government funds. State agencies follow the Financial Integrity and State Manager's Accountability Act (FISMA), which requires each agency to conduct an internal review of its controls and prepare a report of its findings. Finance provides education and guidance to assist agencies in meeting the FISMA requirements.

Each state department with reportable internal control weaknesses or instances of noncompliance is responsible for developing and implementing corrective action plans. We will monitor the findings and reported corrective actions to identify potential changes in statewide fiscal procedures.

Finance is committed to ensuring the proper financial operations and business practices of the state, and that internal controls exist for the safeguarding and effective use of assets and resources.

If you have any questions concerning this letter, please contact David Botelho, Chief, Office of State Audits and Evaluations, at (916) 322-2985.

Sincerely,

ANA J. MATOSANTOS

And Waster

Director

Enclosure

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Auditee's Section

OVERVIEW OF CALIFORNIA'S ECONOMY

FISCAL YEAR 2010-11

alifornia, like the nation, ended 2011 in the midst of an uneven economic recovery. Some sectors of the economy, including high technology and export markets, were doing well. However, economic conditions were still hamstrung by weak real estate markets, recessionary consumer confidence levels, and volatile equity markets.

Global and national events created economic uncertainty and had an impact on the recovery. Congressional gridlock on budgetary issues, including the debt ceiling, added to economic uncertainty and stock market volatility. Further, the European debt, banking, and budgetary crisis adversely affected the California and national economies.

By the end of 2011, it appeared that the national economy had begun a slow, steady expansion, including a recovery from midyear weakness. In October 2011, the Index of Leading Indicators posted the largest monthly increase since November 2010, suggesting that the economy should continue to experience at least moderate growth well into 2012. After slowing sharply during May and June, nonfarm employment gains rebounded to over 100,000 jobs per month on average during the last half of the year. The unemployment rate dropped from 9.1 percent in June to 8.5 percent in December.

Consumer confidence also improved steadily. The Conference Board Consumer Confidence Index rose in November, posting its largest monthly increase since April 2003. Even though indicators remain at recessionary levels, the improved confidence level led to increased spending. Overall consumer spending in December 2011 was up 3.9 percent from a year earlier led by a surge in motor vehicle sales, which in November and December reached their best level since June 2008 (excluding the August 2009 one-time Cash-for-Clunkers surge).

Single Audit Report 2010-2011

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OVERVIEW OF CALIFORNIA'S ECONOMY

Businesses remained cautious but boosted spending on equipment and software. Corporations with healthy profits invested in replacement needs neglected during the recession.

After losing ground in August and September, industrial production accelerated in October and continued to grow modestly. Construction spending also grew moderately during the last five months of 2011.

In September, U.S. exports were up 16 percent over the year, led by industrial supplies and consumer goods. Even though exports softened in the final months of 2011 in response to the economic slowdown in Europe, they were still substantially greater than during the same months of 2010. During 2011, exports added 0.87 percentage point to Gross Domestic Product growth; trailing only the growth rates for personal consumption expenditures.

Despite these indications that the economy was improving at the close of 2011, a number of factors will dampen economic growth in 2012. Since spending growth outpaced income gains, the boost from consumers may slow again. Much of the additional spending was financed by the greater use of credit and reduced savings. Businesses also have been reluctant to expand payrolls too quickly and national economic growth has been extraordinarily dependent on exports, and thus more sensitive to global economic developments. The European debt, banking and budgetary crisis resulted in slower economic growth and possibly a recession in Europe, thereby weakening the demand for U.S. exports, reducing corporate earnings, and strengthening the dollar.

Most of the indicators that affect the nation, both positive and negative, also affect California. In addition, California is affected by other positive and negative factors ranging from a robust high-technology sector to being one of the states hardest hit by the collapse of the housing market.

The state added 46,100 industry jobs in January and February of 2011, and then lost 63,700 jobs from March through July after the Japanese earthquake. Nonfarm employment accelerated substantially from August through December and the unemployment rate dropped to 11.2 percent in December, the lowest rate since May 2009. Comparing December 2011 with a year earlier, 167,900 new jobs were created.

California wages also made substantial gains at the end of 2010 that continued into 2011. In the fourth quarter of 2010, California wages made their strongest quarter-to-quarter jump since the middle of 2000—the height of the dot-com bubble. Seven high-paying industries accounted for two-thirds of the overall wage gains in the fourth quarter of 2010, including computer and electronic manufacturing, finance and insurance, professional, scientific and

technical services, mining, information (which includes motion pictures), management of companies, and health care and social assistance. In 2011, California personal income grew nearly \$100 billion, the largest gain since 2006.

A disproportionately large share of the wage gain was driven by the state's high-technology and professional service sectors and by robust global demand for California exports. The surge reflected growing high-tech exports, booming Silicon Valley investment activity, strong stock market gains, and high oil prices. If these trends continue, it is expected that these sectors will expand their workforces.

Strong growth and rising profits among Silicon Valley companies and by booming investment activity likely led to wage gains in electronics manufacturing. In 2010, the 150 largest Silicon Valley corporations had their most profitable year in history. By the end of the first quarter of 2011, their combined stock market value rose over 11 percent from 2010.

2010 was a banner year for California-made exports with the total value rising 19 percent from 2009. This boom was dominated by computers, electronics, and electronic machinery, which combined accounted for over 60 percent of California's 2010 export growth.

Similar to the nation, consumption spending in California rebounded in 2011 with growing vehicle sales playing a significant role. Taxable retail sales during 2011 grew 8.1 percent from 2010. New motor vehicle registrations during the first eleven months of 2011 were up nearly 10 percent from the same months of 2010.

California industries that are not connected to high technology and export markets, however, did not fare as well. In particular, the state's housing market, still burdened by high foreclosure rates, weakened considerably during the midyear slowdown. Existing home sales during 2011 were up slightly from the same months of 2010. However, this came at the expense of falling prices.

In contrast to the healthy wage gains noted above, wage rate growth in other industries, such as agriculture, construction, retail trade, and accommodation and food services, did not even keep pace with inflation. These sectors employ nearly half of the state's private sector workforce.

The prospects for the national and California economies are guardedly positive. Another recession is not anticipated. The national recovery regained momentum in the closing months of 2011. While disappointing, labor markets have improved slowly. Exports are making solid improvements over 2010. Manufacturing activity was growing, albeit sluggishly.

SINGLE AUDIT REPORT 2010-2011

Part One

State of California Financial Report for the Year Ended June 30, 2011

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Independent Auditor's Report

THE GOVERNOR AND THE LEGISLATURE OF THE STATE OF CALIFORNIA

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of California, as of and for the year ended June 30, 2011, which collectively comprise the State of California's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the State of California's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the following significant amounts in the financial statements:

Government-wide Financial Statements

- Certain enterprise funds that, in the aggregate, represent 86 percent and 36 percent, respectively, of the assets and revenues of the business-type activities.
- The University of California, State Compensation Insurance Fund, California Housing Finance Agency, Public Employees' Benefits, and certain other funds that, in the aggregate, represent over 99 percent of the assets and revenues of the discretely presented component units.

Fund Financial Statements

- The following major enterprise funds: Electric Power fund, Water Resources fund, Public Building Construction fund, State Lottery fund, and California State University fund.
- Certain nonmajor enterprise funds that represent 92 percent and 66 percent, respectively, of the assets and revenues of the nonmajor enterprise funds.
- The funds of the Public Employees' Retirement System and the State Teachers' Retirement System, and certain other funds that, in the aggregate, represent 90 percent and 76 percent, respectively, of the assets and additions of the fiduciary funds and similar component units.
- The discretely presented component units noted above.

Those financial statements were audited by other auditors whose reports have been furnished to us, and our opinions, insofar as they relate to the amounts included for those funds and entities, is based on the reports of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence

supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of California, as of June 30, 2011, and the respective changes in financial position, and where applicable, cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we will issue a separate report on our consideration of the State's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis, schedule of funding progress, infrastructure information, budgetary comparison information, reconciliation of budgetary and GAAP-basis fund balances, and related notes are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We and the other auditors have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the State of California's basic financial statements. The combining financial statements and schedules listed in the accompanying table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements. The combining statements and schedules have been subjected to the auditing procedures applied by us and the other auditors in the audit of the basic financial statements and, in our opinion, based on our audit and the reports of other auditors, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory and statistical sections of this report have not been subjected to the auditing procedures applied by us and the other auditors in the audit of the basic financial statements, and accordingly, we express no opinion on them.

CALIFORNIA STATE AUDITOR

John F. Collins I

JOHN F. COLLINS II, CPA

Deputy State Auditor

February 24, 2012

Management's Discussion and Analysis

The following Management's Discussion and Analysis is a required supplement to the State of California's financial statements. It describes and analyzes the financial position of the State, providing an overview of the State's activities for the year ended June 30, 2011. We encourage readers to consider the information we present here in conjunction with the information presented in the Controller's letter of transmittal at the front of this report and in the State's financial statements and notes, which follow this section.

Financial Highlights - Primary Government

Government-wide Highlights

During the 2010-11 fiscal year, California showed signs of fiscal recovery, but it continued to struggle financially as a result of the recent recession. The State's general revenues increased by \$10.1 billion (10.7%) from last year; however, revenues were \$5.1 billion lower than those received in the 2007-08 fiscal year. Expenses for the State's governmental activities increased slightly from the prior year, but exceeded revenue received resulting in a \$3.5 billion decrease in governmental activities' net assets. Total expenses for the State's business-type activities exceeded revenues for fiscal year 2010-11. In fiscal year 2010-11, the California State University financial activities were reclassified from governmental activities to enterprise activities. Reduced general revenues, expenses that exceeded revenues, and increased long-term obligations resulted in a 50% decrease in the total net assets for governmental and business-type activities from the 2009-10 fiscal year.

Net Assets — The primary government's net assets as of June 30, 2011, were a negative \$9.7 billion. After the total net assets are reduced by \$86.8 billion for investment in capital assets (net of related debt) and by \$31.5 billion for restricted net assets, the resulting unrestricted net assets totaled a negative \$128.0 billion. Restricted net assets are dedicated for specified uses and are not available to fund current activities. Almost one-half of the negative \$128.0 billion consists of \$62.6 billion in outstanding bonded debt issued to build capital assets for school districts and other local governmental entities. The bonded debt reduces the unrestricted net assets; however, local governments, not the State, record the capital assets that would offset this reduction.

Changes in Net Assets — The primary government's total net assets decreased by \$3.2 billion (50.0%) during the year ended June 30, 2011. Net assets of governmental activities decreased by \$3.5 billion (51.3%), while net assets of business-type activities increased by \$330 million (69.3%).

Fund Highlights

Governmental Funds — GASB Statement No. 54 provides new fund balance classifications for governmental funds. The previous reserved and unreserved classifications have been replaced with nonspendable, restricted, and unrestricted balances. Additional information on the State's fund balances can be found in Note 1K in the notes to the basic financial statements. As of June 30, 2011, the primary government's governmental funds reported a combined ending fund balance of \$10.8 billion, a decrease of \$1.0 billion from the prior fiscal year's restated ending fund balance. The unrestricted fund balance, comprised of committed, assigned, and unassigned balances, was negative \$17.3 billion. The nonspendable and restricted fund balances were \$187 million and \$27.9 billion, respectively.

Proprietary Funds — As of June 30, 2011, the primary government's proprietary funds reported combined ending net assets of \$1.4 billion, an increase of \$375 million from the prior fiscal year. After the total net assets are reduced by \$1.5 billion for investment in capital assets (net of related debt), expendable restrictions of \$3.6 billion, and nonexpendable restrictions of \$22 million, the unrestricted net assets totaled a negative \$3.8 billion.

Noncurrent Assets and Liabilities

As of June 30, 2011, the primary government's noncurrent assets totaled \$134.8 billion, of which \$109.0 billion is related to capital assets. State highway infrastructure assets of \$61.4 billion represent the largest portion of the State's capital assets.

The primary government's noncurrent liabilities totaled \$158.1 billion, which consists of \$78.3 billion in general obligation bonds, \$29.4 billion in revenue bonds, and \$50.3 billion in all other noncurrent liabilities. During the 2010-11 fiscal year, the primary government's noncurrent liabilities increased by \$8.7 billion (5.8%) over the prior fiscal year. This increase was primarily the result of a \$3.8 billion increase in the unemployment programs' loan payable to the U.S. Department of Labor, and a \$2.6 billion increase in net other postemployment benefits obligations.

Overview of the Financial Statements

This discussion and analysis is an introduction to the section presenting the State's basic financial statements, which includes four components: (1) government-wide financial statements, (2) fund financial statements, (3) discretely presented component units financial statements, and (4) notes to the financial statements. This report also contains required supplementary information and combining financial statements and schedules.

Government-wide Financial Statements

Government-wide financial statements are designed to provide readers with a broad overview of the State's finances. The government-wide financial statements do not include fiduciary programs and activities of the primary government and component units because fiduciary resources are not available to support state programs.

To help readers assess the State's economic condition at the end of the fiscal year, the statements provide both short-term and long-term information about the State's financial position. These statements are prepared using the economic resources measurement focus and the accrual basis of accounting, similar to methods used by most businesses. These statements take into account all revenues and expenses connected with the fiscal year, regardless of when the State received or paid the cash. The government-wide financial statements include two statements: the Statement of Net Assets and the Statement of Activities.

- The Statement of Net Assets presents all of the State's assets and liabilities and reports the difference between the two as net assets. Over time, increases or decreases in net assets indicate whether the financial position of the State is improving or deteriorating.
- The Statement of Activities presents information showing how the State's net assets changed during the
 most recent fiscal year. The State reports changes in net assets as soon as the event giving rise to the
 change occurs, regardless of the timing of the related cash flows. Thus, this statement reports revenues
 and expenses for some items that will result in cash flows in future fiscal periods (e.g., uncollected taxes

and earned but unused vacation leave). This statement also presents a comparison between direct expenses and program revenues for each function of the State.

The government-wide financial statements separate into different columns the three types of state programs and activities: governmental activities, business-type activities, and component units.

- Governmental activities are mostly supported by taxes, such as personal income and sales and use taxes, and intergovernmental revenues, primarily federal grants. Most services and expenses normally associated with state government fall into this activity category, including health and human services, education (public kindergarten through 12th grade [K-12] schools and institutions of higher education), business and transportation, correctional programs, general government, resources, state and consumer services, and interest on long-term debt.
- Business-type activities typically recover all or a significant portion of their costs through user fees and
 charges to external users of goods and services. The business-type activities of the State of California
 include providing unemployment insurance programs, providing housing loans to California veterans,
 providing water to local water districts, providing building aid to school districts, providing services to
 California State University students, leasing public assets, selling California State Lottery tickets, and
 selling electric power. These activities are carried out with minimal financial assistance from the
 governmental activities or general revenues of the State.
- Component units are organizations that are legally separate from the State, but are at the same time
 related to the State financially (i.e., the State is financially accountable for them) or the nature of their
 relationship with the State is so significant that their exclusion would cause the State's financial statements
 to be misleading or incomplete. The State's financial statements include the information for blended,
 fiduciary, and discretely presented component units.
 - Blended component units, although legally separate entities, are in substance a part of the primary government's operations. Therefore, for reporting purposes, the State integrates data from blended component units into the appropriate funds. The Golden State Tobacco Securitization Corporation and certain building authorities that are blended component units of the State are included in the governmental activities.
 - Fiduciary component units are legally separate from the primary government but, due to their fiduciary nature, are included with the primary government's fiduciary funds. The Public Employees' Retirement System and the State Teachers' Retirement System are fiduciary component units that are included with the State's pension and other employee benefit trust funds, which are not included in the government-wide financial statements.
 - Discretely presented component units are legally separate from the primary government and provide services to entities and individuals outside the primary government. The activities of discretely presented component units are presented in a single column in the government-wide financial statements.

Information on how to obtain financial statements of the individual component units is available from the State Controller's Office, Division of Accounting and Reporting, P.O. Box 942850, Sacramento, California 94250-5872.

Fund Financial Statements

Fund financial statements are provided for governmental funds, proprietary funds, fiduciary funds and similar component units, and discretely presented component units. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The State of California, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal and contractual requirements. Following are general descriptions of the three types of funds.

• Governmental funds are used to account for essentially the same functions that are reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on short-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's short-term financing requirements. This approach is known as the flow of current financial resources measurement focus and the modified accrual basis of accounting. These governmental fund statements provide a detailed short-term view of the State's finances, enabling readers to determine whether adequate financial resources exist to meet the State's current needs.

Because governmental fund financial statements provide a narrower focus than do government-wide financial statements, it is useful to compare governmental fund statements to the governmental activities information presented in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's short-term financing decisions. Reconciliations located on the pages immediately following the fund statements show the differences between the government-wide statements and the governmental fund Balance Sheet and the governmental fund Statement of Revenues, Expenditures, and Changes in Fund Balances. Primary differences between the government-wide and fund statements relate to noncurrent assets, such as land and buildings, and noncurrent liabilities, such as bonded debt and amounts owed for compensated absences and capital lease obligations, which are reported in the government-wide statements but not in the fund-based statements.

- *Proprietary funds* show activities that operate more like those found in the private sector. The State of California has two proprietary fund types: enterprise funds and internal service funds.
 - Enterprise funds record activities for which a fee is charged to external users; they are presented as business-type activities in the government-wide financial statements.
 - Internal service funds accumulate and allocate costs internally among the State of California's various functions. For example, internal service funds provide information technology, printing, fleet management, and architectural services primarily for state departments. As a result, their activity is considered governmental.
- Fiduciary funds account for resources held for the benefit of parties outside the State. Fiduciary funds and
 the activities of fiduciary component units are not reflected in the government-wide financial statements
 because the resources of these funds are not available to support State of California programs. The
 accounting used for fiduciary funds and similar component units is similar to that used for proprietary
 funds.

Discretely Presented Component Units Financial Statements

As discussed previously, the State has financial accountability for discretely presented component units, which have certain independent qualities and operate in a similar manner as private-sector businesses. The activities of the discretely presented component units are classified as enterprise activities.

Notes to the Financial Statements

The notes to the financial statements in this publication provide additional information that is essential for a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements, which describe particular accounts in more detail, are located immediately following the discretely presented component units' financial statements.

Required Supplementary Information

A section of required supplementary information follows the notes to the basic financial statements in this publication. This section includes a schedule of funding progress for certain pension and other postemployment benefit trust funds, information on infrastructure assets based on the modified approach, a budgetary comparison schedule, and a reconciliation of the budgetary basis and the GAAP basis fund balances for the major governmental funds presented in the governmental fund financial statements.

Combining Financial Statements and Schedules

The Combining Financial Statements and Schedules – Nonmajor and Other Funds section presents combining statements that provide separate financial statements for nonmajor governmental funds, nonmajor proprietary funds, fiduciary funds, and nonmajor component units. The basic financial statements present only summary information for these activities.

Government-wide Financial Analysis

Net Assets

The primary government's combined net assets (governmental and business-type activities) decreased by 50.0%, from a negative \$6.4 billion as restated at June 30, 2010, to a negative \$9.7 billion a year later.

The primary government's \$86.8 billion investment in capital assets, such as land, buildings, equipment, and infrastructure (roads, bridges, and other immovable assets) comprise a significant portion of its net assets. This amount of capital assets is net of any outstanding debt used to acquire those assets. The State uses capital assets when providing services to citizens; consequently, these assets are not available for future spending. Although the State's investment in capital assets is reported net of related debt, the resources needed to repay this debt must come from other sources because the State cannot use the capital assets themselves to pay off the liabilities.

Another \$31.5 billion of the primary government's net assets represents resources that are externally restricted as to how they may be used, such as resources pledged to debt service. Internally imposed earmarking of resources is not presented in this publication as restricted net assets. As of June 30, 2011, governmental activities showed an unrestricted net assets deficit of \$124.0 billion and business-type activities showed an unrestricted net assets deficit of \$4.2 billion.

A large portion of the negative unrestricted net assets of governmental activities consists of \$62.6 billion in outstanding bonded debt issued to build capital assets for school districts and other local governmental entities. Because the State does not own these capital assets, neither the assets nor the related bonded debt is included in the portion of net assets reported as "investment in capital assets, net of related debt." Instead, the bonded debt is reported as a non-current liability that reduces the State's unrestricted net assets. Readers can expect to see a continued deficit in unrestricted net assets of governmental activities as long as the State has significant outstanding obligations for school districts and other local governmental entities.

Table 1 presents condensed financial information derived from the Statement of Net Assets for the primary government.

Table 1

Net Assets – Primary Government
June 30, 2010 and 2011
(amounts in millions)

	Governmental Activities		Business-ty	pe A	ctivities	Total					
	2011		2010	2011		2010		2011		2010	
ASSETS											
Current and other assets	\$ 50,820	\$	56,355	\$ 33,884	\$	30,324	\$	84,704	\$	86,679	
Capital assets	100,464		98,798	8,551		6,794		109,015		105,592	
Total assets	151,284		155,153	42,435		37,118		193,719	_	192,271	
LIABILITIES											
Noncurrent liabilities	120,905		115,465	37,203		33,951		158,108		149,416	
Other liabilities	40,835		43,887	4,426		3,923		45,261	_	47,810	
Total liabilities	161,740		159,352	 41,629		37,874		203,369	_	197,226	
NET ASSETS											
Investment in capital assets											
net of related debt	85,461		84,085	1,383		90		86,844		84,175	
Restricted	27,866		14,988	3,638		3,405		31,504		18,393	
Unrestricted	(123,783)		(103,272)	(4,215)		(4,251)		(127,998)		(107,523)	
Total net assets (deficit)	\$ (10,456)	\$	(4,199)	\$ 806	\$	(756)	\$_	(9,650)	\$	(4,955)	

Changes in Net Assets

The expenses of the primary government totaled \$234.6 billion for the year ended June 30, 2011. Of this amount, \$126.4 billion (53.9%) was funded with program revenues (charges for services or program-specific grants and contributions), leaving \$108.2 billion to be funded with general revenues (mainly taxes). The primary government's general revenues of \$105.0 billion were less than the unfunded expenses. As a result, the total net assets decreased by \$3.2 billion, or 50%.

Of the total decrease, net assets for governmental activities decreased by \$3.5 billion, while those for business-type activities increased by \$330 million.

Table 2 presents condensed financial information derived from the Statement of Activities for the primary government.

Table 2

Changes in Net Assets – Primary Government
Year ended June 30, 2010 and 2011
(amounts in millions)

	_G	overnmen	tal A	Activities	Business-type Activities				Total			
		2011		2010		2011		2010		2011		2010
REVENUES								_		_		
Program revenues:												
Charges for services	\$	21,122	\$	21,610	\$	34,819	\$	20,661	\$	55,941	\$	42,271
Operating grants and contributions		67,849		75,470		1,217		_		69,066		75,470
Capital grants and contributions		1,272		962		86		92		1,358		1,054
General revenues:												
Taxes		104,705		94,593		_		_		104,705		94,593
Investment and interest		63		115		_		_		63		115
Miscellaneous		229		150		_				229		150
Total revenues		195,240		192,900		36,122		20,753		231,362		213,653
EXPENSES												
Program expenses:												
General government		13,520		12,455		_		_		13,520		12,455
Education		56,487		61,764		_		_		56,487		61,764
Health and human services		92,475		80,800		_		_		92,475		80,800
Resources		5,853		6,019		_		_		5,853		6,019
State and consumer services		1,405		980		_		_		1,405		980
Business and transportation		11,120		14,156		_		_		11,120		14,156
Correctional programs		10,296		10,310		_		_		10,296		10,310
Interest on long-term debt		4,377		4,146		_		_		4,377		4,146
Electric Power		_		_		2,317		3,908		2,317		3,908
Water Resources		_		_		1,116		1,070		1,116		1,070
Public Building Construction		_		_		390		494		390		494
State Lottery		_		_		3,507		3,166		3,507		3,166
Unemployment Programs		_		_		25,619		29,615		25,619		29,615
Nonmajor enterprise						6,095		1,140		6,095		1,140
Total expenses		195,533		190,630		39,044		39,393		234,577		230,023
Excess (deficiency) before transfers		(293)		2,270		(2,922)		(18,640)		(3,215)		(16,370
Transfers		(3,252)		(13,442)		3,252		13,442				_
Change in net assets		(3,545)		(11,172)		330		(5,198)		(3,215)		(16,370
Net assets, beginning of year (restated)		(6,911)		6,973		476		4,442	*	(6,435)		11,415
Net assets (deficit), end of year	\$	(10,456)	\$	(4,199)	\$	806	\$	(756)	\$	(9,650)	\$	(4,955

Not restated

Governmental Activities

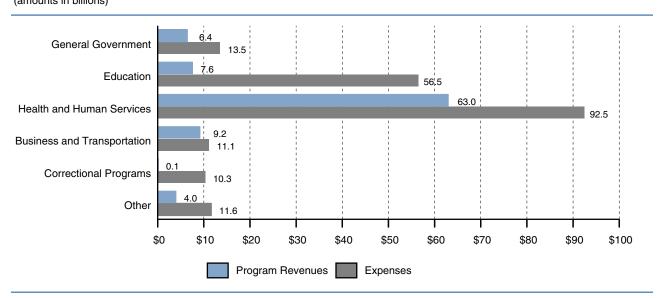
Governmental activities' expenses and transfers totaled \$198.8 billion. Program revenues, including \$69.1 billion received in federal grants, funded \$90.2 billion (45.4%) of expenses and transfers, leaving \$108.5 billion to be funded with general revenues (mainly taxes). However, general revenues for governmental activities totaled only \$105.0 billion, so governmental activities' total net assets decreased by \$3.5 billion, or 51.3%, during the year ended June 30, 2011.

Chart 1 presents a comparison of governmental activities' expenses by program, with related revenues.

Chart 1

Expenses and Program Revenues – Governmental Activities Year Ended June 30, 2011

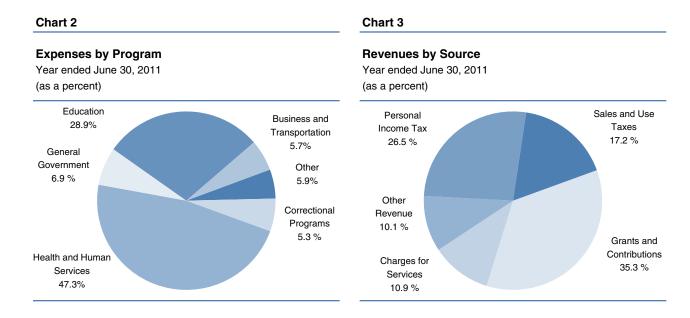
(amounts in billions)



For the year ended June 30, 2011, total state tax revenues collected for governmental activities increased by \$10.1 billion (10.7%) from the prior year. Personal income taxes increased by \$7.9 billion (17.9%) as a result of higher personal income reported. The other taxes category increased by \$2.5 billion. This \$2.5 billion increase was primarily the result of Assembly Bill X8-6, also known as the Fuel Tax Swap, which redirected a portion of gasoline taxes from sales taxes to other taxes. Sales and use taxes would have reflected this increase if these taxes had not been redirected.

Overall expenses for governmental activities increased by \$4.9 billion (2.6%) from the prior year. The largest increase in expenses was an \$11.7 billion increase in health and human services spending primarily due to the creation of the Hospital Quality Assurance Revenue Fund, which was established by Assembly Bill 1383 effective October 2009. This increase in expenses was somewhat offset by a \$5.3 billion decrease in education expenditures reported as a result of the reclassification of the California State University financial activities from a governmental fund to an enterprise fund.

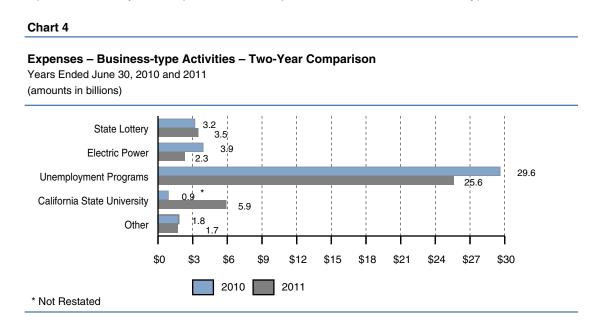
Charts 2 and 3 present the percentage of total expenses for each governmental activities program and the percentage of total revenues by source.



Business-type Activities

Business-type activities expenses totaled \$39.0 billion. Program revenues of \$36.1 billion, primarily generated from charges for services, and \$3.3 billion in transfers were sufficient to cover these expenses. Consequently, business-type activities' total net assets increased by \$330 million, or 69.3%, during the year ended June 30, 2011.

Chart 4 presents a two-year comparison of the expenses of the State's business-type activities.



Fund Financial Analysis

The national recession and the State's weakened economy had the greatest impact on governmental funds, which rely heavily on taxes to support the majority of their services and programs. The State's governmental funds had a \$1.0 billion decrease in fund balance over the prior year's restated ending fund balance. Some proprietary funds incurred net asset reductions, as their expenses exceeded revenues for the fiscal year 2010-11. The Unemployment Programs Fund incurred the largest decline in net assets, \$324 million, despite a \$13.4 billion increase in operating revenues due to a draw of federal unemployment funds. More federal funds were drawn to compensate for the decreased in funding from the federal American Reinvestment and Recovery Act (ARRA).

Governmental Funds

The governmental funds' Balance Sheet reported \$60.7 billion in assets, \$49.9 billion in liabilities, and \$10.8 billion in fund balance as of June 30, 2011. Total assets of governmental funds decreased by 12.0%, while total liabilities decreased by 9.6%, resulting in a total fund balance decrease of \$1.0 billion (8.7%) over the prior fiscal year. As in the prior year, the General Fund had to rely heavily on internal borrowing from the State's other funds to meet its payment obligations. However, by June 30, 2011, long-term borrowing had decreased by \$1.3 billion to \$8.9 billion.

Within the governmental funds' total fund balance, \$187 million is classified as nonspendable because this amount consists of long-term interfund receivables and loans receivable, or due to legal or contractual requirements. Additionally, \$27.9 billion is classified as restricted for specific programs by external constraints such as debt covenants and contractual obligations, or by constitutional provisions or enabling legislation. Furthermore, the total fund balance of \$2.7 billion is classified as committed for specific purposes and \$269 million is classified as assigned for specific purposes. The unassigned balance of the governmental funds is a negative \$20.3 billion. These new fund balance classifications reflect the implementation of GASB Statement No. 54 and are defined in more detail in Note 1K.

The Statement of Revenues, Expenditures, and Changes in Fund Balances of the governmental funds shows \$195.3 billion in revenues, \$198.0 billion in expenditures, and a net \$1.6 billion in receipts from other financing sources. The ending fund balance of the governmental funds for the year ended June 30, 2011, was \$10.8 billion, a \$1.0 billion decrease over the prior year's restated ending fund balance of \$11.8 billion. The reasons for the change in the fund balance were a net decrease in intergovernmental revenue in the Federal Fund, as a result of a reduction in economic stimulus funds received from the Federal ARRA, which exceeded the increase of tax revenue.

Personal income taxes, which account for 49.3% of tax revenues and 26.5% of total governmental fund revenues, increased by \$7.8 billion from the prior fiscal year. Sales and use taxes, which account for 32.0% of tax revenues and 17.1% of total governmental fund revenues, decreased by \$208 million over the prior fiscal year. Corporation taxes, which account for 9.0% of tax revenues and 4.8% of total governmental fund revenues, decreased by \$34 million from the prior fiscal year. Governmental fund expenditures increased by \$7.2 billion from the prior fiscal year, primarily in health and human services programs. General obligation bonds and commercial paper of \$4.5 billion were issued during the 2010-11 fiscal year; however, this was \$7.5 billion less than the amount issued in the prior fiscal year.

The State's major governmental funds are the General Fund, the Federal Fund, and the Transportation Fund. The General Fund ended the fiscal year with a fund deficit of \$19.9 billion. The Federal Fund and the

Transportation Fund ended the fiscal year with fund balances of \$122 million and \$7.8 billion, respectively. The nonmajor governmental funds ended the year with a total fund balance of \$22.8 billion.

General Fund: As shown on the Balance Sheet, the General Fund (the State's main operating fund) ended the fiscal year with assets of \$12.0 billion, liabilities of \$31.9 billion, nonspendable, restricted, and committed fund balances of \$148 million, \$156 million, and \$30 million, respectively, leaving the General Fund with a negative unassigned fund balance of \$20.3 billion. Total assets of the General Fund decreased by \$849 million from the prior fiscal year, mainly because of a \$627 million decrease in amounts due from other governments. During the 2010-11 fiscal year, the General Fund continued to experience cash shortages and relied on internal borrowing from the State's other funds to meet its payment obligations. However, by June 30, 2011, long-term borrowing from other funds had decreased by \$1.3 billion to \$8.9 billion. Even with this increase in short- and long-term interfund payables, the total liabilities of the General Fund decreased by \$518 million (1.6%).

As shown on the Statement of Revenues, Expenditures, and Changes in Fund Balances of the governmental funds, the General Fund had \$93.5 billion in revenues, \$90.4 billion in expenditures, and a net \$3.5 billion disbursement from other financing sources (uses) for the year ended June 30, 2011. Approximately 93.3% of General Fund revenue (\$87.2 billion) is derived from the State's big three taxes—personal income taxes (\$50.8 billion), sales and use taxes (\$27.0 billion), and corporation taxes (\$9.4 billion). A total of \$194 million in revenue is included in the General Fund in compliance with GASB Statement No. 54. These revenues are not considered General Fund Revenues for any budgetary purposes or for the *Budgetary/Legal Basis Annual Report*. Most of these revenues (\$190 million) are from unemployment programs.

During the 2010-11 fiscal year, total General Fund revenue increased by \$8.4 billion, or 9.8%. Revenue from personal income taxes and sales and use taxes increased by \$7.7 billion (17.9%) and \$132 million (0.5%), respectively. These increases were primarily the result of California's slowly improving economy and decreasing unemployment rate. Revenue from corporation taxes decreased by \$34 million (0.4%). Revenue from licenses and permits continued to surpass that of fiscal year 2008-09, the result of a temporary increase in the assessment rate for vehicle license fees effective May 2009 through June 2011; however, this year's revenues were \$50 million less than in fiscal year 2009-10.

General Fund expenditures increased by \$3.2 billion, to \$90.4 billion. The programs with the largest increases were health and human services, which increased by \$3.7 billion, to \$27.8 billion, and general government, which increased by \$829 million, to \$3.4 billion. The General Fund's ending fund balance for the year ended June 30, 2011, was a negative \$19.9 billion, a decrease of \$448 million from the prior year's restated ending fund balance of negative \$19.5 billion. The increased expenditures for health and human services were mainly the result of the reduction in Federal ARRA funds. The ARRA funding, which had reduced the General Fund's share of Medical Assistance program costs, was phased out during the last half of the fiscal year and ended June 30, 2011.

Federal Fund: This fund reports federal grant revenues and the related expenditures to support the grant programs. The largest of these program areas is health and human services, which accounted for \$47.9 billion (76.9%) of the total \$62.3 billion in fund expenditures. The Medical Assistance program and the Temporary Assistance for Needy Families program are included in this program area. Education programs also constituted a large part of the fund's expenditures—\$9.1 billion (14.6%), down \$1.2 billion (11.8%) from the prior year—most of which were apportionments made to local educational agencies (school districts, county offices of education, and community colleges). The Federal Fund's revenues decreased by \$8.6 billion (11.2%), approximately the same amount as its combined expenditures and transfers, which decreased (\$8.6 billion), resulting in only a \$30 million fund balance increase from the prior year's restated ending fund balance of \$91 million. The decrease in Federal Fund revenues and transfers was primarily the result of the phase out of

stimulus funding from the Federal ARRA, which provided additional funding for many health and human services and education expenditures in the prior year.

Transportation Fund: This fund accounts for fuel taxes, bond proceeds, and other revenues used primarily for highway and passenger rail construction. The Transportation Fund's revenues increased by 23.6% and expenditures decreased by 17.3%. Other financing sources provided net receipts of \$527 million. The Transportation Fund ended the fiscal year with a \$7.8 billion fund balance, an increase of \$788 million over the prior year.

Proprietary Funds

Enterprise Funds: The Unemployment Programs and State Lottery Fund each saw decreases of \$324 million and \$23 million, respectively, in their net assets. Other State enterprise funds experienced increases in their net assets during the 2010-11 fiscal year. The most significant increase was in the California State University Fund, whose net assets increased by \$575 million during the year.

As shown on the Statement of Net Assets of the proprietary funds, total assets of the enterprise funds were \$43.0 billion as of June 30, 2011. Of this amount, current assets totaled \$12.7 billion and noncurrent assets totaled \$30.3 billion. The largest changes in asset account balances were a \$2.7 billion increase in amount on deposit with the U.S. Treasury in the Unemployment Programs Fund and a \$484 million decrease in cash and pooled investments in the Public Building Construction Fund. The total liabilities of the enterprise funds were \$42.2 billion. The largest liability of the enterprise funds is for bonds payable—\$22.1 billion of revenue bonds payable and \$1.1 billion of general obligation bonds payable. During the 2010-11 fiscal year, the State continued to obtain loans from the U.S Department of Labor to cover deficits in the Unemployment Programs Fund. The balance due on these loans as of June 30, 2011, was \$11.0 billion, an increase of \$3.8 billion over the prior year.

Total net assets of the enterprise funds were \$806 million as of June 30, 2011. Total net assets consisted of four segments: nonexpendable restricted net assets of \$22 million, restricted expendable net assets of \$3.6 billion, investment in capital assets (net of related debt) of \$1.4 billion, and unrestricted net assets of negative \$4.2 billion. The Unemployment Programs Fund had a deficit of \$6.9 billion, a \$324 million (4.9%) decrease in net assets from the prior year. The net assets of all other enterprise funds experienced small changes during the year with the exception of the California State University Fund which had an increase to net assets of \$575 million.

As shown on the Statement of Revenues, Expenses, and Changes in Fund Net Assets of the proprietary funds, the enterprise funds ended the year with operating revenues of \$33.7 billion, operating expenses of \$36.6 billion, and net disbursements from other transactions of \$108 million. The largest sources of operating revenue were unemployment and disability insurance receipts of \$24.7 billion in the Unemployment Programs Fund and lottery ticket sales of \$3.4 billion collected by the State Lottery Fund. The unemployment and disability insurance receipts in the Unemployment Programs Fund increased by \$13.4 billion from \$11.3 billion in fiscal year 2009-10. These receipts came primarily from the federal government unemployment account to pay unemployment and disability benefits. The State received more federal unemployment funds because less funding from Federal ARRA economic stimulus was available to cover unemployment and disability benefits. The largest operating expenses were distributions to beneficiaries of \$25.4 billion by the Unemployment Programs Fund and personal services of \$3.7 billion by the California State University Fund. The Unemployment Programs Fund expenses were partially subsidized by \$617 million of Federal ARRA economic stimulus funding transferred from the Federal Fund. The ending net assets of the enterprise funds at

June 30, 2011, were \$806 million—\$330 million greater than the prior year's restated ending net assets of \$476 million.

Internal Service Funds: Total net assets of the internal service funds were \$574 million as of June 30, 2011. These net assets consist of two segments: investment in capital assets (net of related debt) of \$141 million and unrestricted net assets of \$433 million.

Fiduciary Funds

The State of California has four types of fiduciary funds: private purpose trust funds, pension and other employee benefit trust funds, investment trust funds, and agency funds. The private purpose trust funds ended the fiscal year with net assets of \$4.6 billion. The pension and other employee benefit trust funds ended the fiscal year with net assets of \$409.6 billion. The State's only investment trust fund, the Local Agency Investment Fund, ended the fiscal year with net assets of \$24.0 billion. Agency funds act as clearing accounts and thus do not have net assets.

For the year ended June 30, 2011, the fiduciary funds' combined net assets were \$438.2 billion, a \$69.7 billion increase from prior year net assets. The increase in net assets for these funds was mainly attributable to an increase in net investment income from the prior year of \$34.6 billion (82.4%).

The Economy for the Year Ending June 30, 2011

Since the recession ended in June 2009, the U.S. has seen consecutive quarterly growth in real Gross Domestic Product. The first quarter of California's 2010-11 fiscal year saw an increase in the national growth rate over the same period the year before, 2.5% versus 1.7%. For the remainder of the fiscal year, U.S. economic output continued a slow growth driven primarily by consistent growth in personal consumption. These positive national signs also started to play out at the state level during the year ending June 30, 2011.

California's economic recovery continued throughout the last fiscal year, but at a slow pace. Although employment levels remain well below their pre-recession peak, total non-farm employment grew fairly consistently. By June 2011, total non-farm employment was 1.3% higher than at the beginning of the fiscal year. The state unemployment rate as of June 2011 was 11.8%, a decrease from the July 2010 rate of 12.4%. Unfortunately, the declining unemployment rate was due in part to discouraged job seekers dropping out of the job market. The state labor force fell by 111,000 unemployed, or 0.6%, from July 2010 to June 2011. Although labor market conditions were generally improving during the second half of the fiscal year, the labor force figures point to an uneven recovery, with many California residents not benefitting from the growth.

The state housing market has remained a weakness in the State's economy. Home sales rose sharply in the last months of 2010, increasing 12% from October 2010 through January 2011, but then fell 8.8% from March through June 2011. However, on a fiscal-year basis, home sales did increase 2.3% from July 2010 to June 2011. Home prices have yet to record any significant increases, but the pace of decline slowed substantially in the 2010-11 fiscal year. Both defaults and foreclosures in California were down in fiscal year 2010-11, with defaults declining 20.2% and foreclosures declining 11.4% from July 2010 through June 2011. Residential construction permits were up 13.3% for the fiscal year, with construction employment up 1.8% for the same time period. The housing market is still sluggish, but economic indicators support the view that the market is slowly improving.

Other economic indicators point to a continued recovery in the State. State personal income showed consistent increases in each quarter of fiscal year 2010-11, increasing 5.5% over the course of the year. Additionally, consumer spending was a consistent strong element for the year. Seasonally adjusted taxable sales increased

9.8% over the course of the fiscal year. International trade and tourism contributed to California's economic recovery during the year as well, with exports of goods and commodities from California increasing by nearly 15%.

General Fund Budget Highlights

The original General Fund budget of \$95.3 billion was reduced by \$266 million. This decrease is mainly comprised of a reduction in funding education programs per Section 12.42 of the 2010 Budget Act that was partially offset by correctional program augmentations authorized by Assembly Bill 122, Chapter 42, Statutes of 2011. During the 2010-11 fiscal year, General Fund actual budgetary basis expenditures were \$91.9 billion, \$3.2 billion less than the final budgeted amounts.

Table 3 presents a summary of the General Fund original and final budgets.

Table 3

General Fund Original and Final Budgets

Year ended June 30, 2011 (amounts in millions)

	Original	Final	 crease/ ecrease)
Budgeted amounts			
State and consumer services	\$ 609	\$ 590	\$ (19)
Business and transportation	494	494	_
Resources	1,224	1,178	(46)
Health and human services	28,967	29,076	109
Correctional programs	8,665	9,567	902
Education	45,079	43,767	(1,312)
General government:			
Tax relief	446	535	89
Debt service	5,014	5,019	5
Other general government	4,833	4,839	6
Total	\$ 95,331	\$ 95,065	\$ (266)

Capital Assets and Debt Administration

Capital Assets

The State's investment in capital assets for its governmental and business-type activities as of June 30, 2011, amounted to \$109.0 billion (net of accumulated depreciation). This investment in capital assets includes land, state highway infrastructure, collections, buildings and other depreciable property, and construction in progress. Depreciable property includes buildings, improvements other than buildings, equipment, personal property, intangible assets, certain infrastructure assets, certain books, and other capitalized and depreciable property. Infrastructure assets, such as roads and bridges, are items that are normally immovable and can be preserved for a greater number of years than can most capital assets.

Table 4 presents a summary of the primary government's capital assets for governmental and business-type activities.

Table 4

Capital Assets

Year ended June 30, 2011 (amounts in millions)

	 vernmental	ness-type	Total
Land	\$ 16,599	\$ 215	\$ 16,814
State highway infrastructure	61,439	_	61,439
Collections – nondepreciable	22	2	24
Buildings and other depreciable property	23,521	10,568	34,089
Intangible assets – amortizable	649	219	868
Less: accumulated depreciation/amortization	(10,114)	(4,113)	(14,227)
Construction in progress	7,814	1,521	9,335
Intangible assets – nonamortizable	534	 139	 673
Total	\$ 100,464	\$ 8,551	\$ 109,015

The budget authorized \$9.3 billion for the State's capital outlay program in the 2010-11 fiscal year, not including funding for state highway infrastructure and K–12 schools. State highway infrastructure assets are discussed in more detail in the Required Supplementary Information that follows the notes to the financial statements. Of the \$9.3 billion authorized, \$224 million was from the General Fund; \$6.2 billion was from lease-revenue bonds; \$1.1 billion was from proceeds of various general obligation bonds; and \$1.8 billion was from reimbursements, federal funds, and special funds. These amounts include reappropriations and other funds carried over from previous budgets for continuing projects.

The major capital projects authorized include:

- \$200 million in lease-revenue bonds for the Department of Correction and Rehabilitation, for local youthful offender rehabilitative facilities;
- \$549 million for numerous construction projects within the University of California, the California State University, and the California Community Colleges;

- \$919 million for projects to replace structurally deficient court facilities; and
- \$155 million from the High-Speed Passenger Train bond fund and federal funds for primary engineering and environmental review along the San Francisco-to-Anaheim section of the high-speed rail system.

Note 7, Capital Assets, includes additional information on the State's capital assets.

Modified Approach for Infrastructure Assets

The State uses the modified approach to report the cost of its infrastructure assets (state roadways and bridges). Under the modified approach, the State does not report depreciation expense for roads and bridges but capitalizes all costs that add to the capacity and efficiency of State-owned roads and bridges. All maintenance and preservation costs are expensed and not capitalized. Under the modified approach, the State maintains an asset management system to demonstrate that it is preserving the infrastructure at or above established condition levels. The State is responsible for maintaining 49,518 lane miles and 12,893 bridges.

During the 2010-11 fiscal year, the actual amount spent on preservation was 13.1% of the estimated budgeted amount needed to maintain the infrastructure assets at the established-condition levels. Although the amount spent fell short of the budgeted amount, the assessed conditions of the State's bridges and roadways are better than the established condition baselines.

The Required Supplementary Information includes additional information on how the State uses the modified approach for infrastructure assets; it also presents the established condition standards, condition assessments, and preservation costs.

Debt Administration

At June 30, 2011, the primary government had total bonded debt outstanding of \$111.5 billion. Of this amount, \$80.7 billion (72.4%) represents general obligation bonds, which are backed by the full faith and credit of the State. Included in the \$80.7 billion of general obligation bonds is \$7.2 billion of Economic Recovery bonds that are secured by a pledge of revenues derived from dedicated sales and use taxes. The current portion of general obligation bonds outstanding is \$2.4 billion and the long-term portion is \$78.3 billion. The remaining \$30.8 billion (27.6%) of bonded debt outstanding represents revenue bonds, which are secured solely by specified revenue sources. The current portion of revenue bonds outstanding is \$1.4 billion and the long-term portion is \$29.4 billion.

Table 5 presents a summary of the primary government's long-term obligations for governmental and business-type activities.

Table 5

Long-term Obligations

Year ended June 30, 2011 (amounts in millions)

	 vernmental ctivities	iness-type ctivities	 Total
Government-wide noncurrent liabilities			
General obligation bonds	\$ 77,217	\$ 1,119	\$ 78,336
Revenue bonds	7,359	22,091	29,450
Certificates of participation and commercial paper	1,328	140	1,468
Capital lease obligations	4,544	734	5,278
Net other postemployment benefits obligation	9,607	319	9,926
Proposition 98 funding guarantee	2,637	_	2,637
Mandated costs	5,741	_	5,741
Loans payable	2,122	10,958	13,080
Other noncurrent liabilities	10,351	1,842	12,193
Total noncurrent liabilities	120,906	37,203	158,109
Current portion of long-term obligations	3,807	 2,006	 5,813
Total long-term obligations	\$ 124,713	\$ 39,209	\$ 163,922

During the year ended June 30, 2011, the primary government's total long-term obligations increased by \$7.3 billion over the prior year's restated balance. Governmental activities net other postemployment benefits obligation had the largest increase (\$2.6 billion), but other notable increases occurred in general obligation bonds payable, compensated absences, and mandated costs. During the fiscal year, the State issued \$4.5 billion in new general obligation bonds for public education facilities, transportation projects, housing and emergency shelters, and various water and flood control projects. The net other postemployment benefits obligation increased because the State does not fully fund the annual cost of these benefits.

Note 10, Long-term Obligations, and Notes 11 through 17 include additional information on the State's long-term obligations.

The State's general obligation bond credit ratings remained unchanged during the fiscal year 2010-11. The current ratings from the three credit rating agencies are as follows: Standard and Poor's – "A-", Moody's Investors Service – "A1", and Fitch – "A-".

Recent Economic Condition and Future Budgets

Recent Economic Condition

From July 1 through December 31, 2011, economic data indicated that the California economy continued to improve during the first half of fiscal year 2011-12. Since the first quarter of fiscal year 2010-11, the state has gained 351,100 non-farm jobs. Other aspects of California's labor markets are showing signs of improvement as well. By December 2011, the state's unemployment rate had dropped from a seasonally adjusted 12.5% in December 2010 to 11.1%. Nearly 213,000 California residents re-entered the labor market during the last five months of 2011, while the number of unemployed residents simultaneously fell by 154,000.

Consumer spending has shown steady increases over the past two years, rising by more than 17.5% since its low point in the second quarter of 2009. Personal income in California has already surpassed its pre-recession peak, totaling \$1.67 trillion in the third quarter of 2011 following almost two years of consecutive growth on a quarterly basis.

In addition to growing consumer demand from domestic sources, international trade has also been instrumental in assisting in California's recovery. The U.S. dollar remained at its lowest level since the mid-1990s, benefitting California's export market. Industrial machinery (including computers) has posted solid gains of almost 12% through November 2011, after growing by more than 30% in 2010. Additionally, other high-technology exports, including vehicles and parts, aircrafts, pharmaceuticals, and plastics, have continued to do well in 2011. Commodity exports have also done well in recent years. Over the past two years, the State's agricultural and natural resources industries have seen double-digit growth in the production of fruit, nuts, dairy products, and fuel and oil.

Home prices have yet to rebound across the state, but the housing market has stabilized. Defaults and foreclosures have been trending downward for almost two years, despite a small uptick in defaults in the first quarter of fiscal year 2011-12. As this "shadow inventory" dwindles, demand for new home construction is expected to increase. While the number of new single-family building permits was still declining through the first six months of fiscal 2011-12, multi-family building permits have been trending upward since mid-2010. In addition, new residential permit values steadily increased throughout 2011.

Overall, California still has a long way to go before it can claim recovery from the recession. Still, most indicators point to an economy that is not only in recovery mode, but is beginning to outpace that of the rest of the United States. The labor markets are showing real signs of improvement and both incomes and consumer spending are up from their respective lows. A weak dollar, coupled with California's proximity to Asia and the State's international trade infrastructure at its ports and airports, have helped to boost exports. Housing remains soft, but even there the market is beginning to show some improvement. Recent economic conditions show that the worst is behind the state and that its recovery will continue.

California's 2011-12 Budget

California's 2011-12 Budget Act was enacted on June 30, 2011. The Budget Act appropriated \$129.5 billion: \$85.9 billion from the General Fund, \$34.2 billion from special funds, and \$9.4 billion from bond funds. The 2011 Budget Act continues to hold General Fund spending essentially flat for a third year – \$85.9 billion in 2011-12, \$86.6 billion in 2010-11, and \$86.3 billion in 2009-10. The General Fund's available resources were projected to be \$88.5 billion, resulting in a projected reserve for economic uncertainties of \$543 million. General Fund revenues come predominantly from taxes, with personal income taxes expected to provide 42% of total revenue. California's major taxes (personal income, sales and use, and corporation taxes) were projected to supply approximately 89% of the General Fund's resources in the 2011-12 fiscal year.

The Budget enacted \$27.2 billion in actions to solve a General Fund gap between resources and expenditures. The Budget solutions can be categorized into three major areas: expenditure-related solutions, revenue actions, and one-time loans and transfers. The \$11.1 billion in expenditure-related solutions include ongoing and temporary cost or service reductions primarily in health and social services, higher education, and employee compensation, and a shift away from the General Fund for transportation debt payments toward using weight fees. The majority of proposed new revenues assume \$11.8 billion in growth due to an increase in the baseline forecast of personal income and corporation tax revenues. These revenue actions would result in a total increase in revenue of \$13.2 billion. The Budget also included \$2.9 billion in one-time loans, transfers, and funding shifts, which include pausing for one year, building construction funded by the Trial Court Trust

Fund for a savings of \$743 million; a one-year decrease in the Stage 1 Child Care program, for a savings of \$369 million; and a one-time transfer of \$155 million from the Gas Consumption Surcharge Fund.

The Budget introduced a major realignment of public safety programs, shifting certain state program responsibilities and revenues to local governments, primarily counties. This realignment affected both revenues and expenditures, as these programs will receive revenues and incur expenditures that previously were the stewardship of the State. In total, the realignment plan provides \$5.6 billion in 2011-12 to local governments to fund various criminal justice, mental health, and social service programs. The savings to the General Fund is estimated to be \$2.6 billion.

The 2011-12 Budget, recognizing the potential risk to the State's fiscal condition if revenues fell short of June 2011 estimates, included a mechanism for further reducing the current year expenditures. As of December 2011, total General Fund revenues were determined to be below forecasted amounts, and on December 13, the Director of Finance, as required, implemented the mechanism and reduced by \$1 billion remaining-year funding to various appropriations.

The proposed 2012-13 Governor's Budget provides revised revenue and expenditure estimates for the 2011-12 fiscal year. If no corrective action is taken by the Governor and the Legislature, the revised gap between General Fund revenues and expenditures is expected to be \$4.1 billion by the end of the 2011-12 fiscal year. State cash flow data as of January 31, 2012 indicates that this gap is a combination of actual expenditures exceeding estimates by \$1.4 billion and revenues falling short of estimates by \$3.8 billion. The revenue shortfall can in part be attributed to lower-than-estimated personal income and corporate taxes. Expenditures are greater than estimated because many of the cost-cutting measures included in the 2011-12 Budget have been disputed in court and have not been implemented. Court orders and delayed federal approval related to several budget-balancing cuts in the health and human services area have increased budgeted costs by nearly \$2 billion. The Governor's proposed solutions are discussed further in the next section.

California's 2012-13 Budget

The Governor released his proposed 2012-13 Budget on January 5, 2012. The proposed Budget projects a \$9.2 billion gap between estimated revenues and state expenditures over the next 18 months. The \$9.2 billion figure is comprised of a \$4.1 billion deficit carried over from the 2011-12 fiscal year and a \$5.1 billion shortfall in the 2012-13 fiscal year. The Governor's Budget proposes \$4.2 billion in expenditure-related solutions, \$4.7 billion in net new revenues, and \$1.4 billion borrowed from special funds and other sources. If enacted, the Governor's proposed Budget would eliminate the 2011-12 and 2012-13 deficit and leave the State with a surplus of \$1 billion. The 2012-13 Budget continues to incorporate those solutions implemented in the prior year Budget. It also assumes passage of the Governor's proposed initiative in the November 2012 election. If approved by the voters, this initiative will temporarily increase the personal income tax on the state's wealthiest taxpayers and temporarily increase the sales tax by one-quarter percent, generating an estimated \$6.8 billion to \$9 billion for 2012-13.

The 2012-13 Governor's Budget projects (with all budget solutions enacted) that 2012-13 fiscal year General Fund revenues and transfers will be \$95.4 billion and expenditures will be approximately \$92.6 billion, with a \$1.1 billion reserve. Proposed 2012-13 General Fund revenues and transfers are 7.7% more than the revised 2011-12 estimate of \$88.6 billion, while 2012-13 expenditures are 7% greater than the revised 2011-12 estimate of \$86.5 billion. Almost all of the Governor's proposed new revenue is derived from plans to temporarily increase the sales tax and temporarily increase personal income tax on wealthy taxpayers, both of which the Governor will submit to voters in November 2012. A portion of the new revenue, \$2.5 billion, will increase the Proposition 98 minimum guarantee to schools; the remaining \$4.4 billion will prevent deeper cuts

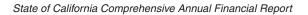
to schools, protect local public safety funding, and assist in balancing the budget. It is estimated that the temporary tax increases will allow the State to pay off \$33 billion in outstanding budgetary borrowing and deferrals by fiscal year 2015-16. While additional tax revenues will mitigate the need for deeper cuts in expenditures, they will not be sufficient to close the entire budget gap. Other expenditure-related solutions include reductions of \$1.4 billion for CalWorks and \$1 billion in combined reductions to Medi-Cal and In-Home Supportive Services.

According to the Legislative Analyst's Office (LAO), California's nonpartisan fiscal and policy advisor, the administration's estimate of the budget shortfall is questionable. LAO's revenue estimate is lower than the Governor's, specifically those revenues attributable to the Governor's initiative to be included in the November 2012 general election. The LAO estimates that personal income taxes from upper-income taxpayers will be lower than the Governor's estimate, which could result in the Legislature having to pursue billions of dollars more in budget-balancing solutions. The LAO credited the Governor's proposed restructuring of the school finance system, community college categorical funding, and education mandates, but also noted that the Governor's \$1.4 billion in proposed savings related to Social Services and subsidized child care has merit but may be too severe, and commented that potential savings could be less under other alternatives.

Requests for Information

The State Controller's Office designed this financial report to provide interested parties with a general overview of the State of California's finances. Address questions concerning the information provided in this report or requests for additional information to the State Controller's Office, Division of Accounting and Reporting, P.O. Box 942850, Sacramento, California 94250-5872. This report is also available on the Controller's Office website at www.sco.ca.gov.

Basic Financial Statements



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Government-wide Financial Statements

Statement of Net Assets

June 30, 2011
(amounts in thousands)

June 30, 2011	Primary Government								
(amounts in thousands)		overnmental		Business-type		_	Component		
		Activities		Activities		Total		Units	
ASSETS		_						_	
Current assets:									
Cash and pooled investments	\$	22,502,134	\$	2,720,440	\$	25,222,574	\$	4,818,120	
Amount on deposit with U.S. Treasury		_		2,855,711		2,855,711		_	
Investments		659,676		2,138,779		2,798,455		8,021,674	
Restricted assets:									
Cash and pooled investments		_		2,773,418		2,773,418		91,958	
Investments		_		_				21,328	
Due from other governments		_		65,598		65,598		_	
Net investment in direct financing leases		_		399,863		399,863		_	
Receivables (net)		11,310,619		798,980		12,109,599		3,730,586	
Internal balances		(868,285)		868,285				_	
Due from primary government		_		_				204,299	
Due from other governments		11,601,567		321,819		11,923,386		734,001	
Prepaid items		107,513		51,252		158,765		2,621	
Inventories		92,328		42,887		135,215		170,700	
Recoverable power costs (net)		_		220,000		220,000		_	
Other current assets		92,036		116,138		208,174		284,364	
Total current assets		45,497,588		13,373,170		58,870,758		18,079,651	
Noncurrent assets:									
Restricted assets:									
Cash and pooled investments		_		1,241,359		1,241,359		100,113	
Investments		_		410,858		410,858		16,052	
Loans receivable		_		238,597		238,597		_	
Investments		_		1,479,984		1,479,984		43,816,511	
Net investment in direct financing leases		_		7,018,573		7,018,573		_	
Receivables (net)		1,757,892		236,649		1,994,541		1,421,223	
Loans receivable		3,383,521		4,102,167		7,485,688		6,494,592	
Recoverable power costs (net)		_		4,809,000		4,809,000		_	
Deferred charges		180,725		944,282		1,125,007		30,033	
Capital assets:									
Land		16,599,386		214,817		16,814,203		928,714	
State highway infrastructure		61,438,984		_		61,438,984		_	
Collections – nondepreciable		22,422		2,697		25,119		332,128	
Buildings and other depreciable property		23,520,649		10,567,993		34,088,642		37,398,584	
Intangible assets – amortizable		648,678		218,547		867,225		508,489	
Less: accumulated depreciation/amortization		(10,114,089)		(4,112,936)		(14,227,025)		(16,751,617)	
Construction in progress		7,814,016		1,521,118		9,335,134		2,959,465	
Intangible assets – nonamortizable		534,092		138,633		672,725		5,090	
Other noncurrent assets		_	_	29,224		29,224	_	800,255	
Total noncurrent assets		105,786,276		29,061,562		134,847,838		78,059,632	
Total assets	\$	151,283,864	\$	42,434,732	\$	193,718,596	\$	96,139,283	
	_	· · ·	_	<u> </u>				<u> </u>	

	Primary Government								
	<u>-</u>	overnmental	E	Business-type			Component		
		Activities		Activities		Total		Units	
LIABILITIES	_		_						
Current liabilities:									
Accounts payable	\$	18,924,834	\$	533,687	\$	19,458,521	\$	2,488,315	
Due to component units	_	204,299	•	_	_	204,299	*		
Due to other governments		7,718,550		180,500		7,899,050		23,688	
Deferred revenue		_		242,254		242,254		1,008,219	
Tax overpayments		5,683,628				5,683,628			
Deposits		476,466		82		476,548		686,586	
Contracts and notes payable		413		_		413		23,345	
Unclaimed property liability		945,360		_		945,360		, <u> </u>	
Advance collections		1,382,542		10,087		1,392,629		96,602	
Interest payable		1,206,982		190,855		1,397,837		102,879	
Securities lending obligations		· · · —		´ _				2,168,485	
Benefits payable		_		793,247		793,247		1,445,032	
Current portion of long-term obligations		3,807,382		2,005,726		5,813,108		1,917,706	
Other current liabilities		484,351		469,302		953,653		2,826,145	
Total current liabilities		40,834,807	_	4,425,740		45,260,547		12,787,002	
Noncurrent liabilities:	_	,	_	.,,		10,200,011		,, , , , , , , , , , , , , , , , ,	
Benefits payable		_		_				15,061,113	
Loans payable		2,122,507		10,957,982		13,080,489		20,000	
Lottery prizes and annuities		2,122,507		886,009		886,009		20,000	
Compensated absences payable		3,720,725		165,470		3,886,195		251,495	
Certificates of participation, commercial paper,		0,720,720		100,470		3,000,193		201,400	
and other borrowings		1,327,876		139,974		1,467,850		77,483	
Capital lease obligations		4,544,008		734,158		5,278,166		2,636,929	
General obligation bonds payable		77,216,976		1,118,559		78,335,535		2,000,020	
Revenue bonds payable		7,358,748		22,091,010		29,449,758		18,932,217	
Net other postemployment benefits obligation		9,606,931		318,793		9,925,724		5,738,777	
Pollution remediation obligation		761,823		5,080		766,903		-	
Other noncurrent liabilities		14,245,999		785,737		15,031,736		3,768,045	
Total noncurrent liabilities	_	120,905,593	_	37,202,772		158,108,365		46,486,059	
Total liabilities		161,740,400	_	41,628,512	_				
NET ASSETS	_	101,740,400	_	41,020,512	_	203,368,912		59,273,061	
		95 460 057		1 202 057		00 040 044		10 100 546	
Investment in capital assets, net of related debt		85,460,957		1,382,957		86,843,914		12,128,546	
Restricted:								4 004 404	
Nonexpendable – endowments		_						4,304,461	
Nonexpendable		_		21,812		21,812		_	
Expendable:								7.040.500	
Endowments and gifts		_		_				7,640,520	
Business and transportation		10,875,076		6,558		10,881,634		1,478,961	
Resources		7,257,940		1,012,430		8,270,370		_	
Health and human services		4,214,342		126,738		4,341,080			
Education		1,490,659		92,604		1,583,263		1,772,420	
General government		3,274,196		511,656		3,785,852		372,088	
Unemployment programs		_		1,810,426		1,810,426			
State and consumer services		749,806		37,530		787,336		1,046,164	
Correctional programs		3,802		18,003		21,805		_	
Workers' compensation liability								5,868,816	
Total expendable		27,865,821		3,615,945		31,481,766		18,178,969	
Unrestricted		(123,783,314)		(4,214,494)		(127,997,808)		2,254,246	
Total net assets (deficit)		(10,456,536)		806,220		(9,650,316)		36,866,222	
Total liabilities and net assets	\$	151,283,864	\$	42,434,732	\$	193,718,596	\$	96,139,283	

Statement of Activities

Year Ended June 30, 2011 (amounts in thousands)

FUNCTIONS/PROGRAMS Expenses Charges for Services Grants and Contributions Grants and Contributions Primary government 8 13,520,557 \$ 5,057,082 \$ 1,344,164 \$ \$ \$ \$ \$ \$ \$ \$ \$ \$ \$ \$ \$ \$ \$ \$ \$ \$ \$	(amounts in thousands)					FIUG	raili nevellues						
Primary governmenta Governmenta Governmenta Governmenta Governmenta Governmenta Governmenta Governmenta Santa Sant	FUNCTIONS/PROGRAMS		Fynenses	fe	•	(Grants and		Capital Frants and				
Governmental activities: General government		_	Ехрепзез		or octvices		ontinbutions		in ibations				
General government													
Education		\$	13 520 557	\$	5 057 082	\$	1 344 164	\$	_				
Health and human services		Ψ		Ψ		Ψ		Ψ	_				
Resources					•				_				
State and consumer services			* *										
Business and transportation							•		_				
Correctional programs					•				 1,272,326				
Interest on long-term debt	•						, ,		1,272,320				
Total governmental activities					14,981		96,885		_				
Business-type activities:	•	_											
Electric Power	_		195,533,434		21,121,640		67,849,215		1,272,326				
Water Resources	• •												
Public Building Construction 390,173 456,467 —							_		_				
State Lottery			1,115,793		1,115,793		_		_				
Unemployment Programs	Public Building Construction		•		456,467		_		_				
California State University 5,851,355 2,505,545 1,216,808 High Technology Education 9,590 10,498 — State Water Pollution Control Revolving 10,953 55,957 — Housing Loan 104,667 89,224 — Other enterprise programs 118,006 105,676 — Total business-type activities 39,044,199 34,819,632 1,216,808 Total primary government \$234,577,633 \$55,941,272 \$69,066,023 \$1,31 Component units: University of California \$24,886,919 \$13,194,408 \$8,480,327 \$2. State Compensation Insurance Fund 1,853,853 1,071,714 — California Housing Finance Agency 621,055 409,297 42,948 Public Employees' Benefits Funds 1,905,816 2,047,922 — Nonmajor component units 2,151,621 1,033,981 624,973 Total component units \$31,419,264 \$17,757,322 \$9,148,248 \$2. General revenues: Personal income taxes Sales and use taxes Corporation taxes Insurance taxes Other taxes Insurance taxes Other taxes Investment and interest Escheat Other. Transfers Total general revenues and transfers Change in net assets Net assets, July 1, 2010	-		3,507,524		3,484,689		_		_				
High Technology Education	Unemployment Programs		25,619,138		24,678,783		_		_				
State Water Pollution Control Revolving	California State University		5,851,355		2,505,545		1,216,808		_				
Housing Loan	High Technology Education		9,590		10,498		_		_				
Other enterprise programs 118,006 105,676 — Total business-type activities 39,044,199 34,819,632 1,216,808 Total primary government \$ 234,577,633 \$ 55,941,272 \$ 69,066,023 \$ 1,33 Component units: University of California \$ 24,886,919 \$ 13,194,408 \$ 8,480,327 \$ 2. State Compensation Insurance Fund 1,853,853 1,071,714 — — California Housing Finance Agency 621,055 409,297 42,948 Public Employees' Benefits Funds 1,905,816 2,047,922 — Nonmajor component units 2,151,621 1,033,981 624,973 5 2. Total component units \$ 31,419,264 \$ 17,757,322 \$ 9,148,248 \$ 2. General revenues: Personal income taxes Sales and use taxes Other taxes Investment and interest Escheat Other Other Transfers Total general revenues and transfers Change in net assets <td colsp<="" td=""><td>State Water Pollution Control Revolving</td><td></td><td>10,953</td><td></td><td>55,957</td><td></td><td>_</td><td></td><td>86,272</td></td>	<td>State Water Pollution Control Revolving</td> <td></td> <td>10,953</td> <td></td> <td>55,957</td> <td></td> <td>_</td> <td></td> <td>86,272</td>	State Water Pollution Control Revolving		10,953		55,957		_		86,272			
Total primary government \$ 39,044,199 \$ 34,819,632 \$ 1,216,808 \$ 1,33	Housing Loan		104,667		89,224		_		_				
Total primary government	Other enterprise programs		118,006		105,676								
Component units: University of California	Total business-type activities		39,044,199		34,819,632		1,216,808		86,272				
University of California \$ 24,886,919 \$ 13,194,408 \$ 8,480,327 \$ 2.5 State Compensation Insurance Fund 1,853,853 1,071,714 — California Housing Finance Agency 621,055 409,297 42,948 Public Employees' Benefits Funds 1,905,816 2,047,922 — Nonmajor component units 2,151,621 1,033,981 624,973 Total component units \$ 31,419,264 \$ 17,757,322 \$ 9,148,248 \$ 2.5 Sales and use taxes Corporation taxes Insurance taxes Other taxes Investment and interest Escheat Other. Transfers Total general revenues and transfers Change in net assets Net assets, July 1, 2010	Total primary government	\$	234,577,633	\$	55,941,272	\$	69,066,023	\$	1,358,598				
University of California \$ 24,886,919 \$ 13,194,408 \$ 8,480,327 \$ 2.5 State Compensation Insurance Fund 1,853,853 1,071,714 — California Housing Finance Agency 621,055 409,297 42,948 Public Employees' Benefits Funds 1,905,816 2,047,922 — Nonmajor component units 2,151,621 1,033,981 624,973 Total component units \$ 31,419,264 \$ 17,757,322 \$ 9,148,248 \$ 2.5 Sales and use taxes Corporation taxes Insurance taxes Other taxes Investment and interest Escheat Other. Transfers Total general revenues and transfers Change in net assets Net assets, July 1, 2010	Component units:												
California Housing Finance Agency 621,055 409,297 42,948 Public Employees' Benefits Funds 1,905,816 2,047,922 — Nonmajor component units 2,151,621 1,033,981 624,973 Total component units \$ 31,419,264 \$ 17,757,322 \$ 9,148,248 \$ 25 General revenues: Personal income taxes Sales and use taxes Corporation taxes Insurance taxes Other taxes Investment and interest Escheat Other Transfers Total general revenues and transfers Change in net assets Net assets, July 1, 2010	•	\$	24,886,919	\$	13,194,408	\$	8,480,327	\$	247,259				
Public Employees' Benefits Funds	State Compensation Insurance Fund		1,853,853		1,071,714		_		_				
Public Employees' Benefits Funds	California Housing Finance Agency		621,055		409,297		42,948		_				
Nonmajor component units 2,151,621 1,033,981 624,973			•		•		´ —		_				
Total component units \$\frac{\\$31,419,264}{\\$}\$. ,						624.973		7,060				
General revenues: Personal income taxes Sales and use taxes Corporation taxes Insurance taxes Other taxes Investment and interest Escheat Other. Transfers Total general revenues and transfers Change in net assets Net assets, July 1, 2010		\$		\$		\$	· · · · · · · · · · · · · · · · · · ·	\$	254,319				
Personal income taxes Sales and use taxes Corporation taxes Insurance taxes Other taxes Investment and interest Escheat Other	Total component anno	=	01,410,204	<u> </u>	17,707,022	<u> </u>	5,140,240	-	204,010				
Sales and use taxes Corporation taxes Insurance taxes Other taxes Investment and interest Escheat Other. Transfers Total general revenues and transfers Change in net assets Net assets, July 1, 2010		Ge	neral revenues:										
Corporation taxes Insurance taxes Other taxes Investment and interest Escheat Other Transfers Total general revenues and transfers Change in net assets Net assets, July 1, 2010		F	ersonal income	taxes									
Insurance taxes Other taxes Investment and interest Escheat Other. Transfers Total general revenues and transfers Change in net assets Net assets, July 1, 2010		S	Sales and use tax	œs									
Other taxes Investment and interest Escheat Other Transfers Total general revenues and transfers Change in net assets Net assets, July 1, 2010		C	Corporation taxes	·									
Investment and interest Escheat Other Transfers Total general revenues and transfers Change in net assets Net assets, July 1, 2010		li	nsurance taxes .										
Escheat Other Transfers Total general revenues and transfers Change in net assets Net assets, July 1, 2010			Other taxes										
Other Transfers Total general revenues and transfers Change in net assets Net assets, July 1, 2010		li	nvestment and in	iterest									
Transfers Total general revenues and transfers Change in net assets Net assets, July 1, 2010		Е	scheat										
Total general revenues and transfers Change in net assets Net assets, July 1, 2010		C	Other										
Change in net assets Net assets, July 1, 2010		Tra	ınsfers										
Change in net assets Net assets, July 1, 2010													
Net assets, July 1, 2010													
		-											
Net assets (deficit), June 30, 2011		•											
* Restated			•), Jun	e 30, 2011	•••••		•••••					

Program Revenues

Net	(Expenses)	Revenues and	Changes i	in Net Assets
-----	------------	--------------	-----------	---------------

	Primary Governmen	t	
Governmental Activities	Business-type Activities	Total	Component Units
\$ (7,119,311)		\$ (7,119,311)	
(48,927,514)		(48,927,514)	
(29,454,423)		(29,454,423)	
(2,598,090)		(2,598,090)	
(707,314)		(707,314)	
(1,922,839)		(1,922,839)	
(10,183,698)		(10,183,698)	
(4,377,064)		(4,377,064)	
(105,290,253)		(105,290,253)	
	\$ —		
	_		
	66,294	66,294	
	(22,835)	(22,835)	
	(940,355)	(940,355)	
	(2,129,002)	(2,129,002)	
	908	908	
	131,276	131,276	
	(15,443)	(15,443)	
	(12,330)	(12,330)	-
(105,290,253)	(2,921,487) (2,921,487)	(2,921,487)	
<u> </u>			-
			\$ (2,964,925
			(782,139
			(168,810
			142,10
			(485,607
			(4,259,375
51,719,107	_	51,719,107	_
33,521,221	_	33,521,221	_
9,384,416	_	9,384,416	_
2,311,880	_	2,311,880	_
7,768,010	_	7,768,010	_
62,946	_	62,946	4,109,189
229,146	_	229,146	_
(0.054.500)			3,040,213
(3,251,598)	3,251,598		
101,745,128	3,251,598	104,996,726	7,149,402
(3,545,125)	330,111	(3,215,014)	
(6,911,411)			
\$ (10,456,536)	\$ 806,220	\$ (9,650,316)	\$ 36,866,222



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Fund Financial Statements

Balance Sheet

Governmental Funds

June 30, 2011 (amounts in thousands)

						Nonmajor	
	General	Federal	Tra	nsportation	G	overnmental	Total
ASSETS							
Cash and pooled investments	\$ 913,703	\$ 342,634	\$	4,034,580	\$	16,504,113	\$ 21,795,030
Investments	_	_		_		659,676	659,676
Receivables (net)	9,302,494	1,034		793,013		1,094,852	11,191,393
Due from other funds	1,193,258	46,245		1,442,199		1,726,953	4,408,655
Due from other governments	382,406	11,009,726		83,257		115,887	11,591,276
Interfund receivables	47,304	_		2,608,626		4,881,517	7,537,447
Loans receivable	159,845	124,879		_		3,098,797	3,383,521
Other assets	 4,643			57,876		29,517	92,036
Total assets	\$ 12,003,653	\$ 11,524,518	\$	9,019,551	\$	28,111,312	\$ 60,659,034
LIABILITIES	 						
Accounts payable	\$ 1,332,391	\$ 1,376,456	\$	447,976	\$	1,667,620	\$ 4,824,443
Due to other funds	10,448,561	7,330,106		92,856		131,573	18,003,096
Due to component units	198,389	_		15		5,156	203,560
Due to other governments	3,171,500	2,663,952		425,675		2,049,456	8,310,583
Interfund payables	8,918,885	_		2,421		16,526	8,937,832
Tax overpayments	5,683,628	_		_		_	5,683,628
Deposits	2,112	_		4,492		469,026	475,630
Advance collections	820,538	8,869		13,683		236,054	1,079,144
Interest payable	_	6,900		_		190,794	197,694
Unclaimed property liability	945,360	_		_		_	945,360
General obligation bonds payable	_	_		_		383,830	383,830
Other liabilities	 421,530	16,681		265,201		152,547	855,959
Total liabilities	 31,942,894	 11,402,964		1,252,319		5,302,582	49,900,759
FUND BALANCES							
Nonspendable	148,019	_		_		39,448	187,467
Restricted	156,496	121,554		7,723,471		19,864,300	27,865,821
Committed	29,850	_		48,525		2,653,177	2,731,552
Assigned	_	_		_		268,888	268,888
Unassigned	 (20,273,606)	 		(4,764)		(17,083)	(20,295,453)
Total fund balances (deficit)	(19,939,241)	121,554		7,767,232		22,808,730	10,758,275
Total liabilities and fund							
balances	\$ 12,003,653	\$ 11,524,518	\$	9,019,551	\$	28,111,312	\$ 60,659,034

Reconciliation of the Governmental Funds Balance Sheet to the Statement of Net Assets

(amounts in thousands)

Total fund balances - governmental funds

\$ 10,758,275

Amounts reported for governmental activities in the Statement of Net Assets are different from those in the Governmental Funds Balance Sheet because:

• Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds.

Land	16,597,328
State highway infrastructure	61,438,984
Collections – nondepreciable	22,422
Buildings and other depreciable property	22,959,145
Intangible assets – amortizable	600,644
Less: accumulated depreciation/amortization	(9,650,127)
Construction in progress	7,794,602
Intangible assets – nonamortizable	534,092

100,297,090

• Other assets are not available to pay for current-period expenditures and, therefore, are not reported.

1,757,892

• Internal service funds are used by management to charge the costs of certain activities, such as architectural, procurement, and technology services, to individual funds. The assets and liabilities of the internal service funds are included in governmental activities in the Statement of Net Assets.

574,355

 Bond discounts, premiums, and deferred issue costs are amortized over the life of the bonds and are included in the governmental activities in the Statement of Net Assets. (350,448)

 General obligation bonds and related accrued interest totaling \$79,080,213, revenue bonds totaling \$7,994,249, and certificates of participation and commercial paper totaling \$1,335,340 are not due and payable in the current period and, therefore, are not reported in the funds. (88,409,802)

• Certain liabilities are not due and payable in the current period; therefore, adjustments to these liabilities are not reported in the funds:

Compensated absences	(3,601,307)
Capital leases	(4,881,488)
Net other postemployment benefits obligation	(9,385,621)
Mandated costs	(5,741,063)
Workers' compensation	(2,660,893)
Loans payable	(2,032,275)
Proposition 98 funding guarantee	(2,636,851)
Net pension obligation	(3,002,637)
Pollution remediation obligations	(804,231)
Other noncurrent liabilities	(337,532)

(35,083,898)

Net assets of governmental activities

(10,456,536)

Statement of Revenues, Expenditures, and Changes in Fund Balances

Governmental Funds

Year Ended June 30, 2011 (amounts in thousands)				Nonmajor	
(amounts in inousanus)	General	Federal	Transportation	Governmental	Total
REVENUES					
Personal income taxes	\$ 50,785,782	\$ —	\$ —	\$ 905,371	\$ 51,691,153
Sales and use taxes	27,013,675	_	327,602	6,147,528	33,488,805
Corporation taxes	9,433,416	_	_	_	9,433,416
Insurance taxes	2,076,804	_	_	235,077	2,311,881
Other taxes	566,241	_	5,467,683	1,795,738	7,829,662
Intergovernmental	_	67,849,164	_	1,311,752	69,160,916
Licenses and permits	1,335,511	_	3,352,528	2,079,398	6,767,437
Charges for services	244,448	_	423,099	341,100	1,008,647
Fees	822,308	_	19,161	8,400,018	9,241,487
Penalties	165,567	52	45,966	809,315	1,020,900
Investment and interest	38,928	1	22,198	150,989	212,116
Escheat	229,133	_	13	_	229,146
Other	768,002	_	63,204	2,110,278	2,941,484
Total revenues	93,479,815	67,849,217	9,721,454	24,286,564	195,337,050
EXPENDITURES					
Current:					
General government	3,423,934	894,403	193,545	8,485,769	12,997,651
Education	43,532,898	9,138,900	2,396	2,872,945	55,547,139
Health and human services	27,783,447	47,880,101	2,740	16,275,021	91,941,309
Resources	879,201	402,608	269,660	3,703,288	5,254,757
State and consumer services	550,020	37,529	93,994	501,993	1,183,536
Business and transportation	8,953	3,805,211	8,895,152	472,074	13,181,390
Correctional programs	9,108,430	8,769	0,000,102	136,592	9,253,791
Capital outlay	204,631		_	923,380	1,128,011
Debt service:	201,001			020,000	1,120,011
Bond and commercial paper retirement	1,793,294	64,785	1,334	1,259,493	3,118,906
Interest and fiscal charges	•	19,509	1,186	1,187,549	4,355,110
•			- -		
Total expenditures Excess (deficiency) of revenues	90,431,674	62,251,815	9,460,007	35,818,104	197,961,600
over (under) expenditures	3,048,141	5,597,402	261,447	(11,531,540)	(2,624,550)
, , ,	3,046,141	5,397,402	201,447	(11,551,540)	(2,024,550)
OTHER FINANCING SOURCES (USES)					
General obligation bonds and commercial			1 400 000	0.050.700	4 505 000
paper issued	- 04 470	_	1,468,300	3,056,700	4,525,000
Premium on bonds issued	31,478	_	102	1,027	32,607
Proceeds from loans	35,538	_	_	_	35,538
Capital leases	204,631	_		7.500.070	204,631
Transfers in	1,176,616		235	7,528,378	8,705,229
Transfers out	(4,944,732)		(942,133)	(448,808)	(11,902,800)
Total other financing sources (uses)	(3,496,469)	(5,567,127)	526,504	10,137,297	1,600,205
Net change in fund balances	(448,328)	30,275	787,951	(1,394,243)	(1,024,345)
Fund balances (deficit), July 1, 2010	(19,490,913)	* 91,279	*6,979,281_	24,202,973	* 11,782,620
Fund balances (deficit), June 30, 2011	\$ (19,939,241)	\$ 121,554	\$ 7,767,232	\$ 22,808,730	\$ 10,758,275
* Restated					

Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances of Governmental Funds to the Statement of Activities

(amounts in thousands)

Net change in fund balances – total governmental funds	\$ (1,024,345)
Amounts reported for governmental activities in the Statement of Activities are different from those in the Statement of Revenues, Expenditures, and Changes in Fund Balances of Governmental Funds because:	
 Governmental funds report capital outlays as expenditures. However, in the Statement of Activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount by which net capital outlays exceed depreciation in the current period. 	2,666,750
• Revenues in the Statement of Activities that do not provide current financial resources are deferred and not reported as revenues in the funds.	(97,143)
 Internal service funds are used by management to charge the costs of certain activities, such as architectural, procurement, and technology services, to individual funds. The net revenue (expense) of the internal service funds is reported with governmental activities. 	45,155
 Bonds and other noncurrent financing instruments provide current financial resources to governmental funds in the form of debt, which increases long-term liabilities in the Statement of Net Assets. Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the Statement of Net Assets. The following amounts represent the difference between proceeds and repayments: 	
General obligation bond (1,564,891)	
Revenue bond 100,846	
Certificates of participation and commercial paper 6,779	
	(1,457,266)
• Some expenses reported in the Statement of Activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds.	
Compensated absences (352,442)	
Capital leases 80,164	
Net other postemployment benefits obligation (2,497,450)	
Mandated costs (642,979)	
Workers' compensation (252,012)	
Loans payable (35,538)	
Proposition 98 funding guarantee 368,842	
Net pension obligation (343,393)	
Pollution remediation obligations (48,619)	
Other noncurrent liabilities 45,151	
	(3,678,276)
Change in net assets of governmental activities	\$ (3,545,125)

Statement of Net Assets

Proprietary Funds

June 30, 2011 (amounts in thousands)

			Dodali - Dodali -
	Electric Power	Water	Public Building
100570	Electric Power	Resources	Construction
ASSETS			
Current assets:			
Cash and pooled investments	\$ —	\$ 464,978	\$ —
Amount on deposit with U.S. Treasury	_	_	_
Investments	_	_	_
Restricted assets:			
Cash and pooled investments	1,751,000	_	955,038
Due from other governments	_	_	_
Net investment in direct financing leases	_	_	377,575
Receivables (net)	_	80,301	170,480
Due from other funds	6,000	2,206	27,199
Due from other governments	_	19,625	_
Prepaid items	_	_	_
Inventories	_	32,984	_
Recoverable power costs (net)	220,000	_	_
Other current assets	116,000		
Total current assets	2,093,000	600,094	1,530,292
Noncurrent assets:			
Restricted assets:			
Cash and pooled investments	907,000	65,689	252,374
Investments	300,000	75,312	23,849
Loans receivable	_	_	_
Investments	_	_	_
Net investment in direct financing leases	_	_	6,585,671
Receivables	_	_	_
Interfund receivables	_	91,517	_
Loans receivable	_	21,040	_
Recoverable power costs (net)	4,809,000	_	_
Deferred charges	_	871,017	62,166
Capital assets:			
Land	_	136,129	_
Collections – nondepreciable	_	, <u> </u>	_
Buildings and other depreciable property	_	4,776,156	_
Intangible assets – amortizable	_	105,605	_
Less: accumulated depreciation/amortization	_	(2,194,406)	_
Construction in progress	_	366,975	794,192
Intangible assets – nonamortizable	_	11,005	
Other noncurrent assets	_	, 3 3 3	_
Total noncurrent assets	6,016,000	4,326,039	7,718,252
Total assets	\$ 8,109,000	\$ 4,926,133	\$ 9,248,544
. 5.41 400010	- 3,103,000	7,020,100	<u> </u>

Activities					Po	pe Activities – Enter					
nternal	ı			Nonmajor	California State Non			employment	Une	State	
vice Funds	Ser	Total		Enterprise	_	University		Programs		Lottery	
707,104	\$	2,720,440	\$	456,687	\$	405,227	\$	1,114,375	\$	279,173	;
_		2,855,711		_		_		2,855,711		_	
_		2,138,779		_		1,958,194		_		180,585	
_		2,773,418		67,380		_		_		_	
_		65,598		65,598		_		_		_	
_		399,863		16,946		5,342		_		_	
119,226		971,951		56,615		159,389		242,655		262,511	
399,837		46,782		6,329		2,170		2,361		517	
10,29		321,819		166,326		_		135,868		_	
107,513		51,252		16		43,801		5,223		2,212	
92,328		42,887		3,188		_		_		6,715	
_		220,000		_		_		_		_	
		116,138		138	_						
1,436,299		12,724,638		839,223	_	2,574,123		4,356,193		731,713	
_		1,241,359		15,386		910		_		_	
_		410,858		11,697		_		_		_	
_		238,597		238,597		_		_		_	
_		1,479,984		32,247		450,532		_		997,205	
_		7,018,573		38,648		394,254		_		_	
_		236,649		_		214,146		22,503		_	
202,245		1,246,997		143,978		161,727		849,775		_	
_		4,102,167		3,985,208		95,919		_		_	
_		4,809,000		_		_		_		_	
_		944,282		8,670		_		_		2,429	
2,05		214,817		1,272		70,947		_		6,469	
_		2,697		_		2,697		_		_	
561,50		10,567,993		70,326		5,562,915		10,748		147,848	
48,034		218,547		1,149		108,201		3,592		_	
(463,963		(4,112,936)		(64,681)		(1,781,417)		(4,620)		(67,812)	
19,414		1,521,118		_		359,951		_		_	
_		138,633		_		1,250		126,378		_	
		29,224		24,150		5,074					
369,293		30,308,559		4,506,647		5,647,106		1,008,376		1,086,139	
1,805,592	\$	43,033,197	\$	5,345,870	\$	8,221,229	\$	5,364,569	\$	1,817,852	\$

Statement of Net Assets (continued)

Proprietary Funds

June 30, 2011 (amounts in thousands)

(amounts in thousands)			
		Water	Public Building
	Electric Power	Resources	Construction
LIABILITIES			
Current liabilities:			
Accounts payable	\$ 174,962	\$ 59,852	\$ 19,450
Due to other funds	_	36,547	62,515
Due to component units	_	_	_
Due to other governments	_	111,004	11,716
Deferred revenue	_	_	_
Deposits	_	_	_
Contracts and notes payable	_	_	_
Advance collections	_	_	6,757
Interest payable	56,000	17,845	99,760
Benefits payable	_	_	_
Current portion of long-term obligations	561,000	181,947	408,191
Other current liabilities		_	<u> </u>
Total current liabilities		407,195	608,389
Noncurrent liabilities:			
Interfund payables	_	_	_
Benefits payable	_	_	_
Loans payable	_	_	_
Lottery prizes and annuities	_	_	_
Compensated absences payable	_	29,052	_
Certificates of participation, commercial paper,		20,002	
and other borrowings	_	54,578	_
Capital lease obligations	_	J+,570	_
General obligation bonds payable		362,375	
Revenue bonds payable	7,275,000	2,346,444	8,425,490
Net other postemployment benefits obligation		97,898	0,425,490
	3,038		_
Pollution remediation obligations	2.000	5,080	_
Other noncurrent liabilities	3,000	418,080	
Total noncurrent liabilities		3,313,507	8,425,490
Total liabilities	8,109,000	3,720,702	9,033,879
NET ASSETS			
Investment in capital assets, net of related debt	_	554,854	_
Restricted:			
Nonexpendable	_	_	_
Expendable:			
Construction	_	650,577	192,140
Debt service	_	_	22,525
Security for revenue bonds	_	_	_
Lottery	_	_	_
Unemployment programs	_	_	_
Other purposes	_	_	_
Total expendable		650,577	214,665
Unrestricted	_	· —	, <u> </u>
Total net assets (deficit)		1,205,431	214,665
` ,	¢ 8 100 000		· · · · · · · · · · · · · · · · · · ·
Total liabilities and net assets	\$ 8,109,000	\$ 4,926,133	\$ 9,248,544

Governmental Activities		 e Funds	rpri	oe Activities – Enter	ess-ty	Busir		
Internal		Nonmajor		California State		Unemploy	State	
Service Funds	Total	Enterprise		University		Progran	ottery	
\$ 207,27	533,048	\$ 52,146	\$	\$ 173,257	4	\$	53,377	\$
146,83	599,104	639		_	,227	222	277,176	
739		_		_	_		_	
54	180,500	22		_	,758	57	_	
_	242,254	74		242,180	_		_	
830	82	82		_	_		_	
15,43		_		_	_		_	
303,39	10,087	193		_	_		3,137	
_	190,855	17,250		_	_		_	
_	793,247	_		_	,247	793	_	
17,22	2,005,726	95,969		292,926	_		465,693	
15,36	469,302	153		328,095	,054	105		
707,65	5,024,205	166,528	_	1,036,458	,290	1,178	799,383	
139,08	_	_		_	_		_	
_		_		_	_		_	
_	10,957,982	_		_	,982	10,957	_	
_	886,009	_		_	_		886,009	
123,18	165,470	2,646		83,641	,165	43	6,966	
_	139,974	_		85,396	_		_	
_	734,158	_		734,158	_		_	
_	1,118,559	756,184		_	_		_	
_	22,091,010	695,959		3,348,117	_		_	
221,31	318,793	4,592		128,545	,312	64	20,408	
_	5,080	_		_	_		_	
39,99	785,737	106,997		255,590			2,070	
523,58	37,202,772	1,566,378		4,635,447	,459_	11,06	915,453	
1,231,23	42,226,977	1,732,906	_	5,671,905	,749	12,243	1,714,836	
141,29	1,382,957	5,689		599,826	,082	136	86,506	
_	21,812	_		21,812	_		_	
_	876,985	_		34,268	_		_	
_	124,237	82,757		18,955	_		_	
_	304,195	304,195		_	_		_	
_	103,016	_		_	_		103,016	
_	1,810,426	_		_	,426	1,810	_	
	397,086	357,705	_	39,381				
_	3,615,945	744,657		92,604	,426	1,810	103,016	
433,06	(4,214,494)	 2,862,618	_	1,835,082	,688)	(8,825	(86,506)	
574,35	806,220	3,612,964	_	2,549,324		(6,879	103,016	
\$ 1,805,592	43,033,197	\$ 5,345,870	\$	\$ 8,221,229	,569		1,817,852	

(concluded)

Statement of Revenues, Expenses, and Changes in Fund Net Assets

Proprietary Funds

Year Ended June 30, 2011 (amounts in thousands)

		Water	Public Building
	Electric Power	Resources	Construction
OPERATING REVENUES			
Unemployment and disability insurance	\$ —	\$ —	\$ —
Lottery ticket sales		_	_
Power sales	1,443,000	193,154	_
Student tuition and fees	_	_	_
Services and sales	_	903,042	_
Investment and interest	_	_	3,864
Rent	_	_	405,832
Grants and contracts	_	_	_
Other			46,771
Total operating revenues	1,443,000	1,096,196	456,467
OPERATING EXPENSES			
Lottery prizes	_	_	_
Power purchases (net of recoverable power costs)	1,401,000	342,446	_
Personal services	_	232,016	_
Supplies	_	_	_
Services and charges	26,000	306,078	507
Depreciation	_	100,257	_
Scholarships & fellowships	_	_	_
Distributions to beneficiaries	_	_	_
Interest expense	_	_	383,185
Amortization of deferred charges	_	_	6,481
Other			
Total operating expenses	1,427,000	980,797	390,173
Operating income (loss)	16,000	115,399	66,294
NONOPERATING REVENUES (EXPENSES)			
Donations and Grants	_	_	_
Private gifts	_	_	_
Investment and interest income	874,000	_	_
Interest expense and fiscal charges	(890,000)	(134,996)	_
Lottery payments for education	_	_	_
Other	_	19,597	_
Total nonoperating revenues (expenses)	(16,000)	(115,399)	
Income (loss) before contributions and transfers	_	_	66,294
Capital contributions	_	_	_
Transfers in	_	_	_
Transfers out	_	_	(32,692)
Change in net assets			33,602
Total net assets (deficit), July 1, 2010		1,205,431	181,063
Total net assets (deficit), June 30, 2011	\$ <u> </u>	\$ 1,205,431	\$ 214,665
* Pactated			

Governmental

		Business-ty	pe Acti	vities – Ente	rprise	Funds		Activities
State	Ur	nemployment		ornia State		Nonmajor		Internal
 Lottery		Programs		University		Enterprise	Total	Service Funds
\$ _	\$	24,655,625	\$	_	\$	_	\$ 24,655,625	\$ —
3,438,578		_		_		_	3,438,578	_
_		_		_		_	1,636,154	_
_		_		1,748,535		_	1,748,535	_
_		_		383,870		111,171	1,398,083	2,398,513
_		_		_		123,777	127,641	_
_		_				16,266	422,098	_
_		_		96,889		_	96,889	_
 			-	174,318		4,063	 225,152	
 3,438,578		24,655,625		2,403,612		255,277	33,748,755	2,398,513
1,904,788		_		_		_	1,904,788	_
_		_		_		_	1,743,446	_
52,084		161,401		3,724,891		16,674	4,187,066	805,991
15,013		_		927,759		_	942,772	7,746
360,000		84,640		_		117,711	894,936	1,438,641
5,875		378		214,757		2,650	323,917	44,181
_		_		802,409		_	802,409	_
_		25,372,719		_		_	25,372,719	_
_		_		_		81,156	464,341	62
_		_		_		2,794	9,275	_
_		_		_		2,400	2,400	_
2,337,760		25,619,138		5,669,816		223,385	36,648,069	2,296,621
 1,100,818	_	(963,513)		(3,266,204)		31,892	(2,899,314)	101,892
_		_		1,216,808		_	1,216,808	_
_		_		30,991		_	30,991	_
46,046		23,158		46,558		4,373	994,135	863
(66,903)		_		(181,539)		(5,996)	(1,279,434)	(905)
(1,102,861)		_		_		_	(1,102,861)	`
66		_		24,384		(12,131)	31,916	(2,668)
(1,123,652)		23,158		1,137,202		(13,754)	(108,445)	(2,710)
(22,834)		(940,355)		(2,129,002)		18,138	(3,007,759)	99,182
_		_		_		86,272	86,272	_
_		616,657		2,703,982		_	3,320,639	397
						(36,349)	(69,041)	(54,424)
(22,834)		(323,698)		574,980		68,061	330,111	45,155
 125,850		(6,555,482)		1,974,344	t	3,544,903 *	 476,109	529,200
\$ 103,016	\$	(6,879,180)	\$	2,549,324	\$	3,612,964	\$ 806,220	\$ 574,355

Statement of Cash Flows

Proprietary Funds

Year Ended June 30, 2011				
(amounts in thousands)				Water
	Ele	ctric Power		Resources
CASH FLOWS FROM OPERATING ACTIVITIES				
Receipts from customers/employers	\$	1,546,000	\$	1,068,964
Receipts from interfund services provided		_		_
Payments to suppliers		(2,182,000)		(526,170)
Payments to employees		_		(232,016)
Payments for interfund services used		_		_
Payments for Lottery prizes		_		_
Claims paid to other than employees				_
Other receipts (payments)		250,000		(3,040)
Net cash provided by (used in) operating activities		(386,000)		307,738
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES				
Changes in interfund payables and loans payable		_		_
Proceeds from bonds		1,923,000		_
Receipts of bond charges		862,000		_
Retirement of general obligation bonds		· —		_
Retirement of revenue bonds		(2,500,000)		_
Interest paid on operating debt		(344,000)		_
Transfers in				_
Transfers out		_		_
Grants received		_		_
Lottery payments for education		_		_
Net cash provided by (used in) noncapital financing activities		(59,000)	_	
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		(55,555)		
Changes in interfund payables and loans payable				_
Acquisition of capital assets				(86,537)
Proceeds from sale of capital assets				(55,557)
Proceeds from notes payable and commercial paper				79,643
Principal paid on notes payable and commercial paper		_		(71,538)
Proceeds from capital leases		_		(71,000)
Payment on capital debt and leases		_		_
Retirement of general obligation bonds		_		(56,375)
Proceeds from revenue bonds		_		111,053
Retirement of revenue bonds				(138,655)
Interest paid		_		(144,406)
Grants received		_		(144,400)
				(206.915)
Net cash provided by (used in) capital and related financing activities		<u></u>		(306,815)
Purchase of investments				(050 174)
		_		(252,174)
Proceeds from maturity and sale of investments		_		252,174
Change in interfund receivables and loans receivable				1,571
Earnings on investments		26,000	_	8,944
Net cash provided by (used in) investing activities		26,000		10,515
Net increase (decrease) in cash and pooled investments		(419,000)		11,438
Cash and pooled investments at July 1, 2010		3,077,000		519,229
Cash and pooled investments at June 30, 2011	\$	2,658,000	\$	530,667
*Restated				

Governmenta Activities		ds	es – Enterprise Fu	ness-type Activiti	Bus	
Internal		Nonmajor	California State	Unemployment	State	ublic Building
Service Funds	Total	Enterprise	University	Programs	Lottery	Construction
0.074.40	00 == 4 = 44	d 400 404	Φ 0.445.400	Φ 04.004.000	Φ 0.407.077	750.070
2,274,49	33,774,741	\$ \$ 160,421	\$ 2,145,168	\$ 24,664,839	\$ 3,437,077	752,272
104,956	1,250	1,250	(1.000.010)	(0.4.0.40)	(1.40.000)	(1.070)
(1,437,493	(4,096,184)	(146,186)	(1,006,616)	(84,640)	(148,893)	(1,679)
(716,285	(4,103,422)	(16,074)	(3,676,731)	(139,133)	(39,468)	_
(72,343	(14,599)	(3,371)	_	_	(11,228)	_
_	(2,200,195)	(0)	_	(05 500 045)	(2,200,195)	_
(00.00)	(25,819,943)	(2)	(070 700)	(25,586,345)	(233,596)	(000 400)
(39,223	(153,555)	 89,574	(678,790)	380,600	138,567	(330,466)
114,10	(2,611,907)	 85,612	(3,216,969)	(764,679)	942,264	420,127
(132	3,786,385	32,746	(1,047)	3,754,686	_	_
_	1,923,000	_	_	_	_	_
_	862,000	_	_	_	_	_
_	(202,750)	(202,750)	_	_	_	_
_	(2,675,155)	(175,155)	_	_	_	_
(14	(351,081)	(7,081)	_	_	_	_
6,39	3,288,684	49	2,671,979	616,656	_	_
(101,079	(71,213)	(38,521)	_	_	_	(32,692)
_	1,208,723	_	1,208,723	_	_	_
	(1,118,081)	 			(1,118,081)	
(94,830	6,650,512	(390,712)	3,879,655	4,371,342	(1,118,081)	(32,692)
_	80	80	_	_		_
(23,83	(1,260,507)	(258)	(596,894)	(93,104)	(49,869)	(433,845)
35,638	3,624	3,152	472	_	_	— (100,010)
_	141,843	_	62,200	_	_	_
(16,222	(71,538)	_		_	_	_
_	20,032	_	20,032	_	_	_
_	(398,759)	_	(398,759)	_	_	_
_	(56,375)	_	_	_	_	_
_	111,053	_	_	_	_	_
_	(533,145)	_	_	_	_	(394,490)
(952	(144,406)	_	_	_	_	
` –	457,908	91,120	366,788	_	_	_
(5,37	(1,730,190)	94,094	(546,161)	(93,104)	(49,869)	(828,335)
	(10 002 025)	_	(6,745,147)	(2,744,881)	(260,723)	_
_	(10,002,925) 7,231,773	35,666	6,498,710	(2,777,001)	445,223	_
(109,169	205,495	24,429	0, 1 30,710	 179,495		_
870	118,721	4,424	30,903	23,158	25,292	_
(108,299	(2,446,936)	64,519	(215,534)	(2,542,228)	209,792	
(94,395	(138,521)	(146,487)	(99,009)	971,331	(15,894)	(440,900)
801,499	6,873,738	685,940	505,146 *	143,044	295,067	1,648,312
707,104	6,735,217	\$ \$ 539,453	\$ 406,137	\$ 1,114,375	\$ 279,173	1,207,412

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Statement of Cash Flows (continued)

Proprietary Funds

Year Ended June 30, 2011		Water
(amounts in thousands)	Electric Power	Resources
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES		
Operating income (loss)	\$ 16,000	\$ 115,399
Adjustments to reconcile operating income (loss) to net cash provided		
by (used in) operating activities:		
Interest expense on operating debt	_	_
Depreciation	_	100,257
Provisions and allowances	_	100,237
Accrual of deferred charges		_
Accidation deletied charges Amortization of discounts	_	_
Amortization of deferred charges	_	83,383
Other	_	•
	_	(3,040)
Change in assets and liabilities: Receivables		4.066
	_	4,266
Due from other funds	_	4 600
Due from other governments	_	4,689
Prepaid items	_	(0.002)
Inventories	_	(9,902)
Net investment in direct financing leases	(366,000)	_
Recoverable power costs (net) Other current assets	, ,	_
Loans receivable	13,000	_
Interfund receivable	_	_
Accounts payable	(49,000)	 14,456
Due to other funds	(49,000)	8,264
Due to component units	_	0,204
Due to other governments		(10,034)
Deposits		(10,034)
Contracts and notes payable		
Advance collections		
Interest payable	_	_
Other current liabilities	_	_
Interfund payables	_	_
Deferred revenue	_	_
Benefits payable	_	_
Lottery prizes and annuities	_	_
Compensated absences payable	_	_
Capital lease obligations	_	_
Other noncurrent liabilities	_	_
Total adjustments	(402,000)	192,339
Net cash provided by (used in) operating activities		\$ 307,738
Net cash provided by (used in) operating activities	\$ (300,000)	9 307,730
Name and investigation could and financian activities		
Noncash investing, capital, and financing activities Interest accreted on annuitized prizes	¢	\$ —
Interest accreted on bonds	т	Ф —
	_	_
Unclaimed Lottery prizes directly transferred to Education Fund	_	_
Capital acquisitions financed through notes payable	_	_
Capital acquisitions infanced through notes payable	_	_
Acquisition of capital asset through capital lease	_	_
Direct deposit of debt to auxiliaries		
Change in accrued capital assets purchases		
Gifts in-kind	_	_
Miscellaneous related to auxiliary organizations and capital assets	_	_
Amortization of bond premium and discount		
Amortization of bond premium and discount Amortization of loss on refundings	_	_
Amortization or loss on returnings		_

ernmenta ctivities			Business-type Activities – Enterprise Funds											
nternal					Nonmajor		lifornia State		employment		State		ic Building	Publi
vice Funds		Total			Enterprise		University		Programs		Lottery		struction	
				_	•									
101,892	\$	(2,899,314)	\$	2	31,892	\$	(3,266,204)	\$	(963,513)	\$	1,100,818	\$	66,294	\$
(42				_	_		_		_		_		_	
44,181		323,917)	2,650		214,757		378		5,875		_	
_		23,265		2	9,592		_		_		13,673		_	
_		194		-	_		_		_		_		194	
_		87		7	87		_		_		_		_	
_		96,519		3	6,898		_		_		(243)		6,481	
_		(6,817)		3)	(4,393)		_		_		5,654		(5,038)	
(12,322		(88,640)		9	1,749		(55,319)		(4,154)		(35,915)		733	
80,003		133,693		9)	(769)		_		146,376		286		(12,200)	
402		(41,119)		2)	(42)		_		(45,766)		_		_	
(9,053		348		1	231		117		_		_		_	
9,158		(11,629)			173		_		_		(1,900)		_	
_		376,219		4	14,844		_		_		_		361,375	
_		(366,000)		-			_		_		_		_	
_		14,102			1,698		_		_		(596)		_	
_		64,060			64,060				_		_		_	
		(157,422)			(9,062)		(161,727)		13,367					
(15,710		(55,265)			(17,147)		(12,990)				9,527		(111)	
(85,899 12		238,700)) -	(3,550)		_		232,857		37		1,092	
325		10,304		5	15		_		21,492		_		(1,169)	
(5,694		210			(2)		212				_		(·,····)	
(1,061							_		_		_		_	
(72,814		(2,340)		5)	(85)		_		_		413		(2,668)	
_		5,054))	(90)		_		_		_		5,144	
9,854		43,148		5)	(4,225)		15,323		32,050		_		_	
476		_		-	_		_		_		_		_	
_		19,613		3)	(83)		19,696		_		_		_	
(6,044		(222,531)		3)	(2,586)		_		(219,945)		_		_	
		(156,968)		-					_		(156,968)		_	
18,523		(2,281)		5)	(345)		(9,322)		6,332		1,054		_	
(4,893				-	(5.000)		_						_	
62,811		48,986			(5,898)	_	38,488		15,847	_	549			
12,213		287,407	Φ.	_	53,720	_	49,235		198,834	_	(158,554)	•	353,833	
114,105 (concluded	\$	(2,611,907)	\$	<u> </u>	85,612	\$	(3,216,969)	\$	(764,679)	\$	942,264	\$	420,127	<u>\$</u>
	¢	66 003	¢		_	\$	_	\$	_	\$	66,903	\$	_	\$
_	\$	66,903 23,652	\$	_	_	Ψ	_	Ψ	_	φ	23,652	φ	_	Ψ
_		25,690		_			_		_		25,690		_	
_		3,315		_			_		_		3,315		_	
6,412				_	_		_		_		-		_	
		14,089		_	_		14,089		_		_		_	
_		16,850		-	_		16,850		_		_		_	
_		27,775		-	_		27,775		_		_		_	
_		27,590		-	_		27,590		_		_		_	
_		3,756		-	_		3,756		_		_		_	
_		1,075		-	_		1,075		_		_		_	
_		3,430		-	_		3,430		_		_		_	
_		1,145		-	_		1,145		_		_		_	

Statement of Fiduciary Net Assets

Fiduciary Funds and Similar Component Units

June 30, 2011 (amounts in thousands)

	Pi	Private urpose Trust		Pension and Other Employee Benefit Trust	Lo	nvestment Trust ocal Agency nvestment		Agency
ASSETS		Trust	_	Trust		iivestilient		Agency
Cash and pooled investments	¢	105,099	\$	2,832,498	\$	04.010.070	\$	4,251,563
Investments, at fair value:	\$	105,099	φ	2,032,490	Φ	24,012,079	φ	4,251,565
Short-term		_		9,435,064				
Equity securities		67,810		199,712,591				_
Debt securities		07,010		82,141,888		_		_
Real estate		_		38,232,098		_		_
Other		4,453,712		76,824,884		_		_
Securities lending collateral		4,455,712		45,620,619		_		_
Total investments	-	4,521,522	_	451,967,144	-			
Receivables (net)		13,218		3,787,609				479,549
Due from other funds		15,216		423,144				13,470,613
Due from other governments		62		8		_		118,459
Prepaid Items		- 02		_		_		27,142
Interfund receivables		_		_		_		90,232
Loans receivable								6,875
Other assets		157,260		934,920				130
			_		_		_	
Total assets		4,797,163	_	459,945,323		24,012,079	\$	18,444,563
LIABILITIES								
Accounts payable		14,204		1,966,332		_	\$	5,448,842
Due to other governments		_		2,356		30,207		11,083,541
Tax overpayments		_		_		_		2,995
Benefits payable		_		2,189,941		_		169,165
Deposits		157,259		_		_		800,521
Advance collections		_		_		_		86,251
Securities lending obligations		_		45,537,244		_		_
Loans payables		_		25,985		_		_
Other liabilities		519		599,699				853,248
Total liabilities		171,982		50,321,557		30,207	\$	18,444,563
NET ASSETS								
Held in trust for pension benefits, pool participants,								
and other purposes	\$	4,625,181	\$_	409,623,766	\$_	23,981,872		

Statement of Changes in Fiduciary Net Assets

Fiduciary Funds and Similar Component Units

Year Ended June 30, 2011 (amounts in thousands)

			Pension		
			and Other		Investment
	Private		Employee		Trust
	Purpose	Benefit			ocal Agency
	Trust		Trust		Investment
ADDITIONS					
Contributions:					
Employer	\$ _	\$	12,023,723	\$	_
Plan member	_		6,699,601		_
Total contributions	_		18,723,324		_
Investment income:					
Net appreciation in fair value of investments	485,844		68,271,940		_
Interest, dividends, and other investment income	132,765		10,229,583		112,656
Less: investment expense	(8,022)		(2,723,168)		_
Net investment income	610,587		75,778,355		112,656
Receipts from depositors	1,532,447		_		28,342,052
Other	 		25,790		
Total additions	2,143,034		94,527,469		28,454,708
DEDUCTIONS					
Distributions paid and payable to participants	_		25,119,671		111,096
Refunds of contributions	_		349,567		_
Administrative expense	22		491,202		1,560
Payments to and for depositors	 1,123,733		592,436		27,623,778
Total deductions	1,123,755		26,552,876		27,736,434
Change in net assets	1,019,279		67,974,593		718,274
Net assets, July 1, 2010	 3,605,902		341,649,173	*	23,263,598
Net assets, June 30, 2011	\$ 4,625,181	\$	409,623,766	\$_	23,981,872
* Destated	·		· · · · · · · · · · · · · · · · · · ·		<u></u>

^{*} Restated



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Discretely Presented Component Units Financial Statements

Statement of Net Assets

Discretely Presented Component Units – Enterprise Activity

June 30, 2011 (amounts in thousands)	University	State	California Housing	Public	Nonmajor	
	of	Compensation	Finance	Employees'	Component	
	California	Insurance	Agency	Benefits	Units	Total
ASSETS						
Current assets:						
Cash and pooled investments	\$ 285,350	\$ 1,016,798	\$ 2,620,139	\$ 220,808	\$ 675,025	\$ 4,818,120
Investments	5,854,981	1,616,110	314,851	6,119	229,613	8,021,674
Restricted assets:						
Cash and pooled investments	_	_	_	_	91,958	91,958
Investments	_	_	_	_	21,328	21,328
Receivables (net)	2,656,059	374,146	246,277	67,014	387,090	3,730,586
Due from primary government	203,541	_	_	571	187	204,299
Due from other governments	687,488	_	_	46,513	_	734,001
Prepaid items	_	_	463	_	2,158	2,621
Inventories	170,358	_	_	_	342	170,700
Other current assets	183,839	8,690	51,972		39,863	284,364
Total current assets	10,041,616	3,015,744	3,233,702	341,025	1,447,564	18,079,651
Noncurrent assets:						
Restricted assets:						
Cash and pooled investments	_	_	_	_	100,113	100,113
Investments	_	_	_	_	16,052	16,052
Investments	20,746,897	17,669,997	378,608	3,730,540	1,290,469	43,816,511
Receivables (net)	952,590	151,080	_	_	317,553	1,421,223
Loans receivable	_	_	6,149,078	_	345,514	6,494,592
Deferred charges	_	_	28,689	_	1,344	30,033
Capital assets:						
Land	742,021	64,873	_	_	121,820	928,714
Collections – nondepreciable	326,508	_	_	_	5,620	332,128
Buildings and other depreciable						
property	34,917,390	557,565	2,008	_	1,921,621	37,398,584
Intangible assets – amortizable	334,516	155,982	_	_	17,991	508,489
Less: accumulated						
depreciation/amortization	(15,551,800)	(356,318)	(894)	_	(842,605)	(16,751,617)
Construction in progress	2,941,642	_	_	_	17,823	2,959,465
Intangible assets – nonamortizable	_	_	_	_	5,090	5,090
Other noncurrent assets	341,752		405,032		53,471	800,255
Total noncurrent assets	45,751,516	18,243,179	6,962,521	3,730,540	3,371,876	78,059,632
Total assets	\$ 55,793,132	\$ 21,258,923	\$ 10,196,223	\$ 4,071,565	\$ 4,819,440	\$ 96,139,283

	University of California	State Compensation Insurance	California Housing Finance Agency	Public Employees' Benefits	Nonmajor Component Units	Total
LIABILITIES						
Current liabilities:						
Accounts payable	\$ 1,862,653	\$ 48,440	\$ 13,810	\$ 420,306	\$ 143,106	\$ 2,488,315
Due to other governments	_	_	23,222	_	466	23,688
Deferred revenue	934,801	_	_	_	73,418	1,008,219
Deposits	463,547	_	220,244	_	2,795	686,586
Contracts and notes payable	_	_	_	_	23,345	23,345
Advance collections	_	69,148	26,931	_	523	96,602
Interest payable	_	_	100,679	_	2,200	102,879
Securities lending obligations	2,168,485	_	_	_	_	2,168,485
Benefits payable	_	1,445,032	_	_	_	1,445,032
Current portion of long-term						
obligations	1,457,064	72,258	178,326	55,041	155,017	1,917,706
Other current liabilities	2,277,909	85,433	113,110	144,961	204,732	2,826,145
Total current liabilities	9,164,459	1,720,311	676,322	620,308	605,602	12,787,002
Noncurrent liabilities:						
Benefits payable	_	12,666,163	_	2,394,950	_	15,061,113
Loans payable	_	_	_	_	20,000	20,000
Compensated absences payable	239,462	_	_	_	12,033	251,495
Certificates of participation,						
commercial paper, and						
other borrowings	_	_	_	_	77,483	77,483
Capital lease obligations	2,273,338	_	_	_	363,591	2,636,929
Revenue bonds payable	10,653,749	_	7,768,042	_	510,426	18,932,217
Net other postemployment						
benefits obligation	5,257,422	312,864	9,939	10,143	148,409	5,738,777
Other noncurrent liabilities		268,667	261,845		207,538	3,768,045
Total noncurrent liabilities	21,453,966	13,247,694	8,039,826	2,405,093	1,339,480	46,486,059
Total liabilities	30,618,425	14,968,005	8,716,148	3,025,401	1,945,082	59,273,061
NET ASSETS						
Investment in capital assets, net of						
related debt	11,161,810	422,102	1,114	_	543,520	12,128,546
Restricted:						
Nonexpendable	3,475,226	_	_	_	829,235	4,304,461
Expendable:						
Endowments and gifts	7,631,367	_	_	_	9,153	7,640,520
Education	1,106,797	_	_	_	647,319	1,754,116
Indenture	_	_	339,441	_	_	339,441
Employee benefits	_	_	_	1,046,164	_	1,046,164
Workers' compensation liability	_	5,868,816	_	_	_	5,868,816
Statute	_	_	1,139,520	_	270,736	1,410,256
Other purposes					119,656	119,656
Total expendable	8,738,164	5,868,816	1,478,961	1,046,164	1,046,864	18,178,969
Unrestricted	1,799,507				454,739	2,254,246
Total net assets	25,174,707	6,290,918	1,480,075	1,046,164	2,874,358	36,866,222
Total liabilities and net assets	\$ 55,793,132	\$ 21,258,923	\$ 10,196,223	\$ 4,071,565	\$ 4,819,440	\$ 96,139,283

Statement of Activities

Discretely Presented Component Units – Enterprise Activity

Year Ended June 30, 2011 (amounts in thousands)

		State	California			
	University	Compensation	Housing	Public	Nonmajor	
	of	Insurance	Finance	Employees'	Component	
	California	Fund	Agency	Benefits	Units	Total
OPERATING EXPENSES						
Personal services	\$ 15,763,785	\$ 693,446	\$ 30,447	\$ —	\$ 530,158	\$ 17,017,836
Scholarships and fellowships	597,350	_	_	_	46,284	643,634
Supplies	2,107,881	_	_	_	8,039	2,115,920
Services and charges	280,995	86,891	25,906	1,905,816	1,311,067	3,610,675
Department of Energy laboratories	970,054	_	_	_	_	970,054
Depreciation	1,404,837	33,026	248	_	72,116	1,510,227
Distributions to beneficiaries	_	850,439	_	_	_	850,439
Interest expense and fiscal charges	572,412	_	249,253	_	46,876	868,541
Amortization of deferred charges	_	97,061	62,858	_	152	160,071
Grants provided	144,235	_	_	_	_	144,235
Other	3,045,370	92,990	252,343		136,929	3,527,632
Total operating expenses	24,886,919	1,853,853	621,055	1,905,816	2,151,621	31,419,264
PROGRAM REVENUES						
Charges for services	13,194,408	1,071,714	409,297	2,047,922	1,033,981	17,757,322
Operating grants and contributions	8,480,327	_	42,948	_	624,973	9,148,248
Capital grants and contributions	247,259				7,060	254,319
Total program revenues	21,921,994	1,071,714	452,245	2,047,922	1,666,014	27,159,889
Net revenues (expenses)	(2,964,925)	(782,139)	(168,810)	142,106	(485,607)	(4,259,375)
GENERAL REVENUES						
Investment and interest income (loss)	2,161,329	1,166,327	(4,851)	560,596	225,788	4,109,189
Other	2,443,574	121,390	99,753	42,691	332,805	3,040,213
Total general revenues	4,604,903	1,287,717	94,902	603,287	558,593	7,149,402
Change in net assets	1,639,978	505,578	(73,908)	745,393	72,986	2,890,027
Net assets, July 1, 2010	23,534,729	5,785,340	1,553,983	300,771	2,801,372 *	33,976,195
Net assets, June 30, 2011	\$ 25,174,707	\$ 6,290,918	\$ 1,480,075	\$ 1,046,164	\$ 2,874,358	\$ 36,866,222
* 5						

^{*} Restated

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Notes to the Financial Statements

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statements present information on the financial activities of the State of California over which the Governor, the Legislature, and other elected officials have direct or indirect governing and fiscal control. These financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP). The provisions of the following Governmental Accounting Standards Board (GASB) Statements have been implemented for the year ended June 30, 2011:

GASB Statement No. 54, Fund Balance Reporting and Governmental Fund Type Definitions; and

GASB Statement No. 59, Financial Instruments Omnibus.

A. Reporting Entity

These financial statements present the primary government of the State and its component units. The **primary government** consists of all funds, organizations, institutions, agencies, departments, and offices that are not legally separate from the State. **Component units** are organizations that are legally separate from the State but for which the State is financially accountable or organizations whose relationship with the State is such that exclusion would cause the State's financial statements to be misleading or incomplete. The decision to include a component unit in the State's reporting entity is based on several criteria, including legal standing, fiscal dependency, and financial accountability. Following is information on the blended, fiduciary, and discretely presented component units of the State.

1. Blended Component Units

Blended component units, although legally separate entities, are in substance part of the primary government's operations. Therefore, data from these blended component units are integrated into the appropriate funds for reporting purposes.

Building authorities are blended component units because they have been created through the use of joint exercise-of-powers agreements with various cities to finance the construction of state buildings. The building authorities are reported as capital projects funds. As a result, capital lease arrangements between the building authorities and the State in the amount of \$501 million have been eliminated from the financial statements. Instead, only the underlying capital assets and the debt used to acquire them are reported in the government-wide financial statements. For information on how to obtain copies of the financial statements of the building authorities, contact the State Controller's Office, Division of Accounting and Reporting, P.O. Box 942850, Sacramento, California 94250-5872.

The Golden State Tobacco Securitization Corporation (GSTSC) is a not-for-profit corporation established through legislation in September 2002 solely for the purpose of purchasing Tobacco Settlement Revenues from the State. The five voting members of the State Public Works Board serve ex officio as the directors of the corporation. GSTSC is authorized to issue bonds necessary to provide sufficient funds for carrying out its purpose. GSTSC is reported in the combining statements in the Nonmajor Governmental Funds section as a special revenue fund. For information on how to obtain copies of the financial statements of GSTSC, contact

the Department of Finance, Natural Resources, Energy, Environmental, and Capital Outlay Section, 915 L Street, 9th Floor, Sacramento, California 94814.

2. Fiduciary Component Units

The State has two fiduciary component units that administer pension and other employee benefit trust funds. These entities are legally separate from the State and meet the definition of a component unit because they are fiscally dependent on the State; however, due to their fiduciary nature, they are presented in the Fiduciary Fund Statements as pension and other employee benefit trust funds, along with other primary government fiduciary funds.

The California Public Employees' Retirement System (CalPERS) administers pension and health benefit plans for state employees, non-teaching school employees, and employees of California public agencies. Its Board of Administration has plenary authority and fiduciary responsibility for the investment of monies and the administration of the plans. CalPERS administers the following seven pension and other employee benefit trust funds: the Public Employees' Retirement Fund, the Judges' Retirement Fund, the Judges' Retirement Fund, the Legislators' Retirement Fund, the State Peace Officers' and Firefighters' Defined Contribution Plan Fund, the public agency Deferred Compensation Program, and the public employee Supplemental Contributions Program Fund. Copies of CalPERS' separately issued financial statements may be obtained in writing from the California Public Employees' Retirement System, Fiscal Services Division, P.O. Box 942703, Sacramento, California 94229-2703.

The *California State Teachers' Retirement System (CalSTRS)* administers pension benefit plans for California public school teachers and certain other employees of the public school system. CalSTRS administers four pension and other employee benefit trust funds: the State Teachers' Retirement Fund; the Teachers' Health Benefits Fund; the Pension2 Program; and the Teachers' Deferred Compensation Fund. Copies of CalSTRS' separately issued financial statements may be obtained from the California State Teachers' Retirement System, P.O. Box 15275, Sacramento, California 95851-0275.

3. Discretely Presented Component Units

Enterprise activity of discretely presented component units is reported in a separate column in the government-wide financial statements. Discretely presented component units are legally separate from the primary government and mostly provide services to entities and individuals outside the primary government. Discretely presented component units that report enterprise activity include the University of California, the State Compensation Insurance Fund, the California Housing Finance Agency, the Public Employees' Benefits Fund, and nonmajor component units.

The *University of California* was founded in 1868 as a public, state-supported, land grant institution. It was written into the State Constitution of 1879 as a public trust to be administered by a governing board, the Regents of the University of California (the Regents). The University of California is a component unit of the State because the State appoints a voting majority of the Regents and because expenditures for the support of various university programs and capital outlay are appropriated by the annual Budget Act. The University of California offers defined benefit pension plans and defined contribution pension plans to its employees through the University of California Retirement System (UCRS), a fiduciary responsibility of the Regents. The financial information of the UCRS is not included in the financial statements of this report due to its fiduciary nature. Copies of the University of California's financial statements may be obtained from the University of California, Financial Accounting, 1111 Franklin Street, 10th Floor, Oakland, California 94607-5200.

The State Compensation Insurance Fund (SCIF) is a self-supporting enterprise created to offer insurance protection to employers at the lowest possible cost. It operates in competition with other insurance carriers to provide services to the State, counties, cities, school districts, and corporations. It is a component unit of the State because the State appoints all 11 voting members of SCIF's governing board and has the authority to approve or modify SCIF's budget. Copies of SCIF's financial statements for the year ended December 31, 2010, may be obtained from the State Compensation Insurance Fund, P.O. Box 420807, San Francisco, California 94142-0807.

The California Housing Finance Agency (CalHFA) was created by the Zenovich-Moscone-Chacon Housing and Home Finance Act, as amended. CalHFA's purpose is financing the housing needs of persons and families of low and moderate income. It is a component unit of the State because the State appoints a voting majority of CalHFA's governing board and has the authority to approve or modify its budget. Copies of CalHFA's financial statements may be obtained from the California Housing Finance Agency, P.O. Box 4034, Sacramento, California 95812.

The *Public Employees' Benefits Fund*, which is administered by the California Public Employees' Retirement System, accounts for contributions and premiums for public employee long-term care plans and for administration of a deferred compensation program. Copies of CalPERS' separately issued financial statements may be obtained in writing from the California Public Employees' Retirement System, Fiscal Services Division, P.O. Box 942703, Sacramento, California 94229-2703.

State legislation created various *nonmajor component units* to provide certain services outside the primary government and to provide certain private and public entities with a low-cost source of financing for programs deemed to be in the public interest. The California Pollution Control Financing Authority, the San Joaquin River Conservancy, and the district agricultural associations are considered component units because they have a fiscal dependency on the primary government. The California Educational Facilities Authority is considered a component unit because its exclusion from the financial statements would be misleading because of its relationship to the primary government. California State University auxiliary organizations are considered component units because they exist entirely or almost entirely for the direct benefit of the universities. The remaining nonmajor component units are considered component units because the majority of members of their governing boards are appointed by or are members of the primary government, because the primary government can impose its will on the entity, or because the entity provides a specific financial benefit to the primary government. For information on how to obtain copies of the financial statements of these component units, contact the State Controller's Office, Division of Accounting and Reporting, P.O. Box 942850, Sacramento, California 94250-5872.

The nonmajor component units are:

The California Alternative Energy and Advanced Transportation Financing Authority, which provides financing for alternative energy and advanced transportation technologies;

The California Infrastructure and Economic Development Bank, which provides financing for business development and public improvements;

The California Pollution Control Financing Authority, which provides financing for pollution control facilities;

The California Health Facilities Financing Authority, which provides financing for the construction, equipping, and acquisition of health facilities;

The California Educational Facilities Authority, which issues revenue bonds to finance loans for students attending public and private nonprofit colleges and universities and to assist private educational institutions of higher learning in financing the expansion and construction of educational facilities (the EdFund financial report included in this entity is as of and for the year ended September 30, 2010);

The *California School Finance Authority*, which provides loans to school and community college districts to assist them in obtaining equipment and facilities;

California State University auxiliary organizations, which provide services primarily to university students through foundations, associated student organizations, student unions, food service entities, book stores, and similar organizations;

District agricultural associations, which exhibit all of the industries, industrial enterprises, resources, and products of the state (the district agricultural association's financial report is as of and for the year ended December 31, 2010);

The *University of California Hastings College of the Law*, which was established as the law department of the University of California to provide legal education programs and operates independently under its own board of directors. The college has a discretely presented component unit, the Foundation, that provides private sources of funds for academic programs, scholarships, and faculty research;

The San Joaquin River Conservancy, which was created to acquire and manage public lands within the San Joaquin River Parkway;

The State Assistance Fund for Enterprise, Business and Industrial Development Corporation, which provides financial assistance to small business; and

The California Urban Waterfront Area Restoration Financing Authority, which provides financing for coastal and inland urban waterfront restoration projects.

4. Joint Venture

A joint venture is an entity resulting from a contractual arrangement; it is owned, operated, or governed by two or more participants as a separate and specific activity subject to joint control. In such an arrangement, the participants retain an ongoing financial interest or an ongoing financial responsibility in the entity. These entities are not part of the primary government or a component unit.

The State participates in a joint venture called the *Capitol Area Development Authority (CADA)*. CADA was created in 1978 by the joint exercise of powers agreement between the primary government and the City of Sacramento for the location of state buildings and other improvements. CADA is a public entity, separate from the primary government and the city, and is administered by a board of five members: two appointed by the primary government, two appointed by the city, and one appointed by the affirmative vote of at least three of the other four members of the board. The primary government designates the chairperson of the board. Although the primary government does not have an equity interest in CADA, it does have an ongoing financial interest. Based upon the appointment authority, the primary government has the ability to indirectly influence CADA to undertake special projects for the citizenry of the participants. The primary government subsidizes CADA's operations by leasing land to CADA without consideration; however, the primary government is not obligated to do so. At June 30, 2011, CADA had total assets of \$37.3 million, total liabilities of \$21.2 million, and total net assets of \$16.1 million. Total revenues for the fiscal year were \$10.6 million and expenses were \$9.2 million, resulting in a change in net assets of \$1.4 million. Because the primary government does not

have an equity interest in CADA, CADA's financial information is not included in the financial statements of this report. Separately issued financial statements may be obtained from the Capitol Area Development Authority, 1522 14th Street, Sacramento, California 95814-5958.

5. Related Organizations

A related organization is an organization for which a primary government is accountable because that government appoints a voting majority of the organization's governing board, but for which it is not financially accountable.

Chapter 854 of the Statutes of 1996 created an *Independent System Operator*, a state-chartered, nonprofit market institution. The Independent System Operator provides centralized control of the statewide electrical transmission grid to ensure the efficient use and reliable operation of the transmission system. The Independent System Operator is governed by a five-member board, the members of which are appointed by the Governor and confirmed by the Senate. The State's accountability for this institution does not extend beyond making the initial oversight board appointments. Because the primary government is not financially accountable for the Independent System Operator, the financial information of this institution is not included in the financial statements of this report. For information on how to obtain copies of the financial statements of the Independent System Operator, contact the State Controller's Office, Division of Accounting and Reporting, P.O. Box 942850, Sacramento, California 94250-5872.

The California Earthquake Authority (CEA), a legally separate organization, offers earthquake insurance for California homeowners, renters, condominium owners, and mobile home owners. A three-member board of state-elected officials governs the CEA. The State's accountability for this institution does not extend beyond making the appointments. Because the primary government is not financially accountable for the CEA, the financial information of this institution is not included in the financial statements of this report. For information on how to obtain copies of the financial statements of the CEA, contact the California Earthquake Authority, 801 K Street, Suite 1000, Sacramento, California 95814.

The Bay Area Toll Authority (BATA), which is not part of the State's reporting entity, was created by the California Legislature in 1997 to administer a portion of the toll revenues collected from the San Francisco Bay Area's seven state-owned toll bridges and to have program oversight related to certain bridge construction projects. In 2005, the California Legislature transferred toll-bridge administration responsibility from the California Department of Transportation (Caltrans) to BATA. This responsibility includes consolidation of all toll-bridge revenue under BATA's administration. BATA is a blended component unit of the Metropolitan Transportation Commission. Additional information may be obtained from the Metropolitan Transportation Commission, 101 Eighth Street, Oakland, California 94607.

B. Government-wide and Fund Financial Statements

Government-wide financial statements (the Statement of Net Assets and the Statement of Activities) give information on all the nonfiduciary activities of the primary government and its component units. The primary government is reported separately from legally separate component units for which the State is financially accountable. Within the primary government, the State's governmental activities, which are normally supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. The effect of interfund activity has been removed from the statements, with the exception of amounts between governmental and business-type activities, which are presented as internal balances and transfers. Centralized services provided by the General Fund for other funds are charged as direct costs to the funds that received those services. Also, the General Fund recovers the cost of centralized services provided to federal programs from the federal government.

The Statement of Net Assets reports all of the financial and capital resources of the government as a whole in a format where assets equal liabilities plus net assets. The statement of activities demonstrates the degree to which the expenses of a given function are offset by program revenues. Program revenues include charges to customers who purchase, use, or directly benefit from goods, services, or privileges provided by a given function. Program revenues also include grants and contributions that are restricted to meeting the operational or capital requirements of a particular function. Taxes and other items that are not program-related are reported as general revenues.

Fund financial statements are provided for governmental funds, proprietary funds, fiduciary funds and similar component units, and discretely presented component units. A fund is a fiscal and accounting entity with a self-balancing set of accounts. Fund accounting segregates funds according to their intended purpose and is used to aid management in demonstrating compliance with finance-related legal and contractual provisions. The State maintains the minimum number of funds consistent with legal and managerial requirements. Fiduciary funds, although excluded from the government-wide statements, are included in the fund financial statements. Major governmental and enterprise funds are reported in separate columns in the fund financial statements. Nonmajor governmental and proprietary funds are grouped into separate columns. Discretely presented component unit statements, which follow the fiduciary fund statements, also separately report the enterprise activity of the major discretely presented component units. In this report, the enterprise activity of nonmajor discretely presented component units is grouped in a separate column.

Governmental fund types are used primarily to account for services provided to the general public without direct charge.

The State reports the following major governmental funds.

The *General Fund* is the main operating fund of the State. It accounts for transactions related to resources obtained and used for those services that do not need to be accounted for in another fund.

The *Federal Fund* accounts for the receipt and use of grants, entitlements, and shared revenues received from the federal government.

The *Transportation Fund* accounts for fuel taxes, including the State's diesel, motor vehicle, and fuel use taxes; bond proceeds; automobile registration fees; and other revenues that are used for transportation purposes, including highway and passenger rail construction and transportation safety programs.

Proprietary fund types focus on the determination of operating income, changes in net assets, financial position, and cash flows.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

For its proprietary funds, the State applies all applicable GASB pronouncements. In addition, the State applies all applicable Financial Accounting Standards Board (FASB) Statements and Interpretations, Accounting Principles Board (APB) Opinions, and Committee on Accounting Procedure (CAP) Accounting Research Bulletins issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements. The State has elected not to apply FASB pronouncements issued after November 30, 1989, for its enterprise funds.

The State has two proprietary fund types: enterprise funds and internal service funds.

Enterprise funds record business-type activity for which a fee is charged to external users for goods and services. In addition, the State is required to report activities as enterprise funds in the context of the activity's principal revenue sources when any of the following criteria are met:

- The activity's debt is secured solely by fees and charges of the activity;
- There is a legal requirement to recover costs; or
- The pricing policies of fees and charges are designed to recover costs.

The State reports the following major enterprise funds.

The *Electric Power Fund* accounts for the acquisition and resale of electric power to retail end-use customers.

The Water Resources Fund accounts for charges to local water districts and the sale of excess power to public utilities.

The Public Building Construction Fund accounts for rental charges from the lease of public assets.

The State Lottery Fund accounts for the sale of California State Lottery (Lottery) tickets and the Lottery's payments for education.

The *California State University Fund* accounts for student fees and other receipts from gifts, bequests, donations, federal and state grants, and loans that are used for educational purposes.

The *Unemployment Programs Fund* accounts for employer and worker contributions used for payments of unemployment insurance and disability benefits.

Nonmajor enterprise funds account for additional operations that are financed and operated in a manner similar to private business enterprises.

Additionally, the State reports *internal service funds* as a proprietary fund type with governmental activity. Internal service funds account for goods or services provided to other agencies, departments, or governments

on a cost-reimbursement basis. The goods and services provided include: architectural services, construction and improvements, printing and procurement services, goods produced by inmates of state prisons, data processing services, and administrative services related to water delivery. Internal service funds are included in the governmental activities at the government-wide level.

Fiduciary fund types are used to account for assets held by the State. The State acts as a trustee or as an agent for individuals, private organizations, other governments, or other funds. Fiduciary funds, including fiduciary component units, are not included in the government-wide financial statements.

The State has the following four fiduciary fund types.

Private purpose trust funds account for all trust arrangements, other than those properly reported in pension or investment trust funds, whereby principal and income benefit individuals, private organizations, or other governments. The following are the State's largest private purpose trust funds.

The Scholarshare Program Trust Fund accounts for money received from participants to fund their beneficiaries' higher-education expenses at certain postsecondary educational institutions.

The *Unclaimed Property Fund* accounts for unclaimed money and properties held in trust by the State. Unclaimed property is remitted to the General Fund where it can be used by the State until it is claimed.

Pension and other employee benefit trust funds of the primary government and fiduciary component units account for transactions, assets, liabilities, and net assets available for plan benefits of the retirement systems and for other employee benefit programs.

An *investment trust fund* accounts for the deposits, withdrawals, and earnings of the Local Agency Investment Fund, an external investment pool for local governments and public agencies.

Agency funds account for assets held by the State, which acts as an agent for individuals, private organizations, or other governments. The following are the State's largest agency funds.

The *Receipting and Disbursing Fund* accounts for the collection and disbursement of revenues and receipts on behalf of local governments. This fund also accounts for receipts from numerous state funds, typically for the purpose of writing a single warrant when the warrant is funded by multiple funding sources.

The *Deposit Fund* accounts for various deposits, such as those from condemnation and litigation proceedings.

Discretely presented component units consist of certain organizations that have enterprise activity. The enterprise activity component units are the University of California, the State Compensation Insurance Fund, the California Housing Finance Agency, the Public Employees' Benefits Fund, and nonmajor component units. In this report, all of the enterprise activity of the discretely presented component units is reported in a separate column in the government-wide financial statements and on separate pages following the fund financial statements.

C. Measurement Focus and Basis of Accounting

1. Government-wide Financial Statements

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when they are earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar transactions are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

2. Fund Financial Statements

The measurement focus and basis of accounting for the fund financial statements vary with the type of fund. **Governmental fund types** are presented using the current financial resources measurement focus. With this measurement focus, operating statements present increases and decreases in net current assets; the unreserved fund balance is a measure of available spendable resources.

The accounts of the governmental fund types are reported using the modified accrual basis of accounting. Under the modified accrual basis, revenues are recorded as they become measurable and available, and expenditures are recorded at the time the liabilities are incurred. The State records revenue sources when they are earned or when they are due, provided they are measurable and available within the ensuing 12 months. Principal tax revenues susceptible to accrual are recorded as taxpayers earn income (personal income and corporation taxes), as sales are made (consumption and use taxes), and as the taxable event occurs (miscellaneous taxes), net of estimated tax overpayments.

Proprietary fund types, the investment trust fund, private purpose trust funds, and pension and other employee benefit trust funds are accounted for using the economic resources measurement focus. Agency funds are custodial in nature and do not measure the results of operations.

The accounts of the proprietary fund types, the investment trust fund, private purpose trust funds, pension and other employee benefit trust funds, and agency funds are reported using the accrual basis of accounting. Under the accrual basis, most transactions are recorded when they occur, regardless of when cash is received or disbursed.

Lottery revenue and the related prize expenses are recognized when sales are made. Certain prizes are payable in deferred installments. Such liabilities are recorded at the present value of amounts payable in the future.

For purposes of the Statement of Cash Flows, all cash and pooled investments in the State Treasurer's pooled investment program are considered to be cash and cash equivalents.

Discretely presented component units are accounted for using the economic resources measurement focus and the accrual basis of accounting.

D. Inventories

Inventories of supplies are reported at cost and inventories held for resale are stated at the lower of average cost or market. In the government-wide financial statements, inventories for both governmental and business-type activities are expensed when they are consumed and unused inventories are reported as an asset on the Statement of Net Assets. In the fund financial statements, governmental funds report inventories as expenditures when purchased, and proprietary funds report inventories as expenditures when consumed. The discretely presented component units have inventory policies similar to those of the primary government.

E. Deposits and Investments

The State reports investments at fair value, as prescribed by GAAP. Additional information on the State's investments can be found in Note 3, Deposits and Investments.

F. Net Investment in Direct Financing Leases

The State Public Works Board, an agency that accounts for its activities as an enterprise fund, has entered into lease-purchase agreements with various other primary government agencies, the University of California, and certain local agencies. The payments from these leases are used to satisfy the principal and interest requirements of revenue bonds issued by the State Public Works Board to finance the cost of projects such as acquisition and construction of facilities and equipment. Upon expiration of these leases, title to the facilities and projects transfers to the primary government agency, the University of California, or the local agency. The State Public Works Board records the net investment in direct financing leases at the net present value of the minimum lease payments.

California State University Systems (CSU) accounts for its lease activities in the State University Dormitory Building Maintenance and Equipment Fund, a major enterprise fund, has entered into 30-year capital lease agreements with certain auxiliary organizations. These agreements lease existing and newly constructed facilities to the auxiliary organizations. A portion of the proceeds from certain revenue bonds issued by CSU were used to finance the construction of these facilities.

G. Deferred Charges

The deferred charges account in the enterprise funds primarily represents operating and maintenance costs and unrecovered capital costs that will be recognized in the Water Resources Fund as expenses over the remaining life of long-term state water supply contracts. These costs are billable in future years. In addition, the account includes unbilled interest earnings on unrecovered capital costs that are recorded as deferred charges. These charges are recognized when billed in future years under the terms of water supply contracts. The deferred charges for the Public Buildings Construction Fund include bond counsel fees, trustee fees, rating agency fees, underwriting costs, insurance costs, and miscellaneous expenses. Bond issuance costs are amortized using the straight-line method over the term of the bonds. Amortization of bond issue costs during the facility construction period is capitalized and included in the construction costs. Deferred charges are also included in the State Lottery Fund and nonmajor enterprise funds. Bond issuance costs recorded as expenditures in governmental funds are reclassified as deferred charges in the governmental activities column of the Statement of Net Assets and are amortized over the life of the bonds.

H. Capital Assets

Capital assets are categorized into land, state highway infrastructure, collections, buildings and other depreciable property, intangible assets, and construction in progress. The buildings and other depreciable property account includes buildings, improvements other than buildings, equipment, personal property, certain infrastructure assets, certain books, and other capitalized and depreciable property. Intangible assets include computer software, land use rights, patents, copyrights, and trademarks. The value of the capital assets, including the related accumulated depreciation and amortization, is reported in the applicable governmental, business-type, or component unit activities columns in the government-wide Statement of Net Assets.

The primary government has a large collection of historical and contemporary treasures that have important documentary and artistic value. These assets are not capitalized or depreciated because they are cultural resources and cannot reasonably be valued and/or the assets have inexhaustible useful lives. These treasures and works of art include furnishings, portraits and other paintings, books, statues, photographs, and miscellaneous artifacts. These collections meet the conditions for exemption from capitalization because the collections are: held for public exhibition, education, or research in furtherance of public service, rather than financial gain; protected, kept unencumbered, cared for, and preserved; and are subject to an organizational policy that requires the proceeds from sales of collection items to be used to acquire other items for collections.

In general, capital assets of the primary government are defined as assets that have a normal useful life of at least one year and a unit cost of at least \$5,000. These assets are recorded at historical cost or estimated historical cost, including all costs related to the acquisition. Donated capital assets are recorded at the fair market value on the date the gift was received. Major capital asset outlays are capitalized as projects are constructed.

Buildings and other depreciable or amortizable capital assets are depreciated using the straight-line method with no salvage value for governmental activities. Generally, buildings and other improvements are depreciated over 40 years, equipment is depreciated over five years, and intangible assets are amortized over 10 to 20 years. Depreciable or amortizable assets of business-type activities are depreciated or amortized using the straight-line method over their estimated useful or service lives, ranging from three to 100 years.

California has elected to use the modified approach for capitalizing the infrastructure assets of the state highway system. The state highway system consists of 49,518 lane-miles and 12,893 bridges that are maintained by the California Department of Transportation. By using the modified approach, the infrastructure assets of the state highway system are not depreciated and all expenditures made for those assets, except for additions and improvements, are expensed in the period incurred. All additions and improvements made after June 30, 2001, are capitalized. All infrastructure assets that are related to projects completed prior to July 1, 2001, are recorded at the historical costs contained in annual reports of the American Association of State Highway and Transportation Officials (AASHTO) and the Federal Highway Administration.

The capital assets of the discretely presented component units are reported at cost at the date of acquisition or at fair market value at the date of donation, in the case of gifts. They are depreciated or amortized over their estimated useful service lives.

I. Long-term Obligations

Long-term obligations consist of certain unmatured general obligation bonds, certain unmatured revenue bonds, capital lease obligations, certificates of participation, commercial paper, the net pension obligation of the pension and other employee benefit trust funds, the net other postemployment benefits obligation, the liability for employees' compensated absences and workers' compensation claims, pollution remediation obligations, amounts owed for lawsuits, reimbursement for costs mandated by the State, the outstanding Proposition 98 funding guarantee owed to schools, the liability for Lottery prizes and annuities, loans from other governments and fiduciary funds, and the primary government's share of the University of California pension liability that is due in more than one year. In the government-wide financial statements, current and noncurrent obligations are reported as liabilities in the applicable governmental activities, business-type activities, and component units columns of the Statement of Net Assets.

Pollution remediation obligations are recorded by the State when one or more of the GASB Statement No. 49 obligating events have occurred and when a reasonable estimate of the remediation cost is available. These liabilities are measured using actual contract costs, where no change in cost is expected, or the expected cash flow technique. The remediation obligation estimates that appear in this report are subject to change over time. Cost may vary due to price fluctuations, changes in technology, changes in potential responsible parties, results of environmental studies, changes to statutes or regulations and other factors that could result in revisions to these estimates. Prospective recoveries from responsible parties may reduce the State's obligation.

Bond premiums, discounts, and loss on refundings for business-type activities and component units are generally deferred and amortized over the life of the bonds. In these instances, bonds payable are reported net of the applicable premium, discount, or loss. Bond premiums and discounts for governmental activities are reported as other financing sources (uses) in the fund financial statements. However, in the government-wide financial statements, the bonds payable for governmental activities is reported net of the applicable unamortized premium, discount, and loss on refundings.

With approval in advance from the Legislature, certain authorities and state agencies may issue revenue bonds. Principal and interest on revenue bonds are payable from the pledged revenues of the respective funds, building authorities, and agencies. The General Fund has no legal liability for payment of principal and interest on revenue bonds. With the exception of certain special revenue funds (Transportation and the Golden State Tobacco Securitization Corporation) and the building authorities' capital projects funds, the liability for revenue bonds is recorded in the respective fund.

J. Compensated Absences

The government-wide financial statements report both the current and the noncurrent liabilities for compensated absences, which are vested unpaid vacation, annual leave, and other paid leave programs. However, unused sick-leave balances are not included in the compensated absences because they do not vest to employees. In the fund financial statements for governmental funds, only the compensated absences for employees that have left state service and have unused reimbursable leave at year-end would be included. The amounts of vested unpaid vacation and annual leave accumulated by state employees are accrued in proprietary funds when incurred. In the discretely presented component units, the compensated absences are accounted for in the same manner as in the proprietary funds of the primary government.

K. Net Assets and Fund Balance

The difference between fund assets and liabilities is called "net assets" on the government-wide financial statements, the proprietary and fiduciary fund statements, and the component unit statements; it is called "fund balance" on the governmental fund statements. The government-wide financial statements include the following categories of net assets:

Investment in capital assets, net of related debt, represents capital assets, net of accumulated depreciation, reduced by the outstanding principal balances of debt attributable to the acquisition, construction, or improvement of those assets.

Restricted net assets result from transactions with purpose restrictions and are designated as either nonexpendable or expendable. Nonexpendable restricted net assets are subject to externally imposed restrictions that must be retained in perpetuity. Expendable restricted net assets are subject to externally imposed restrictions that can be fulfilled by actions of the State. As of June 30, 2011, the government-wide financial statements show restricted net assets for the primary government of \$31.5 billion, of which \$6.3 billion is due to enabling legislation.

Unrestricted net assets are neither restricted nor invested in capital assets, net of related debt.

In the fund financial statements, proprietary funds include categories of net assets similar to those in the government-wide statements. The fund balance amounts for governmental funds have been reclassified in accordance with GASB Statement No. 54. Amounts previously reported as reserved and unreserved are now reported as *nonspendable*, *restricted*, *committed*, *assigned*, or *unassigned*.

Nonspendable fund balance includes amounts that cannot be spent because they are not in spendable form (inventories; prepaid amounts; long-term portion of loans or notes receivable; or property held for resale unless the proceeds are restricted, committed, or assigned) or they are legally or contractually required to remain intact, such as a principal balance in a permanent fund.

Restricted fund balances have constraints placed upon the use of the resources either by an external party (creditors, grantors, contributors, or laws or regulations of other governments) or by law through a constitutional provision or enabling legislation.

Committed fund balances can be used only for specific purposes pursuant to constraints imposed by a formal action of the State's highest level of decision-making authority. Those committed amounts cannot be used for any other purpose unless the State removes or changes the specified use by taking the same type of action. The formal action that commits a fund balance to a specific purpose should occur prior to the end of the reporting period, but the amount subject to the constraint may be determined in a subsequent period. Committed fund balance should incorporate contractual obligations to the extent that existing resources in the fund have been specifically committed for use in satisfying those contractual requirements.

Assigned fund balances include amounts that are constrained by the State's intent to be used for a specific purpose, but are neither restricted nor committed. For governmental funds other than the General Fund, this is the residual amount of the fund that is not classified as nonspendable and is neither restricted nor committed.

Unassigned fund balance is the residual amount of the General Fund not included in the four classifications described above. In other governmental funds where expenditures incurred for specific purposes exceed amounts restricted, committed, or assigned to those purposes, a negative unassigned fund balance may need to be reported.

Fiduciary fund net assets are amounts held in trust for benefits and other purposes.

L. Restatement of Beginning Fund Balances and Net Assets

1. Fund Financial Statements

The beginning fund balance of the **governmental funds** decreased by \$2.0 billion as a result of a prior year overstatement of \$613 million in the Unemployment Programs Administration Fund, and a reclassification of \$1.4 billion in the California State University Programs Fund to the **enterprise funds**. In addition, the following changes occurred as a result of the implementation of GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*: a \$118 million increase in the General Fund, a **major governmental fund**, a \$50 million increase in the Business and Professions Regulatory and Licensing Fund, a **nonmajor governmental fund**, a \$39 million increase in the Environmental and Natural Resources Fund, a **nonmajor governmental fund**, a \$96 million decrease in the Unemployment Programs Administration Fund, a **nonmajor governmental fund**, a \$1.5 billion decrease in the Financing for Local Governments and the Public Fund, a **nonmajor governmental fund**, a \$585 million increase in the Hospital Construction Fund, a **nonmajor governmental fund**, a \$1.6 billion increase in the Local Government Construction Fund, a **nonmajor governmental fund**, and a \$1.5 billion decrease in the Other Special Revenue Programs, a **nonmajor governmental fund**.

The beginning net assets of the **enterprise funds** increased by \$1.2 billion as a result of reclassifications from governmental activities to the new California State University Fund. In addition, **nonmajor enterprise funds**' beginning net assets decreased by \$742 million as a result of the reclassification to the new California State University Fund, a **major enterprise fund**. This had no effect on the overall beginning net assets balance for **enterprise funds**.

The beginning net assets of the **pension and other employee benefit trust funds** increased by \$723 thousand as a result of the reclassification of the State Employees' Pretax Parking Fund from governmental activities.

The beginning net assets of the **discretely presented component units—enterprise activity** increased by \$1 million. The net increase is comprised of a \$3 million net decrease in the California State University auxiliary organizations as a result of error corrections and a change in capitalization threshold for capital assets and a \$4 million increase due to the inclusion of the State Assistance Fund for Enterprise, Business, and Industrial Development Corporation.

2. Government-wide Financial Statements

The beginning net assets of the **governmental activities** decreased by \$2.7 billion. In addition to the amounts described in the previous section for governmental funds, the restatement is comprised of a \$192 million increase to adjust compensated absences payable; a \$63 million increase to adjust the net pension obligation; a \$50 million increase to adjust the net other postemployment benefits obligation; a \$54 million decrease to

adjust pollution remediation obligations; a \$19 million decrease to prepaid items; and a \$964 million decrease to capital assets related to reclassifications to the new California State University Fund.

The beginning net assets of the **business-type activities** and **component units** were restated as described in the previous section for enterprise funds and discretely presented component units—enterprise activity.

M. Guaranty Deposits

The State is custodian of guaranty deposits held to protect consumers, to secure the State's deposits in financial institutions, and to ensure payment of taxes and fulfillment of obligations to the State. Guaranty deposits of securities and other properties are not shown on the financial statements.

NOTE 2: BUDGETARY AND LEGAL COMPLIANCE

A. Budgeting and Budgetary Control

The State's annual budget is prepared primarily on a modified accrual basis for governmental funds. The Governor recommends a budget for approval by the Legislature each year. This recommended budget includes estimated revenues; however, revenues are not included in the annual budget bill adopted by the Legislature. Under state law, the State cannot adopt a spending plan that exceeds estimated revenues.

Under the State Constitution, money may be drawn from the treasury only through a legal appropriation. The appropriations contained in the Budget Act, as approved by the Legislature and signed by the Governor, are the primary sources of annual expenditure authorizations and establish the legal level of control for the annual operating budget. The budget can be amended throughout the year by special legislative action, budget revisions by the Department of Finance, or executive orders of the Governor. Amendments to the original budget for the year ended June 30, 2011, were legally made, and they had the effect of decreased spending authority for the Budgetary/Legal Basis reported General Fund and the Transportation Funds.

Appropriations are generally available for expenditure or encumbrance either in the year appropriated or for a period of three years if the legislation does not specify a period of availability. At the end of the availability period, the encumbering authority for the unencumbered balance lapses. Some appropriations continue indefinitely, while others are available until fully spent. Generally, encumbrances must be liquidated within two years from the end of the period in which the appropriation is available. If the encumbrances are not liquidated within this additional two-year period, the spending authority for these encumbrances lapses.

B. Legal Compliance

State agencies are responsible for exercising basic budgetary control and ensuring that appropriations are not overspent. The State Controller's Office is responsible for overall appropriation control and does not allow expenditures in excess of authorized appropriations.

Financial activities are mainly controlled at the appropriation level but can vary, depending on the presentation and wording contained in the Budget Act. The Budget Act appropriations are identified by department, reference item, and fund. The annual appropriated budget may establish detailed allocations to specific programs, projects, or sources of reimbursement within an appropriation. The Department of Finance can authorize adjustments between the detail allocations but cannot increase the amount of the overall appropriation. While the financial activities are controlled at various levels, the legal level of budgetary

control—the extent to which management may amend the budget without seeking approval of the governing body—has been established in the Budget Act for the annual operating budget.

NOTE 3: DEPOSITS AND INVESTMENTS

The State Treasurer administers a single pooled investment program comprising both an internal investment pool and an external investment pool (the Local Agency Investment Fund). A single portfolio of investments exists, with all participants having an undivided interest in the portfolio. Both pools are administered in the same manner, as described below.

As required by generally accepted accounting principles, certain risk disclosures are included in this note to the extent that the risks exist at the date of the statement of net assets. Disclosure of the following risks is included:

Interest Rate Risk is the risk that the value of fixed-income securities will decline because of changing interest rates. The prices of fixed-income securities with longer time to maturity tend to be more sensitive to changes in interest rates than those with shorter durations.

Credit Risk is the risk that a debt issuer will fail to pay interest or principal in a timely manner, or that negative perceptions of the issuer's ability to make these payments will cause security prices to decline.

Custodial Credit Risk is the risk that, in the event a financial institution or counterparty fails, the investor will not be able to recover the value of deposits, investments, or collateral.

Concentration of Credit Risk is the risk of loss attributed to the magnitude of an investor's holdings in a single issuer.

Foreign Currency Risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit.

A. Primary Government

The State's pooled investment program and certain funds of the primary government are allowed by state statutes, bond resolutions, and investment policy resolutions to invest in United States government securities, federal agency securities, negotiable certificates of deposit, bankers' acceptances, commercial paper, corporate bonds, bank notes, other debt securities, repurchase agreements, reverse repurchase agreements, and other investments.

Certain discretely presented component units participate in the State Treasurer's Office pooled investment program. As of June 30, 2011, the discretely presented component units accounted for approximately 3.5% of the State Treasurer's pooled investment portfolio. This program enables the State Treasurer's Office to combine available cash from all funds and to invest cash that exceeds current needs.

Both deposits and investments are included in the State's investment program. For certain banks, the State Treasurer's Office maintains cash deposits that cover uncleared checks deposited in the State's accounts and that earn income which compensates the banks for their services.

Demand and time deposits held by financial institutions as of June 30, 2011, totaling approximately \$5.9 billion, were insured by federal depository insurance or by collateral held by the State Treasurer's Office

or an agent of the State Treasurer's Office in the State's name. The California Government Code requires that collateral pledged for demand and time deposits be deposited with the State Treasurer.

As of June 30, 2011, the State Treasurer's Office had on deposit with a fiscal agent amounts totaling \$28.6 million related to principal and interest payments to bondholders. These deposits were insured by federal depository insurance or by collateral held by an agent of the State Treasurer's Office in the State's name.

The State Treasurer's Office reports its investments at fair value. The fair value of securities in the State Treasurer's pooled investment program generally is based on quoted market prices. The State Treasurer's Office performs a quarterly fair market valuation of the pooled investment program portfolio. In addition, the State Treasurer's Office performs a monthly fair market valuation of all securities held against carrying cost. These valuations are posted to the State Treasurer's Office website at www.treasurer.ca.gov. As of June 30, 2011, the weighted average maturity of the securities in the pooled investment program administered by the State Treasurer's Office was approximately 245 days. Weighted average maturity is the average number of days, given a dollar-weighted value of individual investments, that the securities in the portfolio have remaining from evaluation date to stated maturity.

The Pooled Money Investment Board provides oversight of the State Treasurer's pooled investment program. The purpose of the board is to design and administer an effective cash management and investment program, using all monies flowing through the State Treasurer's Office bank accounts and keeping all available funds invested in a manner consistent with the goals of safety, liquidity, and yield. The Pooled Money Investment Board is comprised of the State Treasurer as chair, the State Controller, and the Director of Finance. This board designates the amounts of money available for investment. The State Treasurer is charged with making the actual investment transactions for this program. This investment program is not registered with the Securities and Exchange Commission as an investment company.

The value of the deposits in the State Treasurer's pooled investment program, including the Local Agency Investment Fund, is equal to the dollars deposited in the program. The fair value of the position in the program may be greater or less than the value of the deposits, with the difference representing the unrealized gain or loss. As of June 30, 2011, this difference was immaterial to the valuation of the program. The pool is run with "dollar-in, dollar-out" participation. There are no share-value adjustments to reflect changes in fair value.

Certain funds have elected to participate in the pooled investment program even though they have the authority to make their own investments. Others may be required by legislation to participate in the program; as a result, the deposits of these funds or accounts may be considered involuntary. However, these funds or accounts are part of the State's reporting entity. The remaining participation in the pool, the Local Agency Investment Fund, is voluntary.

Certain funds that have deposits in the State Treasurer's pooled investment program do not receive the interest earnings on their deposits. Instead, by law, the earnings are to be assigned to the State's General Fund. Most of the \$37.1 million in interest revenue received by the General Fund from the pooled investment program in the 2010-11 fiscal year was earned on balances in these funds.

The State Treasurer's pooled investment program values participants' shares on an amortized cost basis. Specifically, the program distributes income to participants quarterly, based on their relative participation during the quarter. This participation is calculated based on (1) realized investment gains and losses calculated on an amortized cost basis, (2) interest income based on stated rates (both paid and accrued), (3) amortization of discounts and premiums on a straight-line basis, and (4) investment and administrative expenses. This amortized cost method differs from the fair value method used to value investments in these

financial statements; the amortized cost method is not designed to distribute to participants all unrealized gains and losses in the fair value of the pool's investments. Because the total difference between the fair value of the investments in the pool and the value distributed to pool participants using the amortized cost method described above is not material, no adjustment was made to the financial statements. The State Treasurer's Office also reports participant fair value as a ratio of amortized cost on a quarterly basis. The State Treasurer's Office has not provided or obtained a legally binding guarantee to support the principal invested in the investment program.

As of June 30, 2011, structured notes and medium-term asset-backed securities comprised approximately 3.19% of the pooled investments. A significant portion of the structured notes consisted of corporate floating-rate certificates of deposit. For the agency and corporate floating-rate securities held in the portfolio during the fiscal year, the interest received by the State Treasurer's pooled investment program rose or fell as the underlying index rate rose or fell. The portion representing the asset-backed securities consists of mortgage backed securities, Small Business Administration (SBA) pools, and asset-backed commercial paper. The mortgage-backed securities are called real estate mortgage investment conduits (REMICs), and are securities backed by pools of mortgages. The REMICs in the State's portfolio have a fixed principal payment schedule. A portion of the asset-backed securities consisted of floating-rate SBA notes. For floating-rate SBA notes held in the portfolio during the fiscal year, the interest received by the State Treasurer's pooled investment program rose or fell as the underlying index rate rose or fell. The structure of the floating-rate notes in the State Treasurer's pooled investment program portfolio provided a hedge against the risk of increasing interest rates. A portion of the asset-backed portfolio holdings was short-term, asset-backed commercial paper (ABCP), which represented 1.82% of pooled investments.

Enterprise funds and special revenue funds also make separate investments, which are presented at fair value.

Table 1 identifies the investment types that are authorized by the California Government Code and the State Treasurer's Office investment policy for the pooled investment program.

Table 1

Authorized Investments

Authorized Investment Type	Maximum Maturity ¹	Maximum Percentage of Portfolio	Maximum Investment in One Issuer	Credit Rating
U.S. Treasury Securities	5 years	N/A	N/A	N/A
Federal Agency and Supranational Securities	5 years	N/A	N/A	N/A
Certificates of Deposit	5 years	N/A	N/A	N/A
Bankers Acceptances	180 days	N/A	N/A	N/A
Commercial Paper	180 days	30%	10% of issuer's outstanding	A-2/P-2/F-2 ²
			Commercial Paper	
Corporate Bonds/Notes	5 years	N/A	N/A	A-/A3/A- ³
Repurchase Agreements	1 year	N/A	N/A	N/A
Reverse Repurchase Agreements	1 year	10% ¹	N/A	N/A

¹ Limitations are pursuant to the State Treasurer's Office Investment Policy for the Pooled Money Investment Account.

² The State Treasurer's Office Investment Policy for the Pooled Money Investment Account is more restrictive than the Government Code, which allows investments rated A-3/P-3/F-3.

³ The Government Code requires that a security fall within the top three ratings of a nationally recognized rating service.

N/A Neither the Government Code nor the State Treasure's Office Investment Policy for the Pooled Money Investment Account sets limits for this investment type.

1. Interest Rate Risk

Table 2 presents the interest rate risk of the primary government's investments.

Table 2

Schedule of Investments - Primary Government - Interest Rate Risk

June 30, 2011 (amounts in thousands)

-	Interest Rates ¹	Maturity	Fair Value at Year End	Weighted Average Maturity (in years)
Pooled investments				
U.S. Treasury bills and notes	0.15 - 1.63	28 days - 2.96 years	\$ 35,621,950	0.91
U.S. agency bonds and discount notes	0.20 - 1.18	5 days - 337 days	4,825,246	0.44
Supranational debentures and discount notes (IBRD)	1.32	299 days	300,552	0.82
Small Business Administration loans	0.53 - 1.38	0.25 year	544,255	0.25 2
Mortgage-backed securities 3	3.92 - 14.25	154 days - 3.51 years	506,294	2.73
Certificates of deposit	0.11 - 0.55	1 day - 1.15 years	7,380,020	0.15
Commercial paper	0.10 - 0.37	1 day - 124 days	7,480,975	0.12
Corporate bonds and notes	0.13 - 0.30	27 days - 33 days	550,048	0.08
Total pooled investments			57,209,340 4	
Other primary government investments				
U.S. Treasuries and agencies			2,203,843	2.17
Commercial paper			339,831	0.04
Guaranteed investment contracts			225,597	11.14
Corporate debt securities			780,812	1.91
Repurchase agreements			5,439	0.00 5
Other			 1,142,914	4.19
Total other primary government investments ⁶			 4,698,436	
Funds outside primary government included in pooled in	nvestments			
Less: investment trust funds			24,012,079	
Less: other trust and agency funds			3,286,091	
Less: discretely presented component units			 2,295,603	
Total primary government investments			\$ 32,314,003	

¹ These numbers represent high and low interest rates for each investment type.

In calculating SBA holdings' weighted average maturity, the State Treasurer's Office assumes that stated maturity is the quarterly reset date.

³ These securities are issued by U.S. government agencies such as the Federal National Mortgage Association.

⁴ Total pooled investments does not include certain assets of the State's pooled investment program. The other assets include \$4.0 billion of time deposits and \$4.8 billion of internal loans to state funds, primarily the General Fund.

⁵ These repurchase agreements of the California State University mature in one day.

⁶ Total other primary government investments include approximately \$9 million of cash equivalents that are included in cash and pooled investments.

Table 3 identifies the debt securities that are highly sensitive to interest rate fluctuations (to a greater degree than already indicated in the information provided previously).

Table 3

Schedule of Highly Sensitive Investments in Debt Securities – Primary Government – Interest Rate Risk June 30, 2011 (amounts in thousands)

	_	Fair Value t Year End	Percent of Total Pooled Investments
Pooled investments			
Mortgage-backed			
Federal National Mortgage Association Collateralized Mortgage Obligations	\$	506,247	0.885 %
Government National Mortgage Association Pools		47	0.000

These mortgage-backed securities entitle the purchaser to receive a share of the cash flows, such as principal and interest payments, from a pool of mortgages. Mortgage securities are sensitive to interest rate changes because principal prepayments either increase (in a low interest rate environment) or decrease (in a high interest rate environment). A change, up or down, in the payment rate will result in a change in the security yield.

2. Credit Risk

Table 4 presents the credit risk of the primary government's debt securities.

Table 4

Schedule of Investments in Debt Securities - Primary Government - Credit Risk

June 30, 2011

(amounts in thousands)

Credit Rating as					
Short-term	Long-term	Fair Value			
Pooled investments ¹					
A-1+/P-1/F-1+	AAA/Aaa/AAA	\$	12,194,405		
A-1/P-1/F-1	AA/Aa/AA		8,342,436		
A-2/P-2/F-2	A/A/A		_		
Not rated			506,247		
Not applicable			36,166,252		
Total pooled investments	s	\$ 57,209,340			
				_	
Other primary government	nt investments				
A-1+/P-1/F-1+	AAA/Aaa/AAA	\$	1,872,515		
A-1/P-1/F-1	AA/Aa/AA		1,001,183		
A-2/P-2/F-2	A/A/A		1,146,134		
A-3/P-3/F-3	BBB/Baa/BBB		4,661		
Not rated			638,397		
Not applicable			35,546		
Total other primary gove	\$	4,698,436			

¹ The State Treasurer's Office uses Standard & Poor's, Moody's, and Fitch ratings services. Securities are classified by the lowest rating of the three agencies.

² Total pooled investments does not include certain assets of the State's pooled investment program. The other assets include time deposits of \$4.0 billion, for which credit risk is mitigated by collateral that the State holds for them—as discussed earlier in this note—and \$4.8 billion in loans to state funds, primarily to the General Fund, for which external credit risk is not applicable because they are internal loans.

3. Concentration of Credit Risk

The investment policy of the State Treasurer's Office contains no limitations on the amount that can be invested in any one issuer beyond those limitations stipulated in the California Government Code. Table 5 identifies debt securities in any one issuer (other than U.S. Treasury securities) that represent 5% or more of the State Treasurer's investments, or of the separate investments of other primary government funds.

Table 5

Schedule of Investments – Primary Government – Concentration of Credit Risk June 30, 2011
(amounts in thousands)

Issuer	Investment Type	Reported Amount	Percent of To Agency Investment	-
California State University				
Federal Home Loan Bank	U.S. agency securities	\$ 274,299	11.39	%
Federal Home Loan Mortgage Corporation	U.S. agency securities	277,850	11.54	
Federal National Mortgage Association	U.S. agency securities	158,806	6.59	
California State Lottery				
State of California	Municipal securities	\$ 226,926	19.27	%
Commonwealth of Massachusetts	Municipal securities	62,772	5.33	
Golden State Tobacco Securitization Corporation	1			
Abbey National North America LLC	Commercial paper	\$ 165,100	33.04	%
Federal Home Loan Mortgage Corporation	U.S. agency securities	203,934	40.81	
Federal National Mortgage Association	U.S. agency securities	130,662	26.15	
Department of Water Resources				
Federal National Mortgage Association	U.S. agency securities	\$ 75,313	89.10	%

4. Custodial Credit Risk

The State of California has a deposit policy for custodial credit risk that requires deposits held by financial institutions to be insured by federal depository insurance or secured by collateral. As of June 30, 2011, \$3 million in deposits of the Electric Power Fund were uninsured and uncollateralized.

B. Fiduciary Funds

The fiduciary funds include pension and other employee benefit trust funds of the following fiduciary funds and component units: the California Public Employees' Retirement System (CalPERS), the California State Teachers' Retirement System (CalSTRS), the fund for the California Scholarshare program, and various other funds. CalPERS and CalSTRS account for 97% of these separately invested funds. CalPERS and CalSTRS exercise their authority under the State Constitution and invest in stocks, bonds, mortgages, real estate, and other investments, including derivative instruments.

CalPERS reports investments in securities at fair value, generally based on published market prices and quotations from pricing vendors. Many factors are considered in arriving at fair value. Real estate investments are held either directly, in separate accounts, or as a limited partnership or in a joint venture or commingled fund. Properties owned directly or in a joint venture are subject to independent third-party appraisals. Short-term investments are reported at market value, when available, or, when market value is not available, at cost plus accrued interest, which approximates market value. For investments where no readily ascertainable market value exists, management, in consultation with its investment advisors, determines the fair values for the individual investments.

CalSTRS also reports investments at fair value, generally based on published market prices and quotations from pricing vendors for securities. Real estate equity investment fair values are based on either recent estimates provided by CalSTRS' contract real estate advisors or by independent appraisers. Short-term investments are reported at fair value or at cost or amortized cost, which approximates fair value. For short-term investments which are reported at fair value, the investments are valued using similar methodologies as used for debt securities. Fair value for commingled funds (other than those funds traded on a national or international exchange) is based on information provided by the applicable fund managers. Private Equity partnerships are valued using their respective Net Asset Value (NAV), and are audited annually. The most significant input into the NAV of such an entity is the fair value of its investment holdings. These holdings are valued by the general partners on a quarterly or semi-annual basis, in conjunction with management and investment advisors. For private equity investments and other investments for which no readily ascertainable market value exists, CalSTRS management, in consultation with its investment advisors, has determined the fair value for the individual investments. Purchases and sales are recorded on the trade date.

The State Constitution, state statutes, and board policies permit CalPERS and CalSTRS to lend their securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. Third-party securities lending agents are under contract to lend domestic and international equity and debt securities. For both CalPERS and CalSTRS, collateral, in the form of cash or other securities, is required at 102% and 105% of the fair value of domestic and international securities loaned, respectively. CalPERS' management believes that CalPERS has minimized its credit risk exposure by requiring the borrowers to provide collateral greater than 100% of the market value of the securities loaned. The securities loaned are priced daily. Securities on loan can be recalled on demand by CalPERS and loans of securities may be terminated by CalPERS or the borrower.

At June 30, 2011, the cash collateral had weighted average maturities of 31, 312, 367, 587, and 479 days for two externally managed portfolios, and durations of 71, 0, 32, 0, and 36 days for three internally managed portfolios.

For CalSTRS, collateral received on each security loan was placed in investments that, at June 30, 2011, had a 45-day difference in weighted average maturity between the investments and loans. Most of CalSTRS' security loans can be terminated on demand by CalSTRS or the borrower. CalSTRS is not permitted to pledge

or sell collateral securities received unless the borrower defaults. The contracts with the security lending agents require them to indemnify CalSTRS if the borrowers fail to return the securities (or if the collateral is not sufficient to replace the securities lent) or if the borrowers fail to pay CalSTRS for income distributions by the securities' issuers while the securities are on loan.

Table 6 presents the investments, including derivative instruments, of the fiduciary funds by investment type.

Table 6

Schedule of Investments - Fiduciary Funds

June 30, 2011

(amounts in thousands)

	Fair Value
Investment Type	
Equity securities	199,780,401
Debt securities*	91,576,952
Mutual funds	10,200,315
Real estate	38,232,098
Inflation linked	8,126,757
Insurance contracts	1,591,300
Private equity	57,537,268
Securities lending collateral	45,620,619
Other	3,822,956
Total investments	\$ 456,488,666

1. Interest Rate Risk

CalPERS and CalSTRS manage the interest rate risk inherent in their investment portfolios by measuring the effective or option-adjusted duration of the portfolio. In using the duration method, these agencies may make assumptions regarding the timing of cash flows or other factors that affect interest rate risk information. The CalPERS investment policies require the option-adjusted duration of the total fixed-income portfolio to stay within 10% of the option-adjusted duration of its benchmark. All individual portfolios are required to maintain a specific level of risk relative to their benchmark. Risk exposures are monitored daily. The CalSTRS investment guidelines allow the core long-term investment grade portfolios the discretion to deviate within plus or minus 20% (0.80 to 1.20) of the weighted average effective duration of the relevant performance benchmark. The permissible range of deviation for the weighted average effective duration within the opportunistic strategy portfolios is negotiated with each manager and detailed within their respective investment guidelines. The CalSTRS investment guidelines state that the average maturity of the short-term fixed-income portfolio shall be managed such that it will not exceed 180 days.

Table 7 presents the interest rate risk of the fixed-income securities of these fiduciary funds.

Table 7

Schedule of Investments in Fixed-Income Securities - Fiduciary Funds - Interest Rate Risk June 30, 2011
(amounts in thousands)

	F	air Value at Year End		Effective Duration (in years) ¹		
California Public Employees' Retirement Fund ²			-	, ,		
U.S. Treasuries and agencies	\$	25,235,748		7.57		
Mortgages		11,258,573		4.45		
Corporate		11,030,330		8.86		
Asset-backed		3,861,730		2.18		
Municipal		33,793		8.98		
International		5,339,734		8.65		
Structured investment vehicle		314,197		41.08		
Floating rate collateralized mortgage-backed security		651,914		0.66		
No effective duration		10,988,713		N/A		
Total	_	68,714,732				
Deferred Compensation Plan Fund						
Investment contracts	\$	1,379,742		2.34		
Scholarshare Program Trust Fund						
Insurance contracts	\$	211,558		1.87		
California State Teachers' Retirement System	•	_::,===				
Long-term fixed-income investments						
U.S. Government and agency obligations	\$	8,004,079		4.82		
Corporate		5,633,392		6.02		
High yield		1,843,672		4.07		
Debt core plus		2,863,252		4.45		
Special situations		189,252		0.19		
Debt transitions		2,836		4.46		
Commercial mortgage-backed securities		761,719		3.77		
Mortgage-backed securities		7,821,042		3.21		
Total	_					
		0-30		31-90		91-120
		days	_	days		days
Short-term fixed-income investments	_		_			
Money market securities		562,757	\$	362,804	\$	30,000
Corporate credit obligations		89,954		153,350		8,958
U.S. Government and agency obligations		05.010				00.007
Noncallables		65,019 40,000		 159,592		30,007
Discount notes		40,000		159,592		15,004
Callable		_				13,004
U.S. Treasury		32,134		11,673		_
	_		\$		•	83,969
Total	\$	789,864		687,419	\$	03,909

¹ Effective duration is described in the paragraph preceding this table.

² Includes investments of fiduciary funds and certain discretely presented component units that CalPERS administers.

_	121-180 days	_	181-365 days			ir Value at Year End	
\$	_	\$	_	\$	_	\$	955,561
	_		_		_		252,262
	48,520		55,077		_		198,623
	177,155		77,430		_		454,177
	9,166		15,002		130,594		169,766
	44,990		171,014		25,097		241,101
	7,628		_		3,386		54,821
\$	287,459	\$	318,523	\$	159,077	\$	2,326,311

2. Credit Risk

The CalPERS investment policies require that 80% of the total fixed-income portfolio be invested in investment-grade securities. Investment-grade securities are those fixed-income securities with a Moody's rating of AAA to BAA or a Standard and Poor's rating of AAA to BBB. Each portfolio is required to maintain a specified risk level. Portfolio exposures are monitored daily. The CalSTRS investment guidelines require that, at the time of purchase, at least 95% of the corporate securities comprising the credit portion of the core fixed-income portfolio be rated Baa3/BBB-/BBB- or better by two out of the three nationally recognized statistical rating organizations (NRSROs), such as Moody's Investors Service, Inc, Standard and Poor's Rating Service, or Fitch Ratings. Furthermore, the total position of the outstanding debt of any one private mortgage-backed and asset-backed securities issuer shall be limited to 10% of the market value of the portfolio. Obligations of other issuers are held to a 5% per issuer limit (at the time of purchase) of the market value of any individual portfolio. The investment guidelines also include an allocation to opportunistic strategies, a portion of which are managed externally and allow for the purchase of bonds rated below investment grade. Limitations on the amount of debt of any one issuer a manager may hold are negotiated on a manager-by-manager basis.

Table 8 presents the credit risk of the fixed-income securities of these fiduciary funds.

Table 8

Schedule of Investments in Fixed-Income Securities – Fiduciary Funds – Credit Risk June 30, 2011

(amounts in thousands)

Credit Rating as		
Short-term	Long-term	Fair Value
A-1+/P-1/F-1+	AAA/Aaa/AAA	\$ 55,143,535
A-1/P-1/F-1	AA/Aa/AA	7,267,664
A-2/P-2/F-2	A/A/A	13,898,855
A-3/P-3/F-3	BBB/Baa/BBB	8,973,790
B/NP/B	BB/Ba/BB	1,753,014
B/NP/B	B/B/B	1,817,266
C/NP/C	CCC/Caa/CCC	870,114
C/NP/C	CC/Ca/CC	89,609
C/NP/C	C/C/C	17,990
D/NP/D	D/D/D	10,057
Withdrawn		893
Not rated		14,655,296
Not applicable		24,065,540
Total fixed-income securitie	s	\$ 128,563,623

3. Concentration of Credit Risk

The Deferred Compensation Plan Fund held \$1.4 billion in investment contracts of Dwight Asset-Management Company; this amount represented 17.1% of the fund's total investments as of June 30, 2011. The Scholarshare Program Trust Fund held \$211 million in investment contracts of TIAA-CREF Life Insurance Company; this amount represented 4.7% of the fund's total investments as of June 30, 2011.

CalPERS and CalSTRS did not have investments in a single issuer that represented 5% or more of total fair value of all investments.

4. Custodial Credit Risk

CalPERS' investments at June 30, 2011 were not exposed to custodial risk. As of June 30, 2011, all of CalSTRS investments, other than those of two tax-deferred defined contribution plans amounting to \$312 million held in the name of TIAA-CREF, are held in CalSTRS' name and/or are not exposed to custodial credit risk. CalPERS and CalSTRS have no general policies relating to custodial credit risk.

5. Foreign Currency Risk

At June 30, 2011, CalPERS and CalSTRS held \$76.2 billion and \$32.6 billion, respectively, in investments, including derivative instruments, subject to foreign currency risk. CalPERS' asset allocation and investment policies allow for active and passive investments in international securities. CalPERS' policy for total global equity specifies investment in international equities be based on market capitalization. For total fixed income, 10% is targeted for investment in international securities. Real estate and alternative investments do not have a target allocation for international investment. CalPERS uses a currency overlay program to reduce risk by hedging approximately 15% of the plan's total exposure to international currencies. Its currency exposures are monitored daily. CalSTRS believes that its Currency Management Program should emphasize the protection of the value of its non-dollar public and private equity assets against a strengthening U.S. dollar first, yet recognizes that opportunities also exist for alpha generation (the ability to derive a return in excess of a market return) within the currency markets. The hedging range has been designed to allow for some degree of symmetry around the underlying exposure to the foreign denominated assets within CalSTRS in order to both protect the translation value of the assets against a strengthening U.S. dollar and to enhance returns in a declining U.S. dollar environment. As a result, the hedging range is - 25% to 50% of the total notional value of the non-U.S. public and non-U.S. private equity portfolios.

Table 9 identifies the investments, including derivative instruments, of the fiduciary funds that are subject to foreign currency risk. Derivative instruments are included in the amounts reported under equity, fixed income, and forward contracts.

Table 9

Schedule of Investments - Fiduciary Funds - Foreign Currency Risk
June 30, 2011
(amounts in thousands of U.S. dollars at fair value)

				Fixed	
Currency	Cash	Equity	Alternative	Income	Real Estate
Argentine Peso\$	— \$	_	\$ —	\$ —	\$ —
Australian Dollar	32,027	5,089,106	77,897	230,765	372,034
Bermuda Dollar	· —	886	· -	· -	· —
Brazilian Real	23,059	2,258,268	_	78,547	470,889
British Pound Sterling	86,544	12,503,870	3,534	1,474,695	147,362
Canadian Dollar	49,765	6,778,385	220,908	372,619	350,086
Cayman Islands Dollar		3,058		072,010	
Chilean Peso	561	186,933	_	1,067	_
Chinese Yuan	_	5,124	_	1,007	_
Columbian Peso	936	66,965	_	_	_
Czech Koruna		88,605	_	_	_
Danish Krone	486 5,812	815,775	_	14,468	_
	221	112,130	_	14,400	_
Egyptian Pound		•	2 700 120	2.050.206	005.000
Euro	601,046	26,752,853	3,702,132	3,050,326	965,862
Guatemalan Quetzal	_	_	_	_	44,988
Guernsey Pound	_	1,849	_	_	_
Hong Kong Dollar	10,666	4,736,982	_	_	1,055,508
Hungarian Forint	88	119,970	_	_	_
Indian Rupee	9,371	1,359,527	_	11	393,237
Indonesian Rupiah	2,349	595,576	_	3,469	_
Israeli Shekel	2,909	396,928	_	_	1,912
Japanese Yen	160,047	12,982,437	110,069	1,093,783	459,185
Kazakhstan Tenge	_	_	_	_	_
Korean Won	_	16,688	_	_	_
Malaysian Ringgit	816	474,259	_	_	_
Mexican Peso	5.071	600,551	_	127,334	220,928
Moroccan Dirham	202	10,268	_	, <u> </u>	_
New Romanian Leu	_	· —	_	_	_
New Russian Ruble	_	_	_	_	_
New Taiwan Dollar	17,311	1,719,433	_	_	_
New Turkish Lira	162	313,172	_		_
New Zealand Dollar	1,902	97,322	_	74,993	1,714
Norwegian Krone	5,112	785,166	_	11,368	2,159
Pakistan Rupee	81	•	_	11,500	2,139
Peruvian Nouveau Sol	41	43,281	_	_	_
		14,734	_	_	_
Philippine Peso	78 510	75,741	_	00.510	_
Polish Zloty	513	237,856	_	86,516	70.704
Singapore Dollar	5,196	1,157,405	_	8,610	76,764
South African Rand	12,438	1,621,253	_	21,131	_
South Korean Won	4,753	3,170,600	_	_	_
Sri Lanka Rupee	3	_	_	_	_
Swedish Krona	11,447	1,893,891	_	67,535	226,486
Swiss Franc	23,649	4,733,863	_	180	20,894
Thailand Baht	1,705	423,410	_	_	_
Tunisian Dinar	_	_	_	_	_
Turkish Lira	156	237,619	_	_	_
UAE Dirham	180	16,263	_	_	_
U.S. Dollar	_	3,058	_	_	_
Total investments subject					
to foreign currency risk \$	1,076,703 \$	92,501,060	\$ 4,114,540	\$ 6,717,417	\$ 4,810,008
<u>=</u>	-,,,,,,,,,,,,,,,,,,,,,,,,,,,,,,,,,,,,,,	,,	-, -, -, -, -, -, -		

Spot	Forward	
Contracts	Contracts	Total
\$ 31	\$ 10	\$ 41
(37)	(2,544)	5,799,248
_		886
(2)	(1,354)	2,829,407
1	18,057	14,234,063
_	(6,317)	7,765,446
_		3,058
155	(108)	188,608
_	226	5,350
_	_	67,901
- .	(1,781)	87,310
(1)	(975)	835,079
	(20)	112,331
128	(73,879)	34,998,468
_	_	44,988
_	_	1,849
_	614	5,803,770
_	(321)	119,737
_	294	1,762,440
_	(5)	601,389
4	(499) (43,682)	401,250 14,761,843
4	(43,002)	14,761,643
		16,688
_	28	475,103
4	317	954,205
	(31)	10,439
_	(394)	(394)
_	` 10 [°]	` 10 [°]
_	(247)	1,736,497
_	`-	313,334
_	(1,325)	174,606
(1)	(953)	802,851
_	_	43,362
63	373	15,211
_	(77)	75,742
_	(1,800)	323,085
-	(188)	1,247,787
14	964	1,655,800
_	580	3,175,933
_	(4.404)	3
4	(1,424)	2,197,939
10	(13,453)	4,765,143 424,771
_	(344)	
_	(12) 347	(12)
-	34 <i>1</i> _	238,122 16,443
_	_	3,058
\$ 373	\$ (129,896)	\$ 109,090,205

C. Discretely Presented Component Units

The discretely presented component units consist of the University of California (University) and its foundations, the State Compensation Insurance Fund (SCIF), the California Housing Finance Agency (CalHFA), the Public Employees' Benefits Fund administered by CalPERS, and various funds that constitute 3% of the total investments of discretely presented component units. State law, bond resolutions, and investment policy resolutions allow component units to invest in U.S. government securities, state and municipal securities, commercial paper, corporate bonds, investment agreements, real estate, and other investments. Additionally, a portion of the cash and pooled investments of SCIF, CalHFA, and other component units is invested in the State Treasurer's pooled investment program.

The investments of the University of California, a discretely presented component unit, are primarily stated at fair value. Investments authorized by the regents include equity securities, fixed-income securities, and certain other asset classes. The equity portion of the investment portfolio includes domestic and foreign common and preferred stocks, which may be included in actively or passively managed strategies, along with a modest exposure to private equities. Private equities include venture capital partnerships, buy-outs, and international funds. The fixed-income portion of the investment portfolio may include both domestic and foreign securities, as well as certain securitized investments including mortgage-backed and asset-backed securities. Absolute return strategies, incorporating short sales, plus derivative positions to implement or hedge an investment position, are also authorized. Where donor agreements have placed constraints on allowable investments, assets associated with endowments are invested in accordance with the terms of the agreements.

The university participates in a securities lending program as a means to augment income. Campus foundations' cash, cash equivalents, and investments that are invested with the university and managed by the university's treasurer are included in the university's investment pools that participate in a securities lending program. The campus foundations' allocated share of the program's cash collateral received, investment of cash collateral, and collateral held for securities lending is determined based upon the foundations' equity in the investment pools. The Board of Trustees for each campus foundation may also authorize participation in a direct securities lending program. The university loans securities to selected brokerage firms and receives collateral that equals or exceeds the fair value of such investments during the period of the loan. Collateral may be cash or securities issued by the U.S. government or its agencies, or the sovereign or provincial debt of foreign countries. Securities collateral cannot be pledged or sold by the university unless the borrower defaults. Loans of domestic equities and all fixed-income securities are initially collateralized at 102% of the fair value of the securities loaned. Loans of foreign equities are initially collateralized at 105%. All borrowers are required to provide additional collateral by the next business day if the value falls to less than 100% of the fair value of the securities loaned. The university earns interest and dividends on the collateral held during the loan period, as well as a fee from the brokerage firm, and it is obligated to pay a fee and a rebate to the borrower. The university receives the net investment income. As of June 30, 2011, the university had insignificant exposure to borrower default because the amounts that it owed the borrowers were substantially the same as the amounts the borrowers owed the university. The university is indemnified by its lending agents against any losses incurred as a result of borrower default.

Securities loans immediately terminate upon notice by either the university or the borrower. Cash collateral is invested by the university's lending agents in short-term investment pools in the university's name, with guidelines approved by the university. As of June 30, 2011, the securities in these pools had a weighted average maturity of 17 days.

Table 10 presents the investments, including derivative instruments, of the discretely presented component units by investment type.

Table 10

Schedule of Investments - Discretely Presented Component Units

June 30, 2011

(amounts in thousands)

	Fair Value
Investment Type	
Equity securities	\$ 5,457,292
Debt securities*	34,395,060
Investment contracts	238,662
Mutual funds	6,199,694
Real estate	702,876
Money market securities	730,843
Private equity	942,256
Mortgage loans	705,970
Externally held irrevocable trusts	265,681
Securities lending collateral	2,168,495
Invested for others	(1,780,375)
Other	1,849,111
Total investments	\$ 51,875,565
* Debt securities include short-term investments not included in cash and pooled investments.	

1. Interest Rate Risk

Interest rate risk for the university's short-term investment pool is managed by constraining the maturity of all individual securities to be less than five and one-half years. There is no restriction on weighted average maturity of the portfolio, as it is managed relative to the liquidity demands of the investors. Portfolio guidelines for the fixed-income portion of the university's general endowment pool limit weighted average effective duration to the effective duration of the Citigroup Large Pension Fund Index and Lehman Aggregate Index, plus or minus 20%.

SCIF guidelines provide that 15% or more of its total portfolio shall be maintained in securities maturing in five years or less. For information about CalPERS' policies related to interest rate risk, refer to Section B, Fiduciary Funds.

Table 11 presents the interest rate risk of the fixed-income or variable-income securities of the major discretely presented component units.

Table 11

Schedule of Investments in Fixed-Income or Variable-Income Securities - Discretely Presented Component Units - Interest Rate Risk

June 30, 2011 (amounts in thousands)

	University of			University of			
	California			California Foundations			
	Fair Value at Effective		Fair Value at		Effective		
Investment Type	Year End Duration ¹		Year End		Duration ¹		
U.S. Treasury bills, notes, and bonds	\$ 1,351,366	1.10	\$	222,691	3.10		
U.S. Treasury strips	102,041	8.00		115	_		
U.S. Treasury inflation-protected securities	225,994	4.50		_	_		
U.S. government-backed securities	_	_		3,071	3.70		
U.S. government-backed asset-backed securities	_	_		145	2.30		
Corporate bonds	5,012,475	3.40		80,190	3.60		
Commercial paper	2,517,403	0.10		_	_		
U.S. agencies	981,541	2.10		10,594	3.00		
U.S. agencies asset-backed securities	238,328	4.50		74,020	1.70		
Corporate asset-backed securities	100,994	4.50		6,510	0.20		
Supranational/foreign	1,263,165	4.60		745	4.20		
Corporate (foreign currency denominated)	18,060	2.10		_	_		
U.S. bond funds	81,410	5.00		318,165	4.50		
Non-U.S. bond funds	_	_		50,741	5.80		
Money market funds	257,403	_		436,960	1.40		
Mortgage loans	705,548	_		422	_		
Forward contracts on a to-be-announced basis	(1,740)	_		(1,081)	_		
Other	221,836	0.30		11,960	5.20		
Total	\$ 13,075,824	=	\$	1,215,248			
	State Compensation		California Housing				
	Insurance Fund		Finance Agency				
	Fair Value at	Weighted Average	-	in Malora at	Effective		
Investment Type	Fair Value at Maturity Year End (in years)		Fair Value at Year End		Duration ¹		
U.S. Treasury and agency securities	\$ 4,488,519	3.43	\$	378,607			
Municipal securities	613,986	16.23	φ	370,007	16.91		
	275,994	4.56		_	_		
Other government Corporate bonds	•	3.78		_	_		
·	3,836,001 1,658,568	3.78 15.18		_	_		
Special revenue		23.19		_	_		
Mutual funds	8,402,552 10,488	23.19 0.04		_	_		
Other	10,400	0.04		— 77,599	_		
	\$ 19,286,108	- -	\$	456,206	_		
Total	φ 19,200,100	=	•	430,200			

¹ Effective duration is the approximate change in price of the security resulting from a 100 basis points (1 percentage point) change in the level of interest rates. It is not a measure of time.

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Table 12 identifies the debt securities that are highly sensitive to interest rate fluctuations (to a greater degree than already indicated in the information provided previously) because of the existence of prepayment or conversion features, although the effective duration of these securities may be low.

Table 12

Schedule of Highly Sensitive Investments in Debt Securities – University of California and its Foundations – Interest Rate Risk June 30, 2011

(amounts in thousands)

		Univers Califor	-
	Fair Value at Year End		Effective Duration
Mortgage-Backed Securities These securities are primarily issued by the Federal National Mortgage Association (Fannie Mae), Government National Mortgage Association (Ginnie Mae) and Federal Home Loan Mortgage Corporation (Freddie Mac) and include short embedded prepayment options. Unanticipated prepayments by the obligees of the underlying asset reduce the total expected rate of return.	\$	203,249	4.90
Collateralized Mortgage Obligations Collateralized mortgage obligations (CMOs) generate a return based upon either the payment of interest or principal on mortgages in an underlying pool. The relationship between interest rates and prepayments makes the fair value highly sensitive to changes in interest rates. In falling interest rate environments, the underlying mortgages are subject to a higher propensity of prepayments. In a rising interest rate environment, the underlying mortgages are subject to a lower propensity of prepayments.		15,133	3.80
Other Asset-Backed Securities Other asset-backed securities also generate a return based upon either the payment of interest or principal on obligations in an underlying pool, generally associated with auto loans or credit cards. As with CMOs, the relationship between interest rates and prepayments makes the fair value highly sensitive to changes in interest rates.		16,369	0.50
Variable-Rate Securities These securities are investments with terms that provide for the adjustment of their interest rates on set dates and are expected to have fair values that will be relatively unaffected by interest rate changes. Variable-rate securities may have limits on how high or low the interest rate may change. These constraints may affect the market value of the security.		140,479	3.50
Callable Bonds Although bonds are issued with clearly defined maturities, an issuer may be able to redeem, or call, a bond earlier than its maturity date. The university must then replace the called bond with a bond that may have a lower yield than the original. The call feature causes the fair value to be highly sensitive to changes in interest rates.		1,150,143	3.30
Convertible Bonds Convertible bonds are fixed-income securities with coupon rates that tend to be lower than those in conventional debt issues. Consequently, an increase in the market's rate of interest causes a greater decline in the price of issues of convertible bonds than that of non-convertible bonds.		1,198	9.10

University of California Foundations						
	r Value at ear End	Effective Duration				
\$	63,422	1.60				
	2,833	2.80				
	6,510	0.20				
	_	_				
	458	4.20				
	_	_				

2. Credit Risk

The investment guidelines for the university's short-term investment pool provide that no more than 5% of the total market value of the pool's portfolio may be invested in securities rated below investment grade (BB, Ba, or lower). The average credit quality of the pool must be A or better and commercial paper must be rated at least A-1, P-1, or F-1. For its general endowment pool, the University uses a fixed-income benchmark, the Barclays Capital Aggregate Index, comprising approximately 25% high grade corporate bonds and 36% mortgage/asset-backed securities, all of which carry some degree of credit risk. The remaining 39% are government-issued bonds. Credit risk in this pool is managed primarily by diversifying across issuers, and portfolio guidelines mandate that no more than 10% of the market value of fixed-income securities may be invested in issues with credit ratings below investment grade. Further, the weighted average credit rating must be A or higher.

SCIF investment guidelines provide that securities issued and/or guaranteed by the government of Canada and its political subdivisions must be rated Aa3/AA- or better by two nationally recognized rating services. No single Canadian political subdivision may exceed 0.75% of the book value of the portfolio. Canadian political subdivisions in aggregate shall not exceed 5% of the portfolio. Securities issued and/or guaranteed by a state or its political subdivision must be rated A3/A- or better by a nationally recognized rating service. Securities issued by a qualifying corporation and purchased prior to May 9, 2008, must be rated A3/A- or better by a nationally recognized rating service.

Table 13 presents the credit risk of the fixed-income or variable-income securities of the major discretely presented component units.

Table 13

Schedule of Investments in Fixed-Income or Variable-Income Securities – Major Discretely Presented Component Units – Credit Risk

June 30, 2011 (amounts in thousands)

Credit Rating		
Short-term	Long-term	 Fair Value
A-1+	AAA	\$ 14,870,491
A-1/P-1	AA2/AA	5,837,000
A-2	A2/A	6,944,642
A-3	BAA2/BBB	1,803,510
В	BA2/BB	277,382
В	B2/B	280,123
С	CC or below	59,730
Not rated		 1,916,551
Total fixed-income securities		\$ 31,989,429

3. Concentration of Credit Risk

Investment guidelines addressing concentration of credit risk related to the investment-grade fixed-income portion of the university's portfolio include a limit of no more than 3% of the portfolio's market value to be invested in any single issuer (except for securities issued by the U.S. government or its agencies). These same guidelines apply to the university's short-term investment pool. The university did not have investments in a single issuer that represented 5% or more of total fair value of all investments as of June 30, 2011. Each campus foundation may have its own individual investment policy designed to limit exposure to a concentration of credit risk.

4. Custodial Credit Risk

The university's securities are registered in its name by the custodial bank as an agent for the university. Other types of investments represent ownership interests that do not exist in physical or book-entry form. As a result, custodial credit risk is remote.

5. Foreign Currency Risk

The university's portfolio guidelines for U.S. investment-grade fixed-income securities allow exposure to non-U.S. dollar denominated bonds up to 10% of the total portfolio market value. Exposure to foreign currency risk from these securities may be fully or partially hedged using forward foreign currency exchange contracts. Under the university's investment policies, such instruments are not permitted for speculative use or to create leverage.

Table 14 identifies the investments of the University of California – including its campus foundations – that are subject to foreign currency risk.

Table 14

Schedule of Investments – University of California – Foreign Currency Risk June 30, 2011
(amounts in thousands of U.S. dollars at fair value)

				Inv	estment				
Currency	Equity	Rea	Real Estate		rivatives	Fixed-Income		Total	
Australian Dollar	\$ 119,606	\$	3,345	\$	(892)	\$	_	\$	122,059
Brazilian Real	_		_		_		2,855		2,855
British Pound Sterling	309,987		1,799		(320)		_		311,466
Canadian Dollar	143,905		_		(778)		_		143,127
Danish Krone	15,635		_		_		_		15,635
Euro	481,601		2,571		(2,919)		2,177		483,430
Hong Kong Dollar	53,939		4,399		_		_		58,338
Indonesian Rupiah	_		_		_		2,023		2,023
Israeli Shekel	7,772		_		_		_		7,772
Japanese Yen	301,507		2,820		435		_		304,762
Malaysian Ringgit	_		_		_		2,207		2,207
Mexican Peso	_		_		_		2,256		2,256
Norwegian Krone	15,039		_		_		_		15,039
Polish Zloty	_		_		_		1,515		1,515
Singapore Dollar	26,617		1,702		_		_		28,319
South African Rand	_		_		_		2,153		2,153
Swedish Krona	46,593		_		(514)		_		46,079
Swiss Franc	130,943		_		_		_		130,943
Turkish Lira	_		_		_		1,191		1,191
Other	17,166		2,599		123		1,683		21,571
Commingled currencies	1,236,531		_		_		41,200		1,277,731
Total investments subject to									
foreign currency risk	\$ 2,906,841	\$	19,235	\$	(4,865)	\$	59,260	\$	2,980,471

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NOTE 4: ACCOUNTS RECEIVABLE

Table 15 presents the disaggregation of accounts receivable attributable to taxes, interest expense reimbursements, Lottery retailer collections, California State University, and unemployment program receipts. Other receivables are for interest, gifts, grants, various fees, penalties, and other charges.

Table 15

Schedule of Accounts Receivable

June 30, 2011 (amounts in thousands)

	Taxes	R	eimbursement of Accrued Interest Expense	 Lottery Retailers	 Jnemployment Programs
Current governmental activities					
General FundFederal Fund	 8,448,123 —	\$		\$ 	\$ _
Transportation Fund	502,001				_
Nonmajor governmental funds	71,063 —				
Total current governmental activities	\$ 9,021,187	\$		\$ 	\$
Amounts not scheduled for collection					
during the subsequent year	\$ 1,494,719	\$		\$ 	\$
Current business-type activities					
Water Resources Fund		\$		\$ 	\$ _
Public Building Construction Fund			170,480		_
State Lottery Fund				262,511	_
Unemployment Programs Fund					242,655
California State University					_
Nonmajor enterprise funds	_				_
Adjustment:					
Account reclassification	 		(170,480)	 	
Total current business-type activities	\$ 	\$		\$ 262,511	\$ 242,655
Amounts not scheduled for collection					
during the subsequent year	\$ 	\$		\$ 	\$ 22,503

	California				
	State				
	University	_	Other		Total
\$	_	\$	854,371	\$	9,302,494
			1,034		1,034
			291,012		793,013
			1,023,789		1,094,852
			119,226		119,226
\$		\$	2,289,432	\$	11,310,619
\$		\$	263,173	\$	1,757,892
-		_		-	
\$		\$	80,301	\$	80,301
	_		_		170,480
	_		_		262,511
	_				242,655
	159,389				159,389
	_		56,615		56,615
	_		(2,491)		(172,971)
\$	159,389	\$	134,425	\$	798,980
_	,,,,,,	<u> </u>	- ,	÷	,
\$	214,146	\$		\$	236,649

NOTE 5: RESTRICTED ASSETS

Table 16 presents a summary of the legal restrictions placed on assets in the enterprise funds of the primary government and the discretely presented component units.

Table 16

Schedule of Restricted Assets

June 30, 2011

(amounts in thousands)

	and	Cash I Pooled estments	lnv	restments	ue From Other vernments	F	Loans Receivable	Total
Primary government								
Debt service	\$	1,626,432	\$	391,132	\$ 65,598	\$	238,597	\$ 2,321,759
Construction		941,545		17,815			_	959,360
Operations		1,444,429		463				1,444,892
Other		2,371		1,448				3,819
Total primary government		4,014,777		410,858	 65,598		238,597	 4,729,830
Discretely presented component units								
Debt service		192,071		37,380	 			 229,451
Total discretely presented component units		192,071		37,380	 			 229,451
Total restricted assets	\$	4,206,848	\$	448,238	\$ 65,598	\$	238,597	\$ 4,959,281

NOTE 6: NET INVESTMENT IN DIRECT FINANCING LEASES

The State Public Works Board, an agency that accounts for its activities as an enterprise fund, has entered into lease-purchase agreements with various other primary government agencies, the University of California, and certain local agencies. Payments from these leases will be used to satisfy the principal and interest requirements of revenue bonds issued by the State Public Works Board.

California State University (CSU) accounts for its lease activities in the State University Dormitory Building Maintenance and Equipment Fund, a major enterprise fund, has entered into 30-year capital lease agreements with certain auxiliary organizations. These agreements lease existing and newly constructed facilities to the auxiliary organizations. A portion of the proceeds from certain revenue bonds issued by CSU were used to finance the construction of these facilities.

Table 17 summarizes the minimum lease payments to be received by the primary government.

Table 17

Schedule of Minimum Lease Payments to be Received by the Primary Government (amounts in thousands)

Year Ending June 30	Primary Government Agencies	University of California	California State University	Local Agencies	Total
2012	\$ 533,166	\$ 199,983	\$ 26,595	\$ 64,641	\$ 824,385
2013	523,965	199,864	28,494	63,671	815,994
2014	525,519	199,665	29,804	63,776	818,764
2015	523,975	191,290	29,741	62,177	807,183
2016	520,255	157,741	27,121	53,892	759,009
2017-2021	2,216,888	801,448	145,369	124,990	3,288,695
2022-2026	1,493,173	561,638	150,786	63,523	2,269,120
2027-2031	1,042,217	424,790	141,118	56,823	1,664,948
2032-2036	374,519	85,747	75,694	7,513	543,473
2037-2041	_	_	25,775	_	25,775
2042-2046	_	_	17,972	_	17,972
Total minimum lease payments	7,753,677	2,822,166	698,469	561,006	11,835,318
Less: unearned income	3,042,494	933,071	298,873	142,444	4,416,882
Net investment in direct financing leases	\$ 4,711,183	\$ 1,889,095	\$ 399,596	\$ 418,562	\$ 7,418,436

NOTE 7: CAPITAL ASSETS

Table 18 summarizes the capital activity for the primary government, which includes \$6.7 billion in capital assets related to capital leases.

Table 18

Schedule of Changes in Capital Assets – Primary Government
June 30, 2011
(amounts in thousands)

		Beginning Balance (Restated)		Additions	D	eductions		Ending Balance
Governmental activities		,	_					
Capital assets not being depreciated/amortized								
Land	\$	16,310,911	\$	308,217	\$	19,742	\$	16,599,386
State highway infrastructure		60,090,779		1,407,056		58,851		61,438,984
Collections		22,488		_		66		22,422
Construction in progress		6,950,846		2,855,891		1,992,721		7,814,016
Intangible assets		480,910		75,779		22,597		534,092
Total capital assets not being depreciated/amortized		83,855,934		4,646,943		2,093,977		86,408,900
Capital assets being depreciated/amortized								
Buildings and improvements		17,937,945		629,183		130,938		18,436,190
Infrastructure		660,679		51,374		29		712,024
Equipment and other assets		4,396,272		308,401		332,238		4,372,435
Intangible assets		511,825		144,472		7,619		648,678
Total capital assets being depreciated/amortized		23,506,721	_	1,133,430		470,824		24,169,327
Less accumulated depreciation/amortization for:								
Buildings and improvements		5,608,501		465,898		76,531		5,997,868
Infrastructure		246,693		23,498		2		270,189
Equipment and other assets		3,349,946		394,345		255,808		3,488,483
Intangible assets		322,960		40,693		6,104		357,549
Total accumulated depreciation/amortization		9,528,100		924,434		338,445		10,114,089
Total capital assets being depreciated/amortized, net	-	13,978,621		208,996		132,379		14,055,238
Governmental activities, capital assets, net	\$	97,834,555	\$	4,855,939	\$	2,226,356	\$	100,464,138
Business-type activities			_				_	
Capital assets not being depreciated/amortized								
Land	\$	217,014	\$	_	\$	2,197	\$	214,817
Collections		1,885		812		_		2,697
Construction in progress		1,595,797		567,058		641,737		1,521,118
Intangible assets		48,477		99,291		9,135		138,633
Total capital assets not being depreciated/amortized		1,863,173		667,161		653,069		1,877,265
Capital assets being depreciated/amortized								
Buildings and improvements		9,146,313		724,339		1,107		9,869,545
Infrastructure		174,427		14,083		_		188,510
Equipment and other assets		435,015		88,586		13,663		509,938
Intangible assets		209,224		10,272		949		218,547
Total capital assets being depreciated/amortized		9,964,979	_	837,280		15,719		10,786,540
Less accumulated depreciation/amortization for:								
Buildings and improvements		3,450,848		252,447		135		3,703,160
Infrastructure		29,507		7,133		_		36,640
Equipment and other assets		256,005		42,329		9,779		288,555
Intangible assets		63,211		22,008		638		84,581
Total accumulated depreciation/amortization		3,799,571	_	323,917		10,552		4,112,936
Total capital assets being depreciated/amortized, net		6,165,408	_	513,363	_	5,167		6,673,604
Business-type activities, capital assets, net	\$	8,028,581	\$	1,180,524	\$	658,236	\$	8,550,869
			_		_	<u> </u>	_	<u> </u>

Table 19 summarizes the depreciation expense charged to the activities of the primary government.

Table 19

Schedule of Depreciation Expense – Primary Government

June 30, 2011

(amounts in thousands)

	Amount
Governmental activities	
General government	\$ 108,852
Education	189,271
Health and human services	68,436
Resources	54,456
State and consumer services	57,913
Business and transportation	221,300
Correctional programs	180,025
Internal service funds (charged to the activities that utilize the fund)	44,181
Total governmental activities	924,434
Business-type activities	323,917
Total primary government	\$ 1,248,351

Table 20 summarizes the capital activity for discretely presented component units.

Table 20

Schedule of Changes in Capital Assets – Discretely Presented Component Units

June 30, 2011

(amounts in thousands)

	Beginning Balance		Additions	n	eductions		Ending Balance
Capital assets not being depreciated/amortized	Bularioc		Additions		caaotiono	_	Bularioc
Land	\$ 903,938	\$	26,324	\$	1,548	\$	928,714
Collections	324,654		12,364		4,890		332,128
Construction in progress	2,864,451		113,922		18,908		2,959,465
Intangible assets	5,083		8		1		5,090
Total capital assets not being depreciated/amortized	4,098,126		152,618		25,347		4,225,397
Capital assets being depreciated/amortized							
Buildings and improvements	25,715,676		1,904,355		50,606		27,569,425
Infrastructure	593,008		39,295		295		632,008
Equipment and other depreciable assets	8,851,474	*	620,763		275,086		9,197,151
Intangible assets	426,290	*	87,264		5,065		508,489
Total capital assets being depreciated/amortized	35,586,448		2,651,677		331,052		37,907,073
Less accumulated depreciation/amortization for:							
Buildings and improvements	8,947,259		889,695		28,701		9,808,253
Infrastructure	240,576		21,700		115		262,161
Equipment and other depreciable assets	5,990,162	*	548,241		224,596		6,313,807
Intangible assets	321,948		50,327		4,879		367,396
Total accumulated depreciation/amortization	15,499,945		1,509,963		258,291		16,751,617
Total capital assets being depreciated/amortized, net	20,086,503		1,141,714		72,761		21,155,456
Capital assets, net	\$ 24,184,629	\$	1,294,332	\$	98,108	\$	25,380,853
Restated							

NOTE 8: ACCOUNTS PAYABLE

Accounts payable are amounts due taxpayers, vendors, customers, beneficiaries, and employees related to different programs. Table 21 presents details related to accounts payable.

The adjustment for the fiduciary funds represents amounts due fiduciary funds that were reclassified as external payables on the government-wide Statement of Net Assets.

Table 21

Schedule of Accounts Payable
June 30, 2011
(amounts in thousands)

	Education		Health and Human Services	R	esources	I	Business and ransportation	G	General overnment and Others	_	Total
Governmental activities											
General Fund	\$ 1,962	\$	697,902	\$	106,277	\$	405	\$	525,845	\$	1,332,391
Federal Fund	125,730		424,212		138,853		222,131		465,530		1,376,456
Transportation Fund	_		55		2,331		412,827		32,763		447,976
Nonmajor governmental funds	61,085		509,224		393,861		22,608		680,842		1,667,620
Internal service funds	126		_		17,229				189,916		207,271
Adjustment:											
Fiduciary funds	9,339,285		3,874,587				24,545		654,703		13,893,120
Total governmental activities	\$ 9,528,188	\$	5,505,980	\$	658,551	\$	682,516	\$	2,549,599	\$	18,924,834
Business-type activities											
Electric Power Fund	\$ —	\$		\$	174,962	\$	_	\$	_	\$	174,962
Water Resources Fund	_				59,852		_		_		59,852
Public Building Construction Fund	_						_		19,450		19,450
State Lottery Fund							_		53,377		53,377
Unemployment Program Fund	_		4				_				4
California State University Fund	173,257						_				173,257
Nonmajor enterprise funds	5,453		580		56		43,071		2,986		52,146
Adjustment:											
Fiduciary funds		_							639		639
Total business-type activities	\$ 178,710	\$	584	\$	234,870	\$	43,071	\$	76,452	\$	533,687

NOTE 9: SHORT-TERM FINANCING

As part of its cash management program, the State regularly issues short-term obligations to meet cash flow needs. The State issues revenue anticipation notes (RANs) to partially fund timing differences between revenues and expenditures. A significant portion of the General Fund revenues are received in the latter half of the fiscal year, while disbursements are paid more evenly throughout the fiscal year. If additional external cash flow borrowing is required, the State issues revenue anticipation warrants (RAWs).

To fund cash flow needs for the 2010-11 fiscal year, the State issued \$6.7 billion of interim RANs through private placement on October 28, 2010. The interim RANs were repaid on November 23, 2010. In addition, the State issued \$10 billion of RANs on November 23, 2010. The RANs were repaid during May and June 2011.

The California Housing Finance Agency, a discretely presented component unit, entered into an agreement with a financial institution to provide a line of credit for short-term borrowings of up to \$100 million, which may increase up to \$150 million. The line of credit ended on February 28, 2011, as such there was no outstanding balance at June 30, 2011.

NOTE 10: LONG-TERM OBLIGATIONS

As of June 30, 2011, the primary government had long-term obligations totaling \$163.9 billion. Of that amount, \$5.8 billion is due within one year. The largest change in governmental activities long-term obligations is an increase of \$2.6 billion in net other postemployment benefits obligations. Another notable increase occurred in general obligation bonds payable.

As of June 30, 2011, the pollution remediation obligations increased by \$103 million, to \$804 million. Under federal Superfund law, responsibility for pollution remediation is placed upon current and previous owners or operators of polluted sites. Currently, the State's most significant superfund site is the Stringfellow Class 1 Hazardous Waste Disposal Facility (Stringfellow) located in Riverside County. As of June 30, 2011, the State estimates that remediation costs at Stringfellow will total \$378 million. At two other sites, Leviathan Mine and BKK Landfill, obligating events have occurred that will probably result in significant liability to the State, but reasonable estimates of the remediation costs cannot be made at this time. Currently, litigation is in process to determine the responsible party for Leviathan Mine, a superfund site. The State's activities at the site relate to water pollution remediation. BKK is a closed Class 1 landfill site at which the State is conducting post-closure care. In addition to superfund sites, the State's other pollution remediation efforts include underground storage tank removal and cleanup, cleanup of polluted groundwater, and contaminated soil removal and cleanup.

Not included in Note 10 are certain state mandated programs that are still in the adjudication process. Until the Commission on State Mandates (CSM) rules on a test claim and parameters and guidelines for the claim has been established, expected costs cannot be reasonably determined; however, a positive finding for any of the claimants could individually or in aggregate pose a significant cost to the State.

The other long-term obligations for governmental activities consist of \$3.0 billion for net pension obligations, \$171 million owed for lawsuits, the University of California unfunded pension liability of \$44 million, and the California Technology Agency notes payable of \$25 million. The compensated absences will be liquidated by the General Fund, special revenue funds, capital projects funds, and internal service funds. Workers' compensation and capital leases will be liquidated by the General Fund, special revenue funds, and internal service funds. The General Fund will liquidate net pension obligations, the Proposition 98 funding guarantee, lawsuits, reimbursement of costs incurred by local agencies and school districts for costs mandated by the State, and the University of California pension liability.

The largest change in business-type long-term obligations is an increase of \$3.8 billion for loans payable to the U.S. Department of Labor to cover shortfalls in the Unemployment Programs Fund. The \$845 million in other long-term obligations for business-type activities is mainly for advance collections.

Table 22 summarizes the changes in the long-term obligations during the year ended June 30, 2011.

Table 22

Schedule of Changes in Long-term Obligations (amounts in thousands)

	Balance	A alalisi	Dadu-#	Balance	Due Within	Noncurrent
	July 1, 2010	Additions	Deductions	June 30, 2011	One Year	Liabilities
Governmental activities	Φ 0.400.004	Φ 05.500	Φ 00.055	Φ 0.400.507	Φ.	Φ 0.100.507
Loans payable Compensated absences payable	\$ 2,109,324 3,367,464	\$ 35,538 * 1,425,240	\$ 22,355 1,054,108	\$ 2,122,507 3,738,596	\$ — 17,871	\$ 2,122,507 3,720,725
Certificates of participation and commercial paper	1,334,319	_	4,471	1,329,848	4,760	1,325,088
Accreted interest	7,800	658	2,966	5,492	2,704	2,788
Certificates of participation and commercial paper payable	1,342,119	658	7,437	1,335,340	7,464	1,327,876
Capital lease obligations	4,967,290	204,631	289,688	4,882,233	338,225	4,544,008
General obligation bonds	76,705,309	4,525,000	2,775,554	78,454,755	2,196,360	76,258,395
Accreted interest	3,792	268	4,060	_		_
Premiums/discounts/other	•	32,607	54,965	1,014,330	55,749	958,581
General obligation bonds payable.	77,745,789	4,557,875	2,834,579	79,469,085	2,252,109	77,216,976
Revenue bonds	7,893,297	_	170,769	7,722,528	163,558	7,558,970
Accreted interest	212,568	59,153		271,721	· —	271,721
Premiums/discounts/other	(493,926)		(10,769)	(483,157)	(11,214)	(471,943)
Revenue bonds payable		59,153	160,000	7,511,092	152,344	7,358,748
Net other postemployment						
benefits obligation	7,049,820	* 4,038,482	1,481,371	9,606,931	_	9,606,931
Pollution remediation obligations	755,612	* 127,802	79,139	804,275	42,452	761,823
Proposition 98 funding guarantee	3,755,693	2,958	671,800	3,086,851	450,000	2,636,851
Mandated costs	5,189,809	785,559	91,725	5,883,643	142,580	5,741,063
Workers' compensation	2,706,739	* 699,770	376,653	3,029,856	338,906	2,690,950
Other long-term obligations	2,958,816	* 570,970	287,220	3,242,566	65,431	3,177,135
Total governmental activities	\$ 119,560,414	\$ 12,508,636	\$ 7,356,075	\$ 124,712,975	\$ 3,807,382	\$ 120,905,593
Business-type activities						
Benefits payable	\$ 2,586	\$ —	\$ 2,586	\$ —	\$ —	\$ —
Loans payable	7,203,296	3,754,686		10,957,982	_	10,957,982
Lottery prizes and annuities	1,464,849	2,112,738	2,225,885	1,351,702	465,693	886,009
Compensated absences payable	296,147	* 125,341	127,025	294,463	128,993	165,470
Certificates of participation and						
commercial paper	64,518	148,510	73,054	139,974	_	139,974
Capital lease obligation	786,216	* 5,273	_	791,489	57,331	734,158
General obligation bonds	1,479,140	_	259,125	1,220,015	100,080	1,119,935
Premiums/discounts/other	(1,477)	101		(1,376)		(1,376)
General obligation bonds payable.	1,477,663	101	259,125	1,218,639	100,080	1,118,559
Revenue bonds	24,454,403	1,860,675	3,090,850	23,224,228	1,193,425	22,030,803
Premiums/discounts/other	83,691	19,578	37,182	66,087	5,880	60,207
Revenue bonds payable	24,538,094	1,880,253	3,128,032	23,290,315	1,199,305	22,091,010
Net other postemployment benefits obligation	230,346	* 142,885	54,438	318,793		318,793
Other long-term obligations	963,597		162,950	845,141	54,324	790,817
Total business-type activities	\$ 37,027,312	\$ 8,214,281	\$ 6,033,095	\$ 39,208,498	\$ 2,005,726	\$ 37,202,772
* Restated	,,		,,		. ,-,-,-	,

NOTE 11: CERTIFICATES OF PARTICIPATION

Table 23 shows debt service requirements for certificates of participation, which are financed by lease payments from governmental activities. The certificates of participation were used to finance the acquisition and construction of a state office building.

Table 23

Schedule of Debt Service Requirements for Certificates of Participation – Primary Government (amounts in thousands)

June 30	Pr	incipal	lr	nterest	Total
2012	\$	7,576	\$	2,065	\$ 9,641
2013		7,503		2,140	9,643
2014		8,140		1,503	9,643
2015		8,565		1,075	9,640
2016		11,915		625	12,540
Total	\$	43,699	\$	7,408	\$ 51,107

NOTE 12: COMMERCIAL PAPER AND OTHER LONG-TERM BORROWINGS

The primary government has two commercial-paper-borrowing programs: a general obligation commercial paper program and an enterprise fund commercial paper program for the Department of Water Resources. Under the general obligation and enterprise fund programs, commercial paper (new issuance or rollover notes) may be issued at the prevailing market rate, not to exceed 11%, for periods not to exceed 270 days from the date of issuance. The proceeds from the initial issuance of commercial paper are restricted primarily for construction costs of general obligation bond program projects and certain state water projects. For both commercial-paper-borrowing programs, the commercial paper is retired by the issuance of long-term debt, so commercial paper is considered a noncurrent liability.

To provide liquidity for the programs, the State has entered into revolving credit agreements with commercial banks. The current "Letter of Credit" agreement for the general obligation commercial paper program, effective March 11, 2010, authorizes the issuance of notes in an aggregate principal amount not to exceed \$2.0 billion. The current agreement for the enterprise fund commercial paper program authorizes the issuance of notes in an aggregate principal amount not to exceed \$142 million. As of June 30, 2011, the enterprise fund commercial paper program had \$55 million in outstanding notes.

As of June 30, 2011, the general obligation commercial paper program had \$1.3 billion in outstanding commercial paper notes for governmental activities.

The primary government has a revenue bond anticipation note (BAN) program that consists of borrowing for capital improvements on certain California State University campuses. As of June 30, 2011, \$85.4 million in outstanding BANs existed in anticipation of the primary government issuing revenue bonds to the public.

The University of California, a discretely presented component unit, has established a \$2.0 billion commercial paper program with tax-exempt and taxable components. The program is supported by available investments in the university's investment pools. Commercial paper has been issued by the University to provide for interim

financing of the construction, renovation, and acquisition of certain facilities and equipment. Commercial paper is secured by a pledge of the net revenues derived from the University's ownership or operation of the projects financed—not by any encumbrance, mortgage, or other pledge of property—and does not constitute a general obligation of the University. At June 30, 2011, outstanding tax-exempt and taxable commercial paper totaled \$246 million and \$554 million, respectively. The University has other borrowings consisting of contractual obligations resulting from the acquisition of land or buildings and the construction and renovation of certain facilities. Included in other borrowings, which total \$197 million as of June 30, 2011, are various unsecured financing agreements with commercial banks totaling \$56 million.

NOTE 13: LEASES

The aggregate amount of lease commitments for facilities and equipment of the primary government in effect as of June 30, 2011, was approximately \$9.0 billion. Primary government leases that are classified as operating leases, in accordance with the applicable standards, contain clauses providing for termination. Operating lease expenditures are recognized as being incurred over the lease term. It is expected that, in the normal course of business, most of these operating leases will be replaced by similar leases.

The total present value of minimum capital lease payments for the primary government is comprised of \$745,000 from internal service funds and \$4.9 billion from other governmental activities. Note 10, Long-term Obligations, reports the additions and deductions of capital lease obligations. Also reported in Note 10 are the current and noncurrent portions of the capital lease obligations. Lease expenditures for the year ended June 30, 2011, amounted to approximately \$951 million.

Included in the capital lease commitments are lease-purchase agreements, amounting to a present value of net minimum lease payments of \$4.7 billion, that certain state agencies have entered into with the State Public Works Board, an enterprise fund agency. This amount represents 96.5% of the total present value of minimum capital lease payments of the primary government. Also included in the capital lease commitments are some lease-purchase agreements to acquire equipment.

The capital lease commitments do not include \$501 million in lease-purchase agreements with building authorities that are blended component units. These building authorities acquire or develop office buildings and then lease the facilities to state agencies. Upon expiration of the lease, title passes to the primary government. The costs of the buildings and the related outstanding revenue bonds and certificates of participation are reported in the government-wide financial statements. Accordingly, the lease receivables or capital lease obligations associated with these buildings are not included in the financial statements. Table 24 summarizes future minimum lease commitments of the primary government.

Table 24

Schedule of Future Minimum Lease Commitments – Primary Government (amounts in thousands)

			Capital	ıL	eases		
			Internal		Other		
Year Ending	Operating		Service		Governmental		
June 30	 Leases	_	Funds	_	Activities	_	Total
2012	\$ 324,128	\$	765	9	596,597	\$	921,490
2013	254,790				572,487		827,277
2014	180,136				565,052		745,188
2015	96,600				548,044		644,644
2016	70,969				528,995		599,964
2017-2021	116,173				2,218,303		2,334,476
2022-2026	7,551				1,493,173		1,500,724
2027-2031	3,871				1,042,217		1,046,088
2032-2036	3,236				374,519		377,755
2037-2041	2,725						2,725
2042-2046	663						663
2047-2051	463						463
2052-2056	126				_		126
2057-2061	77				_		77
2062-2066	33				_		33
2067-2071	33				_		33
2072-2076	33				_		33
2077-2081	33				_		33
2082-2086	33				_		33
2087-2091	33				_		33
2092-2096	33				_		33
2097-2101	12						12
Total minimum lease payments	\$ 1,061,751		765		7,939,387	\$	9,001,903
Less: amount representing interest			20		3,057,899		
Present value of net minimum lease payments		\$	745	\$	4,881,488		
. ,				=			

The aggregate amount of the major discretely presented component units' lease commitments for land, facilities, and equipment in effect as of June 30, 2011, was approximately \$4 billion. Table 25 presents the future minimum lease commitments for the University of California and the State Compensation Insurance Fund. Operating lease expenditures for the year ended June 30, 2011, amounted to approximately \$233 million for major discretely presented component units.

Table 25

Schedule of Future Minimum Lease Commitments – Major Discretely Presented Component Units (amounts in thousands)

Year Ending		Univ C Calif	of	•		State Compensation nsurance Fund	
June 30		Capital	_	Operating	_	Operating	Total
2012	\$	289,624	\$	91,946	\$	35,633	\$ 417,203
2013		272,568		74,137		29,490	376,195
2014		304,238		57,634		19,256	381,128
2015		237,140		43,240		11,469	291,849
2016		199,782		30,875		3,343	234,000
2017-2021		943,709		71,707			1,015,416
2022-2026		714,393		9,609			724,002
2027-2031		551,957		4,067			556,024
2032-2036		183,251		4,641			187,892
2037-2041				3,692			3,692
Total minimum lease payments		3,696,662	\$	391,548	\$	99,191	\$ 4,187,401
Less: amount representing interest		1,253,406					
Present value of net minimum lease payments	\$	2,443,256					

NOTE 14: COMMITMENTS

As of June 30, 2011, the primary government had commitments of \$7.4 billion for certain highway construction projects. The primary government also had commitments of \$682 million for terrorism prevention and disaster preparedness response projects, \$451 million for various education programs, \$425 million for services under the workforce development program, \$358 million for services provided under various public health programs, \$349 million for community service programs, \$89 million for services provided under the welfare program, \$64 million for services provided under the rehabilitation program, and \$21 million for services provided under the child support program.

The primary government had other commitments, totaling \$8.8 billion, that are not included as a liability on the Balance Sheet or the Statement of Net Assets. The \$8.8 billion in commitments includes grant agreements totaling approximately \$5.7 billion to reimburse other entities for construction projects for school building aid, parks, transportation-related infrastructure, housing and other improvements, and to reimburse counties and cities for costs associated with various programs. Any constructed assets will not belong to the primary government, whose payments are contingent upon the other entities entering into construction contracts. The \$8.8 billion in commitments includes \$581 million in undisbursed loan commitments for various programs aimed at providing housing and emergency shelter to needy persons. In addition, the \$8.8 billion in commitments includes \$779 million in long-term contracts to purchase power. Most of these contracts qualify

for the Normal Purchase Normal Sale (NPNS) exception under GASB 53 and, therefore, are not included on the Statement of Net Assets of the Electric Power Fund nor disclosed in Note 17.

The \$8.8 billion in commitments also includes contracts of \$607 million for the construction of water projects and the purchase and transmission of power that are not included as a liability on the Statement of Net Assets of the Water Resources Fund. Included in this amount are certain power purchase, sale, and exchange contracts. These contracts had a fair value of \$183 million as of June 30, 2011. The primary government had commitments of \$409 million for California State University construction projects. The University participates in forward-purchase contracts of natural gas and electricity. As of June 30, 2011, the University's obligation under these special purchase arrangements requires it to purchase at fixed prices an estimated total of \$32 million of electricity through March 2014 and \$59 million of natural gas through June 2017. The primary government also had commitments of \$2 million to veterans for the purchase of properties under contracts of sale. The California State Lottery Commission had commitments of \$681 million, of which \$673 million is for gaming and telecommunication systems and services and \$8 million is for a construction contract. These are long-term projects, and all of the contracts' needs may not have been defined. The projects will be funded with existing and future program resources or with the proceeds of revenue and general obligation bonds.

As of June 30, 2011, the primary government encumbered expenditures of \$803 million for the General Fund, \$3.8 billion for the Transportation Fund, and \$1.2 billion for the nonmajor governmental funds. See Note 2A for an explanation of the primary government's policy concerning encumbrances.

As of June 30, 2011, the discretely presented component units had other commitments that are not included as liabilities on the Statement of Net Assets. The University of California had authorized construction projects totaling \$3.0 billion. The university also made commitments to make investments in certain investment partnerships pursuant to provisions in the partnership agreements. These commitments totaled \$368 million as of June 30, 2011. The California Housing Finance Agency had no outstanding commitments to provide loans under its housing programs. The California Public Employees' Retirement System had capital commitments to private equity funds of \$16.2 billion and commitments to purchase real estate equity of \$6.9 billion that remained unfunded and not recorded as liabilities on the Statement of Net Assets of either the fiduciary or discretely presented component units.

NOTE 15: GENERAL OBLIGATION BONDS

The State Constitution permits the primary government to issue general obligation bonds for specific purposes and in such amounts as approved by a two-thirds majority of both houses of the Legislature and by a majority of voters in a general or direct primary election. The debt service for general obligation bonds is appropriated from the General Fund. Under the State Constitution, the General Fund is used first to support the public school system and public institutions of higher education; the General Fund can then be used to service the debt on outstanding general obligation bonds. Enterprise funds and certain other funds reimburse the General Fund for any debt service it provides on their behalf. General obligation bonds that are directly related to, and are expected to be paid from, the resources of enterprise funds are included as a liability of such funds in the financial statements. However, the General Fund may be liable for the payment of any principal and interest on these bonds that is not met from the resources of such funds.

As of June 30, 2011, the State had \$78.5 billion in outstanding general obligation bonds related to governmental activities and \$1.2 billion related to business-type activities. In addition, \$38.3 billion of general obligation bonds had been authorized but not issued, of which \$37.0 billion is related to governmental activities and \$1.3 billion is related to business-type activities. The total amount authorized but not issued includes \$11.3 billion authorized by the applicable finance committee for issuance in the form of commercial paper

notes. Of this amount, \$1.3 billion in general obligation indebtedness in the form of commercial paper notes was not yet retired by long-term bonds.

Note 10, Long-term Obligations, discusses the change to general obligation bonds payable.

A. Variable-rate General Obligation Bonds

The State issues both fixed and variable-rate general obligation bonds. As of June 30, 2011, the State had \$2.7 billion of variable-rate general obligation bonds outstanding, consisting of \$912 million in daily rate bonds and \$1.8 billion in weekly rate bonds. The interest rates associated with the daily rates and weekly rates are determined by the remarketing agents to be the lowest rate that would allow the bonds to sell on the effective date of such rate at a price (without regard to accrued interest) equal to 100% of the principal amount. The interest is paid on the first business day of each calendar month.

Letters of credit were issued to secure payment of principal and interest on the daily and weekly variable-rate bonds. Under these letters of credit, the credit providers pay all principal and interest payments to the bondholders; the State is then required to reimburse the credit providers for the amounts paid. Different credit providers exist for each series of variable-rate bonds issued. The letters of credit for the variable-rate bonds issued during the 2002-03 fiscal year have expiration dates of November 23, 2011, December 1, 2011, and December 1, 2012. The letters of credit for the variable-rate bonds issued during the 2004-05 fiscal year have an expiration date of October 15, 2012. The letters of credit for the variable-rate bonds issued during the 2005-06 fiscal year have expiration dates of November 10, 2011, January 12, 2012, and November 12, 2013.

Based on the schedules provided in the Official Statements, sinking fund deposits for the variable-rate general obligation bonds will be set aside in a mandatory sinking fund at the beginning of each of the following fiscal years: the 2015-16 through 2033-34 fiscal years and the 2039-40 fiscal year. The deposits set aside in any fiscal year may be applied, with approval of the State Treasurer and the appropriate bond finance committees, to the redemption of any other general obligation bonds then outstanding. To the extent that the deposit is not applied by January 31 of each fiscal year, the variable-rate general obligation bonds will be redeemed in whole or in part on an interest payment date in that fiscal year.

B. Economic Recovery Bonds

In 2004 voters approved the one-time issuance of Economic Recovery Bonds. The debt service for these bonds is payable from and secured by amounts available in the Economic Recovery Bond Sinking Fund, a debt service fund that consists primarily of revenues from a dedicated sales tax. However, the General Fund may be liable for the payment of any principal and interest on the bonds that cannot be paid from the Economic Recovery Bond Sinking Fund.

As of June 30, 2011, the State had \$7.2 billion of Economic Recovery Bonds outstanding. Of the \$7.2 billion outstanding, bonds totaling \$625 million are variable rate bonds, consisting of \$500 million in daily rate bonds and \$125 million in weekly rate bonds. The interest rates associated with the daily rates and weekly rates are determined by the remarketing agents to be the lowest rates that would enable them to sell the bonds for delivery on the effective date of such rate at a price (without regard to accrued interest) equal to 100% of the principal amount. The interest is paid on the first business day of each calendar month. As described in the Official Statement, payment of principal, interest, and purchase price upon tender, for a portion of these bonds, is secured by a direct-pay letter of credit. The State reimburses its credit providers for any amounts paid, plus interest. Different credit providers exist for each series of variable-rate bonds issued. The expiration date for these letters of credit is June 15, 2012.

C. Mandatory Tender Bonds

Of the \$7.2 billion in outstanding Economic Recovery Bonds, \$500 million have interest-reset dates of July 1, 2014. At that time, the bonds are subject to mandatory tender for purchase at a price equal to 100% of the principal amount, plus accrued interest, without premium. Upon mandatory tender, the State will seek to remarket these bonds. The debt service requirements published in the Official Statement differ from the calculation included in Table 26 because the statement presumes a successful remarketing at an interest rate of 4.0% per year. The debt service calculation in Table 26 uses the interest rates in effect at year-end, which are the same interest rates in effect until the applicable reset date. In the event of a failed remarketing, the State is required to return all tendered bonds to their initial purchasers and pay an annual interest rate of 11% until the bonds are successfully remarketed.

As of June 30, 2011, the State had \$1.0 billion in outstanding various-purpose general obligation bonds with interest reset dates beginning April 2, 2012. On each reset date, these bonds are subject to mandatory tender for purchase at a price equal to 100% of the principal amount thereof, plus accrued interest, without premium, unless the bonds have been called for redemption on or prior to that date. If the bonds are not redeemed, the interest rate mode for the bonds will be adjusted to a new mode, and the bonds will be remarketed by a remarketing agent appointed by the State. The State has not obtained any credit enhancement with respect to the mandatory tender of these bonds on the first mandatory tender date and does not expect to do so. The debt service calculation in Table 26 uses the interest rates in effect at year-end, which are the same interest rates in effect until the applicable reset dates, and assumes full redemption of the bonds beginning on April 1, 2029. In the event of a failed remarketing, funding for the payment of principal and interest will be provided by the General Fund.

D. Build America Bonds

In November 2010, the State issued taxable various-purpose general obligation bonds as "Build America Bonds" in the amount of \$3.0 billion. As of June 30, 2011, the State had \$13.5 billion in taxable various-purpose general obligation bonds outstanding that were issued as "Build America Bonds" under the American Recovery and Reinvestment Act of 2009 signed into law on February 17, 2009 (ARRA). While the bonds mature between 2020 and 2040, two series are part of the mandatory tender bonds previously described that have reset dates of April 2, 2012, and April 1, 2013. Pursuant to the ARRA, the State receives a cash subsidy payment from the United States Treasury equal to 35% of the interest payable by the State on the Build America Bonds on or near each interest payment date. The cash payment does not constitute a full faith and credit guarantee of the United States Government, but is required to be paid by the United States Treasury under the ARRA. The cash subsidy payments received are available for use by the General Fund.

E. Debt Service Requirements

Table 26 shows the debt service requirements for all general obligation bonds as of June 30, 2011. The estimated debt service requirements for the \$2.7 billion variable-rate general obligation bonds and the \$625 million variable-rate Economic Recovery Bonds are calculated using the actual interest rates in effect on June 30, 2011. The amounts do not reflect any interest subsidy under the Build America Bond program or any other offsets to general fund costs of debt service.

Table 26

Schedule of Debt Service Requirements for General Obligation Bonds (amounts in thousands)

Year Ending _	Gov	ernmental Activ	/ities	Business-type Activities					
June 30	Principal	Interest	Total	Principal	Interest	Total			
2012 \$	2,196,360	\$ 4,095,748	\$ 6,292,108	\$ 100,080	\$ 51,421	\$ 151,501			
2013	2,075,785	3,987,359	6,063,144	82,195	47,815	130,010			
2014	2,757,880	3,883,443	6,641,323	104,110	44,406	148,516			
2015	2,894,975	3,748,477	6,643,452	77,565	41,129	118,694			
2016	2,878,125	3,603,947	6,482,072	75,620	38,115	113,735			
2017-2021	14,391,665	16,046,531	30,438,196	234,665	152,216	386,881			
2022-2026	12,361,100	12,850,414	25,211,514	86,555	120,048	206,603			
2027-2031	12,026,305	10,139,984	22,166,289	191,620	89,636	281,256			
2032-2036	14,024,350	6,765,468	20,789,818	176,040	37,540	213,580			
2037-2041	12,848,210	2,341,240	15,189,450	90,840	10,163	101,003			
2042-2046				725	38	763			
Total \$	78,454,755	\$ 67,462,611	\$ 145,917,366	\$ 1,220,015	\$ 632,527	\$ 1,852,542			

F. General Obligation Bond Defeasances

1. Current Year

The primary government did not issue any refunding bonds in the 2010-11 fiscal year.

2. Prior Years

In prior years, the primary government placed the proceeds of the refunding bonds in a special irrevocable escrow trust account with the State Treasury to provide for all future debt service payments on defeased bonds. The assets of the trust accounts and the liability for defeased bonds are not included in the State's financial statements. As of June 30, 2011, the outstanding balance of general obligation bonds defeased in prior years was approximately \$2.8 billion.

NOTE 16: REVENUE BONDS

A. Governmental Activities

The State Treasurer is authorized by state law to issue Federal Highway Grant Anticipation Revenue Vehicles (GARVEE bonds). The purpose of these bonds is to accelerate the funding and construction of critical transportation infrastructure projects in order to provide congestion relief benefits to the public significantly sooner than with traditional funding mechanisms. These bonds are secured and payable from the annual federal appropriation for the State's federal-aid transportation projects. The primary government has no legal liability for the payment of principal and interest on these revenue bonds. Total principal and interest remaining on the bonds is \$394 million, payable through 2020. In addition, the California Alternative Energy and Advanced Transportation Financing Authority is authorized to issue Clean Renewable Energy Bonds to fund the acquisition and installation of certain transportation related solar energy facilities located throughout the state. Both of these bonds fund activity in the Transportation Fund and are included in the governmental activities column of the government-wide Statement of Net Assets.

The Golden State Tobacco Securitization Corporation (GSTSC), a blended component unit, is authorized by state law to issue asset-backed bonds to purchase the State's rights to future revenues from the Master Settlement Agreement with participating tobacco companies. These bonds are secured by and payable solely from future Tobacco Settlement Revenue and interest earned on that revenue. The primary government has no legal liability for the payment of principal and interest on these bonds. Total principal and interest remaining on the bonds is \$20.0 billion, payable through 2047. The annual principal and interest payments on these bonds are expected to require all of the Tobacco Settlement Revenue and interest. Principal and interest paid in the current year and total Tobacco Settlement Revenue and interest were \$375 million and \$362 million, respectively. These bonds are included in the governmental activities column of the government-wide Statement of Net Assets.

Under state law, certain building authorities may issue revenue bonds. These bonds are issued for the purpose of constructing state office buildings. Leases with state agencies pay the principal and interest on the revenue bonds issued by the building authorities. The primary government has no legal liability for the payment of principal and interest on these revenue bonds. These revenue bonds are included in the governmental activities column of the government-wide Statement of Net Assets.

B. Business-type Activities

Revenue bonds that are directly related to, and are expected to be paid from, the resources of enterprise funds are included in the accounts of such funds. Principal and interest on revenue bonds are payable from the pledged revenues of the respective funds of agencies that issued the bonds. The General Fund has no legal liability for payment of principal and interest on revenue bonds.

Revenue bonds to acquire, construct, or renovate state facilities or to refund outstanding revenue bonds in advance of maturity are issued for water resources, public building construction, financing of electric power purchases for resale to utility customers, and certain nonmajor enterprise funds.

C. Discretely Presented Component Units

The University of California issues revenue bonds to finance various auxiliary, administrative, academic, medical center, and research facilities. The revenue bonds are not collateralized by any encumbrance, mortgage, or other pledge of property, except pledged revenues, and do not constitute general obligations of the university.

Under state law, the California Housing Finance Agency (CalHFA) issues fixed- and variable-rate revenue bonds to fund loans to qualified borrowers for single-family houses and multifamily developments. Variable-rate debt is typically related to a common index, such as the Securities Industry and Financial Markets Association (SIFMA) or the London Interbank Offered Rate (LIBOR) and is reset periodically. CalHFA issues both federally taxable and tax-exempt bonds. The bonds issued by CalHFA are payable solely from and collateralized by revenues and other pledged assets.

Table 27 shows outstanding revenue bonds of the primary government and the discretely presented component units.

Table 27

Schedule of Revenue Bonds Outstanding

June 30, 2011

(amounts in thousands)

Primary government	
Governmental activities	
Transportation Fund	\$ 380,113
Nonmajor governmental funds	
Golden State Tobacco Securitization Corporation Fund	6,771,714
Building authorities	 359,265
Total governmental activities	7,511,092
Business-type activities	
Electric Power Fund	7,836,000
Water Resources Fund	2,462,594
Public Building Construction Fund	8,833,681
California State University Fund	3,415,092
Nonmajor enterprise funds	742,948
Total business-type activities	 23,290,315
Total primary government	30,801,407
Discretely presented component units	
University of California	10,937,240
California Housing Finance Agency	7,942,003
Nonmajor component units	 527,962
Total discretely presented component units	19,407,205
Total	\$ 50,208,612

Table 28 shows the debt service requirements for fixed- and variable-rate bonds. It excludes certain unamortized refunding costs, premiums, discounts, and other costs that are included in Table 27.

Table 28

Schedule of Debt Service Requirements for Revenue Bonds (amounts in thousands)

		Prima	rv Gov	vernment		Discretely Presented Component Units					
Year Ending		nmental vities	,	Busine	•						
June 30	Principal	Interest		Principal	Interest*	Principal		Interest*			
2012 \$	163,558	\$ 347,	921 5	\$ 1,193,425	\$ 1,109,741	\$ 434,241	\$	827,681			
2013	149,048	353,	955	1,265,555	1,051,679	504,374		801,666			
2014	158,403	360,	647	1,316,655	991,239	470,184		786,763			
2015	132,858	352,	917	1,361,490	928,516	492,300		762,411			
2016	70,984	346,	388	1,387,120	864,724	509,738		736,484			
2017-2021	724,262	1,662,	575	7,510,113	3,302,673	2,621,468		3,311,795			
2022-2026	679,060	1,667,	543	4,180,730	1,870,518	2,957,488		2,673,745			
2027-2031	770,913	1,500,	231	2,953,545	1,001,125	3,266,218		2,011,945			
2032-2036	745,010	1,244,	322	1,622,745	336,585	3,210,415		1,330,168			
2037-2041	1,891,609	948,	766	392,810	56,231	2,192,245		685,760			
2042-2046	1,812,000	783,	185	40,040	2,495	1,837,525		304,724			
2047-2051	696,544	3,322,	012	_	_	472,290		89,257			
2052-2056	<u> </u>			_	 	222,470		957			
Total <u>\$</u>	7,994,249	\$ 12,890,	462	\$ 23,224,228	\$ 11,515,526	\$ 19,190,956	\$	14,323,356			

^{*} Includes interest on variable-rate bonds based on rates in effect on June 30, 2011.

D. Revenue Bond Defeasances

Current Year—Governmental Activities

The primary government did not issue any refunding bonds in the 2010-11 fiscal year.

2. Current Year—Business-type Activities

In November 2010, the primary government issued \$98 million in water system revenue bonds. The bond proceeds were used to current-refund \$30 million of outstanding water system revenue bonds. The proceeds were deposited into an escrow account to provide for all future debt service payments on the refunded bonds. As a result, the bonds are considered defeased and the liability for those bonds has been removed from the financial statements. This refunding will decrease debt service payments by \$3 million over the life of the bonds and will result in an economic gain of \$2 million for the refunded bonds. These water system revenue bonds are reported in the Water Resources Fund.

In October 2010, the primary government issued \$1.8 billion in fixed-rate power supply revenue bonds to current-refund \$1.1 billion of outstanding variable-rate bonds and advance-refund \$813 million of outstanding fixed-rate bonds. The refunding reduced the amount of outstanding variable-rate debt and reduced the risk

and dependency from credit support providers and interest-rate swap counterparties. The proceeds were deposited into an escrow account to provide for all future debt service payments on the refunded bonds. As a result, the bonds are considered defeased and the liability for these bonds has been removed from the financial statements. The refunding decreased overall debt service payments by \$76 million and resulted in an economic gain of \$25 million. The power supply revenue bonds are reported in the Electric Power Fund.

3. Current Year—Discretely Presented Component Units

In July 2010, the University of California issued \$144 million in general revenue bonds. A portion of the proceeds were used to refund \$146 million in outstanding revenue bonds. The bonds mature at various dates through 2024 and have a weighted average interest rate of 4.9 percent. The deferred premium will be amortized as a reduction to interest expenses over the term of the bonds.

4. Prior Years

In prior years, the primary government defeased certain bonds by placing the proceeds of new bonds in irrevocable trust accounts to provide for all future debt service requirements. Accordingly, the assets and liabilities for these defeased bonds are not included in the financial statements. As of June 30, 2011, the outstanding balance of revenue bonds defeased in prior years was \$4.2 billion for governmental activities and \$3.7 billion for business-type activities.

In prior years, the University of California, a discretely presented component unit, defeased certain bonds. Investments that have maturities and interest rates sufficient to fund retirement of defeased liabilities are being held in irrevocable trusts for the debt service payments. Accordingly, the assets of the trust accounts and the liabilities for the defeased bonds are not included in the State's financial statements. As of June 30, 2011, the outstanding balance of University of California revenue bonds defeased in prior years was \$754 million.

NOTE 17: DERIVATIVE FINANCIAL INSTRUMENTS

Certain primary government business-type activities and discretely presented component units use derivatives—including futures, forward contracts, options and interest rate swap contracts—as a substitute for investment in equity and fixed-income securities, to reduce the effect of fluctuating foreign currencies on foreign currency-denominated investments, or to limit its exposure of variable-rate bonds to changes in market interest rates.

A futures contract is an agreement between two parties to buy and sell a security, financial index, interest rate, foreign currency, or other financial instrument at a set price on a future date. They are standardized contracts that can be easily bought and sold and are exchange-traded. A futures contract obligates a buyer to purchase the commodity or financial instrument and a seller to sell it, unless an offsetting contract is entered into to offset one's obligation. The resources or obligations acquired through these contracts are usually terminated by entering into offsetting contracts.

Forward contracts are similar to futures contracts, although they are not exchange-traded. One example of a forward contract is a foreign currency exchange contract used to hedge against foreign currency exchange rate risks on non-U.S. dollar-denominated investment securities and to increase or decrease exposure to various foreign currencies. Another example is when forward contracts are used to purchase certain mortgage-backed securities on a to-be-announced (TBA) basis when the price cannot be determined until the coupon rate is known. A forward contract on a TBA basis is a commitment to purchase a mortgage-backed pass-through pooled security when issued by the Federal National Mortgage Association (Fannie Mae),

Federal Home Loan Mortgage Corporation (Freddie Mac), and Government National Mortgage Association (Ginnie Mae).

An option contract gives the State the right, but not the obligation, to buy or sell a financial instrument or commodity at a fixed price during a specified period.

The State considers its futures, forward contracts, and options to be investment derivatives. A swap is a contractual agreement to exhange future cash flows. These cash flows may be either fixed or variable and may be either received or paid. The State holds interest rate swaps as both investment derivatives and hedging derivatives.

Table 29 shows debt service requirements as of June 30, 2011, for variable-rate debt included in Table 28, as well as net swap payments, assuming that current interest rates remain the same for their terms. As interest rates vary, variable-rate bond interest payments and net swap payments will vary.

Table 29 Schedule of Debt Service and Swap Requirements for Variable-rate Revenue Bonds (amounts in thousands)

	Discretely Presented Component Units								
Year Ending June 30	Principal	Interes	<u>t*</u>	Interest- Rate* Swap Net		Total			
2012	\$ 36,253	\$ 8	,181 \$	114,719	\$	159,153			
2013	40,006	6	,647	106,622		153,275			
2014	49,430	6	,488	98,913		154,831			
2015	56,251	6	,326	91,851		154,428			
2016	65,274	6	,156	85,319		156,749			
2017-2021	374,190	28	,004	346,550		748,744			
2022-2026	454,045	22	,918	247,228		724,191			
2027-2031	689,524	17	,368	167,578		874,470			
2032-2036	604,131	10	,208	83,441		697,780			
2037-2041	242,069	5	,315	26,822		274,206			
2042-2046	92,497	2	,059	8,053		102,609			
2047-2051	485		5	18		508			
Total	\$ 2,704,155	\$ 119	,675_	\$ 1,377,114	\$	4,200,944			

A. Primary Government

The Department of Water Resources (DWR) is party to interest-rate swap agreements and natural gas hedging positions that are considered to be derivatives. Table 30 summarizes the fair values, classification, and notional amounts outstanding for the DWR's natural gas hedges accounted for as derivative financial instruments.

Table 30

Schedule of Fair Values and Notional Amounts - Electric Power Fund June 30, 2011

(dollars in thousands)

				Notional Amount
	Classification	_	Fair Value	(in MMBtu) ¹
Effective hedges				
Natural gas swaps	Other current assets	\$	3,000	7,485,000
	Other current liabilities		(30,000)	16,925,000
Total effective hedges		\$	(27,000)	
Investment hedges				
Natural gas swaps	Other current assets	\$	2,000	10,982,500
	Other current liabilities		(3,000)	3,250,000
	Other noncurrent liabilities		(3,000)	990,000
Natural gas options	Other current assets		2,000	33,937,500
Total investment hedges		\$	(2,000)	
¹ Millions of British thermal units.				

^{1.} Natural Gas Swaps and Options

Objective: The DWR enters into forward gas futures and options contracts to hedge the cost of natural gas. Most of the DWR's forward gas futures are being treated as normal purchase normal sale (NPNS) contracts and are therefore not required to be recorded prior to settlement. Forward gas futures not qualifying as NPNS are recorded on the statement of net assets at fair value. All natural gas options are treated as derivatives and are classified as investment derivatives. For the DWR's gas hedging contracts that are effective hedges, unrealized gains and losses are deferred on the statement of net assets as other current assets or liabilities for contracts with fewer than 12 months remaining until expiration, or as other noncurrent assets or liabilities for contracts with more than 12 months remaining until expiration. The deferred amount recorded on the statement of net assets reflects the deferred inflow or outflow associated with the derivative financial instruments. Changes in fair value of derivatives that are classified as investment derivatives are included as investment and interest income on the statement of revenues, expenses, and changes in fund net assets.

Fair Value: The reported fair values from Table 30 above were determined based on quoted market prices for similar financial instruments.

Credit Risk: The DWR's open natural gas hedge positions at June 30, 2011 are with nine different counterparties, all of which have credit ratings of at least A-/Baa1. At June 30, 2011, the DWR has credit risk exposure to three counterparties totaling \$2 million, representing transactions with market values that are in the DWR's favor. There is no substantial credit exposure to the remaining six counterparties, as the decrease in natural gas prices has resulted in valuations in the counterparties' favor. The remaining gas hedge positions have been entered into through the DWR's brokerage accounts and the associated clearing accounts have collateral requirements that limit the DWR's counterparty credit risk.

Termination Risk: With regards to gas hedge agreements, the DWR or the counterparty may terminate an agreement if the other party fails to perform under the terms of the contract. In addition, the agreements allow either party to terminate in the event of a significant loss of creditworthiness by the other party. If a termination were to occur, the DWR or the counterparty would owe the other a payment equal to the fair value of the open positions.

2. Interest-Rate Swaps

Termination of Interest Rate Swaps: As part of the Series 2010 M refunding transaction in October 2010, the DWR terminated all remaining interest rate swaps for \$102 million to settle the negative fair market value of the swap agreements. The interest rate swap derivative values were removed from the statements of net assets and the loss incurred on termination is being deferred and amortized as part of the refunding transaction.

B. Fiduciary Funds

Under the State Constitution and statutory provisions governing the investment authority of the California Public Employees' Retirement System (CalPERS), CalPERS holds investments in swaps, options, futures, rights, and warrants and enters into forward foreign currency exchange. The fair value of options, futures, rights, and warrants is determined based upon quoted market prices. The fair value of derivative investments that are not exchange traded, such as swaps, is determined by an external pricing service using various proprietary methods. Futures contracts are marked-to-market at the end of each trading day and the settlement of gains or losses occur on the following business day through variation margins. The fair value of international currency forwards represents the unrealized gain or loss on the related contracts, which is calculated as the difference between the specified contract exchange rate and the exchange rate at the end of the reporting period.

CalPERS uses forward foreign currency exchange contracts primarily to hedge against changes in exchange rates related to foreign securities. Derivatives with positive fair values are recorded as either investments or receivables (net) in the statement of fiduciary net assets. Derivatives with negative fair values are recorded as other liabilities in the statement of fiduciary net assets. Changes in fair value are recorded as net appreciation or depreciation in fair value of investments in the statement of changes in fiduciary net assets.

The California State Teachers' Retirement System (CalSTRS) also holds investments in derivative instruments. CalSTRS' investments that are not exchange traded, such as credit default swaps and interest rate swaps, are valued using methods employed for debt securities. Futures contracts are marked-to-market at the end of each trading day and the settlement of gains or losses occur on the following business day. As a result, the derivative instruments themselves have no fair value at June 30, 2011, or at the end of any trading day. Daily settlement of gains and losses is a risk control measure to limit counterparty credit risk. Futures variation margin amounts are settled each trading day and are recognized as net appreciation or depreciation in fair value of investments as they are incurred.

CalSTRS holds foreign currency forwards, which are obligations to buy or sell a currency at a specified exchange rate and quantity on a specific future date. The fair value of foreign currency forwards is the unrealized gain or loss calculated based on the difference between the specified exchange rate and the closing exchange rate at June 30, 2011. Derivatives with positive fair values are recorded as investments in the statement of fiduciary net assets. Derivatives with negative fair values are recorded as accounts payable in the statement of fiduciary net assets. Changes in fair value are recorded as net appreciation or depreciation in fair value of investments in the statement of changes in fiduciary net assets.

All fiduciary fund derivative instruments are included in the investments disclosed in Note 3, Deposits and Investments. Table 31 presents the net appreciation (depreciation) in fair value, the fair values, and notional amounts of derivative instruments outstanding of these fiduciary funds.

Table 31

Schedule of Changes in Fair Values, Fair Values, and Notional Amounts - Fiduciary Funds
June 30, 2011
(dollars in thousands)

Investment Type	Net Appreciation (Depreciation) in Fair Value	Classification	Fair Value	Notional Amount
Credit default swaps	\$ 605	Debt securities	\$ 75	\$ 29,936
Credit default swaps bought	(3,304)	Debt securities	6,218	44,150
Credit default swaps written	2,307	Debt securities	1,184	77,150
Equity options bought	(8,427)	Equity securities	1,960	1,462,500 shares
Equity options written	7,286	Equity securities	(2,354)	(120,000) shares
Fixed-income futures long	910	Investment sales/purchases		195,643
Fixed-income futures short	(8,336)	Investment sales/purchases	_	(785,991)
Fixed-income options written	11,029	Equity securities	(4,568)	(496,183)
Foreign currency options bought	(3,238)	Equity securities	1,488	275,954
Foreign currency options written	1,210	Equity securities	(51)	(5,219)
Foreign currency forwards	(115,428)	Foreign currency contracts	(1,224)	7,105,386
Futures options bought	(5,475)	Debt securities	12,120	¹ 786,625
Futures options written	2,409	Debt securities	(70)	(46,540)
Futures options written	1,195	Equity securities		_
Futures (domestic and foreign)	84,232	Futures		(751,635)
Foreign exchange forwards	(1,186,921)	Investment sales/purchases	(128,672)	28,140,569
Index futures long	1,453,941	Investment sales/purchases		31,587
Index futures short	30	Investment sales/purchases		_
Interest-rate swaps	(5,803)	Debt securities	(9,613)	429,153
Pay-fixed interest-rate swaps	(5,683)	Debt securities	(1,745)	118,228
Receive-fixed interest-rate swaps .	2,739	Debt securities	769	149,011
Rights	(1,042)	Equity securities	5,088	27,885,963 shares
Total return bond swaps	(126,841)	Debt securities	(131,061)	2,642,443
Warrants	(2,751)	Equity securities	4,002	991,950 shares
Total	\$ 94,644		\$ (246,454)	

¹ The total Futures options bought of \$12,120 is comprised of debt and equity securities option bought of \$11,611 and \$509, respectively.

Interest Rate Risk: Table 32 describes the maturity periods of the derivative instruments during which these fiduciary funds were exposed to interest rate risk.

Table 32

Schedule of Derivative Instruments Subject to Interest Rate Risk - Fiduciary Funds
June 30, 2011
(amounts in thousands)

		Fair	Investment Maturities (in years)						
Investment Type		Value		Under 1		1-10	10+		
Credit default swaps	\$	75	\$	_	\$	(93)	\$	168	
Credit default swaps bought		6,218		(194)		179		6,233	
Credit default swaps written		1,184		18		1,166		_	
Fixed income options		11,611		_		11,611		_	
Fixed income options written		(4,568)		(4,055)		(513)		_	
Interest-rate swaps		(9,613)		_		(7,510)		(2,103)	
Pay fixed interest-rate swaps		(1,745)		_		(614)		(1,131)	
Receive fixed interest-rate swaps		769		_		(851)		1,620	
Total return bond swaps		(131,061)		(97,249)		(33,884)		72	
Total	\$	(127,130)	\$	(101,480)	\$	(30,509)	\$	4,859	

Table 33 details the reference rate, fair value and notional amount of the derivative instruments held by these fiduciary funds that were highly sensitive to changes in interest rate risk.

Table 33

Schedule of Derivative Instruments Highly Sensitive to Interest Rate Changes - Fiduciary Funds
June 30, 2011
(amounts in thousands)

Investment Type	Reference Rate	Fair Value	 Notional Amount
Interest-rate swaps	Receive variable 3-month LIBOR, pay fixed 4.25%	\$ (1,131)	\$ 34,600
	Receive variable 3-month LIBOR, pay fixed 3.928%	(1,860)	75,000
	Receive variable 3-month LIBOR, pay fixed 3.905%	(4,711)	175,000
	Receive variable 3-month LIBOR, pay fixed 3.829%	(743)	12,000
	Receive variable 3-month LIBOR, pay fixed 3.575%	(938)	150,000
	Receive variable 3-month LIBOR, pay fixed 3.50%	(686)	31,200
	Receive variable 3-month LIBOR, pay fixed 3.36%	815	40,428
	Receive variable 3-month LIBOR, pay fixed 0%	(2,104)	29,153
	Receive fixed 5.8%, pay variable 6-month CDOR ¹	219	8,807
	Receive fixed 2.0%, pay variable 6-month LIBOR ²	(58)	19,812
	Receive fixed 1.5%, pay variable 6-month LIBOR	1,459	61,912
	Receive fixed 4.385%, pay variable 3-month LIBOR	(215)	17,336
	Receive fixed 6.96%, pay variable 1-month TIIE ³	(667)	38,484
	Receive fixed 6.75%, pay variable 1-month TIIE	23	1,885
	Receive fixed 6.59%, pay variable 1-month TIIE	8	776
Subtotal Interest-rate swaps		\$ (10,589)	\$ 696,393
Fixed-income options	Swaption 5YR RTP FEB13 5.11 PUT	\$ 1,554	\$ 250,000
•	Swaption 5YR RTR MAR13 3.405 CALL	5,038	175,000
	Swaption 5YR RTR APR13 3.428 CALL	2,123	75,000
	Swaption 5YR RTR MAY13 3.075 CALL	1,450	75,000
	Swaption 5YR RTR MAY13 3.075 CALL	1,446	75,000
Subtotal Fixed-income options		\$ 11,611	\$ 650,000
Total return bond swaps	Receive fixed 1.00%, pay fixed 1.00%	\$ (131,120)	\$ 2,623,499
Total		\$ (130,098)	\$ 3,969,892

¹ Canadian Dealer Offered Rate (CDOR)

² London Interbank Offered Rate (LIBOR)

³ Tasa de Interes Interbancaria de Equilibrio (TIIE)

Credit Risk: Due to the level of risk associated with certain derivative investment securities, it is reasonably possible that changes in the values of investment securities will occur in the near term, and such changes could affect the amounts reported in the financial statements. CalPERS could be exposed to risk if the counterparties to the contracts are unable to meet the terms of the contracts. CalPERS seeks to control this risk through counterparty credit evaluations and approvals, counterparty credit limits, posting collateral and exposure monitoring procedures.

Table 34 details the counterparty, percent of net exposure, and credit ratings for the derivative instruments held by CalPERS that were subject to credit risk.

Table 34

Schedule of Derivative Instruments Subject To Credit Risk - California Public Employees' Retirement System
June 30, 2011

Counterparty	Percent of Net Exposure	S&P Ratings	Fitch Ratings	Moody's Ratings
Societe Generale	21.53 %	A+	A+	Aa2
JP Morgan Chase Bank NA	21.45	AA-	AA-	Aa1
Credit Suisse Securities (USA), LLC	14.72	A+	AA-	Aa1
JBS AG	12.47	A+	A+	Aa3
Barclays Capital	11.32	AA-	AA-	Aa3
Goldman Sachs International	11.27	Α	A+	A1
Royal Bank of Scotland PLC	3.64	A+	AA-	Aa3
Morgan Stanley and Co. International PLC	1.82	Α	Α	A2
BNP Paribas	1.27	AA	AA-	Aa2
Deutsche Bank AG London	0.51	A+	AA-	Aa3

In cases where a wholly owned broker-dealer does not engage the rating companies for a standalone rating, the subsidiary is assigned the parent company rating as the broker-dealer is an integral part of their business model(s). With the exception of foreign currency forwards, it is CalSTRS' practice to require counterparty collateral posting provisions in its non-exchange-traded derivative instruments where it is consistent with market practice. As of June 30, 2011, the aggregate amount of cash collateral held at CalSTRS on behalf of the non-exchange traded derivatives was \$3 million. The aggregate fair value of investment derivative instruments in an asset position subject to counterparty credit risk at June 30, 2011, was \$8.1 million. This represents the maximum loss that would be recognized at the reporting date if all counterparties failed to perform as contracted. At June 30, 2011, CalSTRS did not have any significant exposure to counterparty credit risk with any single party.

While CalSTRS did not have any master netting agreements with its counterparties at June 30, 2011, Table 35 presents exposure for similar instruments with the same counterparty on a net basis and describes the counterparty credit ratings for the non-exchange-traded derivative instruments held by CalSTRS that were outstanding and subject to loss.

Table 35

Schedule of Counterparty Credit Rating - California State Teachers' Retirement System
June 30, 2011
(amounts in thousands)

							F				
Ratings		Credit Defalt Swaps		Interest-Rate Swaps		Total Return Swaps		Currency Forwards		Total	
AA	\$	_	\$	_	\$	34	\$	1,995	\$	2,029	
A		688		_		27		5,367		6,082	
Subtotal investments in asset											
position		688				61		7,362		8,111	
Investments in liability position		(613)		(9,613)		(2)		(8,586)		(18,814)	
Total investments in asset/											
(liability) position	\$	75	\$	(9,613)	\$	59	\$	(1,224)	\$	(10,703)	

C. Discretely Presented Component Unit—University of California

The University of California, a discretely presented component unit, holds investment derivatives in futures and forward contracts, and interest-rate swap contracts. The Board of Trustees for each campus foundation may also authorize derivatives in its investment policy. The university enters into futures contracts for the purpose of acting as a substitute for investment in equity and fixed-income securities. The university also holds interest-rate swaps that are derivative instruments that meet the criteria for an effective hedge. Certain of the interest-rate swaps are considered hybrid instruments since, at the time of execution, the fixed rate on each of the swaps was off-market and the university received an up-front payment. As such, these swaps are comprised of a derivative instrument, an at-the-market swap that is an effective hedge, and a companion instrument, a borrowing represented by the up-front payment. The unamortized amount of the borrowing under the companion instrument was \$30 million at June 30, 2011. Derivatives are recorded at fair value as either assets or liabilities in the statement of net assets. Certain derivatives are determined to be hedging derivatives and designated as either a fair value or cash-flow hedge. Under hedge accounting, changes in the fair value of hedging derivatives are considered to be deferred inflows (for hedging derivatives with positive fair values) or deferred outflows (for hedging derivatives with negative fair values). Deferred inflows are included with other noncurrent liabilities and deferred outflows with other noncurrent assets in the statement of net assets. Changes in the fair value of derivatives that are not hedging derivatives are reported as net appreciation or depreciation in fair value of investments in the statement of activities. Table 36 summarizes the fair value balances and notional amounts of derivative instruments outstanding, categorized by type, and the changes in fair value of such derivatives.

Table 36

Schedule of Changes in Fair Values, Fair Values, and Notional Amounts - University of California
June 30, 2011
(amounts in thousands)

	Changes in Fair Value	Classification	Fair Value	Notional Amount
Investment derivatives				
Domestic equity futures contracts long \$	45,109	Investments	\$ 1,725	\$ 238,874
Domestic equity futures contracts short	(303)	Investments	_	_
Foreign equity futures contracts long	3,267	Investments	397	33,368
Foreign equity futures contracts short	(883)	Investments	(130)	(9,524)
Foreign currency exchange contracts long	40,678	Investments	(127)	37,705
Foreign currency exchange contracts short	(78,301)	Investments	(5,005)	(486,844)
Stock rights/warrants	498	Investments	1,400	_
Total investment derivatives \$	10,065		\$ (1,740)	\$ (186,421)
Cash flow hedges				
Interest-rate swaps		Other noncurrent		
Pay fixed, receive variable \$	16,990	assets (liabilities)	\$ (47,092)	\$ 260,690

Table 29 includes the university's debt service requirements and net swap payments as of June 30, 2011. Total principal, variable interest, and interest rate net swap payments are \$261 million, \$42 million, and \$209 million, respectively.

Objective and Terms: The university entered into interest-rate swap agreements in connection with certain variable-rate Medical Center Pooled Revenue Bonds as a means to lower borrowing costs, rather than using fixed-rate bonds at the time of issuance. Under each swap agreement, the university pays the swap counterparties a fixed-interest-rate payment and receives a variable-interest-rate payment that effectively changes the variable-interest-rate bonds to synthetic fixed-rate bonds.

Fair Value: There is a risk that the fair value of a swap will become negative as a result of market conditions. The swaps have an estimated negative fair value of \$47 million as of June 30, 2011. The fair value of the interest rate swaps is the estimated amount the university would have either received or paid if the swap agreements had been terminated on June 30, 2011. The fair value was estimated by financial institutions or independent advisors using available quoted market prices or discounted expected future net cash flows.

Table 37 summarizes the terms and fair value of the swap agreements.

Table 37

Schedule of Terms and Fair Values of Swap Agreements (amounts in thousands)

Swap Termination Date	Effective Date	Outstanding Notional Amount at June 30, 2011		Fair Value at June 30, 2011	Fixed Rate Paid by University of California	Variable Rate Received by University of California	Counterparty Credit Ratings (Moody's, S&P's)
2032	2001	\$ 85,915	\$	(9,133)	3.5897 %	58% of 1-Month LIBOR + 0.48%*	A2, A
2047	2008	174,775		(37,959)	4.6873	67% of 3-Month LIBOR + 0.73%*	Aa3, A+
Total		\$ 260,690	\$	(47,092)			
* Weighted average	ge spread		=				

Interest Rate Risk: There is a risk the value of the interest-rate swaps will decline because of changing interest rates. The values of the interest-rate swaps with longer maturities tend to be more sensitive to changing interest rates and, therefore, more volatile than those with shorter maturities.

Basis Risk: The university is exposed to basis risk whenever the interest rates on the bonds are reset. The interest rate on the bonds is a tax-exempt interest rate, while the variable receipt rate on the interest rate swaps is taxable. However, there is no basis or tax risk related to the swap with the \$175 million notional amount since the variable rate the university pays to the bond holders matches the variable-rate payments received from the swap counterparty and the interest rates are reset at the same intervals.

Termination Risk: The university is exposed to risk in the event of nonperformance by counterparties resulting in cancellation of the synthetic interest rate and returning the interest-rate payments to the variable interest rates on the bonds. In addition, depending on the agreement, certain swaps may be terminated if the counterparty's credit quality rating, as issued by Moody's or Standard & Poor's, falls below certain thresholds. At termination, the university may also owe a termination payment if there is a realized loss based on the fair value of the swap.

Credit Risk: The university could be exposed to credit risk if the interest-rate swap counterparties to the contracts are unable to meet the terms of the contracts. Contracts with positive fair values are exposed to credit risk. The university faces a maximum possible loss equivalent to the amount of the derivative's fair value, less any collateral held by the university provided by the counterparty. Contracts with negative fair values are not exposed to credit risk. There are no collateral requirements related to the interest-rate swap with the \$86 million notional amount. Depending on the fair value related to the swap with the \$175 million notional amount, the university may be entitled to receive collateral from the counterparty to the extent the positive fair value exceeds \$35 million, or be obligated to provide collateral to the counterparty if the negative fair value of the swap exceeds \$75 million or the cash and investments held by the medical centers fall below \$250 million. As of June 30, 2011, no collateral was required.

D. Discretely Presented Component Unit—California Housing Finance Agency

The California Housing Finance Agency (CalHFA), a discretely presented component unit, holds interest-rate swaps that are derivative instruments. As of June 30, 2011, the fair value of the swaps is reported as other noncurrent assets or as other noncurrent liabilities in the statement of net assets. The cumulative gain or loss on the fair value of the effective swaps is reported as other noncurrent assets or as other noncurrent liabilities in the statement of net assets. Alternatively, the gain or loss on the fair value of the ineffective swaps is reported as other general revenues in the statement of activities. CalHFA did not pay or receive any cash when the swap transactions were initiated except for in-substance assignments. Except as discussed under rollover risk, CalHFA's swap agreements contain scheduled reductions to outstanding notional amounts that are expected to approximately follow scheduled or anticipated reductions in the associated bonds payable. Table 38 summarizes the swap fair value activity in the statement of net assets and the statement of activities.

Table 38

Schedule of Swap Agreement Fair Value - California Housing Finance Agency June 30, 2011

(amounts in thousands)

	Amount	
Statement of net assets:		
Other noncurrent assets	\$	212,487
Other noncurrent liabilities		252,486
Statement of activities:		
Other general revenues (expenses)		(3,360)

Table 29 includes debt service requirements and net swap payments as of June 30, 2011, for CalHFA. Total principal, variable interest, and interest rate net swap payments are \$2.4 billion, \$77 million, and \$1.2 billion, respectively.

Objective: CalHFA has entered into interest-rate swap agreements with various counterparties to protect itself against rising rates by providing synthetic fixed rates for a like amount of variable-rate bond obligations. The majority of CalHFA's interest-rate swap transactions are structured to pay a fixed rate of interest while receiving a variable rate of interest, with some exceptions. CalHFA has used multiple swap formulas. As of June 30, 2011, the formulas for the swap portfolio used the SIFMA, the one-month LIBOR, the three-month LIBOR, and the six-month LIBOR rates. The swap formula will continue to be monitored for its effectiveness in

case CalHFA chooses to enter into any future interest-rate swaps. In addition, CalHFA entered into eight basis swaps as a means to change the variable-rate formula received from counterparties for \$240 million outstanding notional amount from 65% of LIBOR to varying floating rates.

Terms, Fair Value, and Credit Risk: CalHFA uses 13 counterparties for its interest-rate swap transactions. All of CalHFA's interest-rate swap agreements require CalHFA to post collateral if its general obligation credit ratings, as issued by Moody's and Standard & Poor's, fall below a certain level or if the fair value of the swaps breach a certain threshold. The collateral can be posted in several forms in the amount of the fair value of the interest-rate swaps. If CalHFA does not post collateral, the interest-rate swap can be terminated by the counterparty. As of June 30, 2011, CalHFA's swap portfolio has an aggregate negative fair value of \$252 million due to a decline in interest rates. Fair values are as reported by CalHFA's counterparties and are estimated using the zero-coupon method. As CalHFA's swap portfolio has an aggregate negative fair value, CalHFA has no net exposure to credit risk. CalHFA has 106 swap transactions, with outstanding notional amounts of \$2.8 billion, effective dates from December 9, 1999, to November 1, 2009, and scheduled termination dates from August 1, 2012, to August 1, 2042. Standard & Poor's credit ratings for these counterparties range from A- to AAA; Moody's credit ratings range from A3 to Aaa.

Interest Rate Risk: CalHFA is exposed to interest rate risk on its fixed-payer swaps. As the LIBOR or the SIFMA swap index decreases, CalHFA's net payments on the swaps increase.

Basis Risk: CalHFA's swaps contain the risk that the floating-rate component of the swap will not match the floating rate of the underlying bonds. This risk arises because floating rates paid by swap counterparties are based on indices that consist of market-wide averages, while interest paid on CalHFA's variable-rate bonds is specific to individual bond issues. CalHFA's variable-rate tax-exempt bonds trade at a slight discount to the SIFMA index. For swaps associated with tax-exempt bonds for which CalHFA receives a variable-rate payment based on a percentage of LIBOR, CalHFA is exposed to basis risk if the relationship between SIFMA and LIBOR converges. As of June 30, 2011, the SIFMA rate was 0.09%, the one-month LIBOR was 0.19%, the three-month LIBOR was 0.25%, and the six-month LIBOR was 0.40%.

Termination Risk: Counterparties to CalHFA's interest-rate swaps have termination rights that require settlement payments by either CalHFA or the counterparty, based on the fair value of the swap.

Rollover Risk: CalHFA is exposed to rollover risk on interest-rate swaps that are hedges of debt that mature or may be terminated prior to the maturity of the hedged debt. When these swaps terminate, CalHFA will be re-exposed to the risks being hedged by the swaps.

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NOTE 18: INTERFUND BALANCES AND TRANSFERS

A. Interfund Balances

Due from other funds and due to other funds represent short-term interfund receivables and payables resulting from the time lag between the dates on which goods and services are provided and received and the dates on which payments between entities are made. In addition, interfund borrowing, mainly from nonmajor governmental funds and fiduciary funds, is used to meet temporary imbalances of receipts and disbursements in the General Fund. Table 39 presents the amounts due from and due to other funds.

Table 39

Schedule of Due From Other Funds and Due To Other Funds
June 30, 2011
(amounts in thousands)

						Due	То					
Due From	General Fund			Federal Fund	Transportation Fund			Nonmajor overnmental Fund	Electric Power Fund		Water Resources Fund	
Governmental funds												
General Fund	\$		\$		\$	215,916	\$	1,130,821	\$	_	\$	
Federal Fund		970,235		_		1,171,808		199,785		_		
Transportation Fund		1						33,426				
Nonmajor governmental funds		29,670				28,755		32,600				
Total governmental funds		999,906		_		1,416,479		1,396,632		_		
Enterprise funds												
Water Resources Fund												
Public Building Construction Fund		1,388										
State Lottery Fund		177						276,999				
Unemployment Programs Fund		175,982		46,245								
Nonmajor enterprise funds		30				_		550				
Total enterprise funds		177,577		46,245				277,549				
Internal service funds		15,775				25,720		52,772		6,000		2,206
Total primary government	\$	1,193,258	\$	46,245	\$	1,442,199	\$	1,726,953	\$	6,000	\$	2,206

					Du	е То)				
Bu Cons	ublic ilding truction und	 State Lottery Fund	Unemployment Programs Fund		California State University Fund		Nonmajor Enterprise Funds	 Internal Service Funds		Fiduciary Funds	 Total
\$		\$ 	\$ —	\$		\$	1,302	\$ 192,585	\$	8,907,937	\$ 10,448,561
							4,165	41,319		4,942,794	7,330,106
	275							24,097		35,057	92,856
					2,170		46	33,113		5,219	131,573
	275	 _		_	2,170	_	5,513	 291,114	_	13,891,007	 18,003,096
	_							36,547			36,547
								60,499		628	62,515
											277,176
		_					_			_	222,227
		 			_			48		11	639
			_		_			97,094		639	599,104
	26,924	517	2,361				816	11,629		2,113	 146,833
\$	27,199	\$ 517	\$ 2,361	\$	2,170	\$	6,329	\$ 399,837	\$	13,893,759	\$ 18,749,033

Interfund receivables and payables are the result of interfund loans that are not expected to be repaid within one year. In addition to the temporary interfund cash-flow borrowing shown in Table 39, annual enacted budgets provide for long-term loans from many of the State's special funds—mainly the Transportation Fund and nonmajor governmental funds—to the General Fund. The \$2.6 billion in Transportation Fund loans payable from the General Fund also includes \$1.3 billion of deferred Proposition 42 transfers for traffic congestion relief and other direct loans from the Traffic Congestion Relief Program. Table 40 presents the interfund receivables and payables.

Table 40

Schedule of Interfund Receivables and Payables

June 30, 2011 (amounts in thousands)

_				Inter	fund Payable	s		
Interfund Receivables	General Fund	Tra	ansportation Fund		Nonmajor overnmental Funds	-	Water Resources Fund	employment Programs Fund
Governmental funds								
General Fund\$		\$	2,598,754	\$	4,880,735	\$	_	\$ 849,775
Transportation Fund			_				_	
Nonmajor governmental funds	6,654		9,872				_	_
Total governmental funds	6,654		2,608,626		4,880,735		_	849,775
Internal service funds	40,650		· · ·		782		91,517	·
Total primary government \$	47,304	\$	2,608,626	\$	4,881,517	\$	91,517	\$ 849,775

Interfund Payables								
California State University Fund		Nonmajor Enterprise Funds		Internal Service Funds		Agency Funds		Total
\$ 161,727	\$	143,978	\$	193,684	\$	90,232	\$	8,918,885
_		_		2,421		_		2,421
 								16,526
161,727		143,978		196,105		90,232		8,937,832
				6,140				139,089
\$ 161,727	\$	143,978	\$	202,245	\$	90,232	\$	9,076,921

Due from primary government and due to component units represent short-term receivables and payables between the primary government and component units resulting from the time lag between the dates on which goods and services are provided and received and the dates on which payments between entities are made. Table 41 presents the due from primary government and due to component units.

Table 41

Schedule of Due From Primary Government and Due to Component Units
June 30, 2011
(amounts in thousands)

_	Due To											
		Component Units										
Due From		University of California		Public Employees' Benefits Fund		Nonmajor Component Units		Total				
		Camorina	_	runa	_	Omio		Total				
Governmental funds General Fund Nonmajor governmental funds		198,389 5,152	\$	_	\$	 19	\$	198,389 5,171				
Total governmental funds		203,541		 571		19 168		203,560				
Total primary government		203,541	\$	571	\$	187	\$	204,299				

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B. Interfund Transfers

As required by law, transfers move money collected by one fund to another fund, which then disburses it. The General Fund and certain other funds transfer money to support various programs accounted for in other funds. The largest transfers from the General Fund were \$2.6 billion to California State University (a major enterprise fund) and \$1.5 billion to nonmajor governmental funds for support of trial courts. The Federal Fund transferred \$4.0 billion to nonmajor governmental funds for hospital services under the Medi-Cal program. Table 42 presents interfund transfers of the primary government.

Table 42

Schedule of Interfund Transfers
June 30, 2011
(amounts in thousands)

_				Transferred To	
Transferred From	General Fund	Transportation Fund	Nonmajor Governmental Funds	Unemployment Programs Fund	California State University Fund
Governmental funds					
General Fund \$	S —	\$	\$ 2,381,813	\$ —	\$ 2,562,919
Federal Fund	749,389		4,201,081	616,657	
Transportation Fund	171,253		770,880	_	
Nonmajor governmental funds	209,888	235	129,917	_	108,371
Total governmental funds	1,130,530	235	7,483,691	616,657	2,671,290
Public Building Construction Fund				_	32,692
Nonmajor enterprise funds	36,349			_	
Internal service funds	9,737		44,687		
Total primary government	1,176,616	\$ 235	\$ 7,528,378	\$ 616,657	\$ 2,703,982

Internal Service Funds	Total
\$ _	\$ 4,944,732
_	5,567,127
_	942,133
397	448,808
397	11,902,800
	32,692
	36,349
	54,424
\$ 397	\$ 12,026,265

NOTE 19: FUND BALANCES, FUND DEFICITS, AND ENDOWMENTS

A. Fund Balances

The fund balance amounts for governmental funds have been reclassified in accordance with GASB Statement No. 54. As a result, amounts previously reported as reserved and unreserved are now reported as nonspendable, restricted, committed, assigned, or unassigned. See Note 1K for the new fund balance classifications as defined by GASB. For purposes of reporting in the State's CAFR, the following are the State's policies based on its interpretation of GASB Statement No. 54.

Committed fund balance: The highest level of decision-making authority within California statewide government is the California Legislature. The formal action required to establish, modify, or rescind a fund balance commitment is a statute that becomes law after a bill is passed. Commitments of fund balance, approved by State Legislative action, must be in place prior to the end of the State's fiscal year. The California State Legislature is made up of two houses: the Senate and the Assembly. Both houses must approve a bill. If both houses approve a bill, it then goes to the Governor. The Governor has three choices: the Governor can sign the bill into law, allow it to become law without his or her signature, or veto it. A governor's veto can be overridden by a two-thirds vote in each house.

Assigned fund balance: California does not have a formal policy to delegate authority to assign resources. However, fund balance can be classified as assigned when a purchase order creates an outstanding encumbrance amount unless the purchase order relates to restricted or committed resources. Furthermore, all resources in governmental funds, other than the General Fund, that are not restricted, committed, or nonspendable are classified as assigned.

Fund balance spending order: For the purpose of reporting fund balance in the CAFR under GASB Statement No. 54, the State considers resources to be spent in the following order when an expenditure is incurred for which these classifications are available: restricted, committed, assigned, and unassigned.

Table 43 presents the composition of the fund balance of the governmental funds.

Table 43

Schedule of Fund Balance by Function

June 30, 2011

(amounts in thousands)

	General		Federal	Tra	ansportation	Nonmajor overnmental
Nonspendable		_				
Long-term interfund receivables	\$ 47,304	\$		\$		\$
Long-term loans receivable	100,715					
Assets not in spendable form					_	32,196
Legally or contractually required to remain intact					_	7,252
Total nonspendable	 148,019		_		_	39,448
Restricted						
General government	4,209				_	3,269,987
Education	59,328		296		4,632	1,426,403
Health and human services	89,026		212		_	4,125,104
Resources			10,651		_	7,247,289
State and consumer services	3,933				206,272	539,601
Business and transportation			110,395		7,512,567	3,252,114
Correctional programs	 					3,802
Total restricted	 156,496		121,554		7,723,471	 19,864,300
Committed						
General government	16,698		_		_	550,710
Education	4,433		_		_	47,149
Health and human services	8,719		_		2,304	189,458
Resources			_		20	1,350,585
State and consumer services			_		_	61,372
Business and transportation			_		46,201	437,593
Correctional programs	 					 16,310
Total committed	 29,850				48,525	 2,653,177
Assigned - General government	_		_		_	268,888
Unassigned	(20,273,606)				(4,764)	(17,083)
Total fund balances (deficit)	\$ (19,939,241)	\$	121,554	\$	7,767,232	\$ 22,808,730

B. Fund Deficits

Table 44 shows the funds that had deficits.

Table 44

Schedule of Fund Deficits

June 30, 2011 (amounts in thousands)

	Go	overnmental Funds	 Enterprise Funds	 Internal Service Funds
General Fund	\$	19,939,241	\$ 	\$
Unemployment Programs Fund			6,879,180	
Architecture Revolving Fund				25,228
Financial Information Systems Fund		_	_	28,915
Office of Systems Integration Fund		_	_	1,348
Service Revolving Fund				 52,412
Total fund deficits	\$	19,939,241	\$ 6,879,180	\$ 107,903

C. Discretely Presented Component Unit Endowments and Gifts

The University of California, a discretely presented component unit, administers certain restricted nonexpendable, restricted expendable, and unrestricted endowments that are included in the related net asset categories of the government-wide and fund financial statements. As of June 30, 2011, the total value of restricted endowments and gifts was \$11.1 billion and unrestricted endowments and gifts was \$1.6 billion. The university's policy is to retain appreciation on investments with the endowment after an annual income distribution. The net appreciation available to meet future spending needs upon approval by the Board of Regents amounted to \$1.6 billion at June 30, 2011. The portion of investment returns earned on endowments and distributed each year to support current operations is based on a rate approved by the Board of Regents. In addition, the California State University Auxiliary Organizations and the University of California Hastings College of the Law, nonmajor component units, have restricted nonexpendable and restricted expendable endowments of \$829 million and \$9 million, respectively.

NOTE 20: RISK MANAGEMENT

The primary government has elected, with a few exceptions, to be self-insured against loss or liability. Generally, the exceptions are when a bond resolution or a contract requires the primary government to purchase commercial insurance for coverage against property loss or liability. There have been no significant reductions in insurance coverage from the prior year. In addition, no insurance settlement in the last three years has exceeded insurance coverage. The primary government generally does not maintain reserves. Losses are covered by appropriations from each fund responsible for payment in the year in which the payment occurs. All claim payments are on a "pay as you go" basis, with workers' compensation benefits for self-insured agencies being initially paid by the State Compensation Insurance Fund.

The discounted liability for unpaid self-insured workers' compensation losses is estimated to be \$3.1 billion as of June 30, 2011. This estimate is primarily based on actuarial reviews of the State's employee workers'

compensation program and includes indemnity payments to claimants, as well as all other costs of providing workers' compensation benefits, such as medical care and rehabilitation. The estimate also includes the liability for unpaid services fees, industrial disability leave benefits, and incurred-but-not-reported amounts. The estimated total liability of approximately \$4.2 billion is discounted to \$3.1 billion using a 3.5% interest rate. Of the total, \$350 million is a current liability, of which \$218 million is included in the General Fund, \$119 million in the special revenue funds, \$2 million in the internal service funds and \$11 million in enterprise funds. The remaining \$2.7 billion is reported as other noncurrent liabilities in the government-wide Statement of Net Assets.

The University of California, a discretely presented component unit, is self-insured for medical malpractice, workers' compensation, employee health care, and general liability claims. These risks are subject to various claim and aggregate limits, with excess liability coverage provided by an independent insurer. Liabilities are recorded when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. These losses include an estimate for claims that have been incurred but not reported. The estimated liabilities are based on an independent actuarial determination of the anticipated future payments, discounted at rates ranging from 2.0% to 5.0%.

The California Public Employees' Retirement System (CalPERS) through its Public Employees' Benefits, a discretely presented component unit, administers three self-funded health care plans as risk pools available to all entities that contract for health insurance coverage under the Public Employees' Medical and Hospital Care Act. The plans retain all the risk of loss of allowable health claims. Claim liabilities are based on estimates of the ultimate costs of claims that have been reported but not settled and of claims that have been incurred but not reported. The estimated claims were calculated by a third-party administrator using a variety of actuarial and statistical techniques and adjusted for actual experience to produce current estimates that reflect recent settlements, claim frequency, and other economic and social factors. Adjustments to claims liabilities are charged or credited to expense in the periods in which they are made. The other major discretely presented component units do not have significant liabilities related to self-insurance.

Table 45 shows the changes in the self-insurance claims liability for the primary government and the discretely presented component units.

Table 45

Schedule of Changes in Self-Insurance Claims
Years Ended June 30
(amounts in thousands)

		Primary						•	ed Component Units				
	_	Gove	nme	ent	University of California					Public Emple	loyee Benefits		
	_	2011		2010		2011		2010		2011		2010	
Unpaid claims, beginning	\$	2,762,761	\$	2,577,638	\$	585,955	\$	598,014	\$	192,195	\$	216,584	
Incurred claims		700,815		542,698		163,191		166,943		1,722,185		1,554,574	
Claim payments		(382,055)		(357,575)		(160,070)		(179,002)		(1,678,058)		(1,578,963)	
Unpaid claims, ending	\$	3,081,521	* <u>\$</u>	2,762,761	\$	589,076	\$	585,955	\$	236,322	\$	192,195	

^{*} Includes \$51,665 for business-type activities.

NOTE 21: NONMAJOR ENTERPRISE SEGMENT INFORMATION

A segment is an identifiable activity reported as or within an enterprise fund or another stand-alone entity for which debt is outstanding and a revenue stream has been pledged in support of that debt. In addition, to qualify as a segment, an activity must be subject to an external requirement to separately account for revenues, expenses, gains and losses, assets, and liabilities of the activity. All of the activities reported in the following condensed financial information meet these requirements.

Table 46 presents the Condensed Statement of Net Assets; the Condensed Statement of Revenues, Expenses, and Changes in Fund Net Assets; and the Condensed Statement of Cash Flows for nonmajor enterprise funds that meet the definition of a segment. The primary sources of revenues for these funds follow.

High Technology Education Fund: Rental payments on public buildings that are used for educational and research purposes related to specific fields of high technology.

State Water Pollution Control Revolving Fund: Interest charged on loans to communities for construction of water pollution control facilities and projects.

Housing Loan Fund: Interest payments from low-interest, long-term farm and home mortgage loan contracts to eligible veterans living in California.

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Table 46

Nonmajor Enterprise Segments

(amounts in thousands)

Image: Properties of the	Condensed Statement of Net Assets						
Assets Eduction Eduction Control Due from other funds 9 4 4 9 9 1 6 2 1 6 2 1 7 1 1 1 1 1 1 1 1 1 1 1 1 1 1 1 1 1	June 30, 2011		High	State Water			
Due from other funds			•				
Due from other funds	Accets		Education		Control		
Due from other governments — 162.717 Other current assets 24,157 330,839 Capital assets — 65,779 2,818,618 Total assets \$ 89,970 \$ 3,316,664 Liabilities — \$ 39,970 \$ 3,316,664 Liabilities — \$ 39,30 30		\$	34	\$	4 490		
Capital assets 24,157 330,839 Capital assets 65,779 2,818,618 Total assets 89,970 \$3,316,664 Liabilities 89,970 \$393 Other current liabilities 17,234 26,657 Noncurrent liabilities 17,234 26,657 Noncurrent liabilities 55,063 1143,736 Net assets - 5,5063 143,736 Investment in capital assets, net of related debt - - 2,820,883 Total net assets 34,907 352,045 34,907 352,045 Unrestricted 34,907 3,172,928 3,172,928 3,172,928 Total net assets 34,907 3,172,928		Ψ	— —	Ψ	,		
Capital assets. 65,779 2,818.618 Total assests. 89,970 3,316.686 Liabilities 89,970 3,316.686 Due to other funds 17,234 26,657 Other current liabilities 37,829 116,686 Total liabilities 55,063 143,736 Net assets 55,063 143,736 Net assets - - Investment in capital assets, net of related debt - - Restricted 34,907 3,172,928 Total net assets 34,907 3,172,928 Total net assets 39,970 3,316,664 Condensed Statement of Revenues, Expenses, and Changes in Fund Net Assets 5,970 3,316,664 Condensed Statement of Revenues, Expenses, and Changes in Fund Net Assets 5,970 3,316,663 Condensed Statement of Revenues, Expenses, and Changes in Fund Net Assets 5,997 3,316,663 Condensed Statement of Revenues, Expenses, and Changes in Fund Net Assets 9,590 4,876 Operating revenues 9,590 4,876 Operating revenues (sepenses) 9,590 </td <td>G</td> <td></td> <td>24,157</td> <td></td> <td>•</td>	G		24,157		•		
Total assets \$ 89,970 \$ 3,316,664 Liabilities S — \$ 393 Due to other funds \$ 17,234 26,657 Noncurrent liabilities 37,829 116,686 Total liabilities 55,063 143,736 Net assets Total liabilities 5,063 143,736 Net assets Investment in capital assets, net of related debt —	Capital assets		· —		· —		
Liabilities \$ \$ 39 Other current liabilities 17,234 26,657 Noncurrent liabilities 37,829 116,686 Total liabilities 55,063 143,736 Net assets Investment in capital assets, net of related debt - - Investricted 34,907 352,045 Unrestricted - - 2,820,883 Total lead assets 34,907 3,172,928 Total liabilities and net assets 34,907 3,172,928 Total liabilities and net assets \$ 89,970 \$ 3316,664 Condensed Statement of Revenues, Expenses, and Changes in Fund Net Assets Year Ended June 30, 2011 Operating revenues (9,590) (4,876) Operating expenses (9,590) (4,876) Operating prevenues 908 49,727 Nonoperating expenses 908 49,727 Nonoperating revenues (expenses) 908 49,727 Nonoperating revenues (expenses) 908 131,276 Total net assets, July 1, 2010 33,999 3,041,652	Other noncurrent assets		65,779		2,818,618		
Due to other funds \$ 4, 33 Other current liabilities 17,234 26,657 Noncurrent liabilities 37,829 116,686 Total liabilities 55,063 143,736 Net assets - - Investment in capital assets, net of related debt - - Restricted 34,907 352,045 Urrestricted 34,907 3,172,928 Total net assets 34,907 3,172,928 Total liabilities and net assets \$ 99,970 \$ 3,316,664 Condensed Statement of Revenues, Expenses, and Changes in Fund Net Assets Yes Ended June 30, 2011 Cperating revenues \$ 10,498 \$ 54,603 Depreciation expense (9,590) (4,876) Operating prevenues (9,590) (4,876) Operating expenses (9,590) (4,876) Operating income (loss) 908 49,727 Nonoperating revenues (expenses) 908 131,276 Capital contributions 908 131,276 Total net assets, July 1, 2010 33,999 3,041,652	Total assets	\$	89,970	\$	3,316,664		
Other current liabilities 17,234 26,657 Noncurrent liabilities 37,829 116,686 Total liabilities 55,063 143,736 Net assets Investment in capital assets, net of related debt	Liabilities						
Noncurrent liabilities 37,829 116,686 Total liabilities 55,063 143,736 Net assets Investment in capital assets, net of related debt ————————————————————————————————————	Due to other funds	\$	_	\$	393		
Total liabilities 55,063 143,736 Net assets ————————————————————————————————————			•		•		
Net assets ————————————————————————————————————	Noncurrent liabilities				116,686		
Investment in capital assets, net of related debt	Total liabilities		55,063		143,736		
Restricted 34,907 352,045 Unrestricted 34,907 2,820,883 Total net assets 34,907 3,172,928 Total liabilities and net assets \$ 89,970 \$ 3,316,664 Condensed Statement of Revenues, Expenses, and Changes in Fund Net Assets Year Ended June 30, 2011 Operating revenues \$ 10,498 \$ 54,603 Depreciation expense — — — — — — — — — — — — — — — — — — —							
Unrestricted — 2,820,883 Total net assets 34,907 3,172,928 Total liabilities and net assets \$ 89,970 \$ 3,316,664 Condensed Statement of Revenues, Expenses, and Changes in Fund Net Assets Year Ended June 30, 2011 Operating revenues \$ 10,498 \$ 54,603 Depreciation expenses — — Other operating expenses (9,590) (4,876) Operating income (loss) 908 49,727 Nonoperating revenues (expenses) — (4,723) Capital contributions — 86,272 Change in net assets 908 131,276 Total net assets, July 1, 2010 33,999 3,041,652 Total net assets, June 30, 2011 \$ 34,907 \$ 3,172,928 Condensed Statement of Cash Flows Year Ended June 30, 2011 \$ 20,247 (41,080) Noncapital financing activities (9,995) (31,471) Capital and related financing activities — 91,20 Investing activities — — (712) Net decrease	•		_				
Total net assets 34,907 3,172,928 Total liabilities and net assets \$ 89,970 \$ 3,316,664 Condensed Statement of Revenues, Expenses, and Changes in Fund Net Assets Year Ended June 30, 2011 Operating revenues \$ 10,498 \$ 54,603 Depreciation expenses (9,590) (4,876) Operating income (loss) 908 49,727 Nonoperating revenues (expenses) — (4,723) Capital contributions — 86,272 Change in net assets 908 131,276 Total net assets, July 1, 2010 33,999 3,041,652 Total net assets, June 30, 2011 \$ 34,907 \$ 3,172,928 Condensed Statement of Cash Flows Year Ended June 30, 2011 \$ 20,247 (41,080) Noncapital financing activities \$ 20,247 (41,080) Noncapital and related financing activities 91,20 Capital and related financing activities — 91,20 Investing activities — 91,20 Investing activities — 91,20 Investing activities — 91,20			34,907		=		
Total liabilities and net assets \$ 89,970 \$ 3,316,664 Condensed Statement of Revenues, Expenses, and Changes in Fund Net Assets Year Ended June 30, 2011 Operating revenues \$ 10,498 \$ 54,603 Depreciation expenses (9,590) (4,876) Operating income (loss) 908 49,727 Operating revenues (expenses) 908 49,727 Capital contributions 908 131,276 Change in net assets 908 131,276 Total net assets, July 1, 2010 33,999 3,041,652 Total net assets, June 30, 2011 \$ 34,907 \$ 3,172,928 Condensed Statement of Cash Flows Year Ended June 30, 2011 \$ 20,247 (41,080) Noncapital financing activities (19,995) (31,471) Capital and related financing activities (19,995) (31,471) Capital and related financing activities - 91,120 Investing activities - (712) Net decrease 252 17,857 Cash and pooled investments at July 1, 2010 18,949 247,329			24.007				
Condensed Statement of Revenues, Expenses, and Changes in Fund Net Assets Year Ended June 30, 2011 \$ 10,498 \$ 54,603 Operating revenues \$ 10,498 \$ 54,603 Depreciation expense — — Other operating expenses (9,590) (4,876) Operating income (loss) 908 49,727 Nonoperating revenues (expenses) — — (4,723) Capital contributions — — — 86,272 Change in net assets 908 131,276 Total net assets, July 1, 2010 33,999 3,041,652 Total net assets, June 30, 2011 \$ 34,907 \$ 3,172,928 Condensed Statement of Cash Flows Year Ended June 30, 2011 \$ 20,247 \$ (41,080) Noncapital financing activities \$ 20,247 \$ (41,080) Noncapital financing activities (19,995) (31,471) Capital and related financing activities — — 91,120 Investing activities — — (712) Net decrease 252 17,857 Cash and pooled investments at July 1, 2010 18,949 247,329		•		•			
Year Ended June 30, 2011 Operating revenues \$ 10,498 \$ 54,603 Depreciation expense — — Other operating expenses (9,590) (4,876) Operating income (loss) 908 49,727 Nonoperating revenues (expenses) — (4,723) Capital contributions — 86,272 Change in net assets 908 131,276 Total net assets, July 1, 2010 33,999 3,041,652 Total net assets, June 30, 2011 \$ 34,907 \$ 3,172,928 Condensed Statement of Cash Flows Year Ended June 30, 2011 Very Control of the contro	Total Habilities and net assets	<u> </u>	89,970	<u> </u>	3,315,554		
Depreciation expense ————————————————————————————————————		ssets	•				
Other operating expenses (9,590) (4,876) Operating income (loss) 908 49,727 Nonoperating revenues (expenses) — (4,723) Capital contributions — 86,272 Change in net assets 908 131,276 Total net assets, July 1, 2010 33,999 3,041,652 Total net assets, June 30, 2011 \$ 34,907 \$ 3,172,928 Condensed Statement of Cash Flows Year Ended June 30, 2011 Vector in a state of the state of	Operating revenues	\$	10,498	\$	54,603		
Operating income (loss) 908 49,727 Nonoperating revenues (expenses) — (4,723) Capital contributions — 86,272 Change in net assets 908 131,276 Total net assets, July 1, 2010 33,999 3,041,652 Total net assets, June 30, 2011 \$ 34,907 \$ 3,172,928 Condensed Statement of Cash Flows Year Ended June 30, 2011 Vecash provided by (used in): (19,995) (31,471) Operating activities (19,995) (31,471) (20,247) (41,080) Noncapital financing activities (19,995) (31,471) (31,471) (31,471) (41,080) (41,	·				_		
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Noncapital financing activities (19,995) (31,471) Capital and related financing activities — 91,120 Investing activities — (712) Net decrease 252 17,857 Cash and pooled investments at July 1, 2010 18,949 247,329		\$	20,247	\$	(41,080)		
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Cash and pooled investments at July 1, 2010	Investing activities				(712)		
	Net decrease		252		17,857		
Cash and pooled investments at June 30, 2011	Cash and pooled investments at July 1, 2010		18,949		247,329		
	Cash and pooled investments at June 30, 2011	\$	19,201	\$	265,186		

Housing Loan	Total
Loan	10(a)
\$ 143	\$ 4,667
ψ 1+0 —	162,717
158,626	513,622
611	611
1,362,147	4,246,544
\$ 1,521,527	\$ 4,928,161
\$ —	\$ 393
63,130	107,021
1,298,718	1,453,233
1,361,848	1,560,647
611	611
159,068	546,020
155,000	2,820,883
159,679	3,367,514
\$ 1,521,527	\$ 4,928,161
9 1,521,521	4,320,101
\$ 87,082 (70)	\$ 152,183 (70)
(90,843)	(105,309)
(3,831)	46,804
(11,612)	(16,335)
	86,272
(15,443)	116,741
175,122	3,250,773
\$ 159,679	\$ 3,367,514
\$ 149,989	\$ 129,156
(302,897)	(354,363)
(176)	90,944
2,529	1,817
(150,555)	(132,446)
258,626	524,904
\$ 108,071	\$ 392,458

NOTE 22: NO COMMITMENT DEBT

Certain debt of the nonmajor component units is issued to finance activities such as construction of new facilities, remodeling of existing facilities, and acquisition of equipment. This debt is secured solely by the credit of private and public entities and is administered by trustees independent of the State. As of June 30, 2011, these component units had \$23.7 billion of debt outstanding, which is not debt of the State.

NOTE 23: CONTINGENT LIABILITIES

A. Litigation

The primary government is a party to numerous legal proceedings, many of which normally occur in governmental operations. To the extent they existed, the following were accrued as a liability in the government—wide financial statements: legal proceedings that were decided against the primary government before June 30, 2011; legal proceedings that were in progress as of June 30, 2011, and were settled or decided against the primary government as of February 24, 2012; and legal proceedings having a high probability of resulting in a decision against the primary government as of February 24, 2012, and for which amounts could be estimated. In the governmental fund financial statements, the portion of the liability that is expected to be paid within the next 12 months is recorded as a liability of the fund from which payment will be made.

In addition, the primary government is involved in certain other legal proceedings that, if decided against the primary government, may impair its revenue sources or require it to make significant expenditures. Because of the prospective nature of these proceedings, no provision for the potential liability has been made in the financial statements.

Following are the more significant lawsuits pending against the primary government.

The primary government is a defendant in two cases, *Bakersfield Mall, LLC v. Franchise Tax Board*, and *CA-Centerside II, LLC v. Franchise Tax Board*, both regarding the constitutionality of a fee imposed on limited liability companies (LLC). In *Bakersfield Mall, LLC v. Franchise Tax Board* the plaintiff contends that not all of its income is derived within the State and therefore not all income should be subject to the LLC fee. The second case, *CA-Centerside II, LLC v. Franchise Tax Board*, alleges that the LLC fee is unconstitutional regarding any activities, whether in–state or out–of–state.

In a previously settled case, *Northwest Energetic Services, LLC v. Franchise Tax Board*, the Court of Appeal found the fee unconstitutional only as applied to the plaintiff. The primary government has already begun to pay refunds to LLCs with the same facts as *Northwest* who have no income earned inside California. In another recently settled case, *Ventas Finance I, LLC v. Franchise Tax Board*, the Court of Appeal also ruled that the fee is unconstitutional as applied to the plaintiff, but it awarded only a partial refund because Ventas received income from both inside and outside of California. *Bakersfield Mall, LLC v. Franchise Tax Board*, raised the same constitutional issues as *Northwest and Ventas*, but initially pertained to LLCs that conduct business solely within California. Bakersfield Mall, LLC later amended its complaint to reflect the fact that not all of its income is derived within the State, making it similar to the *Ventas* case. This plaintiff also intended to bring a class action suit for refund on behalf of all similarly situated LLCs and to declare the LLC fee unconstitutional. However, the Court of Appeal ruled that Bakersfield Mall, LLC did not follow mandatory class action claim procedures. *CA–Centerside II, LLC v. Franchise Tax Board* raised the same constitutional issues

as *Northwest and Ventas*, and alleges that the LLC fee is unconstitutional regarding any activities, whether in–state or out–of–state. Actual and expected future claims for refunds from LLCs are estimated to be as high as \$1.2 billion. In addition, plaintiffs will in all likelihood seek a very large award of attorneys' fees in these cases should they prevail.

The primary government is the defendant in both *California Redevelopment Association et al. v. Michael C. Genest et al.* and *County of Los Angeles, et al. v. Genest, et al.* These two cases challenge the constitutionality of Assembly Bill X4-26 that requires that redevelopment agencies remit a total of \$1.7 billion in 2009-10 fiscal year and \$350 million in 2010-11 fiscal year to a county Supplemental Education Revenue Augmentation Fund to be used by local schools. The State successfully defeated the claims in the superior court and is currently defending against the claims in the Court of Appeal. If the Court of Appeal grants judgment for the plaintiff, the State would need to pay the challenged amount to the schools from the General Fund.

The primary government is the defendant in numerous cases regarding the Governor's executive orders directing the furlough, without pay, of state employees. The first executive order, issued on December 19, 2008, directed furloughs of two days per month, effective February 1, 2009, through June 30, 2010. The second order, issued on July 1, 2009, required a third furlough day per month, effective through June 30, 2010. On July 28, 2010, the Governor issued a new executive order requiring furloughs for three days per month beginning August 1, 2010, until a new 2010-11 fiscal year budget was adopted and the Director of Finance determined that the State had sufficient cash flow to pay for essential services. Furloughs officially ended for all Service Employees International Union represented State employees in November 2010 and for all remaining bargaining units in April 2011.

Most cases related to the furloughs have been settled or dismissed with only five cases still pending. Neither the outcome nor the estimated potential loss for any of the cases can be determined at this time.

The California School Boards Association has filed a case against the primary government. *California School Boards Association, et al.v. State of California et al.* is challenging the amount of funds appropriated for education in the 2011-12 fiscal year, arguing that the amount violates the minimum funding guarantee in the California Constitution Article XVI, section 8 (Proposition 98). Plaintiffs argue that certain funds directed to local governments should have been included in the Proposition 98 calculation and that by not including these funds in the calculation the state underfunded education by approximately \$2.8 billion in the 2011-12 fiscal year. The State has denied the material allegations and has filed an answer to the complaint. Currently it is anticipated that the State will ultimately add the \$2.8 billion back to the minimum Proposition 98 calculation over the next five years; however, an unfavorable outcome of this case would require the State to add back the amount entirely in the 2012-13 fiscal year.

Until recently the primary government was a defendant in five cases related to Medi-Cal reimbursement rate reductions. As a result of intervening events including sunsetting of specific legislation, resolution of these matters will no longer have a future fiscal impact.

The University of California, the State Compensation Insurance Fund (SCIF), the California Housing Finance Agency (CalHFA), the Public Employees' Benefits Fund, and certain nonmajor discretely presented component units are contingently liable in connection with claims and contracts, including those currently in litigation, arising in the normal course of their activities. Although there are inherent uncertainties in any litigation, the management and the general counsel of the University of California, SCIF, CalHFA, the Public Employees' Benefit Fund, and certain nonmajor discretely presented component units are of the opinion that the outcome of such matters either will not have a material effect on the financial statements or cannot be estimated at this time.

B. Federal Audit Exceptions

The primary government receives substantial funding from the federal government in the form of grants and other federal assistance. The primary government, the University of California, CalHFA, and certain nonmajor discretely presented component units are entitled to these resources only if they comply with the terms and conditions of the grants and contracts and with the applicable federal laws and regulations; they may spend these resources only for eligible purposes. If audits disclose exceptions, the primary government, the University of California, CalHFA, and certain nonmajor discretely presented component units may incur a liability to the federal government.

NOTE 24: PENSION TRUSTS

Two retirement systems, the California Public Employees' Retirement System (CalPERS) and the California State Teachers' Retirement System (CalSTRS), which are fiduciary component units, are included in the pension and other employee benefit trust funds column of the fiduciary funds and similar component units' financial statements. The pension liability for all pension and other employee benefit trust funds was determined in accordance with GASB Statement No. 27, Accounting for Pensions by State and Local Government Employers. The amounts of the pension liability for all pension and other employee benefit trust funds are presented in Table 48 as the net pension obligation (NPO) as of June 30, 2011. The investments of these fiduciary component units are presented in Table 6 in Note 3, Deposits and Investments.

CalPERS administers four defined benefit retirement plans: the Public Employees' Retirement Fund, the Judges' Retirement Fund II, and the Legislators' Retirement Fund. CalPERS also administers three defined contribution plans: the State Peace Officers' and Firefighters' Defined Contribution Plan Fund, the Public Agency Deferred Compensation Program, and the public employee Supplemental Contributions Program Fund. CalPERS issues a publicly available financial report that includes financial statements and required supplementary information for these plans. This report may be obtained by writing to the California Public Employees' Retirement System, Fiscal Services Division, P.O. Box 942703, Sacramento, California 94229 or by visiting the CalPERS website at www.CalPERS.ca.gov.

CalPERS uses the accrual basis of accounting. Member contributions are recognized in the period in which the contributions are due. Employer contributions are recorded when due and the employer has made a formal commitment to provide the contributions. Benefits under the defined benefit plans and refunds are recognized when due and payable in accordance with the terms of each plan.

CalSTRS administers four defined benefit retirement plans within the State Teachers' Retirement Plan: the Defined Benefit Program (DB Program), the Defined Benefit Supplement Program, the Cash Balance Benefit Program, and the Replacement Benefit Program. CalSTRS also offers the Pension2 Program through a third-party administrator. The Pension2 Program is a tax-deferred defined contribution plan meeting the requirements of Internal Revenue Code Sections 403(b) and 457. The Teachers' Health Benefits Fund provides postemployment health benefits to retired members of the DB Program. CalSTRS issues a publicly available financial report that includes financial statements and required supplementary information for these plans. This report may be obtained from the California State Teachers' Retirement System, P.O. Box 15275, Sacramento, California 95851.

CalSTRS uses the accrual basis of accounting. Member contributions are recognized in the period in which the contributions are due. Employer and primary government contributions are recognized when due and when the employer or the primary government has made a formal commitment to provide the contributions.

Benefits and refunds are recognized when due and payable, in accordance with the retirement and benefits programs.

A. Public Employees' Retirement Fund

1. Fund Information

Plan Description: CalPERS administers the Public Employees' Retirement Fund (PERF), which is an agent multiple-employer defined benefit retirement plan. Employers participating in the PERF include the primary government and certain discretely presented component units, 61 school employers, and 1,512 public agencies as of June 30, 2011.

The amount by which the actuarial accrued liability exceeded the actuarial value of assets in the PERF for the primary government and other participating agencies was \$51.3 billion at June 30, 2010. This is a result of the difference between the actuarial value of assets of \$257.1 billion and the actuarial accrued liability of \$308.3 billion. Contributions are either actuarially determined or determined by statute.

2. Employer's Information

Plan Description: The primary government and certain discretely presented component units contribute to the PERF. CalPERS acts as a common investment and administrative agent of the primary government and the other member agencies. The discretely presented component units' participation in the PERF is not a material portion of the program. The primary government employees served by the PERF include: first-tier and second-tier miscellaneous and industrial employees, California Highway Patrol employees, peace officers and firefighters, and other safety members. In the June 30, 2010 actuarial valuation, the payroll for primary government employees covered by the PERF for fiscal year 2008-09 was \$16.3 billion.

All employees in a covered class of employment who work half-time or more are eligible to participate in the PERF. The PERF provides benefits based on members' years of service, age, final compensation, and benefit formula. Vesting occurs after five years or after ten years for second-tier employees. The PERF provides death, disability, and survivor benefits. The benefit provisions are established by statute.

Funding Policy: Benefits are funded by contributions from members and the primary government and by earnings from investments. Member and primary government contributions are a percentage of applicable member compensation. Member rates are defined by law and based on the primary government's benefit formula. The primary government contribution rates are determined by periodic actuarial valuations or by statute.

Employees, with the exception of employees in the second-tier plans and the State's Alternate Retirement Program, contribute to the fund based on the required contribution rates. The contribution rates of active plan members are based on a percentage of salary over a monthly base compensation amount of \$0 to \$863. Employees' required contributions vary from 5.0% to 11.0% of their salary over the base compensation amount.

All of the primary government employees served by the PERF are now covered by group term life insurance. Table 47 shows the required employer contribution rates for the primary government.

Table 47

Schedule of Required Employer Contribution Rates for the Primary Government by Member Category

Year Ended June 30, 2011

			Group		
<u>-</u>	Normal Cost	Unfunded Liability	Term Life Benefit	Total Rate	
Miscellaneous members					
First tier	9.862 %	10.060 %	0.000 %	19.922 %	
Second tier	9.562	10.060	0.000	19.622	
Industrial (first and second tier)	13.623	4.390	0.170	18.183	
California Highway Patrol	15.400	17.225	0.000	32.625	
Peace officers and firefighters	18.363	10.447	0.077	28.887	
Other safety members	16.439	4.109	0.124	20.672	

For the year ended June 30, 2011, the annual pension cost (APC) and the amount of contributions made by the primary government were each \$3.3 billion. The APC and the percentage of APC contributed for the last three years are shown in Table 48. Actuarial valuations of the PERF are performed annually. Information from the last valuation, which was performed as of June 30, 2010, is also shown in Table 48 for the primary government.

The Schedule of Funding Progress, presented as required supplementary information (RSI) following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Actuarial Methods and Assumptions: In the June 30, 2010 actuarial valuation, the individual entry age normal cost method was used. The actuarial assumptions included a 7.75% investment rate of return, projected salary increases of 3.45% to 19.95%, depending on duration of service, and postemployment benefit increases of 2.00% or 3.00%, compounded annually. The projected salary increases include a 3.00% inflation assumption. The unfunded actuarial accrued liability (UAAL) is being amortized as a level percentage of projected payroll on a closed basis.

B. Judges' Retirement Fund

Plan Description: CalPERS administers the Judges' Retirement Fund (JRF), which is an agent multiple-employer defined benefit retirement plan. The JRF membership includes justices of the Supreme Court and courts of appeal, as well as judges of superior courts, appointed or elected prior to November 9, 1994. There are 59 employers participating in the JRF for the year ended June 30, 2011. The payroll for employees covered by the JRF for the year ended June 30, 2011, was approximately \$80 million. The primary government pays the employer contributions for all employees covered by the JRF.

The JRF provides benefits based on a member's years of service, age, final compensation, and benefit formula. Vesting occurs after five years. The JRF provides death, disability, and survivor benefits. Benefits for the JRF are established by the Judges' Retirement Law.

Funding Policy: The contribution rate of active plan members is defined by law and is based on a percentage of salary over a base compensation amount. For the year ended June 30, 2011, the required member rate for the JRF was 8.0%.

The contributions of the primary government to the JRF are made pursuant to state statute and are not actuarially determined. As of June 30, 2011, employer contributions are required to be 8.0% of applicable member compensation. Other funding to meet benefit payment requirements of the JRF is currently provided by: filing fees, which require varying amounts, depending on fee rate and number of filings; investments, which earn the current yield on short-term investments; and the primary government's balancing contributions, as required by the Judges' Retirement Law. The balancing contributions are an amount at least equal to the estimated benefits payable during the ensuing fiscal year, less the sum of the estimated member contributions during the ensuing fiscal year and net assets available for benefits at the beginning of the fiscal year ("pay as you go" basis).

The APC and the amount of employer contributions made to the JRF for the year ended June 30, 2011, were \$514 million and \$167 million, respectively. The NPO of the JRF at June 30, 2011, was \$3.0 billion, an increase of \$346 million over last year's balance of \$2.7 billion. The APC is comprised of \$1.3 billion for the annual required contribution (ARC), \$119 million for interest on the NPO, and a negative \$868 million adjustment to the ARC. An actuarial valuation of the JRF's assets and liabilities is made annually. The APC, the percentage of APC contributed, and the NPO for the last three years are shown in Table 48. Information on the last valuation, which was performed as of June 30, 2010, is shown in Table 48.

The Schedule of Funding Progress, presented as RSI following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Actuarial Methods and Assumptions: In the June 30, 2010 actuarial valuation, the individual entry age normal cost method was used. The actuarial assumptions included a 4.50% investment rate of return, projected salary increases of 3.25%, and postemployment benefit increases of 3.25%. The projected salary increases include a 3.00% inflation assumption.

C. Judges' Retirement Fund II

Plan Description: CalPERS administers the Judges' Retirement Fund II (JRF II), which is an agent multiple-employer defined benefit retirement plan. The membership of the JRF II includes justices of the same courts covered by the JRF who were appointed or elected on or subsequent to November 9, 1994. There are 59 employers participating in the JRF II. The payroll for employees covered by the JRF II for the year ended June 30, 2011, was approximately \$224 million. The primary government pays the employer contributions for all employees covered by the JRF II.

The JRF II provides benefits based on a member's years of service, age, final compensation, and benefit formula. Vesting occurs after five years. The JRF II provides death, disability, and survivor benefits. Benefits for the JRF II are established by the Judges' Retirement System II Law.

Funding Policy: The required contribution rate of active plan members is defined by law and is based on a percentage of salary over a base compensation amount. For the year ended June 30, 2011, the required member rate for the JRF II was 8.0%, and the primary government's contribution rate for the JRF II was 24.04% of applicable member compensation.

Actuarial valuations for the JRF II are required to be carried out annually. The legislated primary government contribution rate is adjusted periodically as part of the annual Budget Act, in order to maintain or restore the actuarial soundness of the fund.

For the year ended June 30, 2011, the amount of contributions made for the JRF II were approximately \$53.9 million, which is more than the actuarially determined APC and required contribution of approximately \$50.9 million. The APC and the percentage of APC contributed for the year ended June 30, 2011, are shown in Table 48. Information on the last valuation, which was performed as of June 30, 2010, is also shown in Table 48.

The Schedule of Funding Progress, presented as RSI following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Actuarial Methods and Assumptions: In the June 30, 2010 actuarial valuation, the individual entry age normal cost method was used. The actuarial assumptions included a 7.25% investment rate of return, projected salary increases of 3.25%, and postemployment benefit increases of 3.00%. The projected salary increases include a 3.00% inflation assumption. The UAAL is being amortized as a level percentage of payroll on a closed basis over 23 years.

D. Legislators' Retirement Fund

Plan Description: CalPERS administers the Legislators' Retirement Fund (LRF), which is a single-employer defined benefit retirement plan. The eligible membership of the LRF includes state legislators serving in the legislature prior to November 7, 1990, constitutional officers, and legislative statutory officers. For the fiscal year ending June 30, 2011, no statutory contribution was required, based on the June 30, 2009 valuation.

The LRF provides benefits based on a member's years of service, age, final compensation, and benefit formula. Vesting occurs after five years. The plan provides death, disability, and survivor benefits. Benefits for the LRF are established by the Legislators' Retirement Law. No current legislators are eligible to participate in the LRF. The only active members in the LRF are 16 constitutional officers (including the Insurance Commissioner and members of the Board of Equalization) and legislative statutory officers.

Funding Policy: The employer contribution requirements of the LRF are based on actuarially determined rates. An actuarial valuation of the LRF's assets and liabilities is required at least every two years. Member contribution rates are defined by law. For the year ended June 30, 2011, employee contributions were not required because the plan was superfunded. "Superfunded" means that the plan's actuarial value of assets exceeds the present value of future benefits for current members.

The NPO of the LRF on June 30, 2011, was approximately \$10 million. There was no APC because the ARC equaled zero and the interest on the NPO closely approximated the adjustment to the ARC. The APC, the percentage of APC contributed, and the NPO for the last three years are shown in Table 48. An actuarial valuation of the LRF's assets and liabilities is required at least every two years. Information on the last valuation, which was performed as of June 30, 2010, is also shown in Table 48. The aggregate cost method that was used for the June 30, 2010 valuation does not identify or separately amortize the unfunded actuarial accrued liability; therefore, the information about funded status in Table 48 is prepared using the entry age actuarial cost method and is intended to serve as a surrogate for the funded status and funding progress of the plan.

The Schedule of Funding Progress, presented as RSI following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Actuarial Methods and Assumptions: In the June 30, 2010 actuarial valuation, the aggregate cost method was used. The actuarial assumptions included a 6.00% investment rate of return, projected salary increases of 3.25%, and postemployment benefit increases of 3.00%. The projected salary increases include a 3.00% inflation assumption.

E. State Peace Officers' and Firefighters' Defined Contribution Plan Fund

Plan Description: CalPERS administers the State Peace Officers' and Firefighters' Defined Contribution Plan Fund (SPOFF), which is a defined contribution pension plan. The plan is a qualified money purchase pension plan under Section 401(a) of Title 26 of the Internal Revenue Code. It is intended to supplement the retirement benefits provided by the Public Employees' Retirement Fund to eligible peace officers and firefighters employed by the State of California.

Funding Policy: Contributions to the plan are funded entirely by the primary government. Contribution requirements are established and may be amended through a memorandum of understanding from the State of California Department of Personnel Administration. Effective April 2011, the State suspended contributing on behalf of rank and file positions; and effective May 2011, the State suspended contributing on behalf of supervisors, management, and exempt positions. As of June 30, 2011, the duration of the suspension is unknown because the program is being administered according to the most recent Memorandum of Understanding. For the year ended June 30, 2011, contributions by the primary government to the SPOFF were approximately \$39 million.

Contributions are invested in the CalPERS Moderate Asset Allocation Fund. Distributions are allowed only at retirement or permanent separation from all State employment. The benefits paid to a participant will depend only on the amount contributed to the participant's account and earnings on the value of the participant's account. Plan provisions are established by and may be amended by statute. At June 30, 2011, there were 39,432 participants in the SPOFF.

F. Teachers' Retirement Fund

Plan Description: CalSTRS administers the Teachers' Retirement Fund, which is an employee benefit trust fund created to administer the State Teachers' Retirement Plan (STRP). The STRP is a defined benefit pension plan that provides for retirement, disability, and survivor benefits. Four programs comprise the STRP: the Defined Benefit (DB) Program, the Defined Benefit Supplement (DBS) Program, the Cash Balance (CB) Benefit Program, and the Replacement Benefit (RB) Program. The STRP is a cost-sharing, multiple-employer, defined-benefit retirement plan that provides pension benefits to teachers and certain other employees of the California public school system.

Membership in the DB Program is mandatory for all employees meeting the eligibility requirements. The DB Program provides benefits based on a member's age, final compensation, and years of service. Vesting occurs after five years. In addition, the retirement program provides benefits to members upon disability and to survivors upon the death of eligible members. The Teachers' Retirement Law establishes the benefits for the DB Program. At June 30, 2011, the DB Program had 1,669 contributing employers and as of June 30, 2010, had 441,544 active and 166,976 inactive program members and 243,796 benefit recipients. The primary

government is a nonemployer contributor to the DB Program. The payroll for employees covered by the DB Program for the year ended June 30, 2011, was approximately \$26.3 billion.

Membership in the DBS Program is automatic for all members of the DB Program. The DBS Program provides benefits based on the balance of member accounts. Vesting occurs immediately. The Teachers' Retirement Law establishes the benefits for the DBS Program. The primary government does not contribute to the DBS Program.

The CB Benefit Program is designed for employees of California public schools who are hired to perform creditable service for less than 50% of the full-time equivalent for the position. Employer participation in the CB Benefit Program is optional. However, if the employer elects to offer the CB Benefit Program, each eligible employee will automatically be covered by the CB Benefit Program unless the member elects to participate in the DB Program or an alternative plan provided by the employer within 60 days of hire. At June 30, 2011, the CB Benefit Program had 33 contributing school districts and 33,261 contributing participants.

The RB Program is a qualified excess benefits arrangement for DB Program members that is administered through a separate pension trust apart from the other three STRP programs and was established in accordance with Internal Revenue Code (IRC) Section 415(m). IRC Section 415(b) imposes a dollar limit on the annual retirement benefits an individual may receive from a qualified defined benefit pension plan. The program is funded as needed. Monthly contributions that would otherwise be credited to the DB program are instead credited to the RB Program to fund monthly program costs. Monthly employer contributions are received and paid to members in amounts equal to the benefits not paid as a result of IRC Section 415(b), subject to withholding for any applicable income or employment taxes. During fiscal year 2010-11, the RB Program had 243 participants.

Funding Policy: DB Program benefits are funded by contributions from members, employers, the primary government, and earnings from investments. Members and employers contribute a percentage of applicable member earnings. The Teachers' Retirement Law governs member rates, employer contribution rates, and primary government contributions.

The DB Program contribution rate of members was 6.00% of creditable compensation through December 31, 2010, and increased to 8.00% thereafter for service less than or equal to one year of creditable service per fiscal year. The employer contribution rate is 8.25% of creditable compensation for service less than or equal to one year of creditable service per fiscal year. For service in excess of one year within one fiscal year, the employer contribution rate is 0.25%. In fiscal year 2010-11, the General Fund contribution was 2.017% of total creditable compensation of the fiscal year ending in the prior calendar year. Education Code section 22955(b) states that the General Fund will contribute additional quarterly payments at a contribution rate of 0.524% of creditable earnings of the fiscal year ending in the immediately preceding calendar year when there is an unfunded obligation or a normal cost deficit. The percentage is adjusted up to 0.25% per year to reflect the contributions required to fund the unfunded obligation or the normal cost deficit. However, the transfer may not exceed 1.505% of creditable compensation from the immediately preceding calendar year. The normal cost deficit is the difference between the normal cost rate and the member and employer contributions, which equal 16.00% of creditable compensation. Based on the most recent actuarial valuation, as of June 30, 2010, there is no normal cost deficit, but there was an unfunded obligation for benefits in place as of July 1, 1990. Therefore, the General Fund is required to contribute the additional quarterly payments at a contribution rate of 0.524% starting October 1, 2011.

The DBS Program member contribution rate is 2.0% of creditable compensation for service less than or equal to one year of creditable service per fiscal year. For service in excess of one year within one fiscal year, the member contribution rate is 8.0% and the employer rate is 8.0%.

For the year ended June 30, 2011, the APC for the DB Program was approximately \$6.0 billion; the employer and primary government contributions were approximately \$2.2 billion and \$568 million, respectively. The APC and the percentage of APC contributed for the last three years are shown in Table 48. Actuarial valuations of the DB Program are performed annually. Information from the last valuation is shown in Table 48.

G. CalSTRS Pension2 Program

Plan Description: CalSTRS administers the Pension2 Program, which is comprised of the IRC 403(b) and 457 programs, through a third-party administrator. The Pension2 is a defined contribution plan and is open to any employee who is eligible to participate. Contributions to the program are voluntary; however, the Internal Revenue Code does impose a maximum amount that can be contributed annually. At June 30, 2011, the Pension2 IRC 403(b) and 457 programs had approximately 761 and 23 participating employers (school districts) and approximately 6,547 and 148 plan members, respectively.

H. Teachers' Health Benefits Fund

Plan Description: CalSTRS administers the Teachers' Health Benefits Fund (THBF), which was established pursuant to Chapter 1032, Statutes of 2000 (SB 1435), to provide the Medicare Premium Payment Program for eligible retired members of the DB Program. At June 30, 2011, there were 7,777 benefit recipients.

Funding Policy: The THBF is funded as needed from the monthly DB Program statutory employer contribution that exceeds the amount needed to finance the liabilities of the DB Program based on the June 30, 2000, actuarial valuation of the DB Program.

Table 48

Actuarial Information – Pension Trusts – Primary Government

Valuation Date As Indicated

	Public Employees' Retirement Fund		Judges' Retirement Fund		Judges' Retirement II Fund	
Last actuarial valuation	June 30, 2010)	June 30, 2010		June 30, 2010	
Actuarial cost method	Individual Entr Age Normal	y	Individual Entry Age Normal	•	Individual Entry Age Normal	
Amortization method	Level % of Payroll, Closed		None		Level % of Payroll, Closed	
Remaining amortization period	Not available ³	1	None		23 Years	
Asset valuation method	Smoothed Market Value		Market Value		Smoothed Market Value	
Actuarial assumption Investment rate of return Projected salary increase Includes inflation at Post-retirement benefit increases	7.75 3.45-19.95 3.00 2.00 - 3.00	5	4.50 ⁴ 3.25 3.00 3.25	%	7.25 °3.25 °3.00 °3.00	%
Annual pension costs (in millions) Year ended 6/30/09 Year ended 6/30/10 Year ended 6/30/11	\$ 3,080 2,878 3,277	\$	662 514		\$ 43 45 51	
Percent contribution Year ended 6/30/09 Year ended 6/30/10 Year ended 6/30/11	100 100 100	%	24 16 13	%	92 9 95 106	%
Net pension obligation (NPO) (in millions) Year ended 6/30/09 Year ended 6/30/10 Year ended 6/30/11	_ _ _	\$	2,226 2,703 2,994		\$ — 2 (1)	
Funding as of last valuation (in millions) Actuarial value – assets	\$ 97,346 121,446		64 3,429		461 521	
(unfunded actuarial accrued liability (UAAL)) Covered payroll Funded ratio EAV (UAAL) as percent of covered payroll	(24,100) 16,281 80.2 (148.0)	%	(3,365) 86 1.9 (3,912.8)		(60) 213 88.5 (28.2)	

¹ The aggregate cost method is used to determine the annual required contribution of the employer for the Legislators' Retirement Fund. Because this method does not identify or separately amortize unfunded actuarial liabilities, information about funded status is prepared using the entry age cost method and is intended to serve as a surrogate for the funded status of the plan.

The State is a non-employer contributor to the State Teacher's Retirement Defined Benefit Program Fund, a cost-sharing multiple-employer plan. The annual pension cost includes the amount related to both the State and the local government employers. The notion of NPO does not apply to cost-sharing employer plans. According to the provisions of the Education Code, the State and local government employers contributed \$568 million and \$2.2 billion, respectively, for the year ending June 30, 2011. Based on the most recent actuarial valuation, dated June 30, 2010, current statutory contributions are sufficient to fund normal costs but are not expected to be sufficient to amortize the unfunded actuarial obligation. However, future estimates of the actuarial unfunded obligation may change due to market performance, legislative actions, and other experience that may differ from the actuarial assumptions.

Legislators' Retirement Fund ¹		Re I Bene	e Teachers etirement Defined efit Progra Fund ²	
 June 30, 2010			e 30, 2010	_
Aggregate Cost		E	ntry Age Normal	
None			evel % of Payroll, Open	
None		3	30 years	
Smoothed Market Value		W Adj	ected Value Vith 33% ustment to rket Value	
6.00	%		7.75	%
3.25			4.00	
3.00			3.00	
3.00			2.00	
		\$	4,547	
			4,924	
_			5,985	
			63	%
			55	
			47	
\$ 10			_	
10			_	
10			_	
127		\$	140,291	
112			196,315	
15			(56,024)	
2			26,275	
113.4			71.5	
750.0	%		(213.2)	%

³ Calculations not yet completed for June 30, 2010 valuations.

⁴ The actuarial assumption for the investment rate of return was reduced from 7.0% to 4.5% to reflect the funding of the JRF on a pay-as-you-go basis.

NOTE 25: POSTEMPLOYMENT HEALTH CARE BENEFITS

A. State of California Other Postemployment Benefits Plan

Plan Description: The primary government and certain discretely presented component units provide health benefits (medical and prescription drug benefits) and dental benefits to annuitants of retirement systems through a substantive single-employer defined benefit plan to which the primary government contributes as an employer (State substantive plan). The primary government also offers life insurance, long-term care, and vision benefits to retirees; however, because these benefits are completely paid for by the retirees, the primary government has no liability. The discretely presented component units represent 3.3% of plan participation. The design of health and dental benefit plans can be amended by the California Public Employees' Retirement System (CalPERS) Board of Administration and the Department of Personnel Administration, respectively. Employer and retiree contributions are governed by the primary government and can be amended by the primary government through the Legislature. The plan contributes to the California Employers' Retiree Benefit Trust Fund (CERBTF). The CERBTF is an agent multiple-employer irrevocable trust fund for the prefunding of health, dental, and other non-pension benefits. CalPERS reports on the CERBTF as part of its annual financial statements, which can be downloaded from the CalPERS website.

Fifty-eight county superior courts (trial courts) are included in the primary government. However, each trial court is a separate employer for GASB Statement 45 reporting purposes. Fifty-two trial courts have a single-employer defined benefit plan, five trial courts (Fresno, Modoc, San Benito, San Bernardino, and Stanislaus) have no plan, and one trial court (San Diego) has a cost-sharing multiple-employer defined benefit plan. These plans have separate biennial actuarial valuations. Forty-eight plans are not accounted for in a trust fund and do not issue separate reports. Five trial courts (Lassen, Orange, San Diego, Sonoma, and Yolo) each contribute to one of four trust funds that issue separate reports.

To be eligible for these benefits, primary government first-tier plan annuitants must retire on or after age 50 with at least five years of service, and second-tier plan annuitants must retire on or after attaining age 55 with at least 10 years of service. In addition, annuitants must retire within 120 days of separation from employment to be eligible to receive these benefits. During the 2010-11 fiscal year, approximately 154,500 annuitants were enrolled to receive health benefits and approximately 128,100 annuitants were enrolled to receive dental benefits. As of July 1, 2009—the most recent actuarial valuation date—the trial courts had approximately 3,300 enrolled retirees and spouses.

Funding Policy: The contribution requirements of plan members and the State are established and may be amended by the Legislature. In accordance with the California Government Code, the State generally pays 100% of the health insurance cost for annuitants, plus 90% of the additional premium required for the enrollment of family members of annuitants. Although the California Government Code does not specify the State's contribution toward dental insurance costs, the State generally pays all or a portion of the dental insurance cost for annuitants, depending upon the completed years of credited state service at retirement and the dental coverage selected by the annuitant. The State funds the cost of providing health and dental insurance to annuitants primarily on a pay-as-you-go basis with a small amount of prefunding for California Highway Patrol members. The maximum 2011 monthly State contribution was \$542 for one-party coverage, \$1,030 for two-party coverage, and \$1,326 for family coverage.

Each of the trial courts determines its respective retirees' benefits and benefit levels as well as the funding policy for its respective plan. Forty-eight trial courts fund retirees' benefits on a pay-as-you-go basis. The 2010 monthly contribution rate for the trial courts with single-employer defined benefit plans—the latest year for which information is available—ranged from zero to \$2,120. Two trial courts (Lassen and Yolo) contribute at

least the annual required contribution (ARC) of the employer, an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed 30 years. Orange contributes 3.50% of payroll, with at least the ARC contributed each year. Sonoma contributes \$50,000 per month to an other postemployment benefit (OPEB) trust and pays a portion of ongoing benefit payments directly from trial court assets. San Diego, a cost-sharing multiple-employer defined benefit plan, had a contribution rate of 1.80% of annual covered pension payroll. For the year ended June 30, 2011, the State contributed \$1.6 billion toward annuitants' health and dental benefits. Of this amount, the trial courts represent \$27 million and certain discretely presented component units represent \$49 million.

Annual OPEB Cost and Net OPEB Obligation: The State's annual OPEB cost (expense) is calculated based on the ARC. Table 49 presents the State's OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for the year ended June 30, 2011, and the two preceding years, including trial courts.

Table 49

Schedule of Annual OPEB Cost, Percentage of Annual OPEB Cost Contributed, and Net OPEB Obligation (amounts in thousands)

		Percentage of Annual OPEB Cost	
Fiscal Year Ended	Annual OPEB Cost	Contributed	Net OPEB Obligation
June 30, 2009	\$ 3,871,290	36.19 %	\$ 4,930,848
June 30, 2010	4,078,493	34.31	7,597,735
June 30, 2011	4,359,929	36.70	10,357,406

Table 50 presents the components of the State's net OPEB obligation to the OPEB plan, including trial courts.

Table 50

Schedule of Net OPEB Obligation

June 30, 2011 (amounts in thousands)

	_	Amount
Annual required contribution.	\$	4,319,632
Interest on net OPEB obligation.		339,070
Adjustment to annual required contribution.		(298,773)
Annual OPEB cost		4,359,929
Contributions made		(1,600,258)
Increase in net OPEB obligation		2,759,671
Net OPEB obligation — beginning of year		7,597,735
Net OPEB obligation — end of year	\$	10,357,406

Funded Status and Funding Progress: As of June 30, 2011—the most recent actuarial valuation date for the State substantive plan—the actuarial accrued liability (AAL), for benefits was \$62.14 billion, and the actuarial value of assets was \$7 million, resulting in an unfunded actuarial accrued liability (UAAL) of negative \$62.14 billion. The covered payroll (annual payroll of active employees covered by the plan) was \$18.01 billion, and the ratio of the UAAL to the covered payroll was negative 345%.

For the trial courts, as of July 1, 2009—the most recent actuarial valuation date—the AAL for benefits was \$1.5 billion, and the actuarial value of assets was \$9 million, resulting in an UAAL of negative \$1.5 billion. The covered payroll was \$1.0 billion, and the ratio of the UAAL to covered payroll was negative 147%.

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about mortality and the healthcare cost trend. Amounts determined regarding the plan's funded status and the employer's annual required contributions are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Actuarial Methods and Assumptions: Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used are consistent with a long-term perspective.

In the June 30, 2011 State substantive plan actuarial valuation, the individual entry age normal cost method was used. The actuarial assumptions included a 4.50% investment rate of return and an annual health care cost trend rate of actual increases for 2012 and 9.00% in 2013, initially, reduced to an ultimate rate of 4.50% after seven years. Both rates included a 3.00% annual inflation assumption. Annual wage inflation is assumed to be 3.25%. The UAAL is being amortized as a level percentage of projected payroll on an open basis over 30 years.

For the trial courts, in the July 1, 2009 biennial actuarial valuations, the entry age normal cost method was used. The actuarial assumptions included a 3.75% investment rate of return for 48 trial courts. Three trial courts (Lassen, Orange, and Yolo) use a 7.75% investment rate of return and Sonoma uses a 5.25% investment rate of return. The actuarial assumptions included an annual health care cost trend rate of 8.50%, initially, reduced by 0.50% increments to an ultimate rate of 5.00% after ten years. Annual inflation and payroll growth are assumed to be 3.00% and 3.25%, respectively. The UAAL is amortized as a level percentage of payroll on an open basis over 30 years for 46 trial courts, on a closed basis over 30 years for three trial courts (Lassen, Sonoma, and Yolo) and on a closed basis over 28 years for Orange. Two trial courts (Alpine and Mendocino) amortize the UAAL on a closed basis over 28 years as a level dollar amount.

B. University of California Retiree Health Plan

Plan Description: The University of California, a discretely presented component unit, administers single-employer health and welfare plans to provide health and welfare benefits, primarily medical, dental and vision, to eligible retirees and their families (retirees) of the university and its affiliates. The Regents have the authority to establish or amend the plans. Additional information can be obtained from the 2010-11 annual report of the University of California Health and Welfare Plans.

Membership in the University of California Retirement Plan is required to become eligible for retiree health benefits. As of July 1, 2010, the date of the latest actuarial valuation, 35,194 retirees are receiving such benefits.

Funding Policy: The contribution requirements of the university and eligible retirees are established and may be amended by the university. The contribution requirements are based upon projected pay-as-you-go financing. Contributions toward medical and dental benefits are shared between the university and the retiree. The university does not contribute toward the cost of other benefits available to retirees. Employees who meet specific requirements including completed years of credited service may continue their medical and dental benefits into retirement and continue to receive university contributions for those benefits. Active employees do not make any contributions toward the retiree health benefit plans. Retirees pay the excess, if any, of the premium over the applicable portion of the university's contribution.

Table 51 presents the university's OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for the year ended June 30, 2011, and the two preceding years.

Table 51

Schedule of Annual OPEB Cost, Percentage of Annual OPEB Cost Contributed, and Net OPEB Obligation - University of California

(amounts in thousands)

		Percentage of Annual OPEB Cost	
Fiscal Year Ended	Annual OPEB Cost	Contributed	Net OPEB Obligation
June 30, 2009	\$ 1,550,562	18.84 %	\$ 2,377,128
June 30, 2010	1,694,847	17.59	3,773,804
June 30, 2011	1,812,905	18.16	5,257,422

Table 52 presents the components of the university's net OPEB obligation to the University of California Health and Welfare Plans.

Table 52

Schedule of Net OPEB Obligation - University of California

June 30, 2011

(amounts in thousands)

	_	Amount
Annual required contribution	\$	1,990,553
Interest on net OPEB obligation		207,997
Adjustment to annual required contribution		(385,645)
Annual OPEB cost		1,812,905
Contributions made		(329,287)
Increase in net OPEB obligation		1,483,618
Net OPEB obligation — beginning of year		3,773,804
Net OPEB obligation — end of year	\$	5,257,422

Funded Status and Funding Progress: For the University of California, as of July 1, 2010—the most recent actuarial valuation date—the AAL for benefits was \$16.0 billion, and the actuarial value of assets was \$74 million, resulting in a UAAL of negative \$16.0 billion. The covered payroll (annual payroll of active employees covered by the plan) was \$8.0 billion, and the ratio of the UAAL to the covered payroll was negative 200%.

Actuarial Methods and Assumptions: For the University of California, in the July 1, 2010 actuarial valuation, the individual entry age normal cost method was used. The actuarial assumptions included a 5.5% investment rate of return, an annual health care cost trend rate of 10.0% to 12.0% initially, depending on the type of plan, reduced by increments to an ultimate rate of 5.0% over nine years, with a projected 3.0% inflation rate. The initial and future UAAL are being amortized as a flat dollar amount over 30 and 15 years, respectively, on a closed basis.

NOTE 26: SUBSEQUENT EVENTS

The following information describes significant events that occurred subsequent to June 30, 2011, but prior to the date of the auditor's report.

A. Debt Issuances

In September and October 2011, the primary government issued a total of \$4.5 billion in general obligation bonds to finance or refinance capital project facilities and other voter-approved costs for public purposes, including: neighborhood parks; safe drinking water; children's hospitals; public education facilities; transportation; highway safety, traffic reduction, air quality, and port security; housing and emergency shelters; watershed and flood protection; river, coast, and beach protection; water quality, supply, and conservation; literacy improvement and public library construction and renovation; medical research; high speed rail facilities; and disaster preparedness and flood prevention.

In November 2011, the primary government issued \$439 million in economic recovery bonds to refund the Refunded Bonds, the proceeds of which were used to address Accumulated State Budget Deficit.

In August, September and October 2011, the Department of Water Resources issued \$309 million in water system revenue bonds and \$960 million in power supply revenue bonds to refund certain outstanding bonds and pay the related issuance costs.

In September 2011, the California State University issued \$430 million in revenue bonds to finance or refinance construction projects at various campuses.

In July and September 2011, the Regents of the University of California, a discretely presented component unit, issued \$1.2 billion in general revenue bonds to finance pension contributions to the UCRP and \$400 million to finance and refinance certain facilities and projects of the university.

Between October and November 2011, the State Public Works Board issued \$888 million in lease revenue bonds to finance and refinance the cost of design and/or construction of various projects for the benefit of the Department of Corrections, University of California, Department of Mental Health and others.

In December 2011 and February 2012, the Department of Veteran Affairs issued a total of \$322 million in home purchase revenue bonds.

B. Cash Management

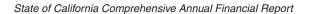
In September 2011, the State issued \$5.4 billion of Revenue Anticipation Notes to assist in cash flow management for the State's 2011-12 fiscal year.

In July 2011, the State Legislature passed Senate Bill 79, which created the State Agency Investment Fund (SAIF), under Government Code section 16330, that allows state agencies to invest a minimum of \$500 million in monies not required by law to be invested in the Pooled Money Investment Account. California State University transferred \$700 million to SAIF in September 2011. The University of California transferred \$1.0 billion in September 2011.

C. Other

California's high demand for unemployment insurance benefits required additional loans from the U.S. Department of Labor during the 2010-11 fiscal year. As of June 30, 2011, the State had \$11.0 billion in outstanding loans from the U.S. Department of Labor that was used to cover deficits in the Unemployment Programs Fund. As of February 24, 2012, the State had an outstanding loan balance of \$10.2 billion, and it expects to request additional loans throughout 2012.

In August 2011, Standard & Poor's lowered its long-term credit rating from AAA to AA+ on debt of the U.S. government, U.S. government sponsored enterprises, and public debt issues that have credit enhancement guarantees by U.S. government sponsored enterprises. These credit downgrades relate to the credit risk associated with investments in U.S. Treasury and U.S. Agency debt securities of the primary government, fiduciary funds, and certain discretely presented component units.



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Required Supplementary Information

Schedule of Funding Progress

(amounts in millions)

Public Employees' Retirement Fund - Primary Government¹

Excess of
Actuarial Value of
Assets Over AAL

				A55	els Over AAL			
Actuarial	Actuarial		Actuarial	(Unfunded			Excess (UAAL) as
Valuation	Value of		Accrued	Actu	arial Accrued	Funded	Covered	a Percentage of
Date	Assets	Lia	ability (AAL)	Lia	bility (UAAL))	Ratio	Payroll	Covered Payroll
	 (a)		(b)		(a - b)	(a / b)	(c)	((a - b) / c)
June 30, 2008	\$ 89,304	\$	107,642	\$	(18,338)	83.0 %	\$ 16,460	(111.4) %
June 30, 2009	93,377		116,827		(23,450)	79.9	16,333	(143.6)
June 30, 2010	97,346		121,446		(24,100)	80.2	16,281	(148.0)

Judges' Retirement Fund

Excess of Actuarial Value of

					Asse	ets Over AAL				
Actuarial	A	ctuarial	A	ctuarial	(l	Jnfunded				Excess (UAAL) as
Valuation	V	alue of	A	ccrued	Actu	arial Accrued	Funded		Covered	a Percentage of
Date		Assets	Liab	oility (AAL)	Liab	oility (UAAL))	Ratio		Payroll	Covered Payroll
		(a)		(b)		(a - b)	(a / b)		(c)	((a - b) / c)
June 30, 2008	\$	19	\$	3,607	\$	(3,588)	0.5	% \$	111	(3,232.4) %
June 30, 2009		41		3,583		(3,542)	1.1		97	(3,651.5)
June 30, 2010		64		3,429		(3,365)	1.9		86	(3,912.8)

Judges' Retirement Fund II

Excess of

Actuarial Value of Assets Over AAL

					Asse	ets Over AAL				
Actuarial	A	Actuarial	A	ctuarial	(U	Infunded				Excess (UAAL) as
Valuation	1	Value of	A	ccrued	Actua	arial Accrued	Funded	(Covered	a Percentage of
Date		Assets	Liab	ility (AAL)	Liab	ility (UAAL))	Ratio		Payroll	Covered Payroll
		(a)		(b)		(a - b)	(a / b)		(c)	((a - b) / c)
June 30, 2008	\$	335	\$	367	\$	(32)	91.3 %	% \$	175	(18.3) %
June 30, 2009		379		451		(72)	84.0		199	(36.2)
June 30, 2010		461		521		(60)	88.5		213	(28.2)

¹ This table reflects the actuarial value of assets; the Comprehensive Annual Financial Report for the fiscal year ended June 30, 2010, reported the market value of assets.

² The Legislators' Retirement Fund (LRF) is funded using the aggregate actuarial cost valuation method. This method does not identify actuarial liabilities and funded ratios. Information about funded status is prepared using the entry age actuarial cost method and is intended to serve as a surrogate for the funding progress of the plan.

³ The trial courts reporting is based on 52 individual biennial actuarial valuations as of July 1, 2009, the latest information available.

Legislators' Retirement Fund²

Excess of
Actuarial Value of
Assets Over AAL

Actuarial Valuation Date	٧	ctuarial /alue of Assets	Α	ctuarial ccrued ility (AAL)	Act	sets Over AAL (Unfunded tuarial Accrued ability (UAAL))	Funded Ratio		Covered Payroll	Excess (UAAL) as a Percentage of Covered Payroll
		(a)		(b)		(a - b)	(a / b)		(c)	((a - b) / c)
June 30, 2008	\$	142	\$	103	\$	39	137.9	% \$	2	1,950.0 %
June 30, 2009		134		112		22	119.6		2	1,100.0
June 30, 2010		127		112		15	113.4		2	750.0

State Teachers' Retirement Defined Benefit Program

Excess of

Actuarial Value of

			Assets Over AAL			
Actuarial	Actuarial	Actuarial	(Unfunded			Excess (UAAL) as
Valuation	Value of	Accrued	Actuarial Accrued	Funded	Covered	a Percentage of
Date	Assets	Liability (AAL)	Liability (UAAL))	Ratio	Payroll	Covered Payroll
	(a)	(b)	(a - b)	(a / b)	(c)	((a - b) / c)
June 30, 2008	\$ 155,215	\$ 177,734	\$ (22,519)	87.3 %	\$ 27,118	(83.0) %
June 30, 2009	145,142	185,683	(40,541)	78.2	27,327	(148.4)
June 30, 2010	140,291	196,315	(56,024)	71.5	26,275	(213.2)

Other Postemployment Benefit Plan

Excess	of
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Actuarial	Value of

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Assets Over AAL (Unfunded Actuarial Accrued Liability (UAAL)) (a - b)	Funded Ratio (a / b)	Covered Payroll (c)	Excess (UAAL) as a Percentage of Covered Payroll ((a - b) / c)
State substanti	ve plan					
June 30, 2009	\$ —	\$ 51,820	\$ (51,820)	— %	\$ 18,450	(280.9) %
June 30, 2010	5	59,911	(59,906)	0.0	17,540	(341.5)
June 30, 2011	7	62,144	(62,137)	0.0	18,010	(345.0)
Trial Courts ³						
July 1, 2007	_	1,291	(1,291)		989	(130.6)
July 1, 2009	9	1,493	(1,484)	0.6	1,009	(147.0)

Schedule of Funding Progress (continued)

(amounts in millions)

University of California Retiree Health Plan

Actuarial Valuation Date	V	ctuarial alue of Assets (a)	Actuarial Accrued bility (AAL) (b)	Actu Ass (I Actu	Excess of larial Value of lets Over AAL Unfunded larial Accrued bility (UAAL))	Funded Ratio (a / b)		Covered Payroll (c)	Excess (UAAL) as a Percentage of Covered Payroll ((a - b) / c)
July 1, 2008	\$	51	\$ 13,800	\$	(13,749)	0.4	% \$	7,450	(184.6) %
July 1, 2009		77	15,062		(14,985)	0.5		7,853	(190.8)
July 1, 2010		74	16,049		(15,974)	0.5		7,995	(199.8)

Infrastructure Assets Using the Modified Approach

Pursuant to Governmental Accounting Standards Board (GASB) Statement No. 34, the State uses the modified approach to report the cost of its infrastructure assets (state roadways and bridges). Under the modified approach, the State does not report depreciation expense for roads and bridges but capitalizes all costs that add to the capacity and efficiency of State-owned roads and bridges. All maintenance and preservation costs are expensed and not capitalized.

A. Infrastructure Asset Reporting Categories

The infrastructure assets reported in the State's financial statements for the fiscal year ending June 30, 2011, are in the following categories and amounts: state highway infrastructure (completed highway projects) totaling \$61.4 billion, land purchased for highway projects totaling \$12.1 billion, and infrastructure construction-in-progress (uncompleted highway projects) totaling \$6.0 billion.

Donation and Relinquishment: Donation and relinquishment activity affects the inventory of statewide lane miles, land, and/or bridges as adjustments to the infrastructure assets and/or land balance in the State's financial statements. There were no donations for the fiscal year ending June 30, 2011. Relinquishments for the fiscal year ending June 30, 2011, are \$59 million of state highway infrastructure and \$12 million of infrastructure land.

B. Condition Baselines and Assessments

1. Bridges

The State uses the Bridge Health Index—a numerical rating scale from 0 to 100 that uses element-level inspection data—to determine the aggregate condition of its bridges. The inspection data is based on the American Association of State Highway Transportation Officials' (AASHTO) "Commonly Recognized Elements for Bridge Inspection."

From a deterioration standpoint, the Bridge Health Index (BHI) represents the remaining asset value of the bridge. A new bridge that has 100% of its asset value has a BHI of 100. As a bridge deteriorates over time, it loses asset value, as represented by a decline in its BHI. When a deteriorated bridge is repaired, it will regain some (or all) of its asset value and its BHI will increase.

The State's established condition baseline and actual BHI for fiscal years 2008-09 through 2010-11 are shown in the following table.

Ending June 30	Established BHI Baseline*	Actual BHI
2009	80.0	94.1
2010	80.0	94.6
2011	80.0	94.3

The following table provides details on the State's actual BHI as of June 30, 2011.

BHI Description	Bridge Count	Percent	Network BHI
Excellent	6,738	52.26 %	99.9
Good	4,575	35.48	96.3
Acceptable	852	6.61	85.7
Fair	206	1.60	73.5
Poor	138	1.07	62.7
Does not carry traffic	384	2.98	92.3
Total	12,893	100.00 %	

2. Roadways

The State conducts a periodic pavement condition survey, which evaluates ride quality and structural integrity and identifies the number of distressed lane miles. The State classifies its roadways' pavement condition by the following descriptions:

- 1. Excellent/good condition minor or no potholes or cracks.
- 2. Fair condition moderate potholes or cracks.
- Poor condition significant or extensive potholes or cracks.

Statewide lane miles are considered "distressed lane miles" if they are in either fair or poor condition. The actual distressed lane miles are compared to the established condition baseline to ensure that the baseline is not exceeded.

The State's established condition baseline and actual distressed lane miles from the last three complete pavement-condition surveys are shown in the following table.

Condition Assessment Date ¹	Established Condition Baseline Distressed Lane Miles (maximum) ²	Actual Distressed Lane Miles	Actual Distressed Lane Miles as Percent of Total Lane Miles
December 2006	18,000	13,845	27.9 %
March 2008	18,000	12,998	26.3
December 2011 ³	18,000	12,333	24.9

¹ Condition assessment for the State's established condition baseline and actual distressed lane miles is being reported as of the *State of the Pavement* report publication date.

The following table provides details on the State's actual distressed lane miles as of the last complete pavement- condition survey.

Pavement Condition	Lane Miles	Distressed Lane Miles
Excellent/Good	37,185	_
Fair	2,486	2,486
Poor	9,847	9,847
Total	49,518	12,333

C. Budgeted and Actual Preservation Costs

The estimated budgeted preservation costs represent the preservation projects approved by the California Transportation Commission and the State's scheduled preservation work for each fiscal year. The actual preservation costs represent the cumulative cost to date for the projects approved and work scheduled in each fiscal year. Prior to the 2008-09 fiscal year, the State excluded the annual expenditures for one of its bridges from preservation costs. Beginning in the 2008-09 fiscal year, the State included the expenditures for the bridge in both budgeted and actual preservation costs and restated the costs for previous years.

The State's budgeted and actual preservation cost information for the most recent and four previous fiscal years is shown in the following table.

Fiscal Year Ending June 30	Estimated Budgeted Preservation Costs (in millions)	Actual Preservation Costs (in millions)
2007	\$ 2,694	\$ 2,249
2008	2,956	1,871
2009	2,910	1,557
2010	2,162	640
2011	2,802	368

² The actual statewide distressed lane miles should not exceed the maximum distressed lane miles established by the State.

³ The State's compliance with GASB 34, which requires a road condition assessment every three years, temporarily lapsed in March 2011. A survey was completed in December 2011 and the State will continue to use the modified approach for roadways.

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Budgetary Comparison Schedule General Fund and Major Special Revenue Funds

Year Ended June 30, 2011 (amounts in thousands)

Part Part		General							
REVENUES		Budgeted Amounts			Actual		Variance With		
Corporation tax			Original		Final		Amounts	Fi	nal Budget
Intergovernmental	REVENUES								
Cigarette and tobacco taxes 93,000 93,000 96,097 3,097 Inheritance, estate, and gift taxes	Corporation tax	\$	11,509,000	\$	9,408,000	\$	9,613,595	\$	205,595
Inheritance, estate, and gift taxes	Intergovernmental		_		_		_		_
Insurance gross premiums tax	Cigarette and tobacco taxes		93,000		93,000		96,097		3,097
Vehicle license fees 1,506,311 1,393,311 1,366,483 (26,828) Motor vehicle fuel tax — — — — Personal income tax 47,784,000 51,945,000 49,602,618 (2,342,382) Retail sales and use taxes 26,709,000 26,740,000 26,975,503 235,503 Other major taxes and licenses 319,521 319,221 335,335 16,114 Other revenues 3,025,931 3,025,931 2,066,515 (959,416) Total revenues 92,784,763 94,940,663 92,133,034 (2,807,429) EXPENDITURES State and consumer services 609,074 590,600 556,654 33,946 Business and transportation 494,065 493,790 493,679 111 Resources 1,223,899 1,177,651 1,067,318 110,333 Health and human services 28,966,812 29,075,611 26,772,957 2,302,654 Correctional programs 8,655,888 9,567,358 9,468,499 98,859 Education 45,079,575 <t< td=""><td>Inheritance, estate, and gift taxes</td><td></td><td>_</td><td></td><td>_</td><td></td><td>_</td><td></td><td>_</td></t<>	Inheritance, estate, and gift taxes		_		_		_		_
Motor vehicle fuel tax — — — — — — — — Personal income tax 47,784,000 51,945,000 49,602,618 (2,342,382) 235,033 235,503 235,503 235,503 205,975,503 235,503 201,114 Other major taxes and licenses 319,521 319,221 335,335 16,114 Other revenues 319,521 319,221 335,335 16,114 Other service 609,074 50,000 50,651 49,4069 92,133,034 (2,807,429) 111 Resources 609,074 509,600 556,654 33,946 80,200 11,17,651 1,067,318 110,333 110,333 110,333 110,333 11,067,318 110,333 110,3	Insurance gross premiums tax		1,838,000		2,016,000		2,076,888		60,888
Personal income tax 47,784,000 51,945,000 49,602,618 (2,342,382) Retail sales and use taxes 26,709,000 26,740,000 26,975,503 235,503 Other major taxes and licenses 319,521 319,221 335,335 16,114 Other revenues 3,025,931 3,025,931 2,066,515 (959,416) Total revenues 92,784,763 94,940,463 92,133,034 (2,807,429) EXPENDITURES State and consumer services 609,074 590,600 556,654 33,946 Business and transportation 494,065 493,790 493,679 111 Resources 1,223,899 1,177,651 1,067,318 110,333 Health and human services 28,966,812 29,075,611 26,772,957 2,302,654 Correctional programs 8,665,888 9,567,358 9,468,499 98,859 Education 45,079,575 43,767,239 43,749,141 18,098 General government: 345,653 534,802 529,050 5,752 Debt service	Vehicle license fees		1,506,311		1,393,311		1,366,483		(26,828)
Retail sales and use taxes 26,709,000 26,740,000 26,975,503 235,503 Other major taxes and licenses 319,521 319,221 335,335 16,114 Other revenues 3,025,931 3,025,931 2,066,515 (959,416) Total revenues 92,784,763 94,940,463 92,133,034 (2,807,429) EXPENDITURES State and consumer services 609,074 590,600 556,654 33,946 Business and transportation 494,065 493,790 493,679 111 Resources 1,223,899 1,177,651 1,067,318 110,333 Health and human services 28,966,812 29,075,611 26,772,957 2,302,654 Correctional programs 8,665,888 9,567,358 9,488,499 98,859 Education 45,079,575 43,767,239 43,749,141 18,098 General government: Tax relief 445,653 534,802 529,050 5,752 Debt service 5,013,571 5,018,950 4,940,066 78,884 Other general government	Motor vehicle fuel tax		_		_		_		_
Other major taxes and licenses 319,521 319,221 335,335 16,114 Other revenues 3,025,931 3,025,931 2,066,515 (959,416) Total revenues 92,784,763 94,940,463 92,133,034 (2,807,429) EXPENDITURES State and consumer services 609,074 590,600 556,654 33,946 Business and transportation 494,065 493,790 493,679 111 Resources 1,223,899 1,177,651 1,067,318 110,333 Health and human services 2,866,812 29,075,611 26,772,957 2,302,654 Correctional programs 8,665,888 9,567,358 9,468,499 98,859 Education 45,079,575 43,767,239 43,749,141 18,098 General government: Tax relief 445,653 534,802 529,050 5,752 Debt service 5,013,571 5,018,950 4,940,066 78,884 Other general government 4,832,602 4,839,151 4,278,636 560,515 Total expenditures 9	Personal income tax		47,784,000		51,945,000		49,602,618		(2,342,382)
Other revenues 3,025,931 3,025,931 2,066,515 (959,416) Total revenues 92,784,763 94,940,463 92,133,034 (2,807,429) EXPENDITURES State and consumer services 609,074 590,600 556,654 33,946 Business and transportation 494,065 493,790 493,679 111 Resources 1,223,899 1,177,651 1,067,318 110,333 Health and human services 28,966,812 29,075,611 26,772,957 2,302,654 Correctional programs 8,665,888 9,567,358 9,468,499 98,859 Education 45,079,575 43,767,239 43,749,141 18,098 General government: Tax relief 445,653 534,802 529,050 5,752 Debt service 5,013,571 5,018,950 4,940,066 78,884 Other general government 4,832,602 4,839,151 4,278,636 560,515 Total expenditures 95,331,139 95,065,152 91,856,000 3,209,152 OTHER	Retail sales and use taxes		26,709,000		26,740,000		26,975,503		235,503
Total revenues 92,784,763 94,940,463 92,133,034 (2,807,429) EXPENDITURES State and consumer services 609,074 590,600 556,654 33,946 Business and transportation 494,065 493,790 493,679 111 Resources 1,223,899 1,177,651 1,067,318 110,333 Health and human services 28,966,812 29,075,611 26,772,957 2,302,654 Correctional programs 8,665,888 9,567,358 9,468,499 98,859 Education 45,079,575 43,767,239 43,749,141 18,098 General government: 445,653 534,802 529,050 5,752 Debt service 5,013,571 5,018,950 4,940,066 78,884 Other general government 4,832,602 4,839,151 4,278,636 560,515 Total expenditures 95,331,139 95,065,152 91,856,000 3,209,152 OTHER FINANCING SOURCES (USES) — — 1,661,966 — Transfers from other funds —	Other major taxes and licenses		319,521		319,221		335,335		16,114
State and consumer services 609,074 590,600 556,654 33,946	Other revenues		3,025,931		3,025,931		2,066,515		(959,416)
State and consumer services 609,074 590,600 556,654 33,946 Business and transportation 494,065 493,790 493,679 111 Resources 1,223,899 1,177,651 1,067,318 110,333 Health and human services 28,966,812 29,075,611 26,772,957 2,302,654 Correctional programs 8,665,888 9,567,358 9,468,499 98,859 Education 45,079,575 43,767,239 43,749,141 18,098 General government: Tax relief 445,653 534,802 529,050 5,752 Debt service 5,013,571 5,018,950 4,940,066 78,884 Other general government 4,832,602 4,839,151 4,278,636 560,515 Total expenditures 95,331,139 95,065,152 91,856,000 3,209,152 OTHER FINANCING SOURCES (USES) — — 1,661,966 — Transfers from other funds — — — (401,614) — Other additions and deductions — — <td>Total revenues</td> <td></td> <td>92,784,763</td> <td></td> <td>94,940,463</td> <td></td> <td>92,133,034</td> <td></td> <td>(2,807,429)</td>	Total revenues		92,784,763		94,940,463		92,133,034		(2,807,429)
Business and transportation 494,065 493,790 493,679 111 Resources 1,223,899 1,177,651 1,067,318 110,333 Health and human services 28,966,812 29,075,611 26,772,957 2,302,654 Correctional programs 8,665,888 9,567,358 9,468,499 98,859 Education 45,079,575 43,767,239 43,749,141 18,098 General government: Tax relief 445,653 534,802 529,050 5,752 Debt service 5,013,571 5,018,950 4,940,066 78,884 Other general government 4,832,602 4,839,151 4,278,636 560,515 Total expenditures 95,331,139 95,065,152 91,856,000 3,209,152 OTHER FINANCING SOURCES (USES) — — 1,661,966 — Transfers from other funds — — 1,661,966 — Transfers to other funds — — 618,745 — Total other financing sources (uses) — — 1,879,097	EXPENDITURES								
Resources 1,223,899 1,177,651 1,067,318 110,333 Health and human services 28,966,812 29,075,611 26,772,957 2,302,654 Correctional programs 8,665,888 9,567,358 9,468,499 98,859 Education 45,079,575 43,767,239 43,749,141 18,098 General government: Tax relief 445,653 534,802 529,050 5,752 Debt service 5,013,571 5,018,950 4,940,066 78,884 Other general government 4,832,602 4,839,151 4,278,636 560,515 Total expenditures 95,331,139 95,065,152 91,856,000 3,209,152 OTHER FINANCING SOURCES (USES) — — 1,661,966 — Transfers from other funds — — (401,614) — Other additions and deductions — — 1,879,097 — Excess (deficency) of revenues and other sources — — 2,156,131 — Fund balances, July 1, 2010 — — —	State and consumer services		609,074		590,600		556,654		33,946
Health and human services 28,966,812 29,075,611 26,772,957 2,302,654 Correctional programs 8,665,888 9,567,358 9,468,499 98,859 Education 45,079,575 43,767,239 43,749,141 18,098 General government: Tax relief 445,653 534,802 529,050 5,752 Debt service 5,013,571 5,018,950 4,940,066 78,884 Other general government 4,832,602 4,839,151 4,278,636 560,515 Total expenditures 95,331,139 95,065,152 91,856,000 3,209,152 OTHER FINANCING SOURCES (USES) Transfers from other funds — — 1,661,966 — Transfers to other funds — — (401,614) — Other additions and deductions — — 618,745 — Total other financing sources (uses) — — 1,879,097 — Excess (deficency) of revenues and other sources — — 2,156,131 — Fund balances, Jul	Business and transportation		494,065		493,790		493,679		111
Correctional programs 8,665,888 9,567,358 9,468,499 98,859 Education 45,079,575 43,767,239 43,749,141 18,098 General government: Tax relief 445,653 534,802 529,050 5,752 Debt service 5,013,571 5,018,950 4,940,066 78,884 Other general government 4,832,602 4,839,151 4,278,636 560,515 Total expenditures 95,331,139 95,065,152 91,856,000 3,209,152 OTHER FINANCING SOURCES (USES) Transfers from other funds - - 1,661,966 - Transfers from other funds - - (401,614) - Other additions and deductions - - 618,745 - Total other financing sources (uses) - - 1,879,097 - Excess (deficency) of revenues and other sources - - 2,156,131 - Fund balances, July 1, 2010 - - - (4,478,542) -	Resources		1,223,899		1,177,651		1,067,318		110,333
Education 45,079,575 43,767,239 43,749,141 18,098 General government: Tax relief 445,653 534,802 529,050 5,752 Debt service 5,013,571 5,018,950 4,940,066 78,884 Other general government 4,832,602 4,839,151 4,278,636 560,515 Total expenditures 95,331,139 95,065,152 91,856,000 3,209,152 OTHER FINANCING SOURCES (USES) Transfers from other funds — — — 1,661,966 — Transfers from other funds — <t< td=""><td>Health and human services</td><td></td><td>28,966,812</td><td></td><td>29,075,611</td><td></td><td>26,772,957</td><td></td><td>2,302,654</td></t<>	Health and human services		28,966,812		29,075,611		26,772,957		2,302,654
General government: Tax relief 445,653 534,802 529,050 5,752 Debt service 5,013,571 5,018,950 4,940,066 78,884 Other general government 4,832,602 4,839,151 4,278,636 560,515 Total expenditures 95,331,139 95,065,152 91,856,000 3,209,152 OTHER FINANCING SOURCES (USES) Transfers from other funds — — 1,661,966 — Transfers to other funds — — (401,614) — Other additions and deductions — — 618,745 — Total other financing sources (uses) — — 1,879,097 — Excess (deficency) of revenues and other sources over (under) expenditures and other uses — — 2,156,131 — Fund balances, July 1, 2010 — — — (4,478,542) —	Correctional programs		8,665,888		9,567,358		9,468,499		98,859
Tax relief 445,653 534,802 529,050 5,752 Debt service 5,013,571 5,018,950 4,940,066 78,884 Other general government 4,832,602 4,839,151 4,278,636 560,515 Total expenditures 95,331,139 95,065,152 91,856,000 3,209,152 OTHER FINANCING SOURCES (USES) Transfers from other funds — — 1,661,966 — Transfers to other funds — — (401,614) — Other additions and deductions — — 618,745 — Total other financing sources (uses) — — 1,879,097 — Excess (deficency) of revenues and other sources over (under) expenditures and other uses — — 2,156,131 — Fund balances, July 1, 2010 — — — (4,478,542) —	Education		45,079,575		43,767,239		43,749,141		18,098
Debt service 5,013,571 5,018,950 4,940,066 78,884 Other general government 4,832,602 4,839,151 4,278,636 560,515 Total expenditures 95,331,139 95,065,152 91,856,000 3,209,152 OTHER FINANCING SOURCES (USES) — — 1,661,966 — Transfers from other funds — — (401,614) — Other additions and deductions — — 618,745 — Total other financing sources (uses) — — 1,879,097 — Excess (deficency) of revenues and other sources over (under) expenditures and other uses — — 2,156,131 — Fund balances, July 1, 2010 — — (4,478,542) — —	General government:								
Other general government 4,832,602 4,839,151 4,278,636 560,515 Total expenditures 95,331,139 95,065,152 91,856,000 3,209,152 OTHER FINANCING SOURCES (USES) Transfers from other funds — — 1,661,966 — Transfers to other funds — — (401,614) — Other additions and deductions — — 618,745 — Total other financing sources (uses) — — 1,879,097 — Excess (deficency) of revenues and other sources over (under) expenditures and other uses — — 2,156,131 — Fund balances, July 1, 2010 — — — (4,478,542) —	Tax relief		445,653		534,802		529,050		5,752
Total expenditures 95,331,139 95,065,152 91,856,000 3,209,152 OTHER FINANCING SOURCES (USES) — — 1,661,966 — Transfers from other funds — — (401,614) — Other additions and deductions — — 618,745 — Total other financing sources (uses) — — 1,879,097 — Excess (deficency) of revenues and other sources over (under) expenditures and other uses — — 2,156,131 — Fund balances, July 1, 2010 — — (4,478,542) —	Debt service		5,013,571		5,018,950		4,940,066		78,884
OTHER FINANCING SOURCES (USES) Transfers from other funds — — 1,661,966 — Transfers to other funds — — (401,614) — Other additions and deductions — — 618,745 — Total other financing sources (uses) — — 1,879,097 — Excess (deficency) of revenues and other sources over (under) expenditures and other uses — — 2,156,131 — Fund balances, July 1, 2010 — — (4,478,542) —	Other general government		4,832,602		4,839,151		4,278,636		560,515
Transfers from other funds — — 1,661,966 — Transfers to other funds — — (401,614) — Other additions and deductions — — 618,745 — Total other financing sources (uses) — — 1,879,097 — Excess (deficency) of revenues and other sources — — 2,156,131 — Fund balances, July 1, 2010 — — (4,478,542) —	Total expenditures		95,331,139		95,065,152		91,856,000		3,209,152
Transfers to other funds — — (401,614) — Other additions and deductions — — 618,745 — Total other financing sources (uses) — — 1,879,097 — Excess (deficency) of revenues and other sources — — 2,156,131 — over (under) expenditures and other uses — — — (4,478,542) — Fund balances, July 1, 2010 — — — (4,478,542) —	OTHER FINANCING SOURCES (USES)								
Other additions and deductions — — 618,745 — Total other financing sources (uses) — — 1,879,097 — Excess (deficency) of revenues and other sources over (under) expenditures and other uses — — 2,156,131 — Fund balances, July 1, 2010 — — (4,478,542) —	Transfers from other funds		_		_		1,661,966		_
Total other financing sources (uses) — — 1,879,097 — Excess (deficency) of revenues and other sources over (under) expenditures and other uses — — 2,156,131 — Fund balances, July 1, 2010 — — (4,478,542) —	Transfers to other funds		_		_		(401,614)		_
Excess (deficency) of revenues and other sources over (under) expenditures and other uses	Other additions and deductions						618,745		
over (under) expenditures and other uses — — 2,156,131 — Fund balances, July 1, 2010 — — (4,478,542) —	Total other financing sources (uses)				_		1,879,097		
Fund balances, July 1, 2010	Excess (deficency) of revenues and other sources								
	,		_		_		2,156,131		_
Fund balances, June 30, 2011	Fund balances, July 1, 2010						(4,478,542)		
	Fund balances, June 30, 2011	\$		\$		\$	(2,322,411)	\$	

	Fed	deral			Transp	sportation		
Budgeted	I Amounts	Actual	Variance With	Budgeted	l Amounts	Actual	Variance With	
Original	Final	Amounts	Final Budget	Original	Final	Amounts	Final Budget	
\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ _	
61,973,830	61,973,830	61,973,830	_	_	_	_	_	
_	_	_	_	_	_	_	_	
_	_	_	_	_	_	_	_	
_	_	_	_	_	_	_	_	
_	_	_	_	-		_	_	
_	_	_	_	4,984,050	5,734,941	5,705,528	(29,413)	
_	_	_	_	_	_	_	_	
_	_	_	_	3,291,704	— 3,259,541	3,241,182	(18,359)	
68	— 68	— 52	(16)	413,872	399,743	376,606	(23,137)	
61,973,898	61,973,898	61,973,882	(16)	8,689,626	9,394,225	9,323,316	(70,909)	
07.500	07.500	07.500		110.007	100 150	00.055	15.005	
37,509	37,509	37,509	_	116,267	109,150	93,255	15,895	
4,153,312 402,594	4,153,312 402,594	4,153,312 402,594	_	11,866,738 388,811	8,244,956 132,298	7,229,602 131,540	1,015,354 758	
402,594	402,394	402,394		3,242	3,171	2,788	383	
8,778	8,778	8,778		5,242	5,171	2,700	- Jos	
7,167,425	7,167,425	7,167,425		2,543	2,492	2,154	338	
7,107,120	7,107,120	7,107,120		2,010	2, 102	2,101	000	
_	_	_		_	_	_	_	
_	_	_		1,000	1,000	46	954	
2,737,481	2,737,481	2,737,481	_	1,902,074	1,900,363	1,888,762	11,601	
54,884,920	54,884,920	54,884,920	_	14,280,675	10,393,430	9,348,147	1,045,283	
_	_	20,576,858	_	_	_	10,909,792	_	
_	_	(27,643,483)	_	_	_	(12,365,008)	_	
_	_	(22,285)	_	_	_	257,128	_	
		(7,088,910)				(1,198,088)		
_	_	52	_	_	_	(1,222,919)	_	
		10,559				28,224,297		
<u> </u>	\$	\$ 10,611	\$	\$ <u>—</u>	<u> </u>	\$ 27,001,378	\$ <u>—</u>	

Reconciliation of Budgetary Basis Fund Balances of the General Fund and the Major Special Revenue Funds to GAAP Basis Fund Balances

June 30, 2011 (amounts in thousands)

(amounts in trousands)		 Special Rev	enue	Funds
	 General	 Federal	T	ransportation
Budgetary fund balance reclassified into				
GAAP statement fund structure	\$ (2,322,411)	\$ 10,611	\$	27,001,378
Basis difference:				
Interfund receivables	47,304	_		2,447,657
Loans receivable	159,845	124,879		_
Interfund payables	(4,112,570)	_		_
Escheat property	(975,577)	_		_
Bonds authorized but unissued		_		(21,272,381)
Tax revenues	682,100			_
GASB 54 classification changes	122,719	2,482		
Other	1,419			(253,697)
Timing difference:				
Liabilities budgeted in subsequent years	 (13,542,070)	 (16,418)		(155,725)
GAAP fund balance (deficit), June 30, 2011	\$ (19,939,241)	\$ 121,554	\$	7,767,232

Notes to the Required Supplementary Information

Budgetary Comparison Schedule

The State annually reports its financial condition based on a Generally Accepted Accounting Principles (GAAP) basis and on the State's budgetary provisions (budgetary basis). The Budgetary Comparison Schedule, General Fund and Major Special Revenue Funds reports the original budget, the final budget, the actual expenditures, and the variance between the final budget and the actual expenditures, using the budgetary basis of accounting.

On a budgetary basis, individual appropriations are charged as expenditures when commitments for goods and services are incurred. However, for financial reporting purposes, the State reports expenditures based on the year in which goods and services are received. The Budgetary Comparison Schedule includes all of the current-year expenditures for the General Fund and major special revenue funds as well as their related appropriations that are legislatively authorized annually, continually, or by project. On a budgetary basis, adjustments for encumbrances are budgeted under other general government, while the encumbrances relate to all programs' expenditures.

The Budgetary Comparison Schedule is not presented in this document at the legal level of budgetary control because such a presentation would be extremely lengthy and cumbersome. The State of California prepares a separate report, the *Comprehensive Annual Financial Report Supplement*, which includes statements that demonstrate compliance with the legal level of budgetary control in accordance with GASB's *Codification of Governmental Accounting and Financial Reporting Standards*, Section 2400.121. This report includes the comparison of the annual appropriated budget with expenditures at the legal level of control. A copy of the *Comprehensive Annual Financial Report Supplement* is available upon request from the State Controller's Office, Division of Accounting and Reporting, P.O. Box 942850, Sacramento, California 94250-5872.

Reconciliaton of Budgetary Basis With GAAP Basis

The reconciliation of Budgetary Basis fund balances of the General Fund and the major special revenue funds to GAAP Basis fund balances are presented on the previous page and are explained in the following paragraphs.

The beginning fund balances for the General Fund, Federal Fund, and Transportation Fund on the budgetary basis are restated for prior-year revenue adjustments and prior-year expenditure adjustments. A prior-year revenue adjustment occurs when the actual amount received in the current year differs from the amount of revenue accrued in the prior year. A prior-year expenditure adjustment results when the actual amount paid in the current year differs from the prior-year accrual for appropriations whose ability to encumber funds has lapsed in previous periods. The beginning fund balance on a GAAP basis is not affected by these adjustments.

Basis Difference

Interfund Receivables and Loans Receivable: Loans made to other funds or to other governments are normally recorded as either expenditures or transfers on the budgetary basis. However, in accordance with GAAP, these loans are recorded as assets. The adjustments related to interfund receivables caused a \$47 million increase to the fund balance in the General Fund and a \$2.4 billion increase to the fund balance in the Transportation Fund. The adjustments related to loans receivable caused increases of \$160 million in the General Fund and \$125 million in the Federal Fund.

Interfund Payables: Loans received from other funds or from other governments are normally recorded as either revenues or transfers on a budgetary basis. However, in accordance with GAAP, these loans are recorded as liabilities. The adjustments related to interfund payables caused a \$4.1 billion decrease to the budgetary fund balance in the General Fund.

Escheat Property: A liability for the estimated amount of escheat property expected to ultimately be reclaimed and paid is not reported on a budgetary basis. The liability is required to be reported on a GAAP basis. This adjustment caused a \$975 million decrease to the General Fund balance.

Bonds Authorized but Unissued: In the year that general obligation bonds are authorized by the voters, the full amount authorized is recognized as revenue on a budgetary basis. In accordance with GAAP, only the amount of bonds issued each year is reported as an other financing source. The adjustments related to bonds authorized but unissued caused a \$21.3 billion decrease to the fund balance in the Transportation Fund.

Tax Revenues: Estimated tax payments are accrued on a budgetary basis pursuant to Chapter 751, Statutes of 2008. However, in accordance with GAAP, tax payments are accrued based on the portion of estimated net final payments related to the fiscal year. This adjustment caused a fund balance increase of \$682 million in the General Fund.

GASB Statement No. 54 Classification Changes: The fund balance amounts for governmental funds have been reclassified in accordance with GASB Statement No. 54. Additional information on GASB 54 can be found in Note 1, Summary of Significant Accounting Policies, Section K. These reclassifications caused fund balance increases of \$123 million in the General Fund and \$2 million in the Federal Fund. The \$123 million of fund balance is not considered part of the General Fund for any budgetary purposes or for the Budgetary/Legal Basis Annual Report.

Other: Certain other adjustments and reclassifications are necessary in order to present the financial statements in accordance with GAAP. The other adjustments caused a fund balance increase of \$1 million in the General Fund and a fund balance decrease of \$254 million in the Transportation Fund.

Timing Difference

Liabilities Budgeted in Subsequent Years: On a budgetary basis, the primary government does not accrue liabilities for which there is no existing appropriation or no currently available appropriation. The adjustments made to account for these liabilities in accordance with GAAP caused fund balance decreases of \$13.5 billion in the General Fund, a fund balance decrease of \$16 million in the Federal Fund, and a fund balance decrease of \$156 million in the Transportation Fund. The large decrease in the General Fund primarily consists of \$7.5 billion for deferred apportionment payments to K-12 schools and community colleges, \$2.6 billion in tax overpayments, \$1.3 billion for medical assistance, \$813 million for June 2011 payroll that was deferred to July 2011, and \$418 million for pension contributions.

We conducted this audit to comply with Section 8546.4 of the California Government Code. The Independent Auditor's Report provides the opinions we expressed on the State of California's basic financial statements.

Respectfully submitted,

ELAINE M. HOWLE, CPA

State Auditor

Date: March 23, 2012

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laine M. Howle

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For questions regarding the contents of this report, please contact Margarita Fernández, Chief of Public Affairs, at (916) 445-0255.

Part Two

State of California Internal Control and State and Federal Compliance Audit Report for the Year Ended June 30, 2011

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AUDITOR'S SECTION

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Independent Auditor's Reports on Internal Control and on Compliance and Other Matters

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Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With Government Auditing Standards

The Governor and the Legislature of the State of California

We have audited the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of California as of and for the year ended June 30, 2011, which collectively comprise the State of California's basic financial statements, and have issued our report thereon dated February 24, 2012. Our report includes a reference to other auditors. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. As described in our report on the State of California's financial statements, other auditors audited the financial statements of the following:

Government-wide Financial Statements

- Certain enterprise funds that, in the aggregate, represent 86 percent and 36 percent, respectively, of the assets and revenues of the business-type activities.
- The University of California, State Compensation Insurance Fund, California Housing Finance Agency, Public Employees' Benefits, and certain other funds that, in the aggregate, represent over 99 percent of the assets and revenues of the discretely presented component units.

Fund Financial Statements

- The following major enterprise funds: Electric Power fund, Water Resources fund, Public Building Construction fund, State Lottery fund, and California State University fund.
- Certain nonmajor enterprise funds that represent 92 percent and 66 percent, respectively, of the assets and revenues of the nonmajor enterprise funds.
- The funds of the Public Employees' Retirement System and the State Teachers' Retirement System, and certain other funds that, in the aggregate, represent 90 percent and 76 percent, respectively, of the assets and additions of the fiduciary funds and similar component units.
- The discretely presented component units noted above.

This report does not include the results of the other auditors' testing of internal control over financial reporting or compliance and other matters that are reported on separately by those auditors.

Internal Control Over Financial Reporting

Management of the State of California is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the State of California's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but

not for the purpose of expressing an opinion on the effectiveness of the State of California's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the State of California's internal control over financial reporting.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting, items 2011-15-1 through 2011-15-4, described in the accompanying schedule of findings and questioned costs that we consider to be significant deficiencies in internal control over financial reporting. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the State of California's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters, items 2011-15-5 and 2011-15-6, as described in the accompanying section on internal control and compliance issues applicable to the financial statements and state requirements, that are required to be reported under *Government Auditing Standards*.

The State of California's responses to the findings identified in our audit are described in the accompanying section on internal control and compliance issues applicable to the financial statements and state requirements. We did not audit the State of California's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the governor and the Legislature of the State of California, the management of the executive branch, and the federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

CALIFORNIA STATE AUDITOR

John F. Collins I

JOHN F. COLLINS II, CPA Deputy State Auditor

February 24, 2012

Independent Auditor's Report on Compliance With Requirements That Could Have a Direct and Material Effect on Each Major Program and on Internal Control Over Compliance in Accordance With OMB Circular A-133

The Governor and the Legislature of the State of California

Compliance

We have audited the compliance of the State of California with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2011. The State of California's major federal programs are identified in the summary of the auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the State of California's management. Our responsibility is to express an opinion on the State of California's compliance based on our audit. We did not audit the State of California's compliance with the requirements of the U.S. Environmental Protection Agency's Capitalization Grants for Clean Water State Revolving Funds (CFDA Number 66.458) and the Capitalization Grants for Drinking Water State Revolving Funds (CFDA Number 66.468). These programs account for less than 1 percent of the total federal assistance received by the State of California and are included in the accompanying schedule of expenditures of federal awards. Other auditors have audited the State of California's compliance with these programs' requirements and their reports thereon have been furnished to us. Our opinion, insofar as it relates to these programs, is based solely on the report of the other auditors.

The State of California's basic financial statements include the operations of the University of California and the California State University systems, as well as the California Housing Finance Agency, a component unit of the State. However, these entities are not included in the accompanying schedule of findings and questioned costs for the year ended June 30, 2011. Further, they are generally not included in the schedule of expenditures of federal awards, except for \$213 million passed through to the University of California and the California State University systems through the State Fiscal Stabilization Fund—Education State Grants, Recovery Act (CFDA Number 84.394). The University of California and the California State University systems, and the California Housing Finance Agency, which reported expenditures of federal awards totaling \$4.4 billion, \$2.3 billion, and \$76.4 million, respectively, engaged other auditors to perform an audit in accordance with OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations* (OMB Circular A-133).

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the State of California's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit and the reports of the other auditors provide a reasonable basis for our opinion. Our audit does not provide a legal determination of the State of California's compliance with those requirements.

As described in the Table and in the accompanying schedule of findings and questioned costs, the State of California did not comply with requirements that are applicable to certain major federal programs:

Table

COMPLIANCE REQUIREMENT(S)	FINDING NUMBER	FEDERAL DEPARTMENT	PROGRAM	CATALOG OF FEDERAL DOMESTIC ASSISTANCE NUMBER
Activities Allowe	d/Allowable Co	sts		
	2011-1-1 and 2011-1-2	Health and Human Services	Medicaid Cluster: State Medicaid Fraud Control Units State Survey and Certification of Health Care Providers and Suppliers Medical Assistance Program	93.775 93.777 93.778
Eligibility				
	2011-5-1	Health and Human Services	HIV Care Formula Grants	93.917
	2011-5-2	Health and Human Services	Medicaid Cluster: State Medicaid Fraud Control Units State Survey and Certification of Health Care Providers	93.775
			and Suppliers Medical Assistance Program	93.777 93.778
Subrecipient Mo	nitoring			
	2011-13-9	Education	Career and Technical Education - Basic Grants to States (Perkins IV)	84.048
	2011-13-10	Education	School Improvement Grants Cluster: School Improvement Grants School Improvement Grants, Recovery Act Funded	84.377 84.388
Special Tests and	Provisions—Pi	rovider Eligibility	· · · · · · · · · · · · · · · · · · ·	
	2011-14-3	Health and Human Services	Medicaid Cluster: State Medicaid Fraud Control Units State Survey and Certification of Health Care Providers	93.775
			and Suppliers Medical Assistance Program	93.777 93.778

Compliance with such requirements is necessary, in our opinion, for the State of California to comply with the requirements applicable to those programs.

In our opinion, except for the noncompliance described in the Table, the State of California complied, in all material respects, with the requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2011. The results of our auditing procedures also disclosed other instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items:

2011-2-1, 2011-3-1, 2011-4-1, 2011-5-4, 2011-5-5, 2011-5-6, 2011-7-5, 2011-7-8, 2011-12-2, 2011-12-3, 2011-12-4, 2011-12-5, 2011-12-7, 2011-13-1, 2011-13-2, 2011-13-3, 2011-13-4, 2011-13-5, 2011-13-7, 2011-13-11, 2011-13-12, 2011-13-14, 2011-13-16, 2011-14-1, 2011-14-2, 2011-14-4, 2011-14-5, 2011-14-6, and 2011-14-7.

Internal Control Over Compliance

The management of the State of California is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the State of California's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the State of California's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in the State of California's internal control over compliance that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items 2011-1-1, 2011-1-2, 2011-3-2, 2011-5-1, 2011-5-2, 2011-5-6, 2011-7-5, 2011-7-7, 2011-13-4, 2011-13-9, 2011-13-10, 2011-13-14, 2011-13-17, 2011-14-3, 2011-14-4, 2011-14-5, 2011-14-6, and 2011-14-7 to be material weaknesses.

A significant deficiency in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items 2011-1-5, 2011-2-1, 2011-2-2, 2011-3-1, 2011-4-1, 2011-5-3, 2011-5-4, 2011-5-5, 2011-7-1, 2011-7-2, 2011-7-8, 2011-12-2, 2011-12-3, 2011-12-5, 2011-12-7, 2011-13-1, 2011-13-2, 2011-13-3, 2011-13-6, 2011-13-6, 2011-13-7, 2011-13-8, 2011-13-11, 2011-13-12, 2011-13-16, 2011-14-1, and 2011-14-2 to be significant deficiencies.

The State of California's responses to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. We did not audit the State of California's responses and, accordingly, we express no opinion on them.

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

We have audited the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the State of California, as of and for the year ended June 30, 2011, and have issued our report thereon dated February 24, 2012. We did not audit the following significant amounts in the financial statements of:

Government-wide Financial Statements

- Certain enterprise funds that, in the aggregate, represent 86 percent and 36 percent, respectively, of the assets and revenues of the business-type activities.
- The University of California, State Compensation Insurance Fund, California Housing Finance Agency, Public Employees' Benefits, and certain other funds that, in the aggregate, represent over 99 percent of the assets and revenues of the discretely presented component units.

Fund Financial Statements

- The following major enterprise funds: Electric Power fund, Water Resources fund, Public Building Construction fund, State Lottery fund, and California State University fund.
- Certain nonmajor enterprise funds that represent 92 percent and 66 percent, respectively, of the assets and revenues of the nonmajor enterprise funds.

- The funds of the Public Employees' Retirement System and the State Teachers' Retirement System that, in the aggregate, represent 90 percent and 76 percent, respectively, of the assets and additions of the fiduciary funds and similar component units.
- The discretely presented component units noted above.

Those financial statements were audited by other auditors whose reports have been furnished to us, and our opinions, insofar as they relate to the amounts included for those funds and entities, are based on the reports of the other auditors. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States of America.

Our audit was performed for the purpose of forming our opinions on the financial statements that collectively comprise the State of California's basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Except for \$213 million passed through to the University of California and the California State University systems from the State Fiscal Stabilization Fund—Education State Grants, Recovery Act (CFDA Number 84.394), the schedule of expenditures of federal awards generally does not include federal awards expended by these systems, and the California Housing Finance Agency. These expenditures are audited by other independent auditors in accordance with OMB Circular A-133. The information in the accompanying schedule has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

This report is intended solely for the information and use of the governor and Legislature of the State of California, the management of the executive branch, and the federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

CALIFORNIA STATE AUDITOR

Denise L. Vose

DENISE L. VOSE, CPA Deputy State Auditor

February 24, 2012

Schedule of Findings and Questioned Costs

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STATE OF CALIFORNIA SCHEDULE OF FINDINGS AND QUESTIONED COSTS FOR THE FISCAL YEAR ENDED JUNE 30, 2011

Summary of Auditor's Results

Financial Statements

Type of auditor's report issued Unqualified

Internal control over financial reporting:

Material weakness (es) identified? No

Significant deficiency (ies) identified that are not considered to be material weaknesses? Yes

Noncompliance material to financial statements noted? No

Federal Awards

Internal control over major programs:

Material weakness (es) identified? Yes

Significant deficiency (ies) identified that are not considered to be material weaknesses? Yes

Type of auditor's reports issued on compliance for major programs:

Career and Technical Education—Basic Grants to States (84.048) Qualified

School Improvement Grants Cluster:

School Improvement Grants; and School Improvement Grants,

Qualified Recovery Act (84.377 and 84.388)

Medicaid Cluster:

State Medicaid Fraud Control Units, State Survey and Certification of Health Care Providers and Suppliers, Medical Assistance Program (93.775, 93.777, and 93.778)

Qualified

HIV Care Formula Grants (93.917) Qualified

All other major programs Unqualified

Any audit findings disclosed that are required to be reported in

accordance with Section .510(a) of Circular A-133? Yes

Dollar threshold used to distinguish between

Type A and Type B programs \$136.3 million

Auditee qualified as low-risk auditee? No Blank page inserted for reproduction purposes only.

Identification of Major Programs:

CFDA Number	Name of Federal Program or Cluster of Programs
	CCDF Cluster
	Child Nutrition Cluster
	Disability Insurance/SSI Cluster
	Highway Planning and Construction Cluster
	Immunization Cluster
	Medicaid Cluster
	School Improvement Grants Cluster
	SNAP cluster
	Special Education Cluster (IDEA)
	State Fiscal Stabilization Fund Cluster
	TANF Cluster
	Title I, Part A Cluster
	Vocational Rehabilitation Cluster
	WIA Cluster
10.557	Special Supplemental Nutrition Program for Women, Infants, and Children
10.558	Child and Adult Care Food Program
14.239	Home Investment Partnerships Program
14.258	Tax Credit Assistance Program (Recovery Act Funded)
17.225	Unemployment Insurance
66.458	Capitalization Grants for Clean Water State Revolving Funds
66.468	Capitalization Grants for Drinking Water State Revolving Funds
81.042	Weatherization Assistance for Low-Income Persons
84.011	Migrant Education—State Grant Program
84.048	Career and Technical Education—Basic Grants to States
84.287	Twenty-First Century Community Learning Centers
84.365	English Language Acquisition Grants
84.367	Improving Teacher Quality State Grants
84.410	Education Jobs Fund
93.563	Child Support Enforcement
93.568	Low-Income Home Energy Assistance
93.658	Foster Care—Title IV-E
93.659	Adoption Assistance
93.667	Social Services Block Grant
93.917	HIV Care Formula Grants
93.959	Block Grants for Prevention and Treatment of Substance Abuse

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Internal Control and Compliance Issues Applicable to the Financial Statements and State Requirements

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EMPLOYMENT DEVELOPMENT DEPARTMENT

Reference Number: 2011-15-1

Condition

Employment Development Department (EDD) improperly reported its current accounts receivable balance for the Unemployment Insurance Fund (UI), the Disability Insurance Fund (DI), and the Benefit Audit Fund (BAF) for fiscal year 2010–11. For these funds, EDD recorded about \$1.1 billion that it expected to collect in periods subsequent to fiscal year 2011–12. However, it was not able to support that the \$1.1 billion could actually be collected, and it also incorrectly recorded these long-term receivables in a current receivables account. This resulted in a \$1.1 billion overstatement of current accounts receivable, a \$700 million understatement of expenses in the UI and DI funds, and a \$400 million overstatement of revenues in the BAF fund. Although EDD has controls in place to review such entries for reasonableness, we found that it's review was ineffective in preventing the improper recording of these amounts. EDD acknowledged the errors, and the State Controller's Office corrected the \$1.1 billion over statement.

Criteria

For governmental funds such as BAF, Governmental Accounting and Financial Reporting Standards (accounting standards) require that revenues be recognized in the accounting period in which they become available and measurable. For proprietary funds such as UI and DI, accounting standards state that generally accepted accounting principles (GAAP), which are similar to those used by businesses in the private sector, are applicable. GAAP requires accounts receivables be reported in the financial statements at net realizable value, that is, in the amount that is expected to be collected. Additionally, GAAP defines current assets as resources that are expected to be realized in cash during the next year.

The *State Administrative Manual*, Section 10500 requires that for these types of transactions to be classified as current accounts receivable they must be estimated to be collectible within the ensuing fiscal year.

Recommendation

EDD should complete a more thorough review of its accounting entries, including a review of applicable accounting standards and the calculations supporting its entries.

Department's View and Corrective Action Plan

EDD agrees with the Bureau of State Audit's finding that the adjusting entries for benefit receivables were not fully supported with respect to the actual collectability of the amounts. EDD also agrees that the debit sides of the adjusting entries were inadvertently submitted as "Accounts Receivable – Current" rather than "Accounts Receivable – Noncurrent". EDD has reversed the entry for BAF and requested that the State Controller's Office reverse the entries for UI and DI. EDD will complete a more thorough review of such entries, if required in the future, to ensure the entries are recorded for the proper amounts and in the proper accounts. This review will include using the financial analyses necessary to make the most accurate future collection projections while adhering to the applicable accounting principles.

Reference Number: 2011-15-2

Condition

The Employment Development Department (EDD) had weak general controls over its information systems for fiscal year 2010–11. General controls are the policies and procedures related to all or a large segment of an entity's information systems. While ineffective general controls do not, by themselves, cause misstatements, they may permit controls over individual systems to operate improperly and allow misstatements to occur and not be detected.

In January 2011, EDD's director certified that EDD had implemented a fully developed Risk Management and Privacy Program that complied with all applicable policy requirements. However, we found major deficiencies in several areas certified as fully implemented. Further, these deficiencies impact the effectiveness of the general controls over its information systems. Specifically, we found EDD's entitywide information security policy was outdated, included references to the *State Administrative Manual* and the California Government Code that no longer exist, referenced expired EDD policies for additional guidance, and was missing several mission-critical programs from a list of EDD Major Systems. In addition, we determined that EDD had an insufficient risk management program due to an inadequate risk assessment completed in August 2011, and an expired policy with outdated references. Furthermore, we found that EDD did not have an incident response plan prior to January 2012. Because we identified these significant weaknesses in EDD's information systems general controls, we did not complete additional testing of EDD's application system controls.

Unless EDD implements adequate general controls over its information systems, the completeness, accuracy, validity, and confidentiality of agency data will continue to be at risk. Specifically, the information systems used by EDD to report information for the Federal Unemployment Insurance program and the State's financial statements—such as the Tax Accounting System, Accounting and Compliance Enterprises System, and Single Client Database—may operate improperly and allow misstatements to occur and not be detected.

Criteria

According to Title 20 of the Code of Federal Regulations, Chapter V – Employment and Training Administration, Department of Labor, Part 602 – Quality Control in the Federal-State Unemployment Insurance System, Subpart B – Federal Requirements, Section 602.11, Secretary's Interpretation.(a), "The Secretary interprets Section 303(a)(1), SSA, to require that a State law provide for such methods of administration as will reasonably ensure the prompt and full payment of unemployment benefits to eligible claimants, and collection and handling of income for the State unemployment fund (particularly taxes and reimbursements), with the greatest accuracy feasible."

The *State Administrative Manual*, Section 5310, states, "The purpose of information security policy... [is] to establish and maintain a standard of due care to prevent misuse or loss of state agency information assets. Policy provides management direction for information security to conform with business requirements, laws, and administrative policies... Each agency must provide for the integrity and security of its information assets by establishing appropriate internal policies... for preserving the integrity and security of each automated, paper file, or data base..."

The State Administrative Manual, Section 5305, states, "Risk management is the process of taking actions to avoid or reduce risk to acceptable levels. This process includes both the identification and assessment of risk through risk analysis (SAM Section 5305.1) and the initiation and monitoring of appropriate practices in response to that analysis through the agency's risk management program."

The *State Administrative Manual*, Section 5350, states, "Proper incident management includes the formulation and adoption of a written incident management plan that provides for the timely assembly of appropriate staff that are capable of developing a response to, appropriate reporting about, and successful recovery from a variety of incidents."

Recommendation

EDD should ensure that all policy requirements included in the *State Administrative Manual* Chapters 4800 and 5300 are fully implemented and updated on a regular basis to strengthen its general controls over its information systems.

Department's View and Corrective Action Plan

EDD acknowledges that some of its information technology policies and plans are outdated or deficient and that it has not fully complied with some provisions of the State Administrative Manual (SAM) relating to documenting its information technology practices. EDD also concurs that meeting the SAM guidelines will help to improve its general controls over its information systems.

However, EDD has strong controls over its information systems and the completeness, accuracy, validity, or confidentiality of EDD data is not at risk. EDD does not agree that the deficiencies identified during the audit constitute significant weaknesses in its controls. An expired policy document does not mean the practices and procedures delineated by that policy are inadequate or no longer being followed. EDD's practice has been to continue following "expired" policy directives until those policies are eliminated or superseded. Likewise, other deficiencies in policy documents do not mean EDD's control practices and procedures are seriously flawed. Actual testing of EDD's controls would have revealed that the ongoing practices EDD uses to develop and manage its information systems results in an acceptably low level of risk of significant misstatements in data and reported information.

EDD has a strong "track record" of successfully managing its information systems, projects, and infrastructure. Since June 2008, EDD has effectively implemented hundreds of major programming changes in response to State and federal legislation related to the Unemployment Insurance (UI) program; most notably those needed for various federal extensions. These programming changes were made quickly and with little advance notice. Over the same period, during its highest workload period ever, EDD successfully implemented millions of dollars worth of information technology projects. Additionally, EDD successfully completed its Internal Revenue Service (IRS) Safeguard Review which focused specifically on data security. This positive track record would not be possible if the information systems controls actually in operation were significantly deficient.

While EDD believes the items identified during the audit have not adversely affected its operations, EDD recognizes that bringing its policies, plans, and documentation current and into full compliance with SAM provisions can only improve its already effective information systems controls. Accordingly, EDD will continue to perform its ongoing policy review to identify, analyze and correct issues pertaining to outdated and/or unnecessary policies. As discussed with the Bureau's auditors, this review will result in filling any gaps in EDD's security-related policies while removing redundant policies and/or policies that speak to technologies or business processes that are no longer relevant to the EDD environment. Throughout this effort EDD will adhere to state guidelines and the National Institute of Standards and Technology's (NIST) framework to ensure that EDD complies with all SAM provisions.

The EDD has already taken steps to address the concerns raised by the auditors. In January 2012, EDD implemented an updated Incident Management Plan consistent with SAM 5350. Earlier, in June 2011, EDD put into effect and practice two policies pertaining to the adoption of System Security Plans (SSP). The first policy sets the criteria for each SSP and the second requires that all new systems complete the SSP before moving to production and all current systems complete the SSP within two years. The SSP process follows the NIST Risk Framework. As was conveyed to the auditors, EDD successfully completed the SSP for the Accounting and Compliance Enterprises System project and is in the process of establishing the General Security Plan which encompasses the Enterprise Common Controls. EDD is currently in the process of drafting policy which would describe the EDD's risk management program. The SSP compliance methodology along with accepted security focused risk management practices will form the basis of the Enterprise Information Security Risk Management program compliant with SAM 5305. Finally, EDD has now released its Policy on the Information Security Program (PISP) for EDD Executive signature. This PISP provides the required security controls and direction for EDD to be in compliance with SAM 5310.

Auditor's Comments on Department's View

We acknowledge that EDD has taken steps to address our concerns. However, we disagree with EDD's assertion that the deficiencies identified during our audit do not constitute significant weaknesses in the controls over its information systems. For example, we determined that EDD had an insufficient risk management program and lacked an incident response plan during the period of our review.

Consequently, EDD could not ensure that it adequately identified and mitigated risks associated with its information assets, or that it appropriately responded and applied lessons learned from security incidents.

While we concur with EDD that an expired policy does not necessarily mean that the practices and procedures prescribed within it are defunct, expired policies may reduce EDD's ability to hold its staff accountable for protecting its information assets. Further, in the absence of an adequate risk assessment, EDD cannot ensure that its security policies incorporate practices and procedures that mitigate the current threats and vulnerabilities of its information assets.

Finally, EDD's assertion that it implemented hundreds of major programming changes does not equate to EDD having sufficient controls over its information systems. Rather, it is precisely the dynamic environment in which it operates that reinforces the need for EDD to conduct adequate risk assessments and regularly update its policies to ensure that it implements strong general controls over its information systems. Further, EDD's statement that it successfully completed its IRS Safeguard Review, which focused specifically on data security, is misleading. The preliminary results of the IRS's Safeguard Review identified 23 significant findings related to general control weaknesses. The IRS will require EDD to report on the corrective action(s) taken to address each finding until closed by the IRS.

DEPARTMENT OF CORRECTIONS AND REHABILITATION

Reference Number:

2011-15-3

Condition

In its fiscal year 2010–11 financial statements, the California Department of Corrections and Rehabilitation (Corrections) again incorrectly reported certain capital asset balances for buildings. Last year, we issued a finding to Corrections related to misclassifications in its governmental funds of buildings associated with capital leases. Corrections committed to revising its financial statements to reflect the overstatement we identified and to performing additional reviews to ensure the correct reporting of buildings balances in its fiscal year 2010–11 financial statements. However, it actually corrected \$14 million less than we previously identified as having been misclassified and made little progress in identifying further missclassifications. To evaluate the level of remaining potential misclassification this year, we identified five buildings included in Corrections' governmental funds, totaling about \$571 million, which had corresponding large capital leases outstanding with the State Public Works Board (Board). Based on our testing of these items, we confirmed that Corrections had incorrectly classified over \$220 million as governmental fund assets. Corrections accordingly reduced its buildings balance for governmental funds by about \$223 million. We also noted a continuing potential overstatement in Corrections' buildings' balance of about \$184 million. The potential overstatement is related to other buildings reported in Corrections' governmental funds that may also be associated with capital leases through the Board. Corrections stated that the misclassifications were caused by a combination of bad data, insufficient communication regarding changes in procedures, and data that was corrupted during the transition to a new accounting system.

At fiscal year-end, the State Controller's Office (SCO) gathers information on California's capital assets from various sources and presents it in the Comprehensive Annual Financial Report (CAFR). Buildings and improvements within the capital assets governmental activities section of the CAFR include buildings owned by state departments as well as buildings that departments are purchasing through leases with the Board. The SCO obtains information on buildings that are owned by departments through departments' financial statements and obtains information on capital leases with the Board through Department of General Services' reports. When departments, in their year-end financial reports to the SCO, include buildings they are buying through capital leases with the Board, they cause assets to be double counted in the CAFR.

March 2012

Criteria

The *State Administrative Manual*, section 6872 states that the title of a building under lease with the Board remains with the Board until the associated debt is retired. Thus, buildings that are still under lease should not be reported in governmental funds.

The *State Administrative Manual*, sections 7977, 7978, and 8660, require departments to report in their financial statements to the SCO all additions and deductions to real property. These sections also require that departments report real property by the source of the funds used to acquire each property. The SCO uses these reports to compile the information related to capital assets that it presents in the CAFR.

Recommendations

In order to ensure its buildings balance is correctly stated, Corrections should identify any remaining buildings in its governmental funds that are associated with capital leases and reclassify them to the appropriate nongovernmental funds. Corrections should also improve internal communications and correct erroneous data related to accounting for capital assets.

Department's View and Corrective Action Plan

Corrections is currently reviewing additional data to identify further potential misclassifications with the goal of correcting information for our upcoming fiscal year 2011–12 financial statements. Corrections will continue to work in the 2012–13 fiscal year to identify and correct financial data to ensure proper classification of assets. Corrections has also developed procedures to ensure that future constructed assets with capital leases are properly classified.

DEPARTMENT OF TRANSPORTATION

Reference Number: 2011-15-4

Condition

In fiscal year 2010–11, the California Department of Transportation (Caltrans) failed to comply with certain requirements related to managing infrastructure assets accounted for under the modified approach. As required by Governmental Accounting and Financial Reporting Standards (accounting standards), Caltrans completed a pavement-condition survey (survey) in March 2008 and thus needed to complete its next survey by March 2011. However, Caltrans did not complete this survey until December 2011, nine months after the required deadline, resulting in a lapse in compliance. Caltrans stated that the survey was delayed due to modifications it made to improve the data for pavement performance modeling. It said it made these changes in order to improve the survey's comparability with prior surveys and to aid in the transition to new survey software. Following the accounting standards related to infrastructure under the modified approach is significant because governments that fail to comply must begin depreciating their infrastructure assets.

Criteria

Accounting standards allow governments to account for infrastructure assets under what is referred to as the "modified approach". Under this approach, which does not require infrastructure assets to be depreciated, governments must meet several requirements including completing condition assessments of their infrastructure assets at least every three years and documenting that these assets are being preserved at an established condition level. Governments must present the assessed condition of infrastructure as required supplementary information in their comprehensive annual financial reports.

Recommendations

Caltrans should establish a process to ensure that it will complete pavement condition surveys at least every three years. Caltrans should complete its next pavement condition survey by the fall of 2014 to ensure that the State Controller's Office has adequate time to review the survey and include relevant information from it in the State's comprehensive annual financial report for fiscal year 2013–14.

Department's View and Corrective Action Plan

Caltrans concurs with the recommendation and is on track to complete the next Pavement Condition Survey by December 2013.

CALIFORNIA COMMUNITY COLLEGES CHANCELLOR'S OFFICE

Reference Number:

2011-15-5

Condition

The California Community Colleges Chancellor's Office (Chancellor's Office) authorized \$5.9 million in general apportionments to three community college districts that were not entitled to receive such amounts in fiscal year 2010–11. Further, the Chancellor's Office has authorized a total of \$45.5 million of such payments to these same districts since fiscal year 2005–06, without explicit legal authority.

Community college districts receive apportionment funding primarily from three sources: property taxes, student fees, and the State's General Fund. When local property taxes and student fees alone do not meet a district's apportionment target, the General Fund provides additional funding, referred to as general apportionments, to each district. The Chancellor's Office calculates each district's general apportionment annually based on criteria set forth in Education Code sections 84750.5 through 84751.5, including data on student enrollment and local revenues. Districts that have local property tax and student fee revenues that exceed their apportionment target are not entitled by law to receive general apportionment funding from the State. These districts are known as excess tax school entities, or basic aid districts.

According to the Director of Fiscal Services of the Chancellor's Office (director), since fiscal year 2005–06, revenues for three of the State's 72 community college districts—Mira Costa, Marin, and South Orange—have exceeded their apportionment target. However, while these districts did not meet the criteria set forth in Education Code Sections 84750.5 through 84751.5 to receive general apportionment funding, the Chancellor's Office authorized such funding for each of the last six years. Annually, these amounts ranged from \$5.7 to \$8.7 million between fiscal years 2005–06 and 2010–11.

The director stated that the Chancellor's Office has authorized a portion of general apportionment funding to the three districts each year since fiscal year 2005–06 to compensate for their loss of Partnership for Excellence funding. The Partnership for Excellence Program, created by Senate Bill 1564 in 1998, provided supplemental funding until January 1, 2005 to community colleges for the purposes of achieving annual performance goals and improving student learning and success. The text that authorized Partnership for Excellence funding was not included in Budget Acts subsequent to fiscal year 2004–05. The director stated that for fiscal year 2005–06, the Department of Finance provided budget-related documents to the Chancellor's Office showing an increase in general apportionment funding that matched the amount previously provided through the Partnership for Excellence Program. He further explained that because net funding did not change, the Chancellor's Office interpreted the increase in general apportionment funding as a reclassification of funding that was not intended to reduce funding to basic aid districts. However, the Chancellor's Office cannot demonstrate that it sought a legal opinion to support its decision to authorize general apportionment funding to basic aid districts after the expiration of Partnership for Excellence funding.

In addition, since fiscal year 2005–06, the Chancellor's Office has not presented these payments as general apportionments in the state apportionment reports it publishes on its website. Instead it reported them as "Partnership" in fiscal year 2005–06, "other base entitlement" in fiscal year 2006–07 and as "other adjustments" since fiscal year 2007–08. For this reason, it has not been clear to the public that the three districts have effectively received general apportionment funding. By allocating general apportionment funding to basic aid districts, the amount of funding available for the remaining 69 community college districts was reduced by \$45.5 million between fiscal years 2005–06 and 2010–11.

Criteria

Education Code Section 84328 requires the Board of Governors of the California Community Colleges to certify each apportionment made by it to the Controller.

Revenue and Taxation Code Section 95 states that an "excess tax school entity" means an educational agency for which the amount of the state funding entitlement determined under Education Code sections 2558, 42238, 84750 or 84751, as appropriate, is zero.

Education Code 84751 provides the methodology used in determining each community college district's revenue level for each fiscal year.

Recommendations

To ensure that community college districts that rely on general apportionment funding receive their entitled amounts, the Chancellor's Office should do the following:

- Discontinue distributing general apportionment funding to districts that do not meet the criteria set forth in the Education Code for receiving general apportionment funding, also known as basic aid districts.
- Recover \$45.5 million in general apportionments paid to the Mira Costa, Marin, and South Orange community college districts, and redistribute these monies to the remaining community college districts.

To ensure community college apportionments are made based on appropriate legal authority, the Chancellor's Office should seek advice from its legal office prior to certifying apportionments when it believes that the authority to allocate community college apportionment funding is unclear.

Department's View and Corrective Action Plan

The Chancellor's Office agrees that these payments should be discontinued, and stated that it has begun phasing out Partnership for Excellence payments to the three basic aid districts. For fiscal year 2011–12, the Chancellor's Office stated that these districts will receive one-half of the value of the Partnership for Excellence payments and will not receive any further Partnership for Excellence funding after fiscal year 2011–12.

The Chancellor's Office disagrees that the prior payments should be recovered from the districts. It believes that the payments were made due to a reasonable interpretation of the situation, and it would be a hardship to compel the districts to repay funds paid out over a number of prior years due to a revision in understanding of legislative intent.

The Chancellor's Office agrees with the State Auditor's recommendation that it should seek advice from its legal staff where the interpretation of statute concerning apportionments is unclear, and stated it will endeavor to do so when appropriate.

CALIFORNIA COMMUNITY COLLEGES CHANCELLOR'S OFFICE STATE CONTROLLER'S OFFICE DEPARTMENT OF FINANCE

Reference Number:

2011-15-6

Condition

The California Community Colleges Chancellor's Office (Chancellor's Office) certified an \$832 million apportionment to community colleges, which the State Controller's Office (SCO) paid in July 2011, based on a law that was no longer in effect. Chapter 724 of the Statutes of 2010 (Chapter 724) authorized an \$832 million appropriation to community colleges to be paid in July of 2011. However, Chapter 7 of the Statutes of 2011 (Chapter 7), which became law in March 2011, eliminated the text of the earlier law. Thus, the appropriation established by Chapter 724 was repealed and could not form the basis for a payment. In signing Chapter 7, the governor noted that community college deferral amounts identified in the legislation would be applied beginning with the 2011-12 fiscal year and that future legislation would clarify this intent. However, the law was not amended to authorize the \$832 million payment until September 2011. If administering departments and control agencies do not ensure that disbursement requests are based on appropriate legal authority, the State risks making unauthorized disbursements.

To ensure that the SCO establishes appropriations in its accounting system in accordance with the law, the chief of the SCO's Bureau of Accounting (accounting chief) asserted that fiscal analysts monitor state legislation on a daily basis to identify new laws that create, eliminate, or modify appropriations. In addition, the chief of the SCO's Bureau of Payments (payments chief) stated that before the SCO sets up appropriations in its accounting system, it coordinates with the Department of Finance (Finance) to establish identifying item numbers. Once the appropriation is set up in its accounting system, the SCO's Local Apportionments Section processes payments based on schedules submitted by the Chancellor's Office. The Chancellor's Office's Vice Chancellor of College Finance and Facilities Planning (Vice Chancellor) stated that he is typically involved with the development of legislation that affects apportionments to community college districts, and he and the Chancellor's Office's Director of Finance monitor daily for changes in the law. He further stated that once apportionments are authorized in law, a fiscal services specialist calculates payments due to each community college district, which the Vice Chancellor then certifies and submits to the SCO in the form of an allocation schedule.

After the passage of Chapter 7 in March 2011, a program principal at Finance contacted the SCO's Division of Accounting and Reporting to inquire about the SCO's interpretation of the language in Chapter 7. The program principal stated that a concern had been raised that the legislation could be interpreted to mean that the community colleges would be subject to a double deferral. In response to this inquiry, a manager within the SCO's Division of Accounting and Reporting told Finance in March 2011 that his division would seek advice from the SCO's legal office. However, the SCO's chief legal counsel indicated that his office never received a request for a legal opinion on this matter. Moreover, he stated that his office was not involved in the issues surrounding the \$832 million payment prior to inquiries made by the State Auditor's staff in August 2011. The payments chief further indicated that the procedures to guide staff in monitoring changes in legislation and establishing appropriations were not formalized, but rather they were documented as hand written notes located on various staffs' desks. She stated that the SCO established formal policies and procedures on August 31, 2011 to guide its staff in these processes, which include obtaining an opinion from the SCO's legal counsel when staff identify conflicting legislation.

The Vice Chancellor stated that neither he nor his fiscal services staff noticed that the \$832 million apportionment had been struck from existing law during their review of Chapter 7. He further stated he was not aware that Chapter 7 had eliminated the apportionment until the State Auditor's staff questioned citing Chapter 724 as the legal authority for the \$832 million payment request, in August 2011.

The SCO payments chief also stated that in coordinating with Finance in July 2011, Finance advised SCO staff to use an appropriation item number related to Chapter 724. SCO staff interpreted this action as Finance's concurrence with making the \$832 million payment under Chapter 724. The manager of Finance's Budget Operations Support Unit stated that Finance coordinates with the SCO under an informal agreement to provide appropriation item numbers only to ensure that both agencies use matching numbers in their financial systems, not as a legal check on appropriations.

Finance's chief legal counsel indicated that given the governor's signing message attached to Chapter 7, Finance intended to include clarifying text within the May Revise of the fiscal year 2011-12 Budget to authorize the \$832 million payment eliminated by Chapter 7. However, it was not until August 25, 2011, one day after the State Auditor's staff met with Finance to discuss the impact of Chapter 7 on this payment, that Finance's Program Budget Manager of Education proposed clarifying legislation in an e-mail to the Staff Director for the Senate's Standing Committee on Budget and Fiscal Review. This text was included in Chapter 15 of the Statutes of 2011, First Extraordinary Session, which the governor approved on September 20, 2011, and retroactively clarified that the \$832 million payment made in July 2011 was authorized.

Both the Vice Chancellor and the SCO's accounting chief stated that they believe the intent of Chapter 7 was not to remove the legal authority for the \$832 million appropriation established in Chapter 724, but rather to establish appropriations related to the fiscal year 2011-12 Budget Act. Further, both assert that their view of the intent of Chapter 7 was supported by schedules created by Finance showing apportionments for fiscal year 2011-12. Nevertheless, neither office took prompt action to ensure that authority for the appropriation existed in law prior to certifying or disbursing the apportionment payment.

Criteria

Education Code Section 84328 requires the Board of Governors of the California Community Colleges to certify each apportionment made by it to the SCO.

Government Code Section 12440 prohibits the SCO from making payments unless authorized by law.

Government Code Section 13070 states Finance has general powers of supervision over all matters concerning the financial and business policies of the State.

Recommendations

To ensure that community college payments are certified based on proper legal authority, the Chancellor's Office should seek advice from its legal office prior to certifying apportionment payments when legislation affecting community college apportionments is unclear.

To ensure that appropriations are established and payments are made under proper legal authority, the SCO should do the following:

- Ensure that staff follow newly formalized policies and procedures related to monitoring for the potential impacts of changing legislation and to establishing appropriation item numbers.
- Seek advice from its legal office when legislation has a potential impact on its legal authority to make payments.

To ensure that appropriations are established under proper legal authority, the SCO and Finance should formally define expectations for coordinating information on appropriation item numbers.

Departments' Views and Corrective Action Plan

The Chancellor's Office agrees with the State Auditor's recommendation that it should seek advice from its legal staff where the interpretation of statute concerning apportionments is unclear, and stated it will endeavor to do so when appropriate.

The SCO concurs with the spirit underlying the recommendations provided by the State Auditor, and understands the importance of staff following formal policies and procedures when monitoring legislation and establishing appropriations. As such, it says it has already strengthened its internal controls in this area and is resolved to continue to do so in order to ensure the integrity of state expenditures. However, it also said that its stewardship of the State's finances demands that it always act in the best interests of the people it serves, including taking reasonable actions to clean-up the unintended mistakes of others. It believes the payment it made was consistent with the intentions of the governor and the Legislature, and produced no material harm.

Finance concurs with the recommendation and stated it will work with the SCO to formalize an updated procedure for coordinating items of appropriation. Finance further stated that a meeting between the two departments has already been scheduled.

Compliance and Internal Control Issues Related to Specific Grants Administered by Federal Departments

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California State Auditor

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THE CORPORATION FOR NATIONAL AND COMMUNITY SERVICE

Reference Number: 2011-7-6

Federal Catalog Number: 94.006

Federal Program Title: AmeriCorps

Federal Award Numbers and Years: 10ESHCA001; 2010

10FXHCA002; 2010 09ACHCA001; 2009 09RCHCA002; 2009 06AFHCA001; 2006

Category of Finding: Matching

State Administering Department: CaliforniaVolunteers

Criteria

TITLE 45—PUBLIC WELFARE, PART 2521—ELIGIBLE AMERICORPS SUBTITLE C PROGRAM APPLICANTS AND TYPES OF GRANTS AVAILABLE FOR AWARD, Section 2521.35—Who Must Comply with Matching Requirements?

- (a) The matching requirements described in sections 2521.40 through 2521.95 apply to you if you are a subgrantee of a State commission or a direct program grantee of the Corporation. These requirements do not apply to Education Award Programs.
- (b) If you are a State commission, you must ensure that your grantees meet the match requirements established in this part, and you are also responsible for meeting an aggregate overall match based on your grantees' individual match requirements.

TITLE 45—PUBLIC WELFARE, PART 2521—ELIGIBLE AMERICORPS SUBTITLE C PROGRAM APPLICANTS AND TYPES OF GRANTS AVAILABLE FOR AWARD, Section 2521.45—What are the Limitations on the Federal Government's Share of Program Costs?

- (a) Member support: The Federal share, including Corporation and other Federal funds, of member support costs, which include the living allowance required under Section 2522.240(b)(1), FICA, unemployment insurance (if required under State law), worker's compensation (if required under State law), is limited as follows:
 - (3) Your share of member support costs must be non-Federal cash.
- (b) Program operating costs: The Corporation share of program operating costs may not exceed 67 percent. These costs include expenditures (other than member support costs described in paragraph (a) of this section) such as staff, operating expenses, internal evaluation, and administration costs.
 - (1) You may provide your share of program operating costs with cash, including other Federal funds (as long as the other Federal agency permits its funds to be used as match), or third party in-kind contributions.
 - (2) Contributions, including third party in-kind must:
 - (i) Be verifiable from your records;
 - (ii) Not be included as contributions for any other Federally assisted program;
 - (iii) Be necessary and reasonable for the proper and efficient accomplishment of your program's objectives; and
 - (iv) Be allowable under applicable OMB cost principles.

Condition

In our prior-year audit, we reported that CaliforniaVolunteers had not ensured its established policies and procedures for fiscal desk reviews were followed. Specifically, we found that it did not verify the allowability of grantee match contributions for the fiscal desk reviews we tested where requirements to verify match contributions existed. CaliforniaVolunteers' chief of staff indicated that the Department of Finance's Office of State Audits and Evaluations (Finance) was performing the remaining desk reviews. However, the chief of staff also indicated that although Finance verified the supporting documentation for the match requirement when performing desk reviews, it did not verify the source of the match. As a result, we reported that CaliforniaVolunteers could not assure that its subgrantees were meeting the match requirement. In its corrective action plan, CaliforniaVolunteers indicated that during 2011, as part of its fiscal year 2009–10 desk reviews, it planned to require subgrantees to document the source of matching funds and it intended to review this documentation to verify that the matching funds were from allowable sources.

We also reported that CaliforniaVolunteers had yet to eliminate its backlog of fiscal desk reviews. The chief of staff indicated that as of January 2011, CaliforniaVolunteers had completed only three fiscal desk reviews initially scheduled for program year 2007–08, and that it intended to have Finance complete the remaining reviews. According to a log that CaliforniaVolunteers maintained to track pending fiscal desk reviews, although Finance had completed nine of 34 pending fiscal desk reviews for program years 2007–08 and 2008–09, CaliforniaVolunteers had not yet approved any of those desk reviews. In its corrective action plan, CaliforniaVolunteers indicated that during 2011, it intended to eliminate the backlog of 2007–08 and 2008–09 fiscal desk reviews and begin processing 2009–10 reviews.

During our follow-up procedures, we found that CaliforniaVolunteers has not fully implemented its corrective action plan to ensure that its established policies and procedures for fiscal desk reviews are followed by verifying the allowability of grantee match contributions. CaliforniaVolunteers is in the process of informing subgrantees that they are required to provide all documentation that supports any match that is reported for the fiscal year 2009–10 awards, including the source of the match, but it does not expect its subgrantees to begin submitting the documentation until the end of 2011. Finally, we also found that CaliforniaVolunteers has not yet eliminated its backlog of fiscal desk reviews. The fiscal desk review officer stated that she is nearly finished with the 2007–08 reviews and she expects to eliminate the backlog of 68 fiscal desk reviews by the end of the 2010–11 fiscal year.

Questioned Costs

No specific questioned costs identified.

Recommendations

CaliforniaVolunteers should follow its policies and procedures when performing fiscal desk reviews to ensure its subgrantees submit documentation to support their matching funds, including the source of the match. It should then verify that the contributions are from allowable sources. Finally, CaliforniaVolunteers should continue implementing its fiscal monitoring workplan to eliminate its backlog of fiscal desk reviews.

Department's View and Corrective Action Plan

CaliforniaVolunteers stated that for the 29 fiscal desk reviews scheduled for the 2009–10 program year, it has requested the supporting documentation and it has already collected documentation from nine of these programs. CaliforniaVolunteers indicated that it plans to complete the majority of 2009–10 program year reviews in-house, but anticipates contracting with Finance for the completion of fiscal desk reviews that appear to be especially time consuming or complex.

U.S. DEPARTMENT OF AGRICULTURE U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES

Reference Number: 2011-13-11

Category of Finding: Subrecipient Monitoring

State Administering Department: Department of Social Services (Social Services)

Federal Catalog Number: 10.561

Federal Program Title: State Administrative Matching Grants for the

Supplemental Nutrition Assistance Program

(SNAP)

Federal Award Number and Year: 7CA440CA4; 2011

Federal Catalog Number: 93.558

Federal Program Title: Temporary Assistance for Needy Families

(TANF)

Federal Award Number and Year: G-1102CATANF; 2011

Federal Catalog Number: 93.658

Federal Program Title: Foster Care—Title IV-E

Federal Award Numbers and Years: 1101CA1401; 2011

1101CA1404; 2011

Federal Catalog Number: 93.659

Federal Program Title: Adoption Assistance—Title IV-E

Federal Award Numbers and Years: 1101CA1403; 2011

1101CA1405; 2011 1101CA1407; 2011

Federal Catalog Number: 93.667

Federal Program Title: Social Services Block Grant

Federal Award Number and Year: G-1101CASOSR; 2011

Criteria

U.S. OFFICE OF MANAGEMENT AND BUDGET CIRCULAR A 133, *AUDITS OF STATES, LOCAL GOVERNMENTS, AND NONPROFIT ORGANIZATIONS* (OMB Circular A-133), Subpart D—Federal Agencies and Pass–Through Entities, Section .400—Responsibilities

(d) Pass—through entity responsibilities. A pass—through entity shall perform the following for the federal awards it makes:

- (1) Identify federal awards made by informing each subrecipient of CFDA title and number, award name and number, award year, if the award is R&D, and name of federal agency. When some of this information is not available, the pass—through entity shall provide the best information available to describe the federal award.
- (2) Advise subrecipients of requirements imposed on them by Federal laws, regulations, and the provisions of contracts or grant agreements as well as any supplemental requirements imposed by the pass-through entity.

Condition

Social Services did not inform its county subrecipients of certain federal award information, such as the Catalog of Federal Domestic Assistance program title and number, and relevant federal laws and regulations that govern each program we reviewed. Specifically, Social Services has periodic, ongoing correspondence with counties through fiscal letters that it uses to notify them of various issues. Although Social Services annually issues a fiscal letter that informs the counties of the required federal award information, it failed to issue this letter in fiscal year 2010–11. The chief of the fund accounting and reporting bureau indicated that Social Services did not issue the letter because of workload issues, but has since implemented a process to ensure the letters are released timely in the future. By not providing award information and requirements to its county subrecipients, Social Services cannot be sure that its subrecipients are aware of and following all program requirements imposed on them.

Questioned Costs

No specific questioned costs identified.

Recommendation

Social Services should annually inform the counties of the federal award information and relevant federal laws, regulations, and terms and conditions governing the programs in its annual county fiscal letters.

Department's View and Corrective Action Plan

The California Department of Social Services (Social Services) agrees with this recommendation.

An annual County Fiscal Letter (CFL) that includes federal award information was not issued to the counties in fiscal year (FY) 2010–11. The annual county letter for FY 2011–12 (CFL 11/12-09) was issued on August 12, 2011. Beginning in FY 2012–13, this annual letter will be issued every October to coincide with the start of the new federal fiscal year. Social Services has revised its procedures to ensure that an annual letter is sent. In addition, reminders will be placed in the County Expense Claim Time Study and Claiming Instructions' quarterly claiming letters. These quarterly claiming letters provide instructions in advance of the next quarter. The first quarterly reminder regarding federal awards will be issued for the January through March 2012 quarter. Social Services will continue to update its federal grant Internet link with updated terms and conditions information on a monthly basis. A link to this Web site will be included in the annual and quarterly county fiscal letters issued to the counties.

U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES

Reference Number: 2011-1-3
Federal Catalog Number: 93.958

Federal Program Title: Block Grants for Community Mental Health

Services

Federal Award Numbers and Years: 2B09SM010005-11; 2011

2B09SM010005-10; 2010 2B09SM010005-09; 2009

Category of Finding: Activities Allowed, Allowable Costs

State Administering Department: Department of Mental Health (Mental Health)

Criteria

TITLE 42—THE PUBLIC HEALTH AND WELFARE, CHAPTER 6A—PUBLIC HEALTH SERVICE, SUBCHAPTER XVII—BLOCK GRANTS, PART B—BLOCK GRANTS REGARDING MENTAL HEALTH AND SUBSTANCE ABUSE, Subpart i—Block Grants for Community Mental Health Services, section 300x—Formula Grants to States

(b) Purpose of grants

A funding agreement for a grant under subsection (a) of this section is that, subject to section 300x-5 of this title, the State involved will expend the grant only for the purpose of—

- (1) carrying out the plan submitted under section 300x-1(a) of this title by the State for the fiscal year involved;
- (2) evaluating programs and services carried out under the plan; and
- (3) planning, administration, and educational activities related to providing services under the plan.

TITLE 42—THE PUBLIC HEALTH AND WELFARE, CHAPTER 6A—PUBLIC HEALTH SERVICE, SUBCHAPTER XVII—BLOCK GRANTS, PART B—BLOCK GRANTS REGARDING MENTAL HEALTH AND SUBSTANCE ABUSE, Subpart i—Block Grants for Community Mental Health Services, section 300x-5—Restrictions on Use of Payments

(a) In general

A funding agreement for a grant under section 300x of this title is that the State involved will not expend the grant—

- (1) to provide inpatient services;
- (2) to make cash payments to intended recipients of health services;
- (3) to purchase or improve land, purchase, construct, or permanently improve (other than minor remodeling) any building or other facility, or purchase major medical equipment;
- (4) to satisfy any requirement for the expenditure of non-Federal funds as a condition for the receipt of Federal funds; or
- (5) to provide financial assistance to any entity other than a public or nonprofit private entity.

Condition

In our audit reports for fiscal years 2006–07 through 2009–10, we reported that Mental Health did not ensure that its subgrantees' expenditures were only for allowable activities and costs. Mental Health relied on the counties' budget and program description components of their applications to determine if funds would be used for allowable activities and costs. Specifically, the grant renewal application

instructions for the Substance Abuse and Mental Health Services Administration's Block Grants for Community Mental Health Services (block grant) directs counties to include in their program narrative a description that specifies what is actually being paid for by the block grant funds. However, Mental Health did not require the counties to submit invoices, receipts, or payroll information to verify amounts they reported as expenditures. Additionally, Mental Health did not perform regular site visits to the counties to verify whether the block grant programs' activities and costs were allowable.

During our follow-up procedures for fiscal year 2010–11, we found that Mental Health has not yet implemented a process to verify that counties' actual expenditure of federal grant funds is for allowable activities and costs. According to Mental Health, in March 2011 it drafted a proposal identifying its options for reviewing counties' expenditures, which included conducting audits of the counties or reviewing invoices and other documentation from the counties to verify that activities and costs are allowable. As of July 2011, Mental Health had not determined which option it will implement.

Questioned Costs

No specific questioned costs identified.

Recommendation

Mental Health should complete its efforts to establish a process to ensure that only allowable activities and costs are paid for with block grant funds.

Department's View and Corrective Action Plan

Mental Health agrees with the finding. By November 2011 Mental Health plans to finalize the proposal and adopt an option to verify that counties' actual expenditures of federal grant funds are for allowable activities and costs. Mental Health plans to implement the process during fiscal year 2011–12.

Reference Number: 2011-5-6

Federal Catalog Number: 93.958

Federal Program Title: Low-Income Home Energy Assistance

(LIHEAP)

Federal Award Numbers and Years: G-11B1CALIEA; 2011

G-10B1CALIEA; 2010 G-09B1CALIEA; 2009

Category of Finding: Eligibility

State Administering Department: Department of Community Services and

Development (CSD)

Criteria

TITLE 42—THE PUBLIC HEALTH AND WELFARE—CHAPTER 94—LOW-INCOME ENERGY ASSISTANCE, Subchapter II—Low-Income Home Energy Assistance, Section 8624—Applications and Requirements

(b) Certifications required for covered activities

As part of the annual application required by subsection (a) of this section, the chief executive officer of each State shall certify that the State agrees to—

(2) make payments under this subchapter only with respect to—

- (B) households with incomes which do not exceed the greater of—
 - (i) an amount equal to 150 percent of the poverty level for such State; or
 - (ii) an amount equal to 60 percent of the State median income.

Condition

CSD is not ensuring that local agencies, such as cities, counties, and non-profit organizations, obtain the appropriate documentation to substantiate their eligibility determinations. Specifically, CSD contracts with local agencies to make eligibility determinations and to provide assistance under LIHEAP to eligible participants residing in their service areas. However, for eight (16 percent) of the 50 applicant files we reviewed, local agencies either did not have appropriate documents supporting applicants' monthly income amounts or did not correctly identify the income on the intake form. For example, CSD's LIHEAP Eligibility and Verification Guide (eligibility guide) states that proof of income documents submitted by the applicant must be dated within six weeks of the applicant's intake date, which is the date the applicant applies for the services. Yet, in three instances local agencies accepted documents from applicants that were not dated within six weeks from the applicants' intake dates. In one of these instances, the local agency accepted income documentation dated nearly one year after the applicant's intake date. In four other instances, the documents supporting the applicant's income did not agree with the income reported on the intake forms. In three of these instances, the applicants' reported monthly incomes were overstated by \$135, \$172, and \$263, respectively, while in the fourth instance, the applicant's monthly income was understated by \$88. Finally, in another case, although the applicant reported no income, the local agency did not obtain a self-certification from the applicant as required by CSD's eligibility guide. By failing to obtain the appropriate documentation to support eligibility determinations, CSD risks providing LIHEAP funds to ineligible applicants.

Questioned Costs

No specific questioned costs identified.

Recommendation

CSD should obtain appropriate documentation to support their eligibility determinations for LIHEAP applicants.

Department's View and Corrective Action Plan

CSD concurs with the recommendation. CSD will contact the subject agencies to advise of eligibility discrepancies and to provide training and technical assistance to ensure understanding. In addition, CSD will host annual training workshops and webinars that will provide detailed information on Eligibility, Income and Intake requirements and program changes to all providers. CSD will continue verifying client eligibility during the on-site monitoring review and provide ongoing training and technical assistance as needed.

Reference Number: 2011-7-3

Federal Catalog Number: 93.958

Federal Program Title: Block Grants for Community Mental Health

Services

Federal Award Numbers and Years: 2B09SM010005-11; 2011

2B09SM010005-10; 2010 2B09SM010005-09; 2009

Category of Finding: Earmarking

State Administering Department: Department of Mental Health (Mental Health)

Criteria

TITLE 42—THE PUBLIC HEALTH AND WELFARE, CHAPTER 6A—PUBLIC HEALTH SERVICE, SUBCHAPTER XVII—BLOCK GRANTS, Part B—Block Grants Regarding Mental Health and Substance Abuse, Subpart i—Block Grants for Community Mental Health Services, Section 300x-5—Restrictions on Use of Payments

(b) Limitation on administrative expenses—

A funding agreement for a grant under section 300x of this title is that the State involved will not expend more than 5 percent of the grant for administrative expenses with respect to the grant.

Condition

In our audit reports for fiscal years 2006–07 through 2009–10, we reported that Mental Health did not have official written policy or procedures in place to ensure that administrative costs were charged appropriately to the Substance Abuse and Mental Health Service's Administration's Block Grants for Community Mental Health Services (block grant). Mental Health charged all or a portion of salaries for certain key Substance Abuse and Mental Health Services Administration staff to the block grant, based on approved timesheets, but other expenditures, such as travel, were allocated to the block grant by staff's choice.

During our follow-up procedures for fiscal year 2010–11, we found that Mental Health still had not completed written policies and procedures to ensure that it consistently and properly applied administrative costs to the block grant. Mental Health stated that it formed a workgroup in February 2010 to develop a written policy, processes, and procedures to ensure that only allowable costs are used to meet the earmarking requirement.

Questioned Costs

No specific questions costs identified.

Recommendations

Mental Health should complete its efforts to establish a written policy, as well as processes and procedures, to ensure that only allowable costs are used to meet the earmarking requirement.

Department's View and Corrective Action Plan

Mental Health agrees with the finding. By November 2011, Mental Health plans to finalize the Administrative Cost Policy and its Substance Abuse and Mental Health Services' Administration Desk Manual. Mental Health plans to implement the processes and procedures to ensure that it consistently and properly applies administrative costs to the block grant during fiscal year 2011–12. In addition, the Substance Abuse and Mental Health Service's Administration Desk Manual will assist staff in the administration of the block grant.

Reference Number: 2011-7-4

Federal Catalog Number: 93.958

Federal Program Title: Block Grants for Community Mental Health

Services

Federal Award Numbers and Years: 2B09SM010005-11; 2011

2B09SM010005-10; 2010 2B09SM010005-09; 2009

Category of Finding: Level of Effort—Maintenance of Effort

State Administering Department: Department of Mental Health (Mental Health)

Criteria

TITLE 42—THE PUBLIC HEALTH AND WELFARE, CHAPTER 6A—PUBLIC HEALTH SERVICE, SUBCHAPTER XVII—BLOCK GRANTS, Part B—Block Grants Regarding Mental Health and Substance Abuse, Subpart i—Block Grants for Community Mental Health Services, Section 300x-2—Certain Agreements

- (a) Allocation for systems of integrated services for children
 - (1) In general

With respect to children with a serious emotional disturbance, a funding agreement for a grant under section 300x of this title is that—

- (A) in the case of a grant for fiscal year 1993, the State involved will expend not less than 10 percent of the grant to increase (relative to fiscal year 1992) funding for the system of integrated services described in section 300x-1(b)(9)(1) of this title;
- (B) in the case of a grant for fiscal year 1994, the State will expend not less than 10 percent of the grant to increase (relative to fiscal year 1993) funding for such a system; and
- (C) in the case of a grant for any subsequent fiscal year, the State will expend for such a system not less than an amount equal to the amount expended by the State for fiscal year 1994.
- (2) Waiver
 - (A) Upon the request of a State, the Secretary may provide to the State a waiver of all or part of the requirement established in paragraph (1) if the Secretary determines that the State is providing an adequate level of comprehensive community mental health services for children with a serious emotional disturbance, (2) as indicated by a comparison of the number of such children for which such services are sought with the availability in the State of the services.
 - (B) The Secretary shall approve or deny a request for a waiver under subparagraph (A) not later than 120 days after the date on which the request is made.
 - (C) Any waiver provided by the Secretary under subparagraph (A) shall be applicable only to the fiscal year involved.

TITLE 42—THE PUBLIC HEALTH AND WELFARE, CHAPTER 6A—PUBLIC HEALTH SERVICE, SUBCHAPTER XVII—BLOCK GRANTS, Part B—Block Grants Regarding Mental Health and Substance Abuse, Subpart i—Block Grants for Community Mental Health Services, Section 300x-4—Additional Provisions

- (b) Maintenance of effort regarding State expenditures for Mental Health
 - (1) In general

A funding agreement for a grant under section 300x of this title is that the State involved will maintain State expenditures for community mental health services at a level that is not less than the average level of such expenditures maintained by the State for the 2-year period preceding the fiscal year for which the State is applying for the grant.

(2) Exclusion of certain funds

The Secretary may exclude from the aggregate State expenditures under subsection (a) of this section, funds appropriated to the principal agency for authorized activities which are of a non-recurring nature and for a specific purpose.

(3) Waiver

The Secretary may, upon the request of a State, waive the requirement established in paragraph (1) if the Secretary determines that extraordinary economic conditions in the State justify the waiver.

DEPARTMENT OF HEALTH AND HUMAN SERVICES

Federal Register Vol. 66, No. 130 (July 6, 2001), contains a notice from the Substance Abuse and Mental Health Service Administration (SAMHSA) executive officer specifying that states are required as a condition of receipt of funds to maintain State expenditures for community based mental health services for adults with serious mental illness (SMI) and children with serious emotional disturbance (SED) at a level that was equal to the average expenditures for such purposes over the previous two years. The federal register also stated that the Secretary, as a matter within his discretion, had the authority to exclude from the calculation of the maintenance of effort "funds appropriated to the principal agency for authorized activities which are of a non-recurring nature and for a specific purpose."

Condition

In our audit reports for fiscal years 2006–07 through 2009–10, we reported that Mental Health needs to refine its process for complying with the MOE requirements. Specifically, Mental Health did not provide documentation to support the percentages it applied against the total of managed care and realignment expenditures to arrive at the amount it reported as expenditures for children with SED. Additionally, for the MOE requirement related to the State's expenditures for community mental health services, Mental Health did not report all state expenditures for adults with SMI and children with SED. Specifically, it did not include any expenditures from the Mental Health Services Act, and it could not positively state whether other state agencies fund community mental health programs for adults with SMI or children with SED. Moreover, Mental Health was unable to provide documentation that showed the components and expenditures used to generate the fiscal year 1994–95 expenditure threshold of \$160 million.

During our follow-up procedures for fiscal year 2010-11, we found that Mental Health still has not implemented a process to comply with the MOE requirements. Specifically, all of the conditions that we reported for fiscal years 2006–07 through 2009–10 continued to exist during fiscal year 2010–11. However, although Mental Health did not implement corrective actions during fiscal year 2010–11, it did take steps to better ensure its compliance for future years. For example, Mental Health developed a methodology for determining the percentages to apply against managed care as part of determining the amount it reports as expenditures for children with SED. Mental Health also indicated that it is researching alternatives to determine the percentage it uses to support the realignment dollars used in its MOE calculation, and stated that it would implement these new methodologies in fiscal year 2011–12. Mental Health further stated that it requested guidance from its community services division on the reporting of all state expenditures for adults with SMI and children with SED. Specifically, it is determining the Mental Health Services Act expenditures that should be included in its MOE calculation. Finally, although Mental Health still has not located documentation to support its fiscal year 1994–95 expenditure threshold of \$160 million, beginning with the 2012 federal block grant award, program changes will allow Mental Health to use state fiscal year 2008–09 as the new expenditure threshold for its allocation to systems of integrated services for children. According to Mental Health, this should resolve the issue for future years.

Questioned Costs

No specific questioned costs identified.

Recommendations

Mental Health should finalize and implement its methods to determine the percentages used to support the realignment dollars used in its MOE calculation and retain the supporting documentation. Mental Health also should finalize a methodology for calculating the community mental health services MOE requirement to ensure that it accurately captures and reports all state expenditures for adults with SMI and children with SED.

Department's View and Corrective Action Plan

Mental Health agrees with the finding. Mental Health plans to continue its efforts to develop a methodology to determine the dollar amount expended on approved actual claims for realignment, and will retain the supporting documentation. After the methodology for realignment is finalized and implemented, Mental Health will update and implement its methodology for calculating the community mental health services MOE requirement to accurately capture and report all state expenditures for adults with SMI and children with SED only.

Reference Number: 2011-7-7

Federal Catalog Number: 93.568

Federal Program Title: Low-Income Home Energy Assistance Program

(LIHEAP)

Federal Award Numbers and Years: G-11B1CALIEA; 2011

G-10B1CALIEA; 2010 G-09B1CALIEA; 2009 G-08B1CALIEA; 2008 G-07B1CALIEA; 2007 G-06B1CALIEA; 2006

Category of Finding: Earmarking

State Administering Department: Department of Community Services and

Development (CSD)

Criteria

TITLE 42—THE PUBLIC HEALTH AND WELFARE—CHAPTER 94—LOW-INCOME ENERGY ASSISTANCE, Subchapter II—Low-Income Home Energy Assistance, Section 8624—Application and Requirements

(b) Certifications required for covered activities

As part of the annual application required by subsection (a) of this section, the chief executive officer of each State shall certify that the State agrees to—

- (9) provide that—
 - (A) the State may use for planning and administering the use of funds under this subchapter an amount not to exceed 10 percent of the funds payable to such State under this subchapter for a fiscal year; and
 - (B) the State will pay from non-Federal sources the remaining costs of planning and administering the program assisted under this subchapter and will not use Federal funds for such remaining costs (except for the costs of the activities described in paragraph (16));

(16) use up to 5 percent of such funds, at its option, to provide services that encourage and enable households to reduce their home energy needs and thereby the need for energy assistance, including needs assessments, counseling, and assistance with energy vendors, and report to the Secretary concerning the impact of such activities on the number of households served, the level of direct benefits provided to those households, and the number of households that remain unserved.

TITLE 45—PUBLIC WELFARE, PART 96—BLOCK GRANTS, Subpart C—Financial Management, Section 96.30—Fiscal and Administrative Requirements

- (a) Fiscal control and accounting procedures. Except where otherwise required by Federal law or regulation, a State shall obligate and expend block grant funds in accordance with the laws and procedures applicable to the obligation and expenditure of its own funds. Fiscal control and accounting procedures must be sufficient to:
 - (a) permit preparation of reports required by the statute authorizing the block grant and
 - (b) permit the tracing of funds to a level of expenditure adequate to establish that such funds have not been used in violation of the restrictions and prohibitions of the statute authorizing the block grant.

Condition

CSD continues to lack sufficient internal controls to ensure that it meets earmarking requirements. Specifically, although CSD implemented a mechanism to track expenditures related to one of its earmarking requirements, it still does not track expenditures related to two others. As we reported in our last two annual audits, CSD's accounting records did not segregate administrative expenditures claimed by subrecipients, which would allow CSD to ensure that total administrative costs do not exceed the maximum 10 percent allowed. Similarly, its accounting records did not segregate amounts spent for "energy need reduction services," which would allow CSD to ensure that these costs do not exceed 5 percent of its LIHEAP funding. CSD planned to track earmarking requirements by assigning a specific code to earmarked dollars in its accounting system by June 2011. However, according to the deputy director for administrative services, currently CSD does not expect to implement this process until January 2012. Because it does not have a mechanism in place to track final LIHEAP expenditures related to the earmarking requirements, CSD cannot reasonably assure that the earmarking requirements have been met.

Questioned Costs

No specific questioned costs identified.

Recommendation

CSD should develop and implement sufficient internal controls to ensure that it can effectively track and monitor its progress toward meeting all of its earmarking requirements.

Department's View And Corrective Action Plan

CSD concurs with the recommendation. In January 2012 CSD implemented the automated tracking system for LIHEAP earmarks in the Expenditure Activity Reporting System.

Reference Number: 2011-12-7

Federal Catalog Number: 93.568

Federal Program Title: Low-Income Home Energy Assistance Program

(LIHEAP)

Federal Award Numbers and Years: G-11B1CALIEA; 2011

G-09B1CALIEA; 2009 G-09B1CALIE2; 2009 G-08B1CALIEA; 2008 G-07B1CALIEA; 2007 G-06B1CALIEA; 2006

Category of Finding: Reporting

State Administering Department: Department of Community Services and

Development (CSD)

Criteria

TITLE 45—PUBLIC WELFARE, PART 96—BLOCK GRANTS, Subpart C—Financial Management, Section 96.30—Fiscal and Administrative Requirements

- (b) Financial summary of obligation and expenditure of block grant funds—
 - (2) Block grants containing time limits on obligation of funds. After the close of each statutory period for the obligation of block grant funds, each grantee shall report to the Department:
 - (i) Total funds obligated by the grantee during the applicable statutory period; and
 - (ii) The date of the last obligation.
 - (4) Submission of information. Grantees shall submit the information required by paragraph (b)(1), (2), and (3) of this section on OMB standard form 269A, Financial Status Report (short form). Grantees are to provide the requested information within 90 days of the close of the applicable statutory grant periods.

Financial Status Report (Short Form) – SF-269A, Instructions

Total Outlays. Enter total program outlays less any rebates, refunds, or other credits. For reports prepared on a cash basis, outlays are the sum of actual cash disbursements for direct costs for goods and services, the amount of indirect expense charged, the value of in-kind contributions applied, and the amount of cash advances and payments made to subrecipients. For reports prepared on an accrual basis, outlays are the sum of actual cash disbursements for direct charges for goods and services, the amount of indirect expense incurred, the value of in-kind contributions applied, and the net increase or decrease in the amounts owed by the recipient for goods and other property received, for services performed by employees, contractors, subgrantees and other payees, and other amounts becoming owed under programs for which no current services or performances are required, such as annuities, insurance claims, and other benefit payments

TITLE 2—GRANTS and agreements, part 170—Reporting subaward and executive information compensation, Appendix A to Part 170—Award Term

- (a) Reporting of first-tier subawards.
 - (1) Applicability. Unless you are exempt as provided in paragraph d. of this award term, you must report each action that obligates \$25,000 or more in Federal funds that does not include Recovery funds (as defined in section 1512(a)(2) of the American Recovery and Reinvestment Act of 2009, Pub. L. 111-5) for a subaward to an entity (see definitions in paragraph e. of this award term),

Condition

CSD continues to lack sufficient internal controls to ensure that it meets reporting requirements. Specifically, as we reported in our last two annual audits, CSD's procedures did not include steps to reconcile the federal share of program outlays shown in its internally developed spreadsheets to

its accounting records. It uses these spreadsheets to prepare its financial status reports. Although CSD implemented such a process in July 2010, it did not retroactively reconcile the expenditures it reported in prior quarterly reports. Because CSD carries forward the cumulative expenditures it previously reported as part of the federal share of program outlay, we could not determine whether the total federal share of program outlay it reported for fiscal year 2010–11 was supported by its accounting records. By failing to reconcile the amounts in its internally developed spreadsheets to its accounting records for all amounts included in the federal share of program outlays, CSD has less assurance that its financial status reports are accurate.

In addition, CSD did not comply with an additional reporting requirement for the 2011 LIHEAP grant. Specifically, although CSD approved subawards greater than \$25,000 from its 2011 LIHEAP grant, it failed to report these subawards to the Federal Funding Accountability Transparency Act Subaward Reporting System as required. CSD stated that it was not aware of this requirement until we brought it to its attention.

Questioned Costs

No specific questioned costs identified.

Recommendations

CSD should reconcile the federal share of program outlays included in its internally developed spreadsheets to its accounting records for those expenditures it included in financial status reports prior to July 2010. In addition, CSD should ensure that it posts subawards greater than \$25,000 to the Federal Funding Accountability Transparency Act Subaward Reporting System as required.

Department's View And Corrective Action Plan

CSD concurs with the recommendations.

CSD will reconcile the federal share of program outlays included in its internally developed spreadsheets to accounting records for expenditures included in financial status reports prior to July 2010.

CSD has been working with the Federal Department of Health and Human Services, Administration for Children and Families (ACF), to post subawards greater than \$25,000 to the Federal Funding Accountability Transparency Act Subaward Reporting System. CSD contacted ACF in November of 2011 to report that the grants issued to CSD were not appearing in the federal reporting engine for CSD to report against our 2011 and 2012 LIHEAP grants. After a lengthy discussion, it was discovered that ACF had not entered CSD's DUNS numbers into the reporting system, which then made it so that CSD could not report.

The problem was resolved, but due to the fact that ACF only uploads to the federal reporting system every two weeks, it would be mid-December 2011 before CSD would have grants to report against. As of December 9, the 2012 LIHEAP grant was available to report against, however CSD had not issued contracts against this grant at that time.

The 2011 LIHEAP grant did not populate in the system, and after further discussions with ACF it was discovered that ACF would have to utilize its information technology staff to resolve this problem. This was discovered in January 2012, and it will be February 2012 before the 2011 grant has populated the reporting engine for CSD to report the 2011 LIHEAP contracts. At that time, all 2011 LIHEAP contracts will be entered into the system, and the 2012 contracts will be entered as they are issued to the contractors.

Reference Number: 2011-13-12

Federal Catalog Number: 93.658

Federal Program Title: Foster Care—Title IV-E

Federal Award Numbers and Years: 1101CA1404; 2011

1101CA1401; 2011

Category of Finding: Subrecipient Monitoring

State Administering Department: Department of Social Services (Social Services)

Criteria

U.S. OFFICE OF MANAGEMENT AND BUDGET CIRCULAR A-133, *AUDITS OF STATES, LOCAL GOVERNMENTS, AND NONPROFIT ORGANIZATIONS* (OMB CIRCULAR A-133), Subpart D—Federal Agencies and Pass-Through Entities, Section .400—Responsibilities

- (d) Pass-through entity responsibilities. A pass-through entity shall perform the following for the Federal awards it makes:
 - (3) Monitor the activities of subrecipients as necessary to ensure that Federal awards are used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.

TITLE 45—PUBLIC WELFARE, PART 92—UNIFORM ADMINISTRATIVE REQUIREMENTS FOR GRANTS AND COOPERATIVE AGREEMENTS TO STATE, LOCAL, AND TRIBAL GOVERNMENTS, Section 92.40, Monitoring and Reporting Program Performance

(a) Monitoring by grantees. Grantees are responsible for managing the day-to-day operations of grant and subgrant supported activities. Grantees must monitor grant and subgrant supported activities to assure compliance with applicable Federal requirements and that performance goals are being achieved. Grantee monitoring must cover each program, function or activity.

Condition

Social Services did not follow its procedures to ensure that counties addressed issues identified during on-site reviews. Specifically, Social Services contracts with the Judicial Council of California (Judicial Council) to provide a variety of services that includes conducting a review of the counties' juvenile court procedures to ensure compliance with Title IV-E of the Social Security Act. After completing an on-site review, the Judicial Council prepares a report with recommendations, which it provides to both Social Services and the applicable county. Social Services' procedures require it to contact the county by letter to offer the county its assistance in addressing the recommendations and to monitor the county's progress in doing so.

During the current year, however, we found that Social Services did not issue letters to the 23 counties that Judicial Council reviewed nor did it perform any other follow-up procedures related to Judicial Council's recommendations. Social Services indicated that it did not issue the letters because of staff turnover in the position responsible for this task. When Social Services does not follow-up on the recommendations made by its contractor, it cannot ensure that the counties are taking appropriate and timely action to correct the deficiencies identify during these on-site reviews.

Ouestioned Costs

No specific questioned costs identified.

Recommendation

Social Services should follow its procedures to promptly communicate with the counties about Judicial Council's recommendations and monitor the progress of the counties to implement them.

Department's View and Corrective Action Plan

The California Department of Social Services (CDSS) concurs and has fully corrected the issue on December 23, 2011. The CDSS has issued all applicable Judicial Review and Technical Assistance Project (JRTA) Site Visits letters to the applicable counties which address the results of on-site reviews for fiscal year 2010–11. This ongoing responsibility now is assigned to a specific existing staff person to ensure timely and consistent compliance.

Reference Number: 2011-13-13

Category of Finding: Subrecipient Monitoring

State Administering Department: Department of Aging (Aging)

Federal Catalog Number: 93.044

Federal Program Title: Special Programs for the Aging—Title III,

Part B—Grants for Supportive Services and

Senior Centers

Federal Award Numbers and Years: 11AACAT3SP; 2011

10AACAT3SP; 2010

Federal Catalog Number: 93.045

Federal Program Title: Special Programs for the Aging—Title III,

Part C—Nutrition Services

Federal Award Numbers and Years: 11AACAT3SP; 2011

10AACAT3SP; 2010

Federal Catalog Number: 93.053

Federal Program Title: Nutrition Services Incentive Program

Federal Award Numbers and Years: 11AACANSIP; 2011

10AACANSIP; 2010

Federal Catalog Number: 93.705

Federal Program Title: ARRA—Aging Home-Delivered Nutrition

Services for States

Federal Award Number and Year: 09AACAC2RR; 2009

Federal Catalog Number: 93.707

Federal Program Title: ARRA—Aging Congregate Nutrition Services

for States

Federal Award Number and Year: 09AACAC1RR; 2009

Criteria

U.S. OFFICE OF MANAGEMENT AND BUDGET CIRCULAR A133, *AUDITS OF STATES, LOCAL GOVERNMENTS, AND NONPROFIT ORGANIZATIONS* (OMB CIRCULAR A133), Subpart D—Federal Agencies and Pass-Through Entities, Section .400—Responsibilities

- (d) Pass-through entity responsibilities. A pass-through entity shall perform the following for the Federal awards it makes:
 - (3) Monitor the activities of subrecipients as necessary to ensure that Federal awards are used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.

TITLE 45—PUBLIC WELFARE, SUBTITLE A—DEPARTMENT OF HEALTH AND HUMAN SERVICES, PART 92—UNIFORM ADMINISTRATIVE REQUIREMENTS FOR GRANTS AND COOPERATIVE AGREEMENTS TO STATE, LOCAL, AND TRIBAL GOVERNMENTS, Subpart C—Post-Award Requirements, Section 92.40—Monitoring and Reporting Program Performance

(a) Monitoring by grantees. Grantees are responsible for managing the day-to-day operations of grant and subgrant supported activities. Grantees must monitor grant and subgrant supported activities to assure compliance with applicable Federal requirements and that performance goals are being achieved. Grantee monitoring must cover each program, function or activity.

Condition

During our current review, we found that Aging still is not ensuring that its subgrantees promptly address issues identified during its onsite assessments. Aging's policy requires its program staff to conduct onsite comprehensive assessments of each subgrantee every four years, as resources permit. As part of this assessment process, Aging requires its staff to issue their final reports to the subgrantees 75 working days after the exit conference it holds at the conclusion of the on-site visit. The subgrantees then have 30 working days to respond to the final report. During fiscal year 2010–11, Aging completed seven comprehensive assessments and held the related exit conferences. Our review of these seven assessments found that Aging did not issue its final reports within 75 working days of the respective exit conference for six of them. Specifically, Aging issued four reports between four days and five months beyond the 75-working-day deadline and, as of September 21, 2011, it had not yet issued the remaining two reports, which at that time exceeded the deadline by roughly four months and six months, respectively. According to the deputy director of Aging's Long-Term Care and Aging Services Division, Aging did not complete these final reports by their due dates because of staffing shortages. Moreover, two of the five subgrantees that received Aging's final report did not submit their responses to Aging within the 30-working-day requirement—one submitted its response two working days late and the other had not yet submitted the response as of September 21, 2011, nearly a month after it was due. When Aging does not issue its final reports on time and does not ensure that subgrantees submit their responses by the required deadlines, it cannot ensure that its subgrantees promptly address the issues identified during its onsite assessments.

Questioned Costs

No specific questioned costs identified.

Recommendations

Aging should ensure that it complies with its 75-working-day requirement for issuing final reports for all onsite comprehensive assessments it performs annually and ensure that subgrantees respond to its final reports within the required 30-working-days.

Department's View and Corrective Action Plan

Aging will immediately ensure staff are following its written procedures dated April 22, 2011, for "Monitoring Award Activities of Sub-Recipients." In addition, Aging will add due dates and internal staff roles and responsibilities to ensure that 1) Aging issues final reports for all on-site comprehensive assessments within 75 working days of the exit conference and, 2) takes steps to ensure subgrantees respond to final on-site comprehensive assessment reports within 30 working days of their receipt. By December 30, 2011, Aging will update its "Monitoring Award Activities of Sub-Recipients" procedures to document these revisions.

Reference Number: 2011-13-16

Federal Catalog Number: 93.568

Federal Program Title: Low-Income Home Energy Assistance Program

(LIHEAP)

Federal Award Numbers and Years: G-11B1CALIEA; 2011

G-10B1CALIEA; 2010 G-1001CALIE2; 2010 G-09B1CALIEA; 2009 G-0901CALIE2; 2009 G-08B1CALIEA; 2008 G-07B1CALIEA; 2007 G-06B1CALIEA; 2006

Category of Finding: Subrecipient Monitoring

State Administering Department: Department of Community Services and

Development (CSD)

Criteria

TITLE 2—GRANTS AND AGREEMENTS, PART 25—UNIVERSAL IDENTIFIER AND CENTRAL CONTRACTOR REGISTRATION, Appendix A to Part 25—Award Term

- I. Central Contractor Registration and Universal Identifier Requirements
- B. Requirement for Data Universal Numbering System (DUNS) Numbers

If you are authorized to make subawards under this award, you:

- 1. Must notify potential subrecipients that no entity (see definition in paragraph C of this award term) may receive a subaward from you unless the entity has provided its DUNS number to you.
- 2. May not make a subaward to an entity unless the entity has provided its DUNS number to you.

C. Definitions

For the purpose of this award term:

- 3. Entity, as it is used in this award term, means all of the following, as defined at 2 CFR part 25, subpart C:
 - a. A governmental organization, which is a State, local government, or Indian Tribe;
 - b. A foreign public entity;
 - c. A domestic or foreign nonprofit organization;

- d. A domestic or foreign for-profit organization; and
- e. A federal agency, but only as a subrecipient under an award or subaward to a non-federal entity.

Condition

Although required by federal law, CSD did not ensure that its subrecipients obtained DUNS numbers before providing them LIHEAP funds. CSD indicated that it was unaware of these requirements, and, as such, it did not implement a process to inform its subrecipients of the requirement or ensure their adherence to it. By not ensuring that its subrecipients have a DUNS number, CSD risks having the federal award agency revoke all, or part, of its LIHEAP award. CSD stated that it is in the process of adding language in its contracts to comply with this requirement.

Questioned Costs

No specific questioned costs identified.

Recommendations

CSD should implement a process to ensure that it informs potential subrecipients that they must obtain a DUNS number, and it should ensure that they have done so before approving their subaward for LIHEAP funds.

Department's View And Corrective Action Plan

CSD concurs with the recommendation. CSD has included language in the 2012 LIHEAP contract that states as follows:

"Pursuant to the Federal Funding Accountability and Transparency Act reporting requirements (2 CFR 170) CSD is required to report information regarding Contractors (sub-awardees) receiving LIHEAP funds. To assist CSD in ensuring timely compliance with these reporting requirements, Contractor shall provide to CSD its DUN & Bradstreet Data Universal Numbering System (DUNS) number, and Central Contractor Registration (CCR) number on the LIHEAP Agency Priority Plan in Exhibit H."

CSD is now collecting DUNS numbers for all LIHEAP agencies as indicated above via the LIHEAP Agency Priority Plan. The Contracts unit is keeping a spreadsheet of the DUNS and CCR numbers as provided to us with the returned contracts.

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U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES U.S. DEPARTMENT OF ENERGY

Reference Number: 2011-3-2

Category of Finding: Cash Management

State Administering Department: Department of Community Services and

Development (CSD)

Federal Catalog Number: 81.042

Federal Program Title: Weatherization Assistance for Low-Income

Persons (Weatherization) Program

Federal Award Numbers and Years: DE-FG26-06R021678; 2009

DE-EE0000180; 2009

Federal Catalog Number: 93.568

Federal Program Title: Low-Income Home Energy Assistance Program

(LIHEAP)

Federal Award Numbers and Years: G-11B1CALIEA; 2011

G-10B1CALIEA; 2010 G-1001CALIE2; 2010 G-09B1CALIEA; 2009 G-0901CALIE2; 2009 G-08B1CALIEA; 2008 G-07B1CALIEA; 2007 G-06B1CALIEA; 2006

Criteria

TITLE 10—ENERGY, PART 600—FINANCIAL ASSISTANCE RULES, Subpart C—Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments, Section 600.220—Standards for Financial Management Systems

- (a) A State must expend and account for grant funds in accordance with State laws and procedures for expending and accounting for its own funds. Fiscal control and accounting procedures for the State, as well as its subrecipients and cost-type contractors, must be sufficient to:
 - (1) permit preparation of reports required by this part and the statutes authorizing the grant, and
 - (2) permit the tracing of funds to a level of expenditures adequate to establish that such funds have not been used in violation of the restrictions and prohibitions of applicable statutes.
- (b)(3) Internal control. Effective control and accountability must be maintained for all grant and subgrant cash, real and personal property, and other assets. Grantees and subgrantees must adequately safeguard all such property and must assure that it is used solely for authorized purposes.

TITLE 45—HEALTH AND HUMAN SERVICES, PART 96—BLOCK GRANTS, Subpart C—Financial Management, Section 96.30—Fiscal and Administrative Requirements

(a) Fiscal control and accounting procedures. Except where otherwise required by Federal law or regulation, a State shall obligate and expend block grant funds in accordance with the laws and procedures applicable to the obligation and expenditure of its own funds. Fiscal control and accounting procedures must be sufficient to:

- (a) permit preparation of reports required by the statute authorizing the block grant and
- (b) permit the tracing of funds to a level of expenditure adequate to establish that such funds have not been used in violation of the restrictions and prohibitions of the statute authorizing the block grant.

TITLE 10—ENERGY, PART 600—FINANCIAL ASSISTANCE RULES, Subpart B—Uniform Administrative Requirements for Grants and Cooperative Agreements With Institutions of Higher Education, Hospitals, and Other Non-Profit Organizations, Post-Award Requirements, Section 600.122—Payment

- (i)(2) Advances of Federal funds shall be deposited and maintained in insured accounts whenever possible.
- (l) For those entities where CMIA and its implementing regulations do not apply, interest earned on Federal advances deposited in interest bearing accounts shall be remitted annually to the HHS Payment Management System through an electronic medium such as the FEDWIRE Deposit system. Recipients which do not have this capability should use a check. The address is the Department of Health and Human Services, Payment Management System, P.O. Box 6021, Rockville, MD 20852. Interest amounts up to \$250 per year may be retained by the recipient for administrative expense. State universities and hospitals shall comply with CMIA, as it pertains to interest. If an entity subject to CMIA uses its own funds to pay pre-award costs for discretionary awards without prior written approval from the Federal awarding agency, it waives its right to recover the interest under CMIA.

TITLE 10—ENERGY, PART 600—FINANCIAL ASSISTANCE RULES, Subpart C—Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments, Post-Award Requirements, Section 600.221—Payment

(i) Interest earned on advances. Unless there are statutory provisions to the contrary, grantees and subgrantees shall promptly, but at least quarterly, remit to the Federal agency interest earned on advances. The grantee or subgrantee may keep interest amounts up to \$100 per year for administrative expenses.

TITLE 42—THE PUBLIC HEALTH AND WELFARE—CHAPTER 94—LOW-INCOME ENERGY ASSISTANCE, Subchapter II—Low-Income Home Energy Assistance, Section 8624—Application and Requirements

(d) Expending funds
The State shall expend funds in accordance with the State plan under this subchapter or in accordance with revisions applicable to such plan.

Condition

CSD does not always follow its policies when advancing cash to subrecipients using federal funds. A fundamental element of internal control is the separation of duties so that one individual cannot perpetuate and conceal errors and irregularities in the normal course of his or her duties. Strong internal controls require the segregation of responsibilities for authorizing transactions, physical custody of assets and the related record keeping. CSD's policies require accounting staff to process payment requests and to prepare requests for drawdown of federal funds and it requires the accounting administrator to review and approve the payment and the drawdown documents. However, for one of 16 cash advance payments to subrecipients that we reviewed, the same individual had approved all phases of the payment process, including the subrecipient's request for an advance, the claim schedule to pay the advance, the drawdown of federal funds, and the remittance advice to the State Controller's Office (SCO). CSD indicated that this occurred because of demands placed on its resources while it was developing procedures to implement a new policy for advancing cash to its subrecipients.

We also found that CSD's controls over its cash advances to subrecipients are not adequate to ensure that it complies with federal requirements. Specifically, during fiscal year 2010–11, CSD provided \$17 million in cash advances to Weatherization program subrecipients and \$20 million in cash advances to LIHEAP subrecipients for a total of \$37 million. Although CSD's contracts with its subrecipients contain clauses requiring them to deposit its advances in interest-bearing accounts, CSD does not verify whether its subrecipients comply with this requirement. Additionally, although CSD indicated that when a contract expires it requires subrecipient to submit a closeout report that includes a summary of interest they have earned, CSD does not verify whether its subrecipients returned the interest quarterly to the federal government as required by federal regulations for the Weatherization program. Additionally, although the state plan for LIHEAP requires that CSD's subrecipients use the interest earned on cash advances for only specified activities including those that are allowable under LIHEAP, CSD does not verify that they used their interest earnings for those purposes. As a result, CSD's subrecipients may use the interest earned on federal program advances for activities that may not be allowable.

Questioned Costs

No specific questioned costs identified.

Recommendations

CSD should ensure that its staff follow procedures that are in place to provide adequate separation of duties. Additionally, CSD should develop and implement procedures to verify that subrecipients are depositing cash advances into interest-bearing accounts. It should further ensure that subrecipients are returning excess interest they earn from Weatherization program cash advances to the federal government and that they are spending the interest earned from LIHEAP cash advances in accordance with program requirements.

Department's View and Corrective Action Plan

CSD concurs with the recommendations. CSD will remind accounting staff of the importance of adhering to the separation of duties policy when advancing cash to subrecipients and will implement a supervisory review of the cash advance payment process. Additionally, CSD will develop and implement procedures as part of the on-site monitoring review protocol to verify that subrecipients deposit cash advances into interest-bearing accounts and comply with the federal requirements for returning or using excess interest earnings as appropriate.

Reference Number: 2011-13-17

Category of Finding: Subrecipient Monitoring

State Administering Department: Department of Community Services and

Development (CSD)

Federal Catalog Number: 81.042

Federal Program Title: Weather Assistance for Low-Income Persons

(Weatherization) program

Federal Award Number and Year: DE-FG26-06R021678; 2009

Federal Catalog Number: 93.568

Federal Program Title: Low-Income Home Energy Assistance Program

(LIHEAP)

Federal Award Numbers and Years: G-11B1CALIEA; 2011

G-10B1CALIEA; 2010 G-1001CALIE2; 2010 G-09B1CALIEA; 2009 G-0901CALIE2; 2009 G-08B1CALIEA; 2008 G-07B1CALIEA; 2007 G-06B1CALIEA; 2006

Criteria

TITLE 10—ENERGY, PART 600—FINANCIAL ASSISTANCE RULES, SUBPART C—UNIFORM ADMINISTRATIVE REQUIREMENTS FOR GRANTS AND COOPERATIVE AGREEMENTS TO STATE AND LOCAL GOVERNMENTS, POST, Section 600.240—Monitoring and Reporting Program Performance

(a) Monitoring by grantees. Grantees are responsible for managing the day-to-day operations of grant and subgrant supported activities. Grantees must monitor grant and subgrant supported activities to assure compliance with applicable Federal requirements and that performance goals are being achieved. Grantee monitoring must cover each program, function or activity.

TITLE 45—PUBLIC WELFARE, PART 92—UNIFORM ADMINISTRATIVE REQUIREMENTS FOR GRANTS AND COOPERATIVE AGREEMENTS TO STATE, LOCAL, AND TRIBAL GOVERNMENTS, Section 92.40—Monitoring and Reporting Program Performance

(a) Monitoring by grantees. Grantees are responsible for managing the day—to—day operations of grant and subgrant supported activities. Grantees must monitor grant and subgrant supported activities to assure compliance with applicable Federal requirements and that performance goals are being achieved. Grantee monitoring must cover each program, function or activity.

Condition

CSD did not always follow the monitoring policies it has in place to ensure that its subrecipients are expending the Weatherization program and LIHEAP funds appropriately. CSD's policy requires that its staff perform an Agency Quarterly Assessment (assessment) for its Weatherization program and LIHEAP subrecipients. During the assessment CSD is required to review a subrecipient's expenditures to evaluate if the subrecipient is in compliance with certain requirements, including whether it is spending its funds for allowable purposes and by established deadlines. If CSD identifies any issues during these assessments, it then takes certain steps to resolve the issue with the subrecipient. Upon completion of the assessment, a supervisor reviews the assessment and signs a routing slip indicating supervisory review has occurred.

We selected 18 assessments to review specifically for the Weatherization program and found that CSD failed to include a review of the Weatherization program for four of them. We also found that it performed one of these assessments nine months late and it could not provide evidence that it had taken steps to work with the subrecipient to resolve the issues it identified during this assessment. Finally, two of the completed assessments lacked evidence of supervisory review. Similarly, we selected 18 assessments to review for LIHEAP and found that it could not provide evidence that CSD had taken steps to work with the subrecipients to resolve issues identified during two assessments and two others lacked evidence of supervisory review.

According to CSD, those oversights occurred as the result of staff turnover and the hiring of new staff. Nevertheless, by not completing all of its monitoring activities in accordance with its policies, CSD is unable to ensure that its subrecipients are properly expending Weatherization program and LIHEAP funds.

Questioned Costs

No specific questioned costs identified.

Recommendations

CSD should ensure that it performs all assessments in a timely manner as required by its policies and that it takes steps to resolve expenditure issues found as a result of these assessments. Further, CSD should ensure that all assessments are reviewed by a supervisor.

Department's View And Corrective Action Plan

CSD concurs with the recommendations. CSD will develop and implement a tracking system to ensure assessments are done in a timely manner. Additionally, CSD will implement changes in the assessment review and documentation procedures to ensure timely resolution of expenditure issues and that all assessments are reviewed by a supervisor.

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U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

Reference Number: 2011-12-4

Federal Catalog Number: 14.239

Federal Program Title: HOME Investment Partnerships Program

(HOME Program)

Federal Award Number and Year: M010-SG060100; 2010

Category of Finding: Reporting

State Administering Department: Department of Housing and Community

Development (Housing)

Criteria

U.S. OFFICE OF MANAGEMENT AND BUDGET CIRCULAR A-133, *AUDITS OF STATES, LOCAL GOVERNMENTS, AND NON-PROFIT ORGANIZATIONS* (OMB CIRCULAR A-133), Subpart C—Auditees, Section .310—Financial Statements

- (b) Schedule of expenditures of Federal Awards. The auditee shall also prepare a schedule of expenditures of federal awards for the period covered by the auditee's financial statements. At a minimum, the schedule shall:
 - (3) Provide total Federal awards expended for each individual Federal program and the CFDA number or other identifying number when the CFDA information is not available.

U.S. OFFICE OF MANAGEMENT AND BUDGET CIRCULAR A-133, *AUDITS OF STATES, LOCAL GOVERNMENTS, AND NON-PROFIT ORGANIZATIONS,* (OMB CIRCULAR A-133), Subpart B—Audits, Section .205—Basis for determining Federal awards expended

- (b) <u>Loan and loan guarantees (loans).</u> Since the Federal Government is at risk for loans until the debt is repaid, the following guidelines shall be used to calculate the value of Federal awards expended under loan programs, except as noted in paragraphs (c) and (d) of this section:
 - (1) Value of new loans made or received during the fiscal year; plus
 - (2) Balance of loans from previous years for which the Federal Government imposes continuing compliance requirements; plus
 - (3) Any interest subsidy, cash, or administrative cost allowance received.

Condition

During our audit for fiscal year 2009–10, we found that the Department of Housing and Community Development (HCD) reported to the Department of Finance (Finance) that it had more than \$93 million in outstanding loans under the HOME Program. However, HCD had not yet completed a reconciliation of its accounting records to its loan records at the time it reported this information and, in fact, HCD expected its outstanding loan balance to increase. As a result, the amount included on the Schedule of Federal Assistance was potentially understated. In its corrective action plan, HCD indicated that it would identify the total amount of loans outstanding and complete its reconciliation by May 31, 2011.

During our current audit, we found that HCD has yet to complete the reconciliation of its accounting records to its loan records for the HOME Program. In fact, according to the fiscal and policy manager for the HOME Program, HCD's loan records reflected a balance of \$108.4 million whereas its accounting records reflected a balance of \$111.3 million, a difference of \$2.9 million. Consequently, the amount of outstanding loans HCD reports to Finance for fiscal year 2010–11 may not be accurate. The HOME Program branch chief stated that HCD expects to complete its reconciliation to identify the total amount of outstanding loans by May 31, 2012.

Questioned Costs

No specific questioned costs identified.

Recommendation

Housing should continue with its efforts to identify the total amount of loans outstanding under the HOME Program.

Department's View and Corrective Action Plan

HCD stated that it will complete its reconciliation to identify the total amount of outstanding loans by May 31, 2012. HCD also indicated that over 95 percent of the loans have already been reconciled.

Reference Number: 2011-12-5

Federal Catalog Number: 14.239

Federal Program Title: HOME Investment Partnerships Program

(HOME Program)

Federal Award Numbers and Years: M10-SG060100; 2010

M09-SG060100; 2009 M08-SG060100; 2008 M07-SG060100; 2007 M06-SG060100; 2006

Category of Finding: Reporting

State Administering Department: Department of Housing and Community

Development (HCD)

Criteria

TITLE 24—HOUSING AND URBAN DEVELOPMENT, PART 135—ECONOMIC OPPORTUNITIES FOR LOW- AND VERY LOW-INCOME PERSONS, Subpart A—General Provisions, Section 135.3—Applicability

- (a) Section 3 covered assistance. Section 3 applies to the following HUD assistance (section 3 covered assistance):
 - (2) Housing and community development assistance. Section 3 applies to training, employment, contracting and other economic opportunities arising in connection with the expenditure of housing assistance (including section 8 assistance, and including other housing assistance not administered by the Assistant Secretary of Housing) and community development assistance that is used for the following projects;
 - (i) Housing rehabilitation (including reduction and abatement of lead-based paint hazards, but excluding routine maintenance, repair and replacement);
 - (ii) Housing construction; and
 - (iii) Other public construction.

TITLE 24—HOUSING AND URBAN DEVELOPMENT, PART 135—ECONOMIC OPPORTUNITIES FOR LOW- AND VERY LOW-INCOME PERSONS, Subpart E—Reporting and Recordkeeping, Section 135.90—Reporting

Each recipient which receives directly from HUD financial assistance that is subject to the requirements of this part shall submit to the Assistant Secretary an annual report in such form and with such information as the Assistant Secretary may request, for the purpose of determining the effectiveness of section 3. Where the program providing the section 3 covered assistance requires submission of an annual performance report, the section 3 report will be submitted with that annual performance report. If the program providing the section 3 covered assistance does not require an annual performance report, the section 3 report is to be submitted by January 10 of each year or within 10 days of project completion, whichever is earlier. All reports submitted to HUD in accordance with the requirements of this part will be made available to the public.

Form HUD-60002, Section 3 Summary Report, Economic Opportunities for Low-and Very Low-Income Persons, Instructions

Part II: Contract Opportunities

Block 1: Construction Contracts

Item A: Enter the total dollar amount of all contracts awarded on the project/program.

Block 2: Non-Construction Contracts

Item A: Enter the total dollar amount of all contracts awarded on the project/program.

Condition

HCD did not ensure that the Section 3 Summary Report (summary report) for fiscal year 2009–10 it submitted to the U.S. Department of Housing and Urban Development (HUD) was accurate and complete. Specifically, HCD understated the total dollar amount of construction contracts awarded in the summary report by \$19.3 million, or 35 percent, related to three subgrantees. Additionally, it incorrectly classified construction contracts totaling \$2.0 million as nonconstruction contracts for one of these three subgrantees.

Questioned Costs

No specific questioned costs identified.

Recommendations

HCD should ensure that it accurately compiles contract data submitted by subgrantees in its summary report to HUD. Further, HCD should consult with HUD to determine whether it should submit a corrected summary report for fiscal year 2009–10.

Department's View and Corrective Action Plan

The HOME Program implemented the following corrective improvements during 2011 to ensure the accurate collection and compiling of data and the accuracy of the subsequent 2010–11 fiscal year report submitted to HUD:

- Fields for contractor's names and the execution date were added to the forms.
- Duplicate forms were removed from the submitted reports prior to data entry.
- Errors identified during verification were returned to the original entry staff and verification is repeated once all corrections are complete.
- Management is completing a full verification of each form and line of data entry as well as the final report submitted to HUD.
- Verification of all submitted electronic reports against those approved by staff and entered in spreadsheets was added to the process to eliminate missed reports.

• Adjustments to the programming of the reports that produce the Active Contracts and Section 3 Required Lists were made to ensure inclusion of all contracts.

In addition, HOME management capacity was strengthened when the HOME section Chief position was filled on January 1, 2010. The position had been vacant at the time the 2009–10 report was prepared. The HOME Section Chief will prepare an additional detailed review of the accuracy of the 2011–12 report, and subsequent reports, prior to filing with HUD.

By March 31, 2012, HCD will consult with HUD to determine whether it should submit a corrected summary to report for fiscal year 2009–10.

Reference Number: 2011-13-15

Federal Catalog Number: 14.228

Federal Program Title: Community Development Block Grants,

State's Program (CDBG)

Federal Award Number and Year: B-10-DC-06-0001; 2010

Category of Finding: Subrecipient Monitoring

State Administering Department: Department of Housing and Community

Development (Housing)

Criteria

U.S. OFFICE OF MANAGEMENT AND BUDGET CIRCULAR A-133, *AUDITS OF STATES, LOCAL GOVERNMENTS, AND NON-PROFIT ORGANIZATIONS* (OMB CIRCULAR A-133), Subpart D—Federal Agencies and Pass-Through Entities, Section .400—Responsibilities

- (d) Pass-through entity responsibilities. A pass-through entity shall perform the following for the Federal awards it makes:
 - (3) Monitor the activities of subrecipients as necessary to ensure that Federal awards are used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.

TITLE 24—HOUSING AND URBAN DEVELOPMENT, PART 570—COMMUNITY DEVELOPMENT BLOCK GRANTS, Subpart I—State Community Development Block Grant Program, Section 570.492—State's Reviews and Audits

(a) The state shall make reviews and audits, including on-site reviews, of units of general local government as may be necessary or appropriate to meet the requirements of section 104(e)(2) of the Act.

Condition

During our audit for fiscal year 2009–10, we found that Housing did not complete an adequate number of site visits to ensure that its subrecipients were complying with program requirements. Specifically, Housing completed only 16 of 40 scheduled site visits. We also noted that these site visits were not always focused on projects identified by Housing as having the highest risk. In response to this finding, Housing stated that it will continue to improve its monitoring process. Beginning June 30, 2011, the CDBG section will complete a risk-based review of all active jurisdictions—those who have active contracts—by December 30 of each year to determine the 15 highest risk jurisdictions and monitor them.

March 2012

However, we found that Housing completed only one monitoring site visit in fiscal year 2010–11. Furthermore, it has not yet developed a monitoring schedule based on a completed risk assessment. As a result, Housing cannot ensure that subrecipients are complying with federal laws, regulations, and provisions of grant agreements. According to the CDBG section chief, program staff is in the process of completing a risk-based review of all active jurisdictions to determine the 15 highest risk jurisdictions to be included in the program's monitoring schedule for fiscal year 2011–12. He indicated that Housing plans to complete the 15 monitoring site visits by December 30, 2011.

Questioned Costs

No specific questioned costs identified.

Recommendations

To ensure that it provides adequate monitoring over its subrecipients, Housing should develop and adhere to a site-visit monitoring schedule. To improve the efficiency of its reviews, Housing should continue to focus on performing site visits of projects that pose the highest risk of noncompliance with federal requirements.

Department's View and Corrective Action Plan

The CDBG Section will continue to improve its monitoring process. The CDBG has completed a risk-based review of all active jurisdictions (those who have active contracts) and identified the 15 highest risk jurisdictions. Further, the CDBG Section has developed a Monitoring Schedule and all 15 identified jurisdictions have been scheduled, with the completion of this year's Monitoring Schedule to be done by March 31, 2012. The CDBG Section will follow the same process for the monitoring schedule for calendar year 2012.

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U.S. DEPARTMENT OF JUSTICE

Reference Number: 2011-1-4

Federal Catalog Number: 16.606

Federal Program Title: State Criminal Alien Assistance Program

(SCAAP)

Federal Award Number and Year: 2010-AP-BX-0211; 2010

Category of Finding: Activities Allowed, Allowable Costs

State Administering Department: Department of Corrections and Rehabilitation

(Corrections)

Criteria

TITLE 8—ALIENS AND NATIONALITY, CHAPTER 12—IMMIGRATION AND NATIONALITY, SUBCHAPTER II—IMMIGRATION, Part IV—Inspection, Apprehension, Examination, Exclusion, and Removal, Section 1231—Detention and Removal of Aliens Ordered Removed

(i) Incarceration

- (1) If the chief executive officer of a State (or if appropriate, a political subdivision of the State) exercising authority with respect to the incarceration of an undocumented criminal alien submits a written request to the Attorney General, the Attorney General shall, as determined by the Attorney General—
 - (A) enter into a contractual arrangement which provides for compensation to the State or a political subdivision of the State, as may be appropriate, with respect to the incarceration of the undocumented criminal alien; or
 - (B) take the undocumented criminal alien into the custody of the Federal Government and incarcerate the alien.
- (3) For purposes of this subsection, the term "undocumented criminal alien" means an alien who—
 - (B)(i) entered the United States without inspection or at any time or place other than as designated by the Attorney General;
 - (ii) was the subject of exclusion or deportation proceedings at the time he or she was taken into custody by the State or political subdivision of the State; or
 - (iii) was admitted as a nonimmigrant and at the time he or she was taken into custody by the State or a political subdivision of the State has failed to maintain the nonimmigrant status in which the alien was admitted or to which it was changed under Section 1258 of this title, or to comply with the conditions of any such status.

Condition

In our prior year audit, we reported that Corrections submitted ineligible inmate data in its federal fiscal year 2009 application for SCAAP funding. Specifically, Corrections' application included nearly 2,000 additional records in instances where an inmate had more than one alien registration number for the same incarceration period. We also reported that our review of 29 inmate records that Corrections submitted found that it had information in its files indicating 10 of these inmates were either U.S. citizens or permanent residents. In its corrective action plan for that fiscal year, Corrections stated that it will continue to partner with the U.S. Department of Justice–Bureau of Justice Assistance and the U.S. Immigration and Customs Enforcement to ensure that it is presenting its application in a manner that complies with federal standards.

During our follow-up procedures, Corrections confirmed that it has not revised its procedures for submitting the application for SCAAP funding. It indicated that the U.S. Department of Justice is revising the application process for SCAAP funding and that it is waiting for further directions before changing its application procedures. However, a policy advisor from the U.S. Department of Justice stated that the potential changes in the 2012 SCAAP application will not impact the application process or the grantee certifications, and that inmates should only be reported with a single, correct alien registration number. Because Corrections did not revise its procedures for submitting the federal fiscal year 2010 application for SCAAP funding, it cannot be sure that it did not include ineligible inmate data.

Questioned Costs

No specific questioned costs identified.

Recommendation

Corrections should work with U.S. Immigration and Customs Enforcement to ensure that it submits eligible inmate data in its application for SCAAP funding.

Department's View and Corrective Action Plan

Corrections has initiated contact with the Department of Homeland Security (DHS)/U.S. Immigration and Customs Enforcement (USICE) and has begun discussions to investigate the feasibility for establishing a process for verifying the Corrections' inmate alien numbers prior to the submission for the SCAAP grant application. Corrections hopes to establish a routine process with DHS/USICE to obtain valid inmate alien numbers and citizenship status for all Corrections' inmates. This process will allow Corrections to collect the alien numbers for all inmates and incorporate this data into Corrections' databases. Corrections believes by initiating discussions with DHS/USICE, it is demonstrating due diligence in faithfully completing our submittal of eligible inmate data as prescribed by the guidelines established by the Bureau of Justice Assistance for the SCAAP grant application.

U.S. DEPARTMENT OF LABOR

Reference Number: 2011-1-5

Federal Catalog Numbers: 17.225, 17.258, 17.259, 17.260

Federal Program Title: Unemployment Insurance (UI), Workforce

Investment Act (WIA) Cluster: WIA Adult

Program, WIA Youth Activities, WIA

Dislocated Workers

Federal Award Numbers and Years: UI-21088-11-55-A-6; 2010

UI-19571-10-55-A-6; 2009 AA-20183-10-55-A-6; 2010 AA-18628-09-55-A-6; 2009

Category of Finding: Activities Allowed, Eligibility, Reporting

State Administering Department: Employment Development Department (EDD)

Condition

The Employment Development Department (EDD) had weak general controls over its information systems for fiscal year 2010-11. For details see finding reference number 2011-15-2 in the Internal Control and Compliance Issue Applicable to the Financial Statements and State Requirements section on page 19.

Questioned Costs

No specific questions costs identified.

Reference Number: 2011-14-6

Federal Catalog Number: 17.225

Federal Program Title: Unemployment Insurance (UI)

Federal Award Numbers and Years: UI-21088-11-55-A-6; 2010

UI-19571-10-55-A-6; 2009

Category of Finding: Special Tests and Provisions

State Administering Department: Employment Development Department (EDD)

Criteria

TITLE 2—GRANTS AND AGREEMENTS, PART 176—AWARD TERMS FOR ASSISTANCE AGREEMENTS THAT INCLUDE FUNDS UNDER THE AMERICAN RECOVERY AND REINVESTMENT ACT OF 2009, PUBLIC LAW 111-5, Subpart D—Single Audit Information for Recipients of Recovery Act Funds, Section 176.210—Award term—Recovery Act Transactions listed in the Schedule of Expenditures of Federal Awards and Recipient Responsibilities for Informing Subrecipients.

(a) To maximize the transparency and accountability of funds authorized under the American Recovery and Reinvestment Act of 2009 (Pub. L. 111-5) (Recovery Act) as required by Congress and in accordance with 2 CFR 215.21 "Uniform Administrative Requirements for Grants and Agreements" and OMB Circular A-102 Common Rules provisions, recipients agree to maintain records that identify adequately the source and application of Recovery Act funds.

Condition

In our audit reports for fiscal years 2008–09 and 2009–10, we reported that EDD had not updated its financial management systems to allow it to separately identify and report on Recovery Act funds expended for certain benefits paid under the UI program. Specifically, we found that for fiscal year 2008–09, EDD could not separately identify or report on Recovery Act funds expended for the Emergency Unemployment Compensation (EUC) program or the Federal-State Extended Benefits (Fed-Ed) program. We noted that EDD could identify Recovery Act expenditures for the Federal Additional Compensation (FAC) program because it was entirely funded by the Recovery Act. Similarly, our follow-up procedures for fiscal year 2009–10 revealed that EDD still could not separately identify or report on Recovery Act expenditures for the EUC and Fed-Ed programs. Furthermore, we determined that EDD could no longer separately identify and report on Recovery Act expenditures for the FAC program because it was no longer entirely funded by the Recovery Act. In both fiscal years EDD agreed with our findings and stated that it intended to update its financial management systems. EDD initially hoped to complete the update of its financial management system by March 2010 but later revised the time frame to early 2012.

During our follow-up procedures for fiscal year 2010–11, we confirmed that EDD was still in the process of updating its financial management systems to separately identify and report on Recovery Act funds. OMB's Circular A-133 Compliance Supplement dated March 2011 regarding special tests and provisions for awards with Recovery Act funding, indicates that the financial management system must permit the preparation of required reports and the tracing of funds adequate to establish that funds were used for authorized purposes and allowable costs. Additionally, according to a program letter provided by the U.S. Department of Labor, some unemployment benefit payments should be reported separately as Recovery Act expenditures. However, EDD's financial management systems do not separately identify Recovery Act funds from non–Recovery Act funds.

During fiscal year 2010–11, the UI program expended \$21 billion, which included both Recovery Act and non–Recovery Act funds. Of the several types of unemployment benefit programs, the EUC, Fed–Ed, and FAC programs expended Recovery Act funds. In fiscal year 2010–11 EDD spent \$12.2 billion on these programs. However, since EDD is unable to separately identify Recovery Act funds, it cannot identify what portion of the total expenditures for these three programs were paid for with Recovery Act funds.

As discussed in our 2009–10 audit report, EDD was unable to begin separately identifying Recovery Act funds when planned due to changes in federal legislation that required high-priority modifications in programming related to benefit extensions and payments. At that time, an EDD division chief stated that, in the absence of new federal legislation changing benefit extensions and payments, EDD intended to have the issue fully corrected by early 2012. In July 2011, EDD provided a status report to the U.S. Department of Labor that explained the delays it has experienced as it attempts to reprogram its system to separately identify Recovery Act funds and reiterated its plans to fully correct the finding. In its response, the U.S. Department of Labor indicated that it considered the finding corrected.

However, on August 31, 2011, another division chief stated that EDD's plans to complete the programming changes necessary to separately account for Recovery Act funds by early 2012 have been delayed because of resource and scheduling conflicts and will not be fully implemented until mid-2013. Thus, EDD cannot account for its Recovery Act expenditures for the EUC, Fed-Ed, and FAC programs components separately until that time.

Questioned Costs

No specific questions costs identified.

Recommendation

EDD should continue its efforts to update its financial management systems so that it can separately identify Recovery Act expenditures from non-Recovery Act expenditures.

Department's View and Corrective Action Plan

EDD concurs with the recommendation stated. However, it added that EDD can and has been reporting all the benefits paid by each federal extension. The audit finding pertains to the inability to identify which federal extension payments should be charged to the different federal accounts. Benefits paid to Unemployment Insurance claimants have been accounted for and reported on by EDD.

As discussed in the August 31, 2011 meeting, the work to complete the programming needed to separately identify Recovery Act funds will be prioritized after the database conversion planned for November 2011. In preparation for the conversion, a freeze on all program changes has been implemented from August 15, 2011 through December 15, 2011. When the code freeze is lifted, the department will prioritize the outstanding work, including the report changes.

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U.S. DEPARTMENT OF TRANSPORTATION

Reference Number: 2011-13-14

Federal Catalog Number: 20.205

Federal Program Title: Highway Planning and Construction

Federal Award Numbers and Years: N4520.208; 2011

N4520.207; 2010 N4520.206; 2010 N4510.705; 2009

Category of Finding: Subrecipient Monitoring

State Administering Department: California Department of Transportation

(Caltrans)

Criteria

U.S. OFFICE OF MANAGEMENT AND BUDGET CIRCULAR A-133—AUDITS OF STATES, LOCAL GOVERNMENTS, AND NON-PROFIT ORGANIZATIONS (OMB CIRCULAR A-133), Subpart D—Federal Agencies and Pass-Through Entities, Section .400—Responsibilities

- (d) Pass-through entity responsibilities. A pass-through entity shall perform the following for the Federal awards it makes:
 - (4) Ensure that subrecipients expending \$300,000 (\$500,000 for fiscal years ending after December 31, 2003) or more in Federal awards during the subrecipient's fiscal year have met the audit requirements of this part for that fiscal year.
 - (5) Issue a management decision on audit findings within six months after receipt of the subrecipient's audit report and ensure that the subrecipient takes appropriate and timely corrective action.

U.S. OFFICE OF MANAGEMENT AND BUDGET CIRCULAR A-133—AUDITS OF STATES, LOCAL GOVERNMENTS, AND NON-PROFIT ORGANIZATIONS (OMB CIRCULAR A-133), Subpart B—Audits, Section .225—Sanctions

No audit costs may be charged to Federal awards when audits required by this part have not been made or have been made but not in accordance with this part. In cases of continued inability or unwillingness to have an audit conducted in accordance with this part, Federal agencies and pass-through entities shall take appropriate action using sanctions such as:

- (a) Withholding a percentage of Federal awards until the audit is completed satisfactorily;
- (b) Withholding or disallowing overhead costs;
- (c) Suspending Federal awards until the audit is conducted; or
- (d) Terminating the Federal award.

Condition

Subrecipient Audits

As we reported in fiscal year 2009–10, Caltrans continues to lack internal controls to ensure subrecipients who spent \$500,000 or more during fiscal year 2009–10 submitted audit reports to the federal government as required under OMB Circular A-133. Based on Caltrans' records of the amounts it disbursed to subrecipients, it could have established reasonable expectations as to which subrecipients would need to submit audit reports. In response to the finding reported in our fiscal

year 2009–10 audit report, Caltrans stated it developed written policies and procedures to determine whether subrecipients submit their single audit reports timely and impose sanctions on those that are delinquent.

Although we confirmed that Caltrans developed these policies and procedures, it did not fully implement them. For example, during the fiscal year 2010–11 audit we identified instances where subrecipients receiving \$500,000 or more—and, according to Caltrans' records, in some cases more than \$1 million —did not submit audit reports to the federal government. Specifically, we identified 12 subrecipients (including various cities, counties, and special districts) as having no record of an audit submission to the federal government for fiscal year 2009–10. Subrecipients with a fiscal year ending on June 30, 2010, were required to submit their audit reports to the federal government nine months after the end of the fiscal year, which would have been March 31, 2011. When subrecipients fail to submit audit reports to the federal government, federal agencies miss an opportunity to identify where federal funds might be misspent.

Management Decisions

The failure of subrecipients to submit audit reports also limits Caltrans' ability to review and issue management decisions on potential findings and exercise effective oversight of the Highway Planning and Construction program. To facilitate the State's preparation of management decisions on its subrecipients' audit findings, the State has established a process whereby local governments submit copies of their OMB Circular A-133 audit reports to the State Controller's Office (SCO). According to the *State Administrative Manual*, Section 20070, the SCO distributes a copy of each audit report and corrective action plan to state entities (such as Caltrans) that are affected by the findings, and such state entities follow up on audit findings pertaining to the federal programs they administer. To assist with its responsibilities, Caltrans provides the SCO with an annual listing of all of its subrecipients and the amounts of federal funds they received. Caltrans provided the SCO with the amounts it disbursed to its subrecipients on August 30, 2011. When the SCO receives audit reports from subrecipients, it updates its list to indicate which subrecipients have or have not submitted their audit reports. As of November 15, 2011, the SCO's Web site indicated the following information for certain Caltrans' subrecipients.

- Two subrecipients had either submitted incomplete audit reports, or had not submitted any audit reports, and the SCO was no longer going to follow up with those entities.
- Six subrecipients were classified by the SCO as "exempt" from the audit requirements because they spent less than \$500,000.
- Eight subrecipients were classified by the SCO as "no review" because SCO concluded after reviewing the audit reports that no funds had passed through state entities (such as Caltrans).

Based on our review, the SCO's data—identifying certain subrecipients as having an "exempt" or "no review" status—was in conflict with Caltrans' records that indicated it disbursed \$500,000 or more to these subrecipients. However, despite internal procedures that direct Caltrans staff to notify the SCO of any discrepancies, we determined that during the course of our review Caltrans did not follow up with the SCO to verify that the information was correct.

Questioned Costs

No specific questioned costs identified.

Recommendations

Caltrans should fully implement policies and procedures to ensure that subrecipients promptly submit required audit reports, and impose sanctions on those that do not.

Department's View and Corrective Action Plan

Caltrans indicated that it has further refined its policies and procedures to ensure its subrecipients submit their single audit reports timely. For example, Caltrans indicated it will reconcile the audit submissions on the federal and SCO's Web sites to its own records of subrecipients that received \$500,000 or more and will continue to follow up on and impose sanctions on noncompliant subrecipients.

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U.S. DEPARTMENT OF VETERANS AFFAIRS

Reference Number: 2011-12-6

Federal Catalog Number: 64.114

Federal Program Title: Veterans Housing—Guaranteed and Insured

Loans

Federal Award Number and Year: None; State fiscal year 2010–11

Category of Finding: Reporting

State Administering Department: California Department of Veterans Affairs

(Veterans Affairs)

Criteria

TITLE 38—PENSIONS, BONUSES, AND VETERANS' RELIEF, PART 36—LOAN GUARANTY, Subpart F—Guaranty or Insurance of Loans to Veterans with Electronic Reporting, Section 36.4817—Servicer Reporting Requirements

- (a) Servicers of loans guaranteed by the Secretary shall report the information required by this section to the Secretary electronically. The Secretary shall accept electronic submission from each entity servicing loans guaranteed under 38 U.S.C. Chapter 37 not later than the effective date of this rule.
- (c) Servicers shall report to the Secretary the following specific loan events in accordance with the time frames described for each event. Unless otherwise specified herein, the servicer shall report these events on a monthly basis (i.e., no later than the seventh calendar day of the month following the month in which the event occurred) only for delinquent loans in its portfolio.
 - (7) Electronic Default Notification (EDN)—when the loan becomes at least 61 days delinquent. The servicer shall report this event no later than the seventh calendar day from when the event occurred. The servicer shall report this event only once per default for delinquent loans in its portfolio.
 - (11) Bankruptcy filed—when any owner files a petition under the Bankruptcy Code. The servicer shall report this event no later than the seventh calendar day from when the event occurred. The servicer shall report this event only on delinquent loans in its portfolio, if appropriate, or with the EDN when it is reported.
 - (13) Loss mitigation letter sent—when the servicer sends the loss mitigation letter to the borrower as required by Section 36.4850(g)(1)(iv).
 - (15) Default cured/loan reinstated—when a previously reported default (i.e., an EDN was filed) has cured/loan reinstated.
 - (16) Default reported to credit bureau—when the servicer notifies the credit bureaus of a defaulted loan or loan termination. The servicer shall report this event only on delinquent loans in its portfolio, and shall report the first occurrence only.
 - (17) Repayment plan approved—when the servicer approves a repayment plan.
 - (21) Compromise sale complete—when a compromise sale closes.
 - (23) Foreclosure referral—when the loan is referred to legal counsel for foreclosure. The servicers shall report this no later than the 7th calendar day from when the event occurred.

Condition

Veterans Affairs, as part of its administration of the loan guaranty program, is approved by the U.S. Department of Veterans Affairs (VA) to offer VA-guaranteed home loans to eligible veterans. Since November 2008 the VA requires loan servicers, such as Veterans Affairs, to electronically report to the VA specific events related to loans that have been issued a VA guarantee. Federal regulations require that events be reported to the VA within the first seven calendar days of the following month, or in certain instances, within seven days of the event itself. Late reporting may hinder the VA's ability to take appropriate oversight action on delinquent loans.

During our audit for fiscal year 2009–10, we reviewed a sample of 25 loans that were delinquent and found that Veterans Affairs did not always report bankruptcies, loss mitigation, foreclosure referrals, compromise sales, loan defaults, and the approval of a repayment plan to the VA within the applicable reporting deadlines. We also reported that in response to our audit report for fiscal year 2008–09, Veterans Affairs established a process in March 2010 to report to the VA as required when it notifies the credit bureaus of delinquent loans. However, we found that although it established this process, it still inconsistently reported this information to the VA. Finally, we also reported that Veterans Affairs lacked a process to use information in its system to determine which borrowers no longer have delinquent payments and therefore have cured their default. By not reporting cured defaults, the VA's reporting system continues to inaccurately show these loans in default.

During our prior year review, Veterans Affairs used a manual process to report most of the events for which we noted late reporting. In its corrective action plan for that year, Veterans Affairs indicated that the automation of the reporting requirement is a management priority and should resolve all noted issues. It stated that it has been working on this automation project and anticipated the system would be in place by March 31, 2011.

During our current audit, we determined that Veterans Affairs still has not fully addressed this finding. Specifically, Veterans Affairs indicated that the weekly reporting of information to the VA and the automation of most of the reporting requirements did not occur until July 2011. This included the automatic reporting to the VA of the repayment plan agreements, bankruptcies, and loss mitigation letters. Further, according to the property agent, Veterans Affairs is still testing the automatic reporting of compromise sales and it is manually reporting these events to the VA until the testing is completed. However, Veterans Affairs indicated that it was able to complete its project to automate its reporting of credit bureau notifications to the VA during fiscal year 2010–11. As such, we selected 24 delinquent loans it reported to the credit bureaus during fiscal year 2010–11 to determine whether Veterans Affairs appropriately notified the VA. Our review found that Veterans Affairs failed to report seven of these delinquent loans to the VA and reported another 11 of them between one and five days after the reporting deadline. According to Veterans Affairs, it failed to report the seven delinquent loans because of an undetected interruption in reporting during the automation of other processes, which it has not corrected.

Questioned Costs

No specific questions costs identified.

Recommendations

Veterans Affairs should complete its automation project and, once the system is fully in place it should ensure that the system allows it to report all required events to the VA by the applicable deadlines.

Department's View and Corrective Action Plan

The Department of Veterans Affairs agrees that some non-essential but required data was not reported according to the time frames required in the VA servicer manual. As stated in the report, no reporting exceptions were found for any items that would have any potential impact on its ability to collect claimed funds and no violations have been cited by VA.

Veterans Affairs is continuing with the development of the automated bulk upload file since this project will help Veterans Affairs meet VA reporting requirements. As noted by the Auditor such processes as repayment plan agreements, bankruptcies, and loss mitigation letters have been integrated into the automated bulk upload file. In addition, the reporting of accounts, which have cured their delinquencies, has also been implemented.

Regarding notification to the VA the reporting of credit bureau reporting, the move to a weekly reporting schedule should eliminate this finding. As noted by the Auditor, this schedule did not commence until July 2011. The seven delinquent loans, which were not reported to USDVA as reported to the Credit Bureaus, occurred during the period of time at the end of fiscal year 2010–11, and was a one-time event. At that time there was an undetected interruption in the reporting of Credit Bureau reports. It appears this occurred during implementation of other processes in the automation of the bulk upload. After discovery, the issue was corrected and normal reporting was resumed.

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U.S. DEPARTMENT OF AGRICULTURE

Reference Number: 2011-13-1

Federal Catalog Number: 10.557

Federal Program Title: Special Supplemental Nutrition Program for

Women, Infants and Children (WIC)

Federal Award Numbers and Years: 7CA700CA7; 2011

7CA700CA7; 2010 7CA700CA1; 2011 7CA700CA1; 2010 7CA700CA2; 2011

Category of Finding: Subrecipient Monitoring

State Administering Department: Department of Public Health (Public Health)

Criteria

TITLE 7—AGRICULTURE—SUBPART B—REGULATIONS OF DEPARTMENT OF AGRICULTURE—Part 246—Special Supplemental Nutrition Program for Women, Infants and Children, Subpart F—Monitoring and Review, Section 246.19—Management Evaluation and Monitoring Reviews, (b) State Agency Responsibilities

- (1) The state agency shall establish an ongoing management evaluation system, which includes at least the monitoring of local agency operations, the review of local agency financial and participation reports, the development of corrective action plans to resolve program deficiencies, the monitoring of the implementation of corrective action plans, and onsite visits. The results of such actions shall be documented.
- (2) Monitoring of local agencies must encompass evaluation of management, certification, nutrition education, participant services, civil rights compliance, accountability, financial management systems, and food delivery systems. If the state agency delegates the signing of vendor agreements, vendor training, or vendor monitoring to a local agency, it must evaluate the local agency's effectiveness in carrying out these responsibilities.
- (3) The state agency shall conduct monitoring reviews of each local agency at least once every two years. Such reviews shall include onsite reviews of a minimum of 20 percent of the clinics in each local agency or one clinic, whichever is greater. The state agency may conduct such additional onsite reviews as the state agency determines to be necessary in the interest of the efficiency and effectiveness of the program.
- (4) The state agency must promptly notify a local agency of any finding in a monitoring review that the local agency did not comply with program requirements. The state agency must require the local agency to submit a corrective action plan, including implementation time frames, within 60 days of receipt of a state agency report of a monitoring review containing a finding of program noncompliance. The state agency must monitor local agency implementation of corrective action plans.

Condition

During procedures performed over during-the-award monitoring, we noted that Public Health performs Program Evaluations (PE) that take place for all local agencies every two years. For issues identified during this review, the agency is required to submit a corrective action plan (CAP) within 60 days of receipt of the finding letter. In our sample of 25 completed reviews, we noted the following:

• For one of the 25 reviews selected, we noted the CAP was submitted by the local agency 69 days after the receipt of the letter of finding which was not within the required 60 days.

Without properly designed processes and controls in place to obtain and review the required CAPs, there is increased risk that subrecipient agencies may not be complying with federal program rules and regulations. Amounts paid to subrecipients totaled \$173 million of the \$1,279 million total WIC program expenditures for the fiscal year ended June 30, 2011.

Questioned Costs

No specific questioned costs identified.

Recommendation

Public Health should implement controls for following up on findings related to the PEs.

Department's View and Corrective Action Plan

Public Health agrees with the finding that it must have properly designed processes and controls in place to obtain and review the required CAPs and has implemented controls for following up on findings related to the Program Evaluations (PE). In 24 of the 25 reviews selected, Public Health received a CAP from subrecipient agencies within the required 60-day time frame. To ensure that Public Health receives 100 percent of all CAPs within the 60-day time frame, WIC has implemented the following control measures:

Effective October 1, 2011, Regional Advisors (RA) within the Local Agency Support Branch flag the date when the Program Evaluation and Policy Branch sends the Letter of Findings (LOF) to the subrecipient agency. Using a tickler system, the RA sends a 30-day "reminder" email to those agencies that have not already submitted a CAP. If an agency has not submitted a CAP within two weeks of the 60-day due date, the RA will call the local agency director to reinforce the federal requirement and document the call in the local agency file. In addition, the RA will notify their supervisor for any additional guidance or follow up action to consider.

Reference Number: 2011-14-1

Federal Catalog Number: 10.557

Federal Program Title: Special Supplemental Nutrition Program for

Women, Infants and Children (WIC)

Federal Award Numbers and Years: 7CA700CA7; 2011

7CA700CA7; 2010 7CA700CA1; 2011 7CA700CA1; 2010 7CA700CA2; 2011

Category of Finding: Special Tests and Provisions—Authorization of

Above-50-Percent Vendors

State Administering Department: Department of Public Health (Public Health)

Criteria

TITLE 7—AGRICULTURE—SUBPART B—REGULATIONS OF DEPARTMENT OF AGRICULTURE—Part 246—Special Supplemental Nutrition Program for Women, Infants and Children, Food Delivery System—Vendor Selection Criteria: competitive prices, 246.12 (g)(4)

The state agency must establish a vendor peer group system, distinct competitive price criteria, and allowable reimbursement levels for each peer group. The State agency must use the competitive price criteria to evaluate the prices a vendor applicant charges for supplemental foods as compared to the prices charged by other vendor applicants and authorized vendors, and must authorize vendors selected from among those that offer the program the most competitive prices. The State agency must consider a vendor applicant's shelf prices or the prices it bids for supplemental foods, which may not exceed its shelf prices. In establishing competitive price criteria and allowable reimbursement levels, the State agency must consider participant access by geographic area.

Condition

During procedures performed over Authorization of Above 50-Percent Vendors (A50), we noted that Public Health performs a Vendor Price Analysis (VPA) as a part of the vendor authorization and re-authorization process. The VPA determines whether vendors have competitive pricing on food products so that the amounts charged do not exceed the maximum allowable reimbursement rate (MADR). MADR rates are determined based on the vendor peer groups and are evaluated periodically using redemption data for all vendors in that peer group. MADR rates for A50 vendors are based on the average redemption price for all food instruments for that food type redeemed at all non A50 vendors statewide. In our sample of 65 A50 vendors, we noted that for one of the vendors selected, the VPA was run using the Peer Group 7, a non A50 vendor peer group. When the Food Price Survey was completed for the vendor, the vendor was improperly identified as belonging to Peer Group 7 rather than Peer Group 1, the peer group for A50 vendors.

Questioned Costs

No specific questioned costs identified.

Recommendations

Public Health should ensure policies and procedures are in place to ensure that vendors are appropriately classified to the correct peer group. Additionally, it should review this information to ensure that the VPA analysis is performed accurately, and correct peer group information is input into ISIS.

Department's View and Corrective Action Plan

Public Health agrees with the finding that WIC's Vendor Management Branch (VMB) staff should improve policies and procedures to ensure that vendors are appropriately classified to the correct peer group when performing a VPA, and that VMB staff should properly review a vendor's peer group assignment before entering the information into WIC's information system (ISIS).

WIC has procedures in place to assign a vendor to the correct peer group properly. In this instance, an analyst did not follow the procedures, and this error caused the analyst to conduct the VPA using an incorrect peer group. Further, staff did not identify the error during the routine review of the file. However, since VMB staff conducts an onsite store review prior to finalizing the store's authorization, staff was able to correct the peer group assignment in ISIS prior to the vendor becoming WIC-authorized to submit food instruments for reimbursement.

To improve this process, staff has modified the vendor authorization checklists to include a check-off box that requires the vendor analyst to re-check that staff is using the correct peer group when performing the VPA analysis and when conducting on-site vendor authorization visits.

WIC will train staff and fully implement this corrective action by December 1, 2011.

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U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES

Reference Number: 2011-1-1 Federal Catalog Number: 93.778

Federal Program Title: Medicaid Cluster—Medical Assistance Program

(Medi-Cal)

Federal Award Numbers and Years: 05-1105CA5MAP; 2011

05-1005CA5MAP; 2010 1105CAARRA; 2011 1005CAARRA; 2010

Category of Finding: Activities Allowed/Allowable Costs

State Administering Department: Department of Health Care Services

(Health Care Services)

Criteria

TITLE 2—GRANTS AND AGREEMENTS, PART 225—COST PRINCIPLES OF STATE, LOCAL, AND INDIAN TRIBAL GOVERNMENT (OMB Circular A-87), Attachment A—General Principles for Determining Allowable Costs, Part C—Basic Guidelines

- (1) Factors affecting allowability of costs. To be allowable under Federal awards, costs must meet the following general criteria
 - (a) Be necessary and reasonable for proper and efficient performance and administration of Federal awards.

Condition

During our procedures performed over the Medi-Cal program, we reviewed the audit and investigation reports to the program that were published and released during the fiscal year ended June 30, 2011. The following is a summary of the findings cited in the fourth annual Medi-Cal Payment Error Study (MPES) performed during the calendar year 2009 (the most recent MPES study completed):

"The sampling universe consists of Medi-Cal fee for service (FFS) claims paid through the fiscal intermediary, Hewlett Packard (formerly known as Electronic Data Systems), during the period of October 1, 2009, through December 31, 2009. There are 1,149 claims in the sample. The sample size was extracted from a universe of 25,236,902 Medi-Cal claims. Proportional allocation of the sample size was used to determine the sample size from each stratum ensuring a minimum sample size of 50 claims for each stratum.

(The results of the MPES indicated that) 5.45 percent of the total dollars paid had some indication that they contained a provider payment error. The 5.45 percent equates to \$1.07 billion of the total \$16 billion in annual payments made for FFS medical and dental services in calendar year 2009, and represents the percentage of payment error attributable to Medi-Cal program dollars "at risk" of being paid inappropriately due to findings related to such factors as a lack of medical necessity, abuse, or fraud. Of the total payments, 1.16 percent, or \$228 million, were for claims submitted by providers that disclosed characteristics of potential fraud.

In the MPES 2009, 55.6 percent of all samples errors were medical necessity errors.

There were no claims processing errors identified.

Based on the error percentage related to Medi-Cal payments, the risk of noncompliance with allowable costs and activities is considered material. The total Federal expenditures for FFS claims during the fiscal year ended June 30, 2011, were \$14.4 billion.

The American Recovery and Reinvestment Act of 2009 (Recovery Act) granted additional funding to the State in the form of an enhanced Federal Medical Assistance Percentage to the State for medical assistance expenditures. Total Recovery Act expenditures related to FFS claims during the fiscal year ended June 30, 2011, amounted to \$2.5 billion.

Questioned Costs

No specific questioned costs were identified.

Recommendations

Health Care Services should strengthen their internal controls to ensure only medically necessary claims are paid. Health Care Services should also strengthen their internal control process to prevent/detect potential provider fraud.

Department's View and Corrective Action Plan

Health Care Services is continuously engaged to strengthen the internal controls and ensure the medical necessity of all services rendered and paid. The findings from the MPES report are used to generate field audits of suspect providers and to confirm specific overpayments leading to recoveries. The Health Care Services' Medical Review Board (MRB) also places select providers on Post-Service Pre-Payment (PPM).

Formerly known as the Special Claims Review (SCR), the PPM is an audit of the medical necessity and the program coverage of services after they are given to the beneficiary but before DHCS reimburses the provider. MRB may impose the PPM when the provider has submitted improper or incorrect claims. Under PPM, Health Care Services may deny payment for claims that are not covered benefits or that are deemed medically unnecessary. While on PPM, the provider is prohibited from electronic billing and is required to submit hard copy (manual) claims with copies of medical documentation to substantiate the medical necessity and the actual provision of the service claimed.

The detection of provider fraud is an ever-evolving science. MRB employs multiple techniques to detect, identify, and pursue fraudulent claims. These methodologies include monitoring for billing spikes, audits of the outlier billers, random claim reviews, and computer-generated suspect lists based on a multifactorial program. The newest technology that we are exploiting is link analysis to enable us to pursue the peripheral contacts of known fraudulent providers.

Reference Number: 2011-1-2

Federal Catalog Number: 93.778

Federal Program Title: Medicaid Cluster—Medical Assistance Program

(Medi-Cal)

Federal Award Numbers and Years: 05-1105CA5MAP; 2011

05-1005CA5MAP; 2010 1105CAARRA; 2011 1005CAARRA; 2011

Category of Finding: Activities Allowed/Allowable Costs

State Administering Department: Department of Health Care Services

(Health Care Services)

Criteria

TITLE 2—GRANTS AND AGREEMENTS, PART 225—COST PRINCIPLES FOR STATE, LOCAL, AND INDIAN TRIBAL GOVERNMENT (OMB Circular A-87), Attachment A—General Principles for Determining Allowable Costs, Part C—Basic Guidelines

- (1) Factors affecting allowability of costs. To be allowable under Federal awards, costs must meet the following general criteria:
 - (a) Be necessary and reasonable for proper and efficient performance and administration of Federal awards.

CALIFORNIA CODE OF REGULATIONS, TITLE 22, Section 51476

• Each provider shall keep, maintain, and have readily retrievable, such records as are necessary to fully disclose the type and extent of services provided to a Medi-Cal beneficiary. Required records shall be made at or near the time at which the service is rendered.

DEPARTMENT OF HEALTH SERVICES PROVIDER MANUAL—PROVIDER REGULATIONS

Medi-Cal requires providers to agree to keep necessary records for a minimum period of three years
from the date of service to disclose fully the extent of services furnished to the patient. The provider
also must agree to furnish these records and any information regarding payments claimed for
providing the services, on request, to the California Department of Health Services.

Condition

In our procedures performed over expenditures charged to the program, we selected a sample of fee-for-service (FFS) claims and utilized Health Care Services' Medical Review Branch of trained medical professionals to ascertain that each expenditure was for an allowable service rendered and was supported by medical records or other evidence, indicating that the service was actually provided and consistent with the medical diagnosis. In our sample of 50 FFS claims, six did not appear to be for an allowable service. These exceptions are noted as follows:

- Two claims were not deemed medically necessary.
- Four claims did not have sufficient supporting documentation to support whether the required medical procedures were rendered on the beneficiary.

Total exceptions amounted to \$11,865 of the total \$147,421 sampled of federal Medicaid expenditures for FFS claims. Total federal Medicaid expenditures for FFS claims amounted to \$14.4 billion for the fiscal year ended June 30, 2011.

The American Recovery and Reinvestment Act of 2009 (Recovery Act) granted additional funding to the State in the form of an enhanced Federal Medical Assistance Percentage to the State for medical assistance expenditures. Total Recovery Act expenditures related to FFS claims during the fiscal year ended June 30, 2011, amounted to \$2.5 billion. The total exceptions amounted to \$2,076 of the total \$27,123 Recovery Act expenditures for FFS claims.

Questioned Costs

\$11,865 of the \$147,421 FFS expenditures sampled and \$2,076 of the \$27,123 Recovery Act expenditures sampled for fiscal year ended June 30, 2011.

Recommendations

Health Care Services should strengthen its internal controls to ensure only medically necessary claims and eligible providers are paid. Health Care Services should also strengthen its internal control process to detect providers in violation of record retention rules.

Department's View and Corrective Action Plan

Health Care Services is continuously engaged to strengthen the internal controls to ensure the medical necessity of all services rendered and paid. The findings from the Medi-Cal Payment Error Study (MPES) report are used to generate field audits of suspect providers and to confirm specific overpayments leading to recoveries. It should be noted that the sequential findings MPES report reflect a *declining* rate of Medi-Cal fraud, waste, and abuse.

The regulations governing record retention in general require providers to retain their records for medial justification for a minimum of three years:

Record Keeping and Retention—Provider agrees to make, keep, and maintain in a systematic and orderly manner, and have readily retrievable, such records as are necessary to fully disclose the type and extent of all services, goods, supplies, and merchandise provided to Family PACT beneficiaries, including, but not limited to, the records described in Section 51476 of Title 22, California Code of Regulations and the records described in Section 431.107 of Title 42 of the Code of Federal Regulations. Provider further agrees that such financial records shall be made at or near the time at which the services, goods, supplies, and merchandise are delivered or rendered, and that such records shall be retained by Provider in the form in which they are regularly kept for a period of three years from the date the goods, supplies, and merchandise were delivered or the services rendered.

Health Care Services' Medical Review Branch continuously audits suspect providers with an emphasis on the documentation to support the medical necessity of rendered services. Providers who cannot substantiate the medical necessity of the rendered service are subject to audits for recovery. Health Care Services' Medical Review Branch recovered \$42,332,914 in the first half of 2011.

Reference Number: 2011-2-1

Federal Catalog Number: 93.778

Federal Program Title: Medicaid Cluster—Medical Assistance Program

(Medi-Cal)

Federal Award Numbers and Years: 05-1105CA5MAP; 2011

05-1005CA5MAP; 2010 1105CAARRA; 2011 1005CAARRA; 2010

Category of Finding: Allowable Costs

State Administering Department: Department of Health Care Services

(Health Care Services)

Criteria

TITLE 19, SOCIAL SECURITY ACT—GRANTS TO STATE FOR MEDICAL ASSISTANCE PROGRAMS, Section 1927—Payment for Covered Outpatient Drugs

- (2) State Provision of Information:
 - (A) State Responsibility. Each State agency under this title shall report to each manufacturer not later than 60 days after the end of each rebate period and in a form consistent with a standard reporting format established by the Secretary, information on the total number of units of each dosage form, strength and package size of each covered outpatient drug dispensed after December 31, 1990, for which payment was made under the plan during the period, and shall promptly transmit a copy of such report to the Secretary.

Condition

Drug manufacturers/labelers are required to provide a listing to the Centers for Medicare and Medicaid Services (CMS) of all covered outpatient drugs and, on a quarterly basis, are required to provide their average manufacturer's price and their best prices for each covered outpatient drug. Based upon this data, CMS calculates a unit rebate amount for each drug and provides the rebate information to the States. The state Medicaid Agency is required to provide to drug manufacturers/labelers the drug utilization data no later than 60 days after the end of the quarter. We tested 40 rebate invoices related to the third and fourth quarters of 2010, as well as the first and second quarters of 2011 and noted the following:

- Health Care Services provided the unit rebate amount for the third quarter 2010 (July to September 2010) drug data on December 02, 2010, which is three days late. Drug utilization data had to be mailed to the labelers by the state Medicaid Agency on November 29, 2010.
- Health Care Services provided the first quarter 2011 (January to March 2011) drug data on May 31, 2011, which is one day late. Drug utilization data had to be mailed to the labelers by the state Medicaid Agency on May 30, 2011.

The total combined federal and state drug rebates for the third quarter of 2010 and first quarter of 2011 amounted to \$159,011,283 and \$427,717,086, respectively (total of \$586.7 million). As a result from this audit finding, there was an increase in the risk that the State would not obtain the \$586.7 million due in a timely manner. In addition, the State potentially missed an opportunity to earn interest on these funds. However, the labelers have the drug pricing information related to the average wholesale prices and they continue to pay the rebate amount.

The American Recovery and Reinvestment Act of 2009 (Recovery Act) granted additional funding to the State in the form of an enhanced Federal Medical Assistance Percentage to the State for medical assistance expenditures. Total Recovery Act expenditures during the fiscal year ended June 30, 2011, amounted to \$5 billion. The lack of timely submission of the drug rebates potentially causes a missed opportunity to earn interest on these funds.

Questioned Costs

No specific questioned costs identified.

Recommendations

Health Care Services should ensure that drug utilization data are provided to drug manufacturers/ labelers on a timely basis (i.e. no later than 60 days at the end of the quarter) and to proactively monitor the receipt of payment from labelers.

Department's View and Corrective Action Plan

Health Care Services proactively monitors and diligently works towards ensuring that drug utilization reports are mailed to the drug manufacturers within 60 days after the end of each quarter. Health Care Services has modified the Rebate Accounting and Information System to allow the invoicing process to

be more efficient and require less manual reviewing, thus allowing for the timely mailing of the invoices. However, recent events have impacted Health Care Services' ability to mail the utilization reports timely. We have noted the following as reasons for the findings noted above:

- The third quarter 2010 utilization reports were three days late in being mailed to the drug manufacturers as a result of the State directed furloughs required of Health Care Services employees.
- The first quarter 2011 utilization reports were one day late as a result of May 30, 2011, coinciding with a national holiday (Memorial Day). The reports were sent the next business day.

Reference Number: 2011-3-1

Federal Catalog Number: 93.268

Federal Program Title: Immunization Grants

Federal Award Numbers and Years: 5H23IP922507-09; 2010

5H23IP922507-08; 2009

Category of Finding: Cash Management

State Administering Department: Department of Public Health (Public Health)

Criteria

TITLE 31—MONEY AND FINANCE: TREASURY, CHAPTER II—FISCAL SERVICE, DEPARTMENT OF THE TREASURY, PART 205—RULES AND PROCEDURES FOR EFFICIENT FEDERAL—STATE FUNDS TRANSFERS, Subpart A—Rules Applicable to Federal Assistance Programs Included in a Treasury—State Agreement, Section 205.11, What Requirements Apply to FundingTechniques?

(a) A state and a federal program agency must minimize the time elapsing between the transfer of funds from the United States Treasury and the state's payout of funds for federal assistance program purposes, whether the transfer occurs before or after the payout of funds.

Condition

During our procedures performed over Public Health's payments made to contractors, we noted that it requests cash advances (drawdowns) from the federal government and then requests payments to be made to contractors by the State Controller's Office (SCO). The program falls under the Cash Management Improvement Act (CMIA) with a required funding technique of preissuance for payments to contractors. The preissuance technique requires the State to disburse payments to contractors not more than three days after the advance is deposited in the state account.

In our sample of 65 drawdowns totaling approximately \$17.3 million, we noted 17 drawdowns totaling approximately \$7 million where the payments to the contractors were issued up to 21 days from the dates of the drawdown requests, which exceeds the three-day requirement per the CMIA agreement. Public Health indicated the delays were caused by the accounting department being unaware that the Immunization Grant was added to the CMIA agreement for the year ended June 30, 2011. By not issuing the warrants within three days from the dates of the drawdown requests, Public Health is not in compliance with the cash management requirements of the Immunization program.

Questioned Costs

No specific questioned costs identified.

Recommendation

Public Health should ensure policies and procedures are in place to ensure payments to contractors are issued within the three-day requirement of the federal draws.

Department's View and Corrective Action Plan

Public Health agrees and has modified its policies and procedures to ensure payments to contractors are issued within the three days of the Federal draws, per CMIA requirements.

Public Health's accounting section implemented a more efficient method of communicating when the federal funds are needed and the release of claim schedules. The accounting section verifies the timing of federal draws with claim schedule payments and provides status of when a claim schedule is to be held for corrections or additional processing before sending to the SCO. The accounting section does not draw the federal money until the claim schedule has been released to SCO.

On October 20, 2011, Public Health implemented the above corrective actions and have updated written procedures.

Reference Number: 2011-5-1

Federal Catalog Number: 93.917

Federal Program Title: HIV Care Formula Grants

Federal Award Numbers and Years: X07HA12778-03-01; 2011

X07HA12778-02-00; 2010

Category of Finding: Eligibility, Activities Allowed/Allowable Costs

State Administering Department: Department of Public Health (Public Health)

Criteria

TITLE 42—THE PUBLIC HEALTH AND WELFARE, CHAPTER 6A—PUBLIC HEALTH SERVICE, SUBCHAPTER XXIV—HIV HEALTH CARE SERVICES PROGRAM, Part B—Care Grant Program, Subpart I—General Grant Provisions, Section 300ff-26, Provision of Treatments

- (b) Eligible individual. To be eligible to receive assistance from a State under this section, an individual must:
 - 1. Have a medical diagnosis of HIV/AIDS; and
 - 2. Be a low income individual, as defined by the State.

TITLE 42—THE PUBLIC HEALTH AND WELFARE, CHAPTER 6A—PUBLIC HEALTH SERVICE, SUBCHAPTER XXIV—HIV HEALTH CARE SERVICES PROGRAM, Part B—Care Grant Program, Subpart I—General Grant Provisions, Section 300ff-22, Required Funding for Core Medical Services

(3) Core medical services

For purposes of this subsection, the term "core medical services," with respect to an individual infected with HIV/AIDS (including the co-occurring conditions of the individual) means the following services:

(A) Outpatient and ambulatory health services.

- (B) AIDS Drug Assistance Program treatments in accordance with section 300ff–26 of this title.
- (C) AIDS pharmaceutical assistance.
- (D) Oral health care.
- (E) Early intervention services described in subsection (d).
- (F) Health insurance premium and cost sharing assistance for low-income individuals in accordance with section 300ff–25 of this title.
- (G) Home health care.
- (H) Medical nutrition therapy.
- (I) Hospice services.
- (J) Home and community-based health services as defined under section 300ff–24(c) of this title.
- (K) Mental health services.
- (L) Substance abuse outpatient care.
- (M) Medical case management, including treatment adherence services.

Condition

Program coordinators are required to visit AIDS Drug Assistance Program (ADAP) enrollment sites every five years in accordance with requirements established by the agreement between the sites and the State. This quality control process re-determines eligibility for individually sampled cases of beneficiary eligibility made by enrollment workers at the local enrollment sites. Enrollment site visits are performed to ensure individuals receiving services meet eligibility requirements. Site visit reports are completed by program coordinators and reviewed by the program chief.

We selected 15 of 71 site visit reports prepared by the Office of AIDS program coordinators during the fiscal year ended June 30, 2011, and noted that 10 of the 15 selected reports had detailed several instances of noncompliance with eligibility requirements including proof of income, proof of HIV status, and up-to-date Cluster of Differentiation Four (CD4)/Viral Load counts. The errors noted in the reports written by program coordinators were as follows.

At the 15 sites, of the 222 files reviewed, we noted the following:

- 15 files (or 6.8 percent) were missing the required identification documentation,
- 23 (or 10.4 percent) files were missing or had incomplete proof of California residency,
- 21 files (or 9.5 percent) were missing either the initial HIV status, the current CD4, or the viral load documentation,
- Five files (or 2.3 percent) were missing proof of Medi-Cal application/referral,
- 53 files (or 23.9 percent) were missing valid proof of income documentation,
- Nine files (or 4.1 percent) were missing a completed/signed ADAP Enrollment Application,
- Four files (or 1.8 percent) had invalid Support Affidavit forms,
- 47 files (or 21.2 percent) were missing the required Grace Period forms.

Based on our review of the site visit reports, it appears there may be material noncompliance regarding documentation to support the eligibility of the participants. The site visit reports did not quantify specific or potential questioned costs related to the exceptions noted. Total expenditures paid to program participants amounted to approximately \$130 million for the fiscal year ended June 30, 2011.

In addition to these site visits, the Audits and Investigations unit for the Department of Health Care Services (Health Care Services) performed a performance review of Ramsell Public Health RX, LLC (Health Care Services' third-party pharmacy benefit manager). Health Care Services' review disclosed that 10 out of the 500 transactions selected were for clients who were Medi-Cal eligible with a share of cost and the AIDS Drug Assistance Program (ADAP) paid in excess of the share of cost for four of the 10 clients. Additionally, Health Care Services' review disclosed that 26 out of the 500 transactions selected were for clients who were Medi-Cal eligible with no share of cost and, thus, should not have been billed to ADAP as Medi-Cal is responsible for all payments of their prescriptions. The review identified \$305,872 in questioned costs relating to these individuals.

We also noted that Health Care Services reviewed 330 prescriptions noting that 21 of the prescriptions from four pharmacies were missing prescription documentation, which amounted to \$9,944.

The lack of adequate eligibility and prescription documentation could result in ineligible recipients receiving Federal assistance.

Questioned Costs

\$315,816

Recommendations

Public Health should strengthen its internal controls over the eligibility process and enhance training for local enrollment workers to ensure that payments are only made to eligible recipients and that all required documentation to verify eligibility is maintained in the recipient's file.

Department's View and Corrective Action

Public Health agrees that it should strengthen its internal controls over the eligibility process and enhance training for local enrollment workers to ensure that payments are made only to eligible recipients.

ADAP continues to work with the pharmacy benefits management (PBM) service provider to ensure controls on client eligibility determinations are implemented, and consequently, payments are only made for eligible recipients. Effective July 1, 2010, Public Health site visits that identify deficient client eligibility files/documentation result in immediate notification to the PBM of the specific client files found to have deficiencies and the necessary documentation required to correct the deficiencies. A 60-day grace period is placed on these clients' eligibility, during which time the missing documentation must be provided by the site/enrollment worker/client, and if not, the client's ADAP eligibility is suspended until compliance is achieved. Public Health's ADAP site visits now occur every three years (formerly every five years) and Public Health will visit all 180 ADAP enrollments sites by June 30, 2013. Public Health's newly accelerated site visit/technical assistance cycle has only completed its first year. Once the initial three-year cycle is completed, the next site visit cycle will have improved program compliance findings, including client eligibility documentation.

To strengthen the technical assistance Public Health staff provide during all site visits, Public Health is modifying mandatory annual enrollment worker training to enhance the effectiveness of all aspects of the eligibility determination training.

Additionally, Public Health is working with Health Care Services, Medi-Cal Program, and the PBM to enhance ADAP data systems to identify clients with Medi-Cal eligibility in a more timely and accurate manner to assure ADAP is the payer of last resort. Public Health is pursuing an interagency Data Use Agreement (DUA) to allow Public Health to access the Health Care Services' Medi-Cal eligibility database on a monthly basis to cross-match client eligibility data and identify ADAP clients with Medi-Cal eligibility. Public Health will then collaborate with the ADAP PBM to ensure proper billing, including potential back-billing for prescriptions billable to Medi-Cal.

Reference Number: 2011-5-2

Federal Catalog Number: 93.778

Federal Program Title: Medical Cluster—Medical Assistance Program

(Medi-Cal)

Federal Award Numbers and Years: 05-1105CA5MAP; 2011

05-1005CA5MAP; 2009 1105CAARRA; 2011 1005CAARRA; 2010

Category of Finding: Eligibility

State Administering Department: Department of Health Care Services

(Health Care Services)

Criteria

TITLE 42—PUBLIC HEALTH—CHAPTER IV—CENTERS FOR MEDICARE AND MEDICAID SERVICES, DEPARTMENT OF HEALTH AND HUMAN SERVICES, Part 435—Eligibility in the States, District of Columbia, the Northern Mariana, Subpart J—Eligibility in the States and the District of Columbia, Section 435.916 Periodic Redeterminations of Medicaid Eligibility

"The agency must redetermine the eligibility of Medicaid recipients, with respect to circumstances that may change, at least every 12 months."

Condition

States are required to operate a Medicaid Eligibility Quality Control (MEQC) in accordance with requirements established by the Centers for Medicare and Medicaid Services (CMS). The MEQC system redetermines eligibility for individual sampled cases of eligible beneficiaries determined by state Medicaid agencies or their designees. The State of California has been granted a waiver from the traditional MEQC program described in regulation. The program waiver differs from the traditional MEQC program by allowing the performance of special studies, targeted reviews, and other activities that are designated to ensure program integrity or improve program administration. Health Care Services' MEQC process reviewed 2,339 cases from July 2010 to June 2011. Of the 2,339 cases sampled, Health Care Services determined 128 were ineligible for Medicaid or eligible for Medicaid with a difference in their Share of Cost of greater than \$400, resulting in a 5.5 percent error rate. Share of Cost represents the amount a beneficiary must provide for health care services received prior to receiving benefits funded by Medicaid, and is similar to a monthly deductible.

We evaluated the accuracy of the MEQC system by obtaining a listing of all eligibility case reviews performed during the fiscal year and selected 65 cases in 10 different counties to reperform the MEQC review. Our sample included 60 without eligibility errors and five with eligibility errors identified by the MEQC review. We note that our conclusions were consistent with those of the MEQC reviewers for the 65 cases we reexamined.

Additionally, we selected 65 case files from the general population of the State's Medicaid beneficiaries in 10 different counties to reperform the counties' eligibility determination. We noted two of the 65 tested cases were ineligible for Medicaid benefits. The nature of our exceptions is as follows:

• Two of the 65 beneficiaries failed to provide a signed annual redetermination form, resulting in the beneficiaries being ineligible to receive Medicaid benefits. The lack of yearly redeterminations may result in funding of individuals who do not meet Medicaid eligibility requirements.

Total direct Federal Medicaid expenditures that the State made for provider payments amounted to \$26 billion for the fiscal year ended June 30, 2011.

The American Recovery and Reinvestment Act of 2009 (Recovery Act) granted additional funding to the State in the form of an enhanced Federal Medical Assistance Percentage to the State for medical assistance expenditures. Total Recovery Act expenditures during the fiscal year ended June 30, 2011, amounted to \$5 billion. The error percentage noted in the MEQC reviews may affect Recovery Act expenditures because it indicates there is a material risk of noncompliance related to Eligibility.

Questioned Costs

No specific questioned costs were identified.

Recommendation

Health Care Services should strengthen controls over its redetermination requirements for Medi-Cal beneficiaries to ensure that benefits are discontinued when redeterminations are not received within 12 months of the most recent redetermination date.

Department's View and Corrective Action Plan

Health Care Services will discuss each of the audit findings with the affected counties. These discussions will include a review of the specific findings with each affected county, possible corrective actions, and best practice referrals. If warranted, Health Care Services will conduct focused reviews in specific counties to address the potential Medi-Cal redetermination performance issues. Health Care Services will continue to reinforce expectations that the counties must complete Medi-Cal redeterminations on a timely basis and reiterate to the counties that the pertinent documentation must be available to review in the county case files and automated system data as required by State policies.

Reference Number: 2011-5-3

Federal Catalog Number: 93.778

Federal Program Title: Medicaid Cluster—Medical Assistance Program

(Medi-Cal)

Federal Award Numbers and Years: 05-1105CA5MAP; 2011

05-1005CA5MAP; 2010 1105CAARRA; 2011 1005CAARRA; 2010

Category of Finding: Eligibility

State Administering Department: Department of Health Care Services

(Health Care Services)

Criteria

OMB Circular A-133 Part 3—Section E—Eligibility

(1) "For some Federal programs with a large number of people receiving benefits, the non-Federal entity may use a computer system for processing individual eligibility determinations and delivery of benefits. Often these computer systems are complex and will be separate from the non-Federal entity's regular financial accounting system".

Social Security Act, Title XIX—Grants to States for Medical Assistance Programs, Section 1902, State Plans for Medical Assistance, Section (e)(12)—Continuous Eligibility for Children

- (12) At the option of the State, the plan may provide that an individual who is under an age specified by the State (not to exceed 19 years of age) and who is determined to be eligible for benefits under a State plan approved under this title under subsection (a)(10)(A) shall remain eligible for those benefits until the earlier of—
 - (A) the end of a period (not to exceed 12 months) following the determination; or
 - (B) the time that the individual exceeds that age.

Condition

We note that Health Care Services contracts with the counties of California to perform eligibility determinations for Medicaid beneficiaries. The following three consortium systems are used by the counties to assist in the determination of Medicaid eligibility: California Work Opportunity and Responsibility to Kids Information Network (CALWIN), Los Angeles Eligibility, Automated Determination, Evaluation and Reporting (LEADER), and Consortium IV (C-IV). An aid code is generated for each beneficiary, which details the beneficiary's scope of benefits as well as if a Share of Cost is required. Share of Cost represents the amount a beneficiary must provide for health care services received prior to receiving benefits funded by Medicaid, and is similar to a monthly deductible. The consortium systems interface with the Medicaid Eligibility Database System (MEDS), which is the State's Medicaid eligibility system. The State uses the aid code information in MEDS to determine the allowability of claims submitted by confirming the beneficiary's eligibility.

We selected 130 eligibility case files from 10 different counties and reperformed the counties' eligibility determination. Of the 130 sampled cases, one case selected had beneficiaries where there was a discrepancy in aid code between the consortium system and MEDS, which may have an impact on future beneficiary eligibility. The nature of the exception is as follows:

• In the case with the discrepancy in aid code, a child moved from her father's care to her mother's care between counties. The child was previously eligible for no share of cost Medi-Cal while under the care of her father, but her mother's countable income exceeded the income limitations for no share of cost Medi-Cal. The mother was properly aided for Medi-Cal with a share of cost. As the daughter was previously aided with a no share of cost aid code under the guidelines of continuous eligibility for children, she would continue to retain eligibility without a share of cost until the father's next annual redetermination. However, the daughter was not assigned a continuous eligibility for children aid code. As a result, there is the possibility that if uncorrected, she would continue to receive aid without a share of cost after the period where her no share of cost benefits should have lapsed.

Total direct Federal Medicaid expenditures that the State made for provider payments amounted to \$26 billion for the fiscal year ended June 30, 2011.

The American Recovery and Reinvestment Act of 2009 (Recovery Act) granted additional funding to the State in the form of an enhanced Federal Medical Assistance Percentage to the State for medical assistance expenditures. Total Recovery Act Expenditures during the fiscal year ended June 30, 2011, amounted to \$5 billion.

Questioned Costs

No specific questioned costs were identified.

Recommendations

Health Care Services should strengthen controls over performing routine reconciliations over MEDS and the consortium systems for Medicaid beneficiaries to ensure corresponding Medi-Cal information is reflected for beneficiaries on each system. In addition, Health Care Services should strengthen controls over eligibility determination to ensure that beneficiaries are assigned proper aid codes which can be adequately supported.

Department's View and Corrective Action Plan

As part of the corrective action process, Health Care Services will reemphasize through county guidance that when an individual moves to a new county, the new county is required to review prior month's eligibility for individuals to ensure that the appropriate aid code is established. Because the child moved from one county to another, the appropriate entries to generate the Continuous Eligibility Coverage (CEC) aid code was not automatically triggered in the new county. Additional actions by the new county should have been taken in the county system to guarantee that the correct CEC aid code was generated.

Additionally, Health Care Services conducts monthly quality control reviews that evaluate counties' eligibility determinations. When Health Care Services identifies discrepancies in aid codes, it immediately informs the county in which the error occurred to correct the aid codes, although aid code discrepancies generally do not result in eligibility or share of cost errors. However, if the quality control case reviews indicate a particular county is having a significant problem with performing accurate aid code assignments, a meeting can be held with the county's Medi-Cal program staff to discuss the issue and possible corrective action measures. In some cases, a county may be required to provide Health Care Services with a formal corrective action plan with a subsequent focused review to ensure the corrective action plan has been implemented.

Reference Number: 2011-5-4

Federal Catalog Number: 93.778

Federal Program Title: Medicaid Cluster—Medical Assistance Program

Medi-Cal

Federal Award Numbers and Years: 05-1105CA5MAP; 2011

05-1005CA5MAP; 2010 1105CAARRA; 2011 1005CAARRA; 2010

Category of Finding: Eligibility

State Administering Department: Department of Health Care Services

(Health Care Services)

Criteria

SOCIAL SECURITY ACT, Title XIX—GRANTS TO STATES FOR MEDICAL ASSISTANCE PROGRAMS, Section 1920—Presumptive Eligibility for Pregnant Women

(a) A State plan approved under section 1902 may provide for making ambulatory prenatal care available to a pregnant woman during a presumptive eligibility period

- (c)(1) The State agency shall provide qualified providers with:
 - (A) Such forms as are necessary for a pregnant woman to make application for medical assistance under the State plan, and
 - (B) Information on how to assist such women in completing and filing such forms.
 - (2) A qualified provider that determines under subsection (b)(1)(A) that a pregnant woman is presumptively eligible for medical assistance under a State plan shall:
 - (A) Notify the State agency of the determination within five working days after the date on which determination is made, and
 - (B) Inform the woman at the time the determination is made that she is required to make application for medical assistance under the State plan by not later than the last day of the month following the month during which the determination is made.

Condition

The presumptive eligibility component of this program grants immediate and temporary Medi-Cal coverage for California residents who are pregnant but do not have health insurance or Medi-Cal coverage for prenatal care. Health Service grants the right to enroll recipients under this program to qualified providers. Because the program provides immediate and temporary care prior to the approval of Medi-Cal eligibility, recipients enrolled in presumptive eligibility are not considered Medi-Cal eligible, and therefore, are not entered into Health Care Services' eligibility systems.

Recipients presumed to be eligible are assigned a pre-numbered identification card (obtained from Health Care Services by the provider) that begins with a county identification number and presumptive eligibility aid code. The paper documentation, including the application and presumptive eligibility identification card, are retained by the provider.

The provider is required by the State plan to submit to Health Care Services a weekly enrollment summary of all presumptive eligibility identification numbers issued to Health Care Services for retention. Health Care Services is required to retain the documents for a period of three years. Since the supporting documentation for presumptive eligibility is retained by Health Care Services, the State's fiscal intermediary, Hewlett Packard Enterprise Services (HP), does not perform procedures over the presumed eligible recipients. The HP mainframe processing is set to bypass the eligibility check if it recognizes the special sequencing of the presumptive eligibility identification number.

Consistent with the prior year, Health Care Services is unable to reconcile the presumptive eligibility number against the enrollment listing filed with Health Care Services at this time because of staffing limitations. However, Health Care Services is pursuing an automated process to post the presumptive eligibility identification numbers to the Medi-Cal eligibility system so records for these recipients can be accessed to authenticate, reconcile, and prevent duplicate issuances of the presumptive eligibility number during the claims adjudication process. As such, there does not appear to be adequate tracking of presumptive eligibility numbers, and there is the risk that duplicate issuances of numbers or unauthorized use may occur as the existence of the recipient is not authenticated.

The American Recovery and Reinvestment Act of 2009 (Recovery Act) granted additional funding to the State in the form of an enhanced Federal Medical Assistance Percentage to the State for medical assistance expenditures. Total Recovery Act expenditures during the fiscal year ended June 30, 2011, amounted to \$5 billion. The lack of reconciliation of presumptive eligibility numbers to the enrollment listing may result in Recovery Act funding being expended on individuals who do not meet Medicaid eligibility requirements.

Questioned Costs

No specific questioned costs were identified.

Recommendations

Health Care Services should strengthen their internal controls process to obtain and track the enrollment presumptive eligibility identification numbers issued to prevent unauthorized use of identification numbers. Further, Health Care Services should perform procedures to authenticate the existence of the recipient, prevent duplicate issuances, and reconcile the presumptive eligibility number against the recipient enrollment listing filed at Health Care Services during the claims adjudication process.

Department's View and Corrective Action Plan

Health Care Services lacks the necessary resources needed to develop and implement automated systems to address this finding. However, we believe that the Patient Protection and Affordable Care Act (PPACA) of 2010 provides an ideal opportunity to implement a solution to this problem as we implement the requirements of federal health care reform. As required by the PPACA and with the passage of Senate Bill 900 (Chapter 659, Statutes of 2010), California is required to develop the California Health Benefit Exchange (Exchange). A component of the Exchange is the ability to screen for and enroll eligible individuals into the Medi-Cal program, utilizing a web-based enrollment portal and streamlined eligibility processes. Under the PPACA, for purposes of Medi-Cal eligibility, Health Care Services is required to develop and implement streamlined eligibility determinations and enrollment processes for individuals seeking Medi-Cal covered services. The Exchange provides an opportunity to allow Presumptive Eligibility (PE) Qualified Providers to complete the PE Enrollment for eligible pregnant women using an internet-based application that will provide real-time validation with the Statewide Medi-Cal Eligibility Database System. Health Care Services is working in collaboration with the Health Benefit Exchange Board in the development of the Exchange, which is required to be operational in 2014.

As an interim measure, Health Care Services will begin using a new print vendor as of November 15, 2011, for purposes of automating the process of issuing the presumptive eligibility identification numbers. The new vendor will automate the ordering process to validate presumptive eligibility identification numbers issued to providers. This quality assurance effort reduces the chance of duplicating the presumptive eligibility identification numbers issued to providers.

Reference Number: 2011-13-2

Federal Catalog Number: 93.778

Federal Program Title: Medicaid Cluster—Medical Assistance Program

(Medi-Cal)

Federal Award Numbers and Years: 05-1105CA5MAP; 2011

05-1005CA5MAP; 2010

Category of Finding: Subrecipient Monitoring

State Administering Department: Department of Health Care Services

(Health Care Services)

Criteria

TITLE 31-MONEY AND FINANCE, SUBTITLE V—GENERAL ASSISTANCE ADMINISTRATION, Section 7502—Audit Requirements; Exemptions

(f)(2) Each pass-through entity shall:

(b) monitor the subrecipient's use of Federal awards through site visits, limited scope audits, or other means.

Condition

The County-based and School-based Medi-Cal Administrative Activities Units (CMAA and SMAA) of Health Care Services are required to actively monitor the award process of Local Government Agencies (LGAs) and Local Education Consortiums (LECs) that receive Medicaid funding for the reimbursement of expenditures of Medi-Cal services and administration costs. This monitoring process is conducted through site visits and desk reviews. The CMAA and SMAA Units have internal policies for actively monitoring the award process that are guided by agreements between the federal branch of Medicaid (Centers for Medicare & Medicaid Services or CMS) and the CMAA and SMAA. These policies require that there must be a site visit conducted for each CMAA LGA once every four years and for each SMAA LGA/LEC once every three years from the date of their last site visit.

In April 2011, Health Care Services imposed a travel restriction on its employees. As such, analysts were unable to perform all planned site visits. The SMAA unit performs desk reviews when unable to travel. These desk reviews are equivalent in scope to the site reviews. The CMAA unit currently does not have a desk review process implemented for when travel is restricted. For CMAA there were 13 LGAs that had not had a site visit within the last four years, and for SMAA, there were five LGAs/LECs that had not had a site visit within the last three years.

In addition, the CMAA unit has a control in place in which subrecipients submit a claiming plan to the unit and acceptance of the plan is communicated to the subrecipient through an approval letter. These approval letters are authorized by the unit chief. In our sample of five approval letters, one of them did not have evidence of a signature. There was no evidence that the approval letter was properly authorized.

Questioned Costs

No specific questioned costs identified.

Recommendations

Health Care Services should ensure that site visits of LGAs/LECs receiving Medicaid funding are conducted once every three or four years to actively monitor the award process. Health Care Services should also enhance its current policies and procedures to ensure that claiming plan approval letters are properly authorized.

Department's View and Corrective Action Plan

Health Care Services concurs with this recommendation.

In April 2011, Health Care Services imposed travel restrictions on its employees and all site visits were cancelled. During fiscal year 2011–12, SMAA staff reinstituted its desk review process and will be in compliance with monitoring requirements by June 30, 2012. CMAA staff has developed a desk review process that is equitable to the site review process. The CMAA staff will develop a desk review schedule to ensure that the CMAA unit adheres to the requirement to conduct LGA reviews every four years. The CMAA staff will be in compliance with monitoring requirements by January 1, 2013.

In addition, there was an instance where there was no evidence that a CMAA unit claiming plan approval letter was properly authorized. This instance was identified as a clerical error due to staffing deficiencies and new procedures have been implemented to ensure proper document tracking and storage in the future. The CMAA unit clerical staff has been instructed to scan a copy of the original signed document and save the document as an Adobe pdf file on the Branch network server. The original will be mailed to the recipient and the pdf file will remain on the Branch server.

Reference Number: 2011-13-3

Federal Catalog Number: 93.778

Federal Program Title: Medicaid Cluster—Medical Assistance Program

(Medi-Cal)

Federal Award Numbers and Years: 05-1105CA5MAP; 2011

05-1005CA5MAP; 2010

Category of Finding: Subrecipient Monitoring

State Administering Department: Department of Health Care Services

(Health Care Services)

Criteria

TITLE 31-MONEY AND FINANCE, SUBTITLE V—GENERAL ASSISTANCE ADMINISTRATION, Section 7502—Audit Requirements; Exemptions

(f)(2) Each pass-through entity shall:

(d) Provide the subrecipient program names (and any identifying numbers) from which such assistance is derived, and the Federal requirements, which govern the use of such awards and the requirements of this chapter.

Condition

During procedures performed over award identification, we were unable to identify controls to ensure that award information was properly communicated to School-based Medi-Cal Administrative Activities (SMAA) Local Government Agencies (LGAs) and Local Education Consortiums (LECs). We noted the program uses SMAA agreements as a means to communicate award identification to its SMAA LGAs/LECs. These agreements do not contain the identifying Catalog of Federal Domestic Assistance (CFDA) number of the federal program that Health Care Services passed through to the subrecipient.

As a result, Health Care Services disbursed more than \$408 million to subrecipients without communicating complete award information for the fiscal year ended June 30, 2011.

Ouestioned Costs

No specific questioned costs were identified.

Recommendation

Health Care Services should implement policies and procedures to ensure that the identifying number of the federal program is included in each of its subgrant agreements.

Department's View and Corrective Action Plan

Health Care Services agrees with this recommendation.

The SMAA agreement, Exhibit B Budget Detail and Payment Provisions will be modified to include the following information:

Title 31—Money and Finance, Subtitle V—General Assistance Administration, Section 7502 requires each pass-through entity provide the subrecipient program names and any identifying numbers from which such assistance is derived. The CFDA number for this federal program is 93.778, Medi-Cal.

Reference Number: 2011-14-2

Federal Catalog Number: 93.268

Federal Program Title: Immunization Grants, Recovery Act Funded

Federal Award Numbers and Years: 5H23IP922507-09; 2011

5H23IP922507-08; 2010

Category of Finding: Special Tests and Provisions—Control,

Accountability, and Safeguarding of Vaccine

State Administering Department: Department of Public Health (Public Health)

Criteria

The *U.S. OFFICE OF MANAGEMENT AND BUDGET CIRCULAR A-133, AUDITS OF STATES, LOCAL GOVERNMENTS, AND NON-PROFIT ORGANIZATIONS* (OMB Circular A-133) the Compliance Supplement indicates that grantees must provide oversight of vaccinating providers to ensure that proper control and accountability is maintained for vaccine, vaccine is properly safeguarded, and eligibility screening is conducted.

Condition

During our procedures performed over special tests and provisions, control, accountability, and safeguarding of vaccine, we selected a sample of Quality Assurance Reviews (QAR) to determine whether Public Health provides oversight of vaccinating providers. Based on a review of the QAR samples, we noted that while Public Health had procedures for assessing provider storage procedures and reviewing provider medical records for documentation of eligibility screening, Public Health's QAR process did not include a review of inventory records.

As a result, inventory storage and handling procedures at vaccinating providers may not be adequate to ensure vaccines are properly accounted for. Additionally, if inventory records are not adequately monitored by the providers, vaccine levels may not be maintained at levels adequate to meet the needed demands.

Questioned Costs

No specific questioned costs were identified.

Recommendation

Public Health should enhance its current policies and procedures to include inventory record review and risk of loss from theft during QARs.

Department's View and Corrective Action Plan

Public Health disagrees that it should enhance its current policies and procedures to include inventory record review, and risk of loss from theft during QAR reviews. Public Health believes that the auditor's concerns do not consider other inventory control measures employed by Public Health outside of the QAR visit. The QAR visit is only one of the methods that Public Health uses to assess providers participating in the Vaccine for Children program (VFC). The requirements for what activities will occur during a QAR visit are dictated by the Centers for Disease Control and Prevention (CDC). CDC does not require a physical inventory during a QAR visit. However, CDC does require performing QAR visits on at least 50 percent of our providers yearly. This requirement means that Public Health

must perform over 2200 QAR visits per year. The time required to conduct a physical inventory would substantially reduce the number of QAR visits and thereby cause Public Health to fail to meet the CDC grant requirement and potentially put current funding levels at risk.

Public Health employs other inventory control measures outside of the QAR visit. Public Health assigns providers an ordering frequency based on the volume of vaccines they administer. Large volume providers order more frequently to minimize the amount of vaccine stored in their refrigerator at one time and thus minimize the risk of loss to the program if there are problems with storing the vaccine. If a provider's usage increases and he or she does not have enough vaccine to last until the next order, Public Health will authorize a supplemental order to ensure that the provider does not run out of vaccine. To ensure accountability for vaccines ordered, Public Health assesses inventory each time a provider orders vaccine. When a provider places an order, they account for each dose of vaccine received from Public Health. Public Health staff verify the number of doses distributed to that provider and ensure satisfactory accounting of all doses. If a provider cannot account for all of the vaccine, Public Health contacts the provider to resolve the issue before approving the order. Public Health then checks the current inventory level and reduces or augments to ensure providers have appropriate vaccine levels. These activities provide a sufficient, meaningful, real-time check that addresses the concern noted by the auditor.

Auditor's Comments on Department's View

While Public Health has other inventory control measures outside of the QAR visit, these consist of monitoring ordering frequency and inventory levels. No procedures exist to sample provider's inventory records to ensure proper recording of receipt, transfer, and usage of vaccines.

Reference Number: 2011-14-3

Federal Catalog Number: 93.778

Federal Program Title: Medicaid Cluster—Medical Assistance Program

(Medi-Cal)

Federal Award Numbers and Years: 05-1105CA5MAP; 2011

05-1005CA5MAP; 2010 05-1105CAARRA; 2011 05-1005CAARRA; 2010

Category of Finding: Special Tests & Provisions—Provider Eligibility

State Administering Department: Department of Health Care Services

(Health Care Services)

Criteria

TITLE 42 PUBLIC HEALTH, Part 431—STATE ORGANIZATION AND ADMINISTRATION, Subpart C—Administrative Requirements: Provider Relations, Section 431.107—Required Provider Agreement.

- (b) Agreements. A State plan must provide for an agreement between the Medicaid agency and each provider or organization furnishing services under the plan in which the provider or organization agrees to:
 - (1) Keep any records necessary to disclose the extent of services the provider furnishes to recipients;

- (2) On request, furnish to the Medicaid agency, the Secretary, or the State Medicaid fraud control unit (if such a unit has been approved by the Secretary under Section 455.300 of this chapter), any information maintained under paragraph (b)(1) of this section and any information regarding payments claimed by the provider for furnishing services under the plan;
- (3) Comply with the disclosure requirements specified in Part 455, Subpart B of this chapter;
- (4) Comply with the advance directives requirements for hospitals, nursing facilities, providers of home health care and personal care services, hospices, and HMOs specified in Part 489, subpart I, and Section 417.436(d) of this chapter;
- (5)(i) Furnish to the State agency its National Provider Identifier (NPI) (if eligible for an NPI); and
 - (ii) Include its NPI on all claims submitted under the Medicaid program.

Condition

Prior to November 1999, the Provider Enrollment Division (PED) of Health Care Services did not require its Medicaid providers to submit a provider agreement with the application package. PED has since updated its enrollment process to require provider agreements. Of the 50 providers we selected for provider eligibility testing, all of the providers selected had the required provider agreement. However, not all providers prior to 1999 have been reenrolled as of fiscal year 2010–11, and, as such, do not have the required re-enrollment package, including the required provider agreement, on file with PED.

Questioned Costs

No specific questioned costs were identified.

Recommendation

We recommend that Health Care Services should continue to strengthen and complete its efforts to re-enroll all active providers in order to ensure that all providers have a provider agreement in place.

Department's View and Corrective Action Plan

PED updated its provider enrollment process to require provider agreements and continues its plan to re-enroll all Medi-Cal providers as a continuous process as resources are available. Re-enrolled providers are required to submit a re-enrollment application package updated to current federal standards to retain Medi-Cal eligibility. PED has also updated its requirements so that all providers must submit a new application package to report a new, additional, or change in service location. In addition, state law requires that a new application be submitted when there is a change in business entity. Health Care Services continually verifies provider information to ensure compliance with state and federal requirements in its ongoing re-enrollment efforts.

The California Department of Public Health's (Public Health) Licensing and Certification Division is responsible for determining the eligibility of facility providers. In 2008, a new provider agreement was jointly developed for facility providers by Health Care Services and Public Health. Public Health continues to collect new provider agreements from facility providers.

Per Interagency Agreement (IA) Number 10-87042 between Public Health and Health Care Services implemented on July 1, 2010, Public Health collects, maintains, and stores enrolled facility provider records, including provider agreements. Public Health also forwards all provider agreements to Health Care Services.

Macias Gini & O'Connell LLP

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U.S. DEPARTMENT OF AGRICULTURE

Reference Number: 2011-13-4

Federal Catalog Numbers: 10.553, 10.555

Federal Program Titles: Child Nutrition Cluster: School Breakfast

Program and National School Lunch Program

Federal Award Number and Year: 58-3198-7430; 1998

Category of Finding: Subrecipient Monitoring

State Administering Department: Department of Education (Education)

Criteria

U.S. OFFICE OF MANAGEMENT AND BUDGET CIRCULAR A-133, *AUDITS OF STATES, LOCAL GOVERNMENTS, AND NON-PROFIT ORGANIZATIONS* (OMB CIRCULAR A-133), Subpart C—Auditees, Section .300—Auditee Responsibilities

(b) Maintain internal control over Federal programs that provides reasonable assurance that the auditee is managing Federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements that could have a material effect on each of its Federal programs.

TITLE 7—AGRICULTURE, CHAPTER II—FOOD AND NUTRITION SERVICE, DEPARTMENT OF AGRICULTURE, PART 210 NATIONAL SCHOOL LUNCH PROGRAM—Table of Contents, Subpart D-Requirements for State Agency Participation, Section 210.19 Additional responsibilities, (a) General Program management

(6) Food service management companies.

Each state agency shall annually review each contract (including all supporting documentation) between any school food authority and food service management company to ensure compliance with all the provisions and standards set forth in this part before execution of the contract by either party. When the state agency develops a prototype contract for use by the school food authority that meets the provisions and standards set forth in this part, this annual review may be limited to changes made to that contract. Each state agency shall review each contract amendment between a school food authority and food service management company to ensure compliance with all the provisions and standards set forth in this part before execution of the amended contract by either party. The state agency may establish due dates for submission of the contract or contract amendment documents. Each state agency shall perform an on-site review of each school food authority contracting with a food service management company, at least once during each five-year period. The state agency is encouraged to conduct such a review when performing reviews in accordance with Section 210.18. Such reviews shall include an assessment of the school food authority's compliance with Section 210.16 of this part. The state agency may require that all food service management companies that wish to contract for food service with any school food authority in the state register with the state agency. State agencies shall provide assistance upon request of a school food authority to assure compliance with program requirements.

Condition

Education lacked documentation of its approval of subrecipient contracts with food service management companies within its Child Nutrition Information and Payment System (CNIPS). Education did not implement appropriate internal controls and monitoring procedures to ensure the approval of the contracts was documented within CNIPS prior to funding reimbursements to subrecipients. Furthermore, four of the 51 contracts requested for testing of compliance with 7CFR210.19 could not be provided by Education. Of the 47 contracts that were tested, three did not

contain the required disclosures pursuant to 7CFR210.19. Education risks that reimbursements are being made to subrecipients for expenditures on contracts with food service management companies that do not meet the requirement of 7CFR210.19.

Questioned Costs

No specific questioned costs identified.

Recommendation

Education should strengthen the design of the application controls within CNIPS to require that food service management company contracts are in compliance with federal requirements and are properly approved prior to the approval of the annual renewal application and subsequent reimbursement of federal funds to subrecipients.

Department's View and Corrective Action Plan

To strengthen monitoring policies and procedures, Education is implementing the following actions to ensure that food service management company (FSMC) contracts are in compliance with Federal requirements:

- 1. Beginning January 2012, Education plans to re-direct existing staff to assist with the FSMC pre-approval process until additional permanent staff can be hired to maintain this process.
- 2. By April 1, 2012, establish a FSMC Registry, and require all FSMCs to register with Education in order to provide services to California's School Food Authorities (SFAs). This will:
 - Ensure that the SFAs are conducting competitive bidding procedures and contracting only with viable FSMCs.
 - Reduce the risk of non-responsive bids, by obtaining and maintaining required certifications.
 - Ensure the use of Education's prototype contracts.
 - Facilitate Education's oversight of FSMC contracting practices.
 - Enhance Education's ability to obtain accurate FSMC and SFA contracting data.
- 3. By April 1, 2012, Education will require SFAs to utilize a prototype contract designed to: (1) ensure that all contracts contain the required clauses; and (2) expedite contract review and approval processes.

U.S. DEPARTMENT OF EDUCATION

Reference Number: 2011-5-5

Federal Catalog Numbers: 84.126, 84.390

Federal Program Titles: Vocational Rehabilitation Cluster: Rehabilitation

Services—Vocational Rehabilitation Grants to States and Rehabilitation Services—Vocational Rehabilitation Grants to States, Recovery Act

Federal Award Numbers and Years: H126A1100005-11B; 2011

H126A100005C; 2010 H126A090005B; 2009

Category of Finding: Eligibility

State Administering Department: Department of Rehabilitation (Rehabilitation)

Criteria

TITLE 29—LABOR, CHAPTER 16—VOCATIONAL REHABILITATION AND OTHER REHABILITATION SERVICES, SUBCHAPTER I—VOCATIONAL REHABILITATION SERVICES, Part A—General Provisions, Section 722—Eligibility and Individualized Plan for Employment

(a)(6) Time frame for making an eligibility determination

The designated state unit shall determine whether an individual is eligible for vocational rehabilitation services under this subchapter within a reasonable period of time, not to exceed 60 days, after the individual has submitted an application for the services unless

- (A) exceptional and unforeseen circumstances beyond the control of the designated state unit preclude making an eligibility determination within 60 days and the designated state unit and the individual agree to a specific extension of time; or
- (B) the designated state unit is exploring an individual's abilities, capabilities, and capacity to perform in work situations under paragraph (2)(B).

Condition

Rehabilitation did not determine applicant eligibility for services within the required 60-day time period for six of the 60 applicant cases reviewed. For two of the six cases, Rehabilitation provided documentation supporting the mutual agreement with the applicant to extend the 60-day time period, however, the extension period had expired prior to final eligibility determination. The cause for the noncompliance with the 60-day time period requirement is primarily due to limitations of Rehabilitation's case management system. The case management system does not contain an automated mechanism for prompting caseworkers to complete eligibility determination for clients as deadlines approach and there is a lack of mitigating manual procedures and controls in place to ensure compliance with the requirement. Failure to determine an applicant's eligibility within the required time period in accordance with federal regulations prohibits qualified applicants from receiving timely vocational rehabilitation services. We reported a similar finding in our audits of fiscal years 2008–09 and 2009–10.

Questioned Costs

No specific questioned costs identified.

Recommendations

Rehabilitation should develop and implement procedures designed to assist caseworkers in managing and meeting eligibility determination deadlines. The procedures should be supplemented with tools developed within Rehabilitation's case management application that alert caseworkers when eligibility determination deadlines are approaching.

Department's View and Corrective Action Plan

Rehabilitation agrees with this finding. Rehabilitation has committed considerable resources over the past years to replace the Field Computer System used for case management during the scope of this audit with a new system (AWARE). Rehabilitation implemented AWARE as of October 2011, and expects to implement procedures designed to assist caseworkers in managing and meeting eligibility determination deadlines in 2012.

Rehabilitation will continue to emphasize the importance of manually tracking eligibility timelines and extensions. Counselors and managers will be oriented to the most effective tools available.

Upon completion of post-implementation AWARE enhancements, Counselors and Rehabilitation supervisors will receive automated "Activity Due" reminder notices in the system before the expiration of the 60 days allowed for eligibility determination. Additionally, the AWARE system contains ad hoc and managed layout reporting features that allow easily attainable reports produced by each user, facilitating increased monitoring at the local level.

Reference Number: 2011-7-1

Category of Finding: Level of Effort—Maintenance of Effort

State Administering Department: Department of Education (Education)

Federal Catalog Number: 84.010

Federal Program Title: Title I, Part A Cluster:

Title I Grants to Local Educational Agencies

Federal Award Numbers and Years: S010A100005A; 2010

S010A090005A; 2009 S010A080005A; 2008

Federal Catalog Number: 84.287

Federal Program Title: Twenty-First Century Community Learning

Centers

Federal Award Numbers and Years: S287C100005; 2010

S287C090005; 2009 S287C080005A; 2008

Federal Catalog Number: 84.365

Federal Program Title: English Language Acquisition Grants

Federal Award Numbers and Years: T365A100005A; 2010

T365A090005A; 2009 T365A080005A; 2008

Federal Catalog Number: 84.367

Federal Program Title: Improving Teacher Quality State Grants

Federal Award Numbers and Years: S367A100005A; 2010

S367A090005A; 2009 S367A080005A; 2008

Criteria

TITLE 34—EDUCATION, PART 299—GENERAL PROVISIONS, Subpart D—Fiscal Requirements, Section 299.5—What Maintenance of Effort Requirements Apply to ESEA Programs?

- (a) General. A LEA receiving funds under an applicable program listed in paragraph (b) of this section may receive its full allocation of funds only if the State Educational Agency (SEA) finds that either the combined fiscal effort per student or the aggregate expenditures of state and local funds with respect to the provision of free public education in the LEA for the preceding fiscal year was not less than 90 percent of the combined fiscal effort per student or the aggregate expenditures for the second preceding fiscal year.
- (d) Expenditures
 - (1) In determining an LEA's compliance with paragraph (a) of this section, the SEA shall consider only the LEA's expenditures from state and local funds for free public education. These include expenditures for administration, instruction, attendance and health services, pupil transportation services, operation and maintenance of plant, fixed charges, and net expenditures to cover deficits for food services and student body activities.
 - (2) The SEA may not consider the following expenditures in determining an LEA's compliance with the requirements in paragraph (a) of this section:
 - (i) Any expenditures for community services, capital outlay, debt service, or supplemental expenses made as a result of a Presidentially declared disaster.
 - (ii) Any expenditures made from funds provided by the federal government.

U.S. OFFICE OF MANAGEMENT AND BUDGET (OMB) *CIRCULAR A-133 COMPLIANCE SUPPLEMENT* (A-133 COMPLIANCE SUPPLEMENT), PART 3–COMPLIANCE REQUIREMENTS, Suggested Audit Procedures–Compliance

Level of Effort—Maintenance of Effort

2.1(c) Perform procedures to verify that the amounts used in the computation were derived from the books and records from which the audited financial statements were prepared.

Condition

Similar to an issue we reported for fiscal year 2009–10, Education was using unaudited local educational agency (LEA) expenditure figures to calculate compliance with the maintenance of effort (MOE) requirements instead of using the final audited expenditures. Upon further inquiry, we noted that LEAs are required to submit their unaudited financial trial balances electronically in the state-required format, Standard Account Code Structure (SACS), to Education by October 15th of each year. These SACS trial balances are then used for all LEA financial measurement calculations (such as level of effort) performed by Education. The final audited financial statements are submitted in hard copy or electronically to Education through the State Controller's Office by December 15th; however, there is not a required follow-up submission of the final SACS trial balance to Education. The financial statements submitted are not at the level of detail that would allow Education to prepare these fiscal effort calculations. There is no policy or procedure in place to review and reconcile the unaudited SACS trial balance to the final audited financial statement or to review the subsequent year's SACS trial balance submission in the following October for any material adjustments to the fund balance for prior-year audit adjustments.

For fiscal year 2010–11, the MOE is based on LEA expenditures for July 1, 2008 through June 30, 2009, which have since been audited and for which the audit reports have been completed and available since December 2009. Education's position is that it will not require LEAs to submit audited data during the 24 months between the audit date and the MOE date of December 2011. Education states that it cannot require LEAs to make an additional submission of the final audited expenditure data used to make these fiscal-effort calculations due to state law. However, by using the unaudited figures, there is a risk that material adjustments or omissions may not be adequately reflected and computed in the MOE calculation.

Questioned Costs

No specific questioned costs identified.

Recommendation

Education should enhance its current MOE policies and procedures to ensure that they comply with required federal guidelines.

Department's View and Corrective Action Plan

Education continues to work with the U.S. Department of Education's Risk Management Service and Office of Inspector General in exploring feasible and acceptable options for enhancing Education's existing MOE calculation process, including the use of unaudited versus audited data; as part of this cooperative effort, other states' processes will be considered.

Reference Number: 2011-7-2

Federal Catalog Number: 84.048

Federal Program Title: Career and Technical Education—

Basic Grants to States

Federal Award Number and Year: V048A080005; 2008

Category of Finding: Level of Effort—Maintenance of Effort

State Administering Department: Department of Education (Education)

Criteria

U.S. OFFICE OF MANAGEMENT AND BUDGET CIRCULAR A-133, *AUDITS OF STATES, LOCAL GOVERNMENTS, AND NON-PROFIT ORGANIZATIONS* (OMB CIRCULAR A-133), Subpart C—Auditees, Section .300—Auditee Responsibilities

(b) Maintain internal control over Federal programs that provides reasonable assurance that the auditee is managing Federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements that could have a material effect on each of its Federal programs.

Condition

Education was not able to provide support for the fiscal year 2007–08 student count that was used to determine Education's fiscal year 2010–11 maintenance of effort (MOE) compliance requirement for the Career and Technical Education program because the student count information was not retained nor can it be recreated from the Perkins Data System. Without proper documentation to support the calculation, Education cannot support compliance with the MOE requirement.

Questioned Costs

No specific questioned costs identified.

Recommendation

Education should strengthen its internal controls over records retention for all compliance requirements.

Department's View and Corrective Action Plan

To strengthen internal controls over the retention of documents related to determining MOE, Education is currently implementing a process in which all documents will be organized and available both electronically and in hard copy.

Current Year Reference Number: 2011-7-5

Federal Catalog Numbers: 84.027, 84.173

Federal Program Titles: Special Education Cluster (IDEA):

Special Education—Grants to States and Special Education—Preschool Grants

Federal Award Numbers and Years: H027A080116; 2008

H173A080120; 2008

Category of Finding: Level of Effort—Maintenance of Effort

State Administering Department: Department of Education (Education)

Criteria

TITLE 20—EDUCATION, CHAPTER 33—EDUCATION OF INDIVIDUALS WITH DISABILITIES, SUBCHAPTER II—ASSISTANCE FOR EDUCATION OF ALL CHILDREN WITH DISABILITIES, Section 1412—State eligibility

- (a) In general, a State is eligible for assistance under this subchapter for a fiscal year if the State submits a plan that provides assurance to the Secretary that the State has in effect policies and procedures to ensure that the State meets each of the following conditions:
 - (18) Maintenance of State financial support
 - (A) In general, the State does not reduce the amount of State financial support for special education and related services for children with disabilities, or otherwise made available because of the excess costs of educating those children, below the amount of that support for the preceding fiscal year.
 - (B) Reduction of funds for failure to maintain support
 - The Secretary shall reduce the allocation of funds under Section 1411 of this title for any fiscal year following the fiscal year in which the State fails to comply with the requirement of subparagraph (A) by the same amount by which the State fails to meet the requirement.
 - (C) Waivers for exceptional or uncontrollable circumstances

The Secretary may waive the requirement of subparagraph (A) for a State, for one fiscal year at a time, if the Secretary determines that—

- (i) granting a waiver would be equitable due to exceptional or uncontrollable circumstances such as a natural disaster or a precipitous and unforeseen decline in the financial resources of the State; or
- (ii) the State meets the standard in paragraph (17)(C) for a waiver of the requirement to supplement, and not to supplant, funds received under this subchapter.

(D) Subsequent years

If, for any year, a State fails to meet the requirement of subparagraph (A), including any year for which the State is granted a waiver under subparagraph (C), the financial support required of the State in future years under subparagraph (A) shall be the amount that would have been required in the absence of that failure and not the reduced level of the State's support.

Condition

The State's maintenance of effort (MOE) expenditures for its 2008–09 federal fiscal year grants totaled \$3,613,203,624, which was \$8,231,743 less than that for its 2007–08 federal fiscal year grants total of \$3,621,435,367. This appears to be a direct result of the downturn in the economy causing a decline of the state's financial resources. Unless Education applies for and receives a waiver, this noncompliance with the maintenance of effort requirement means that Education is subject to a reduction of federal funding in any following fiscal year by \$8,231,743.

Questioned Costs

No specific questioned costs identified.

Recommendations

Education should apply for the waiver. Furthermore, Education should develop procedures to monitor compliance throughout the grant period to ensure MOE requirements are being met; or if they are not being met, allow Education plenty of time to determine if the waiver criteria applies, and if so, apply for the waiver.

Department's View and Corrective Action Plan

As the auditors report, the economy caused an uncontrollable precipitous decline in the state's fiscal year 2008–09 financial resources. In addition, data for calculating MOE often changes for several years after the initial calculations. Therefore, Education is updating the data for calculating MOE, and will use this data to determine whether or not MOE requirements were met for fiscal year 2008–09. If necessary, Education will obtain the necessary fiscal information to support a request for waiver of the state's maintenance of effort requirement. To ensure that maintenance of effort requirements are currently being met and to allow for additional time if a request for waiver of the state maintenance of effort requirement is deemed necessary, Education will increase the frequency of calculating preliminary comparisons.

Reference Number: 2011-12-2

Federal Catalog Number: 84.388

Federal Program Title: School Improvement Grants Cluster:

School Improvement Grants, Recovery Act

Federal Award Number and Year: S388A090005A; 2009

Category of Finding: Reporting

State Administering Department: Department of Education (Education)

Criteria

Per OMB memorandum M-09-21, *Implementing Guidance for the Reports on Use of Funds Pursuant to the American Recovery and Reinvestment Act of 2009* dated June 22, 2009, Section 4.2, prime recipients, as owners of the data submitted, have the principal responsibility for the quality of the information submitted. Prime recipient:

- Owns recipient data and sub-recipient data
- Initiates appropriate data collection and reporting procedures to ensure that Section 1512 reporting requirements are met in a timely and effective manner
- Implements internal control measures as appropriate to ensure accurate and complete information
- Performs data quality reviews for material omissions and/or significant reporting errors, making appropriate and timely corrections to prime recipient data and working with the designated sub-recipient to address any data quality issues

Per Section 4.3, Federal agency, recipients, and sub-recipients should establish internal controls to ensure data quality, completeness, accuracy and timely reporting of all amounts funded by the Recovery Act. Possible approaches to this include:

- Establishing control totals (e.g., total number of projects subject to reporting, total dollars allocated to projects) and verify that reported information matches the established control totals;
- Creating an estimated distribution of expected data along a "normal" distribution curve and identifying outliers;
- Establishing a data review protocol or automated process that identifies incongruous results (e.g., total amount spent on a project or activity is equal to or greater than the previous reporting); and
- Establishing procedures and/cross-validation of data to identify and/or eliminate potential "double counting" due to delegation of reporting responsibility to sub-recipient.

Per Section 4.4, recipients and sub-recipients reporting Section 1512 data into the www.FederalReporting.gov solution must initiate a review of the data both prior to, and following, the formal submission of data. The post-submission review period runs from the 11th day of the reporting month to the 21st day of the reporting month for prime recipients. During this post-submission review period, significant reporting errors or material omissions that are discovered can be corrected using the www.FederalReporting.gov solution. Specific instructions for submitting new or corrected data will be provided on the www.FederalReporting.gov Web site. The prime recipients are responsible for reviewing data submitted by subrecipients. Where a recipient identifies a data quality issue with respect to information submitted by the subrecipient, the recipient is required to alert the relevant subrecipient of the nature of the problem identified by the recipient. All corrections by recipients and subrecipients during this phase of the review must be transmitted by the 21st day of the reporting month.

Condition

Education requires subrecipients of American Recovery and Reinvestment Act (ARRA) funding to submit Section 1512 report data using the Education developed web-based ARRA Reporting & Data Collection System and to maintain the records supporting the submitted data. During our testing of subrecipient monitoring, we noted that Education did not monitor subrecipients for accuracy in Section 1512 reporting. Education did not design and implement a monitoring process prior to the receipt of the grant.

Education's fourth quarter Section 1512 reporting reflected expenditures totaling \$67,540,741 being passed-through to subrecipients from inception to June 30, 2011, which represents 19 percent of Education's total Recovery Act award.

By not properly monitoring the accuracy of Section 1512 reporting, Education cannot ensure the quality and completeness of data submissions.

In addition, federal agencies will work to identify and remediate instances in which recipients that demonstrate systemic or chronic deficiencies in meeting its responsibilities to review and identify data quality problems of subrecipients consistent with the requirements of this guidance. On a case-by-case basis, such findings of a federal agency can result in termination of federal funding and/or initiation of suspension and debarment proceedings of either the recipient or subrecipient or both. Furthermore, in some cases, intentional reporting of false information can result in civil and/or criminal penalties.

Questioned Costs

No specific questioned costs identified.

Recommendations

Education should revise its current practices to conform with the requirements set-forth in OMB memorandum M-09-21. Management should design internal controls to ensure that such controls are operating effectively to ensure ongoing compliance with the aforementioned compliance requirements.

Department's View and Corrective Action Plan

To ensure reported Section 1512 data are complete, accurate, and consistent with guidance, Education has taken the following actions:

Subrecipient data pre-loaded from existing databases. This data includes the following:

- 1. Name, address, subrecipient type
- 2. CDS code (county-district-school, our code to identify local education agencies (LEAs))
- 3. Sub-award number
- 4. Sub-award amount
- 5. Amount disbursed

System checks

- 1. LEA data will not be saved unless all required fields are completed
- 2. DUNS number must contain nine digits
- 3. Congressional, State Senate, and State Assembly districts in right numerical range
- 4. Amount spent cannot be greater than award
- 5. Infrastructure spending permitted only with certain grants (State Fiscal Stabilization Fund Grants, Individuals with Disabilities Education Act, and Child Care and Development Block Grant, Quality Repair and Renovation)
- 6. Vendor information must include either DUNS number OR name and zip+4

Other checks

1. Use zip code software to validate addresses and add +4 if available (http://zip4.usps.com/zip4/welcome.jsp)

- 2. Check that Congressional district in the right range based on county code (part of CDS code [NativeCode])
- 3. Review jobs data for reasonableness
 - a. Divide grant award by \$50,000 for a reasonable job entry
 - b. If the total jobs entry (classified, certificated, and vendor job) exceeds the above reasonable check by 25 or more, then we follow up with LEAs.
- 4. Check that DUNS numbers not equal to 000000000; followed up with LEAs as appropriate.
- 5. Review data from the 10 largest LEAs; check for completeness, job reasonableness, and prior quarter entries such as following up on drops in full-time equivalents by 50 or more or any abnormalities in reported expenditures.
- 6. Notify subrecipients of the continuous correction period and encourage subrecipients to make corrections during that time.

In addition, Education's Fiscal Monitoring Unit (FMU) currently reviews selected LEA's reporting of Section 1512 data. Although not specific to the School Improvement Grant (SIG), the FMU assesses the accuracy of an LEA's compliance with Section 1512 reporting requirements. The implementation of on-site monitoring of SIG funds will commence in December 2011 through Education's Federal Program Monitoring process.

Reference Number: 2011-12-3

Federal Catalog Numbers: 84.126, 84.390

Federal Program Titles: Vocational Rehabilitation Cluster: Rehabilitation

Services—Vocational Rehabilitation Grants to States and Rehabilitation Services—Vocational Rehabilitation Grants to States, Recovery Act

Federal Award Numbers and Years: H126A1100005-11B; 2011

H126A100005C; 2010 H126A090005B; 2009

Category of Finding: Reporting

State Administering Department: Department of Rehabilitation (Rehabilitation)

Criteria

TITLE 34—EDUCATION—PART 80—UNIFORM ADMINISTRATIVE REQUIREMENTS FOR GRANTS AND COOPERATIVE AGREEMENTS TO STATE AND LOCAL GOVERNMENTS Subpart C—Post-Award Requirements—Reports, Records Retention, and Enforcement, Section 80.41—Financial Reporting

- (b) Financial Status Report—
 - (1) Form. Grantees will use Standard Form 269 or 269A, Financial Status Report, to report the status of funds for all nonconstruction grants and for construction grants when required in accordance with Section 80.41(e)(2)(iii).
 - (4) *Due date.* When reports are required on a quarterly or semiannual basis, they will be due 30 days after the reporting period. When required on an annual basis, they will be due 90 days after the grant year. Final reports will be due 90 days after the expiration or termination of grant support.

TITLE 34—EDUCATION—PART 361—STATE VOCATIONAL REHABILITATION SERVICES PROGRAM, Subpart B—State Plan and Other Requirements for Vocational Rehabilitation Services Administration—Section 361.40 Reports

- (a) The State plan must assure that the designated State agency will submit reports, including reports required under sections 13, 14, and 101(a)(10) of the Act—
 - (1) In the form and level of detail and at the time required by the Secretary regarding applicants for and eligible individuals receiving services under this part;

Condition

Rehabilitation did not submit four of five required financial reports tested on a timely basis. Rehabilitation was aware of the reporting due dates, however budget cuts and increased work assignments prevented the preparation and submission of the financial reports in a timely manner. Rehabilitation was proactive in notifying the federal contact that the reports would be submitted late; however, Rehabilitation did not receive a waiver/extension on the required report submittals. The impact of submitting late financial reports can result in disciplinary action from the federal agency and delay funding of federal draws.

Ouestioned Costs

No specific questioned costs identified.

Recommendation

Rehabilitation should reorganize staff assignments to ensure adequate resources are available to prepare and submit the required financial reports in a timely manner.

Department's View and Corrective Action Plan

Rehabilitation agrees with this finding. Rehabilitation will review its federal reporting staff assignments to ensure financial reports are submitted in a timely manner.

Reference Number: 2011-13-7

Category of Finding: Subrecipient Monitoring

State Administering Department: Department of Education (Education)

Federal Catalog Numbers: 84.010, 84.389

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Federal Program Titles: Title I, Part A Cluster:

Title I Grants to Local Educational Agencies; Title I Grants to Local Educational Agencies,

Recovery Act

Federal Award Numbers and Years: S010A100005A; 2010

S010A090005A; 2009 S010A080005A; 2008 S010A070005A; 2007 S389A090005A; 2009 Federal Catalog Number: 84.365

Federal Program Title: English Language Acquisition Grants

Federal Award Numbers and Years: T365A100005A; 2010

T365A090005A; 2009 T365A080005A; 2008 T365A070005A; 2007

Federal Catalog Number: 84.394

Federal Program Title: State Fiscal Stabilization Fund (SFSF)—

Education State Grants, Recovery Act

Federal Award Number and Year: S394A090005A; 2009

Federal Catalog Number: 84.410

Federal Program Title: Education Jobs Fund
Federal Award Number and Year: S410A100005; 2010

Criteria

TITLE 31—MONEY AND FINANCE, SUBTITLE V—GENERAL ASSISTANCE ADMINISTRATION, CHAPTER 75—REQUIREMENTS FOR SINGLE AUDITS, Section 7502—Audit Requirements; Exemptions

- (f)(2) Each pass-through entity shall:
 - (B) monitor the subrecipient's use of federal awards through site visits, limited scope audits, or other means.
 - (C) review the audit of a subrecipient as necessary to determine whether prompt and appropriate corrective action has been taken with respect to audit findings, as defined by the director, pertaining to federal awards provided to the subrecipient by the pass-through entity.

TITLE 34—EDUCATION, PART 80—UNIFORM ADMINISTRATIVE REQUIREMENTS FOR GRANTS AND COOPERATIVE AGREEMENTS TO STATE AND LOCAL GOVERNMENTS, Subpart C—Post-Award Requirements—Reports, Records Retention, and Enforcement, Section 80.40—Monitoring and Reporting Program Performance

(a) Monitoring by grantees. Grantees are responsible for managing the day-to-day operations of grant and subgrant supported activities. Grantees must monitor grant and subgrant supported activities to assure compliance with applicable federal requirements and that performance goals are being achieved. Grantee monitoring must cover each program, function, or activity.

Condition

As in the case of a similar condition we reported for fiscal year 2009–10, we reviewed the support for the follow-up by the Federal Program Monitoring Unit (FPM—formerly Categorical Monitoring) to ensure corrective action on deficiencies noted during FPM's reviews of local educational agencies (LEAs). We tested 45 of the 121 FPM onsite and online reviews completed during the year. We noted the number of days between the Notice of Findings (NOF) and the Proposed Resolution of Findings of Noncompliance (PRFN). Education requires the LEAs to submit a PRFN within 45 days of the NOF date. Of the 45 reviews tested, three had PRFN dates more than 45 days subsequent to the NOF date.

We noted that there were no communications from Education to those LEAs regarding the delinquency of the PRFN submission. We also noted the number of days between the NOF date and the receipt of the corrective actions that resulted in all deficiencies being resolved. Education requires the LEAs to allow reasonable time to resolve all deficiencies within 225 days of the NOF date. Of the 45 reviews tested, five had an unresolved status of more than 225 days subsequent to the NOF date. Upon further review, four of those five LEAs had either not yet submitted their corrective actions or had submitted insufficient corrective actions for all deficiencies noted during the review. The fifth LEA had submitted corrective actions for the deficiencies noted during the reviews within the 225-day period; however, Education had not resolved the deficiencies within the 225-day period.

The delayed resolution of outstanding monitoring deficiencies appear to be due to a combination of delayed follow up and ineffective sanctions imposed by Education on the LEAs for belated implementation of corrective action plans. Without effective consequences for the delays, LEAs do not have an incentive to implement corrective actions in a timely manner.

Questioned Costs

No specific questioned costs identified.

Recommendations

Education should enhance its current monitoring policies and procedures to ensure that LEAs implement promptly the proposed corrective actions on deficiencies noted during monitoring reviews and that consequences for delayed resolutions are effective for deterring such noncompliance. In addition, once it receives corrective action documents from LEAs, Education should be more prompt in resolving deficiency issues.

Department's View and Corrective Action Plan

To improve federal program monitoring, the FPM Office is implementing new functionalities in the Web-based on-line California Accountability and Improvement System (CAIS). The new electronic functionalities will replace paper-based processes to increase the effectiveness of monitoring the LEAs' resolution of findings. Currently, the resolution of findings process is conducted by using a paper system that is initiated by the LEA, uploaded to CAIS, and then reviewed by FPM Office staff. The new CAIS functionalities will provide FPM Office staff real-time compliance resolution tracking functions and access to LEA data such as the status of corrective actions taken to resolve identified deficiencies. As part of this improvement process, the FPM Office refined the monitoring protocols, and will: (1) provide program managers monthly updates on the resolution of findings; and (2) train staff on the use of CAIS' finding resolution process.

On an annual basis, Education submits for conditional approval LEAs with outstanding findings over 225 days to the State Board of Education. Education will continue this practice as a means to encourage LEAs to resolve findings in a timely matter. Furthermore, to encourage LEAs to resolve findings within the 225 day time frame, Education plans to post select findings on the Education Web site beginning in spring 2012.

Reference Number: 2011-13-8

Category of Finding: Subrecipient Monitoring

State Administering Department: Department of Education (Education)

Federal Catalog Numbers: 84.010, 84.389

Federal Program Titles: Title I, Part A Cluster:

Title I Grants to Local Educational Agencies; and Title I Grants to Local Educational Agencies,

Recovery Act

Federal Award Numbers and Years: S010A100005A; 2010

S010A090005A; 2009 S010A080005A; 2008 S010A070005A; 2007 S389A090005A; 2009

Federal Catalog Number: 84.011

Federal Program Title: Migrant Education—State Grant Program

Federal Award Numbers and Years: S011A100005A; 2010

S011A090005A; 2009 S011A080005A; 2008 S011A070005C; 2007

Federal Catalog Number: 84.048

Federal Program Title: Career and Technical Education—

Basic Grants to States

Federal Award Numbers and Years: V048A100005; 2010

V048A090005; 2009 V048A080005; 2008 V048A070005; 2007

Federal Catalog Number: 84.287

Federal Program Title: Twenty-First Century Community Learning

Centers

Federal Award Numbers and Years: S287C100005; 2010

S287C090005; 2009 S287C080005A; 2008 S287C070005; 2007

Federal Catalog Number: 84.365

Federal Program Title: English Language Acquisition Grants

Federal Award Numbers and Years: T365A100005A; 2010

T365A090005A; 2009 T365A080005A; 2008 T365A070005A; 2007 Federal Catalog Number: 84.367

Federal Program Title: Improving Teacher Quality State Grants

Federal Award Numbers and Years: S367A100005A; 2010

S367A090005A; 2009 S367A080005A; 2008 S367A070005A; 2007

Federal Catalog Number: 84.394

Federal Program Title: State Fiscal Stabilization Fund (SFSF)—

Education State Grants, Recovery Act

Federal Award Number and Year: S394A090005A; 2009

Federal Catalog Number: 84.410

Federal Program Title: Education Jobs Fund
Federal Award Number and Year: S410A100005; 2010

Criteria

U.S. OFFICE OF MANAGEMENT AND BUDGET CIRCULAR A-133, *AUDITS OF STATES, LOCAL GOVERNMENTS, AND NON-PROFIT ORGANIZATIONS* (OMB CIRCULAR A-133), Subpart C— Auditees, Section .300—Auditee Responsibilities

(b) Maintain internal control over federal programs that provides reasonable assurance that the auditee is managing federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements that could have a material effect on each of its federal programs.

Condition

Education uses a third-party application called WestEd Tracker (Tracker). This system was designed and is maintained by WestEd, a nonprofit public research and development agency. Tracker has two primary modules: Program Monitoring and Improvement Planning. The Federal Program Monitoring (FPM) unit of Education uses the Program Monitoring module, referred to as CAIS (California Accountability and Improvement System), to facilitate federal and state program monitoring. The use of CAIS was implemented during the fiscal year ended June 30, 2010, during the pilot phase of transitioning from a paper-based monitoring system to an electronic-based system. Since implementation there have been multiple changes to the program code as end-user functionality was enhanced and customized for use in subrecipient monitoring. Therefore, we assessed the controls over application change management and noted the following:

1. Tracker was developed by WestEd through the Southwest Comprehensive Center (SWCC) and the California Comprehensive Center (CACC), in collaboration with other state Departments of Education. Education does not have a contract or service level agreement with WestEd over the management of Tracker. This increases the risk that changes may be made to Tracker or the maintenance of Tracker may affect the accuracy, integrity and availability of the CAIS database. Education should consider working with the SWCC and CACC to develop a service-level agreement with WestEd for the use, maintenance and enhancements of Tracker. Additionally, Education, working with the SWCC and CACC, should request that WestEd have a Service Organization Review performed over their management controls of the Tracker application, in accordance with Statement on Standards for Attestation Engagements No. 16. We consider this to be a *significant deficiency*.

- 2. Education has little say in how Tracker is managed or what functionality it has or will have. Education is a user of a service provided by the CACC. This may impact Education if changes are made to the application that have a negative impact. Education must evaluate all implemented changes to Tracker in order to properly maintain records and controls in compliance with the approved FPM Subrecipient Monitoring Protocols (FPM Protocols). There is also little recourse for Education if Tracker adversely impacts monitoring efforts. In order to ensure that monitoring documents and materials are kept available, Education may want to consider maintaining their own backup copies of the database. Education may also want to consider documenting its analysis of implemented changes and conclusions as to the impact of those changes on maintaining compliance with FPM Protocols and resulting changes to FPM Protocols, if any. We consider this to be a *significant deficiency*.
- 3. Education is not generally aware of changes or updates to the application that are being considered or developed by WestEd. This places Education at increased risk of changes being applied to the application that may not be beneficial or may affect their ability to properly maintain records and controls in compliance with the approved FPM Protocols. Education should consider requesting that WestEd maintain an online log of planned changes to the application and their status in the development process. Additionally, Education should work to establish a service level agreement with WestEd to ensure that announcements of changes are made with enough advance notice so that Education's subrecipient users can be properly notified. We consider this to be a *significant deficiency*.
- 4. After planned changes are developed and tested within WestEd, the release is made available to Education users on PMT. WestEd.org Web site for user testing. WestEd should make greater effort to communicate the planned changes to Education and provide sufficient time for end-user acceptance testing before applying the changes to the production system. Standard test scripts should be used by Education to evaluate the release and ensure that program changes do not adversely affect the application functions. Education should work with WestEd to develop a set of test scripts that should be used whenever program changes are being made. We consider this to be a *significant deficiency*.

The overall risk to Education is that the current change controls over Tracker give rise to a higher risk of noncompliance with established FPM Protocols and therefore, to Education's ability to properly monitor subrecipients in accordance with federal regulations.

Questioned Costs

No specific questioned costs identified.

Recommendation

Education should enhance controls over CAIS program change management such that the risks noted in the deficiencies above are reduced to an acceptable level that allows Education to properly monitor subrecipients in accordance with federal regulations.

Department's View and Corrective Action Plan

To enhance existing controls, in the spring 2011, Education created a CAIS Steering Committee to monitor and provide direction related to the use of the CAIS within WestEd's "Tracker "modules. Education also designated a single point of contact between WestEd and Education to improve overall communication by meeting regularly to discuss issues of concern to the CAIS Steering Committee. In addition, in regard to the conditions noted by the auditors, the following actions will be, or have been, taken:

1. Although a formal contract or Memorandum of Understanding (MOU) between Education and WestEd was not initiated specific to Tracker, the CAIS Steering Committee has engaged internal information technology resources to assist in mitigating the risk that changes made to

Tracker may negatively impact CAIS. In December 2011, Education will discuss with the SWCC and CACC, the feasibility of requesting WestEd to have a Service Organization Review of its management controls over Tracker.

- 2. The CAIS Steering Committee identified the evaluation of existing and expanded functionality of the system as a critical issue and plans to resolve this matter through the establishment of a technical advisory committee. In spring 2012, the technical advisory committee will develop a process for reviewing requests for functionality and creating a tracking system to monitor such requests. The CAIS Steering Committee has engaged with internal information technology resources to assist with the issues raised relating to backup copies of the database.
- 3. The CAIS Steering Committee requested additional information from WestEd to identify pending changes and updates to Tracker. The CAIS Steering Committee also requested assistance from internal information technology resources to advise the technical advisory committee on the development of best practices to review change requests and establish a priority system for such requests by spring 2012. The designated point of contacts within WestEd and Education meet regularly to discuss these issues and Education plans to network with other states using Tracker to obtain feedback on best practices related to change requests.
- 4. The CAIS Steering Committee plans to resolve production system change issues through the establishment of a technical advisory committee to create protocols in December 2011. The CAIS Steering Committee also requested assistance from internal information technology resources to advise the technical advisory committee on the development of best practices related to user testing. The designated point of contacts with WestEd and Education meet regularly to discuss these issues and will continue to work to improve communication related to this matter.

Current Year Reference Number: 2011-13-9

Federal Catalog Number: 84.048

Federal Program Title: Career and Technical Education—

Basic Grants to States

Federal Award Numbers and Years: V048A100005; 2010

V048A090005; 2009 V048A080005; 2008

Category of Finding: Subrecipient Monitoring

State Administering Department: Department of Education (Education)

Criteria

U.S. OFFICE OF MANAGEMENT AND BUDGET CIRCULAR A-133, *AUDITS OF STATES, LOCAL GOVERNMENTS, AND NON-PROFIT ORGANIZATIONS* (OMB CIRCULAR A-133), Subpart B—Audits, Section ___.210—Subrecipient and vendor determinations

- (b) Federal award. Characteristics indicative of a Federal award received by a subrecipient are when the organization:
 - (1) Determines who is eligible to receive what federal financial assistance;
 - (2) Has its performance measured against whether the objectives of the federal program are met;
 - (3) Has responsibility for programmatic decision making;
 - (4) Has responsibility for adherence to applicable federal program compliance requirements; and
 - (5) Uses the federal funds to carry out a program of the organization as compared to providing goods or services for a program of the pass-through entity.

TITLE 31—MONEY AND FINANCE, SUBTITLE V—GENERAL ASSISTANCE ADMINISTRATION, CHAPTER 75—REQUIREMENTS FOR SINGLE AUDITS—Sec. 7502. Audit requirements; Exemptions

- (f)(2) Each pass-through entity shall
 - (A) provide such subrecipient the program names (and any identifying numbers) from which such assistance is derived, and the Federal requirements which govern the use of such awards and the requirements of this chapter;
 - (B) monitor the subrecipient's use of Federal awards through site visits, limited scope audits, or other means;
 - (C) review the audit of a subrecipient as necessary to determine whether prompt and appropriate corrective action has been taken with respect to audit findings, as defined by the director, pertaining to federal awards provided to the subrecipient by the pass-through entity; and
 - (D) require each of its subrecipients of Federal awards to permit, as a condition of receiving Federal awards, the independent auditor of the pass-through entity to have such access to the subrecipient's records and financial statements as may be necessary for the pass-through entity to comply with this chapter.

Condition

Similar to an issue we reported for year ended June 30, 2010, Education is not properly monitoring the Board of Governors of the California Community Colleges (CCC) use of Career and Technical Education—Basic Grants to States (CTE) program funds. Education had considered its relationship with the CCC to be that of a vendor, therefore, was not monitoring the CCC's use of CTE funds even though Education's interagency agreement with the CCC defines a subrecipient relationship. For fiscal year 2011—12, Education has added a monitoring clause to interagency contracts with the CCC, however, Education has not yet begun monitoring the CCC's use of the CTE funds.

During the fiscal year ended June 30, 2011, Education disbursed \$62,364,915 to CCC, which represents 50% of the total award funds disbursed for the fiscal year ended June 30, 2011.

Thus, Education is not in compliance with the subrecipient monitoring requirements of OMB Circular A-133 as it relates to CCC.

Questioned Costs

No specific questioned costs identified.

Recommendation

Education should enhance its policies and procedures to ensure that subrecipient and vendor relationships are properly identified in order to ensure that all subrecipients are properly included in Education's subaward monitoring activities.

Department's View and Corrective Action Plan

As reported by the auditors, Education has enhanced its policies and procedures by adding a monitoring clause to its interagency contracts with the CCC. In addition, in January 2012, Education will meet with the new Dean of Career Education Practices at CCC to finalize and implement the process of the ongoing monitoring of CCC's use of CTE funds.

Reference Number: 2011-13-10

Federal Catalog Numbers: 84.377, 84.388

Federal Program Titles: School Improvement Grants Cluster:

School Improvement Grants, and

School Improvement Grants, Recovery Act

Federal Award Numbers and Years: S377A100005; 2010

S388A090005A; 2009 S377A090005A; 2009 S377A080006; 2008

Category of Finding: Subrecipient Monitoring

State Administering Department: Department of Education (Education)

Criteria

TITLE 31—MONEY AND FINANCE, SUBTITLE V—GENERAL ASSISTANCE ADMINISTRATION, CHAPTER 75—REQUIREMENTS FOR SINGLE AUDITS, Sec. 7502—Audit requirements; Exemptions

- (f)(2) Each pass-through entity shall—
 - (B) monitor the subrecipient's use of Federal awards through site visits, limited scope audits, or other means;

Condition

During our information gathering to gain an understanding of the internal controls over the administration of the School Improvement Grant (SIG) program, it was noted that Education does not monitor subrecipients for their use of program funds through site visits, limited scope audits, or other means. Education did not design and implement a monitoring process prior to the receipt of the grant.

By not properly monitoring subrecipients for their use of SIG funds through site visits, limited scope audits, or other means, Education cannot ensure that subrecipients administer federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.

Questioned Costs

No specific questioned costs identified.

Recommendation

Education should enhance its subrecipient monitoring policy to ensure that subrecipients administer federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.

Department's View and Corrective Action Plan

Education plans to enhance monitoring over SIG sub-grantees by implementing new fiscal and programmatic processes.

Fiscal Monitoring:

On-site monitoring of SIG sub-grantees will commence in December 2011 through Education's Federal Program Monitoring (FPM) process; additional monitoring will also be scheduled outside of the FPM process. Education will require SIG sub-grantees to submit quarterly

expenditure reports for the duration of their sub-grant awards. The expenditure reports will be reviewed for reasonableness and to ensure that each school has expended at least 75 percent of the SIG funds before receiving more SIG funding.

Programmatic Monitoring:

To ensure compliance and implementation of proposed SIG program activities, Education developed implementation charts to track local educational agencies (LEAs) progress and timelines. In addition, over a three-year grant period, Education will conduct a minimum of one site visit at SIG-funded LEAs to verify implementation; LEAs will be required to submit evidence of compliance with grant requirements.

Education also will require LEAs to submit SIG program data annually. The required data includes: (1) a description of the intervention the school used (i.e., turnaround, restart, school closure, or transformation); (2) the number of minutes within the school year; (3) the average scale scores on State assessments in reading/language arts and mathematics, by grade, for all student groups, for each achievement quartile, and for each subgroup; (4) the number and percentage of students completing advanced coursework (e.g., Advanced Placement (AP)/ International Baccalaureate (IB)); (5) lists of early-college high schools, or dual enrollment classes; and (6) the teacher attendance rate. Education will also require LEAs to submit initial baseline data in addition to the yearly data.

To monitor LEAs' achievement of their annual school goals, such as student achievement on the State's Elementary and Secondary Education Act (ESEA) assessments in both reading/language arts and mathematics, and progress on the leading indicators described in the final requirements, Education will annually assess LEAs' progress on student achievement for each of its Tier I and Tier II schools to determine renewal of SIG funds.

Reference Number: 2011-14-5

Federal Catalog Number: 84.388

Federal Program Title: School Improvement Grants Cluster:

School Improvement Grants, Recovery Act

Federal Award Number and Year: S388A090005A; 2009

Category of Finding: Special Tests & Provisions

State Administering Department: Department of Education (Education)

Criteria

TITLE 2—GRANTS AND AGREEMENTS, CHAPTER I—U.S.OFFICE OF MANAGEMENT AND BUDGET GOVERNMENTWIDE GUIDANCE FOR GRANTS AND AGREEMENTS, PART 176—AWARD TERMS FOR ASSISTANCE AGREEMENTS THAT INCLUDE FUNDS UNDER THE AMERICAN RECOVERY AND REINVESTMENT ACT OF 2009, Subpart D—Single Audit Information for Recipients of Recovery Act Funds

Section 176.210 Award term—Recovery Act transactions listed in Schedule of Expenditures of Federal Awards and Recipient Responsibilities for Informing Subrecipients.

(c) Recipients agree to separately identify to each subrecipient, and document at the time of subaward and at the time of disbursement of funds, the federal award number, Catalog of Federal Domestic Assistance (CFDA) number, and amount of Recovery Act funds. When a recipient awards Recovery Act funds for an existing program, the information furnished to subrecipients shall distinguish the subawards of incremental Recovery Act funds from regular subawards under the existing program.

Condition

During our testing of the Special Tests and Provisions compliance requirement, including discussions with program management, we noted that Education is not identifying to each of its subrecipients, and documenting at the time of subaward the federal award number, CFDA number, and amount of American Recovery and Reinvestment Act of 2009 (Recovery Act) funds. Also, at the time of disbursement of Recovery Act funds, Education is not informing each subrecipient the federal award number, CFDA number, and the amount of Recovery Act funds. Education was not aware of the additional Recovery Act requirements regarding subrecipient notification of award information at the time of award and at the time of disbursement.

Education's Section 1512 reporting for the quarter ended June 30, 2011, reflected expenditures totaling \$67,540,741 being passed-through to subrecipients, which represents 19 percent of the total Recovery Act award to Education.

By not properly informing its subrecipients of the federal award number, CFDA number, and the amount of Recovery Act funds, there is a risk that subrecipients may not be identifying and properly accounting for and reporting Recovery Act funds. This may result in reducing Education's ability to properly monitor the subrecipients expenditure of Recovery Act funds, as well as, assisting in any oversight by the federal awarding agency, Office of Inspector General and the Government Accountability Office.

Questioned Costs

No specific questioned costs identified.

Recommendations

Education should revise its current practices to conform with the requirements set forth in 2 CFR, Section 176.210. Management should design internal controls to ensure that such controls are operating effectively to ensure ongoing compliance with the aforementioned compliance requirements.

Department's View and Corrective Action Plan

Effective September 2011, Education revised its AO-400 grant award form and instructions to ensure conformance with the requirements set forth in 2 CFR, Section 176.210, including the identification of the federal award numbers, CFDA numbers, and the amount of Recovery Act funds. The U.S. Department of Education (ED) found Education's internal controls of tracking grant award allocations separately, and the reporting of Recovery Act 1512 data using its Standardized Account Code Structure resource codes adequate to avoid confusion when accounting between Recovery Act and regular funds.

Given the fact that all Recovery Act funds have already been distributed, Education does not consider it cost beneficial to make further changes to Grant Award Notification letters. Moreover, ED's Office of Special Education and Rehabilitative Services (SERS) issued a program determination addressing the same condition for another federal program; ED did not require Education to modify Grant Award Notification letters in order to comply with Recovery Act reporting requirements.

Auditor's Comments on Department's View

Per our conversation with ED's Office of Special Education and Rehabilitative Services (SERS) that issued the determination letter dated September 30, 2011, as referenced above, the determination letter solely applies to the Special Education Cluster grants as SERS has no authority over the School Improvement Grants. However, as Education has included it as precedent in the response above, we respond as follows:

We agree with ED and Education that it is ineffective to modify the AO-400 grant award form given that all Recovery Act funds have been awarded. Per our conversation with SERS, ED agreed that this does not, however, preclude Education from providing the appropriate notifications given that subrecipients have one final Single Audit report for the fiscal year ending June 30, 2012, that will include expenditures of Recovery Act funds.

Also per our conversation with ED, while the determination letter did not require further revisions to the AO-400 grant award form, it did not consider the issue of proper notification to subrecipients at the time of disbursement to be resolved and closed. This finding does not take issue with Education's method of separately tracking Recovery Act funds for Education's recordkeeping. This finding is with regard to properly notifying subrecipients at the time of award and at the time of disbursement so that subrecipient records can properly track Recovery Act funds separate from other award funds.

Current Year Reference Number: 2011-14-7

Federal Catalog Numbers: 84.391, 84.392

Federal Program Titles: Special Education Cluster (IDEA):

Special Education—Grants to States, Recovery Act and Special Education—Preschool Grants,

Recovery Act.

Federal Award Numbers and Years: H391A090116A; 2009

H392A090120A; 2009

Category of Finding: Special Tests & Provisions

State Administering Department: Department of Education (Education)

Criteria

TITLE 2—GRANTS AND AGREEMENTS, CHAPTER I—OFFICE OF MANAGEMENT AND BUDGET GOVERNMENTWIDE GUIDANCE FOR GRANTS AND AGREEMENTS, PART 176—AWARD TERMS FOR ASSISTANCE AGREEMENTS THAT INCLUDE FUNDS UNDER THE AMERICAN RECOVERY AND REINVESTMENT ACT OF 2009, Subpart D—Single Audit Information for Recipients of Recovery Act Funds

Section 176.210 Award term—Recovery Act transactions listed in Schedule of Expenditures of Federal Awards and Recipient Responsibilities for Informing Subrecipients.

(c) Recipients agree to separately identify to each subrecipient, and document at the time of subaward and at the time of disbursement of funds, the Federal award number, CFDA number, and amount of Recovery Act funds. When a recipient awards Recovery Act funds for an existing program, the information furnished to subrecipients shall distinguish the subawards of incremental Recovery Act funds from regular subawards under the existing program.

Condition

Similar to a finding reported in the prior year, during our testing of the Special Tests and Provisions compliance requirement, including discussions with program management, we noted that Education had not identified to each of its American Recovery and Reinvestment Act (Recovery Act) subrecipients and documented at the time of subaward the federal award number. At the time Education was notified of this deficiency, it was noted that there would be no further awards of Recovery Act grants to subrecipients. However, Education did not take action to subsequently notify existing subrecipients of the required information. Also, at the time of disbursement of Recovery Act funds, Education is not informing each subrecipient the federal award number, CFDA number, and the amount of Recovery Act funds.

Education's fourth quarter Section 1512 reporting reflected expenditures totaling \$1,128,433,193 being passed-through to subrecipients, which represents 89 percent of the total Recovery Act award to Education.

By not properly informing its subrecipients of the federal award number, CFDA number, the amount of Recovery Act funds, there is a risk that subrecipients may not be identifying and properly accounting and reporting Recovery Act funds. This may result in reducing Education's ability to properly monitor the subrecipients expenditure of Recovery Act funds, as well as, assisting in any oversight by the federal awarding agency, Office of Inspector General and the Government Accountability Office.

Questioned Costs

No specific questioned costs identified.

Recommendations

Education should revise its current practices to conform with the requirements set forth in 2 CFR, Section 176.210. Management should design internal controls to ensure that such controls are operating effectively to ensure ongoing compliance with the aforementioned compliance requirements.

Department's View and Corrective Action Plan

Education does not disagree with this finding. Effective September 2011, Education revised its AO-400 grant award form and instructions to ensure conformance with the requirements set forth in 2 CFR, Section 176.210, including the identification of the federal award numbers, CFDA numbers, and the amount of Recovery Act funds.

Given the fact that all IDEA Part B Recovery Act funds have already been distributed, the U.S. Department of Education's (ED) September 30, 2011, program determination letter found no compelling reason to require Education to make further changes to its Grant Award Notification in order to comply with Recovery Act reporting requirements. Furthermore, ED found Education's internal controls of tracking grant award allocations separately, and the reporting of Recovery Act 1512 data using its Standardized Account Code Structure resource codes adequate to avoid confusion when accounting for Individuals with Disabilities Education Act (IDEA) Part B Recovery Act funds separately from regular IDEA Part B funds. The ED's Assistant Secretary required no further corrective action and considered this condition to be resolved and closed.

Auditor's Comments on Department's View

We agree with ED and Education that it is ineffective to modify the AO-400 grant award form given that all Recovery Act funds have been awarded. Per our conversation with ED's Office of Special Education and Rehabilitative Services that issued the determination letter dated September 30, 2011 as referenced above, ED agreed that this does not, however, preclude Education from providing the appropriate notifications given that subrecipients have one final Single Audit report for the fiscal year ending June 30, 2012, that will include expenditures of Recovery Act funds.

Also, per our conversation with ED, while the determination letter did not require further revisions to the AO-400 grant award form, it did not consider the issue of proper notification to subrecipients at the time of disbursement to be resolved and closed. This finding does not take issue with Education's method of separately tracking Recovery Act funds for Education's record keeping. This finding is with regard to properly notifying subrecipients at the time of award and at the time of disbursement so that subrecipient records can properly track Recovery Act funds separate from other award funds.

U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES

Reference Number: 2011-7-8

Federal Catalog Number: 93.959

Federal Program Title: Block Grants for Prevention and Treatment of

Substance Abuse (SAPT)

Federal Award Numbers and Years: 2B08TI010005-11; 2010

2B08TI010005-10; 2009

Category of Finding: Level of Effort—Maintenance of Effort

State Administering Department: Department of Alcohol and Drug Programs

(ADP)

Criteria

TITLE 42—THE PUBLIC HEALTH AND WELFARE, CHAPTER 6A—PUBLIC HEALTH SERVICE, SUBCHAPTER XVII—BLOCK GRANTS, Part B—Block Grants Regarding Mental Health and Substance Abuse, Subpart ii—Block Grants for Prevention and Treatment of Substance Abuse, Section 300x-30—Maintenance of Effort Regarding State Expenditures

(a) In general

With respect to the principal agency of a State for carrying out authorized activities, a funding agreement for a grant under section 300x-21 of this title for the State for a fiscal year is that such agency will for such year maintain aggregate State expenditures for authorized activities at a level that is not less than the average level of such expenditures maintained by the State for the two-year period preceding the fiscal year for which the State is applying for the grant.

(c) Waiver

(1) In general

Upon the request of a State, the Secretary may waive all or part of the requirement established in subsection (a) of this section if the Secretary determines that extraordinary economic conditions in the State justify the waiver

TITLE 45—PUBLIC WELFARE, Part 96—BLOCK GRANTS, Subpart L—Substance Abuse Prevention and Treatment Block Grant, Section 96.134—Maintenance of Effort Regarding State Expenditures

(a) With respect to the principal agency of a State for carrying out authorized activities, the agency shall for each fiscal year maintain aggregate State expenditures by the principal agency for authorized activities at a level that is not less than the average level of such expenditures maintained by the State for the two-year period preceding the fiscal year for which the State is applying for the grant. The block grant shall not be used to supplant State funding of alcohol and other drug prevention and treatment programs.

Condition

ADP did not maintain the required level of aggregate State expenditures in fiscal year 2010–11. Specifically, ADP reported a maintenance of effort (MOE) shortfall of \$37,426,500, which is based on an MOE level that is calculated as the average expenditures from the two prior fiscal years—2008–09 and 2009–10. ADP acknowledges that it did not meet the MOE requirement.

In requesting the waiver from the U.S. Department of Health and Human Services Substance Abuse and Mental Health Services Administration (SAMHSA), ADP stated that the extraordinary decline in tax revenues in state fiscal year 2008–09 resulted in significant state budget deficits. The State's constitution requires a balanced budget and therefore, for state fiscal year 2009–10, the Governor

proposed and the Legislature acted upon numerous means to balance the budget, including program savings, increasing savings targets, instituting program reforms, reductions in education funding, increasing targeted fees, borrowing, and eliminating funding for some programs, which ADP administers. Because these funding cuts flowed through ADP through the fiscal year ended June 30, 2011, they were part of its MOE calculation. Complete elimination of the Substance Abuse and Crime Prevention Act (Prop. 36) in large part resulted in the MOE shortfall.

ADP is not in compliance with the MOE requirement and risks a reduction to its future SAPT funding. ADP submitted the waiver request in October 2011 and SAMHSA has 120 days to make a waiver determination.

Questioned Costs

No specific questioned costs identified.

Recommendation

ADP should continue to follow up with SAMHSA regarding its waiver request.

Department's View and Corrective Action Plan

ADP agrees with the finding and recommendation that ADP did not maintain the required level of aggregate state expenditures in fiscal year 2010–11, and should continue to follow up with SAMHSA regarding its waiver request.

The principal agency of a State for carrying out authorized activities, shall for each fiscal year maintain aggregate expenditures by the principal agency at a level that is not less than the average level of such expenditures maintained by the State for the two year period preceding the fiscal year for which the State is applying for the grant. As such, the elimination of funding in previous fiscal years continued to impact ADP's MOE calculation in fiscal year 2010–11.

As a result of the budget shortfall, and in compliance with Title 45, Code of Federal Regulations, (CFR) Part 96, Section 96.134(b), ADP submitted an MOE Waiver request, for reason of extraordinary economic conditions, to the Substance Abuse and Mental Health Administration (SAMHSA) on October 18, 2011. The statute and regulation require the Secretary of the U.S. Department of Health and Human Services to approve or deny a State's request for waiver not later than 120 days after the date on which the request is made.

ADP will continue to follow up with SAMHSA regarding the waiver request.

Reference Number: 2011-13-5

Federal Catalog Numbers: 93.575, 93.596, and 93.713

Federal Program Titles: CCDF Cluster:

Child Care and Development Block Grant; Child Care Mandatory and Matching Funds of the Child Care and Development Fund; and Child Care and Development Block Grant,

Recovery Act

Federal Award Numbers and Years: G1001CACCDF; 2010

G0901CACCD7; 2009 G0901CACCDF; 2009 G0801CACCDF; 2008

Category of Finding: Subrecipient Monitoring

State Administering Department: Department of Education (Education)

Criteria

TITLE 31—MONEY AND FINANCE, SUBTITLE V—GENERAL ASSISTANCE ADMINISTRATION, CHAPTER 75—REQUIREMENTS FOR SINGLE AUDITS, Section 7502—Audit Requirements; Exemptions

- (f)(2) Each pass-through entity shall:
 - (B) monitor the subrecipient's use of federal awards through site visits, limited scope audits, or other means.
 - (C) review the audit of a subrecipient as necessary to determine whether prompt and appropriate corrective action has been taken with respect to audit findings, as defined by the director, pertaining to federal awards provided to the subrecipient by the pass-through entity.

TITLE 34—EDUCATION, PART 80—UNIFORM ADMINISTRATIVE REQUIREMENTS FOR GRANTS AND COOPERATIVE AGREEMENTS TO STATE AND LOCAL GOVERNMENTS, Subpart C—Post-Award Requirements—Reports, Records Retention, and Enforcement, Section 80.40—Monitoring and Reporting Program Performance

(a) Monitoring by grantees. Grantees are responsible for managing the day-to-day operations of grant and subgrant supported activities. Grantees must monitor grant and subgrant supported activities to assure compliance with applicable federal requirements and that performance goals are being achieved. Grantee monitoring must cover each program, function, or activity.

Condition

As in the case of a similar condition we reported for fiscal year 2009–10, we reviewed the support for the follow-up by the Federal Program Monitoring Unit (FPM—formerly Categorical Monitoring) to ensure corrective action on deficiencies noted during FPM's reviews of local educational agencies (LEAs). We tested 23 of the 25 FPM onsite and online reviews completed during the year. We noted the number of days between the Notice of Findings (NOF) and the Proposed Resolution of Findings of Noncompliance (PRFN). Education requires the LEAs to submit a PRFN within 45-days of the NOF date. Of the 23 reviews tested, one had a PRFN date more than 45 days subsequent to the NOF date. We noted that there were no communications from Education to that LEA regarding the delinquency of the PRFN submission. We also noted the number of days between the NOF date and the receipt of the corrective actions that resulted in all deficiencies being resolved. Education requires the LEAs to allow reasonable time to resolve all deficiencies within 225 days of the NOF date. Of the 23 reviews tested, two had an unresolved status of more than 225 days subsequent to the NOF date. Upon further review, one of those two LEAs had not yet submitted its corrective actions for all deficiencies noted during the review. The second LEA had submitted corrective actions for the deficiencies noted during the review within the 225-day period; however, Education had not resolved the deficiencies within the 225-day period.

The delayed resolution of outstanding monitoring deficiencies appears to be due to a combination of delayed follow up and ineffective sanctions imposed by Education on the LEAs for belated implementation of corrective action plans. Without effective consequences for the delays, LEAs do not have an incentive to implement corrective actions in a timely manner.

Questioned Costs

No specific questioned costs identified.

Recommendations

Education should enhance its current monitoring policies and procedures to ensure that LEAs implement promptly the proposed corrective actions on deficiencies noted during monitoring reviews and that consequences for delayed resolutions are effective for deterring such noncompliance. In addition, once it receives corrective action documents from LEAs, Education should be more prompt in resolving deficiency issues.

Department's View and Corrective Action Plan

To improve federal program monitoring, the FPM Office is implementing new functionalities in the Web-based on-line California Accountability and Improvement System (CAIS). The new electronic functionalities will replace paper-based processes to increase the effectiveness of monitoring the LEAs' resolution of findings. Currently, the resolution of findings process is conducted by using a paper system that is initiated by the LEA, uploaded to CAIS, and then reviewed by FPM Office staff. The new CAIS functionalities will provide FPM Office staff real-time compliance resolution tracking functions and access to LEA data such as the status of corrective actions taken to resolve identified deficiencies. As part of this improvement process, the FPM Office refined the monitoring protocols, and will: (1) provide program managers monthly updates on the resolution of findings; and (2) train staff on the use of CAIS' finding resolution process.

On an annual basis, Education submits for conditional approval LEAs with outstanding findings over 225 days to the State Board of Education. Education will continue this practice as a means to encourage LEAs to resolve findings in a timely matter. Furthermore, to encourage LEAs to resolve findings within the 225 day time frame, Education plans to post select findings on the Education Web site beginning in Spring 2012.

Reference Number: 2011-13-6

Federal Catalog Numbers: 93.575, 93.596, and 93.713

Federal Program Titles: Child Care Development Fund Cluster:

Child Care and Development Block Grant; Child Care Mandatory and Matching Funds of the Child Care and Development Fund;

and Child Care and Development Block Grant,

Recovery Act Funded

Federal Award Numbers and Years: G1001CACCDF; 2010

G0901CACCD7; 2009 G0901CACCDF; 2009 G0801CACCDF; 2008

Category of Finding: Subrecipient Monitoring

State Administering Department: Department of Education (Education)

Criteria

U.S. OFFICE OF MANAGEMENT AND BUDGET CIRCULAR A-133, *AUDITS OF STATES, LOCAL GOVERNMENTS, AND NON-PROFIT ORGANIZATIONS* (OMB CIRCULAR A-133), Subpart C—Auditees, Section .300—Auditee Responsibilities

(b) Maintain internal control over Federal programs that provides reasonable assurance that the auditee is managing Federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements that could have a material effect on each of its Federal programs.

Condition

Education uses a third-party application called WestEd Tracker (Tracker). This system was designed and is maintained by WestEd, a nonprofit public research and development agency. Tracker has two primary modules: Program Monitoring and Improvement Planning. The Federal Program Monitoring (FPM) unit of Education uses the Program Monitoring module, referred to as CAIS (California Accountability and Improvement System), to facilitate Federal and State program monitoring. The use of CAIS was implemented during the fiscal year ended June 30, 2010, during the pilot phase of transitioning from a paper based monitoring system to an electronic based system. Since implementation there have been multiple changes to the program code as end user functionality was enhanced and customized for use in subrecipient monitoring. Therefore, we assessed the controls over application change management and noted the following:

- 1. Tracker was developed by WestEd through the Southwest Comprehensive Center (SWCC) and the California Comprehensive Center (CACC), in collaboration with other state Departments of Education. Education does not have a contract or service level agreement with WestEd over the management of Tracker. This increases the risk that changes may be made to Tracker or the maintenance of Tracker may affect the accuracy, integrity and availability of the CAIS database. Education should consider working with the SWCC and CACC to develop a service level agreement with WestEd for the use, maintenance and enhancements of Tracker. Additionally, Education, working with the SWCC and CACC, should request that WestEd have a Service Organization Review performed over their management controls of the Tracker application, in accordance with Statement on Standards for Attestation Engagements Number 16. We consider this to be a significant deficiency.
- 2. Education has little say in how Tracker is managed or what functionality it has or will have. Education is a user of a service provided by the CACC. This may impact Education if changes are made to the application that have a negative impact. Education must evaluate all implemented changes to Tracker in order to properly maintain records and controls in compliance with the approved FPM Subrecipient Monitoring Protocols (FPM Protocols). There is also little recourse for the Education if Tracker adversely impacts monitoring efforts. In order to ensure that monitoring documents and materials are kept available, Education may want to consider maintaining their own backup copies of the database. Education may also want to consider documenting its analysis of implemented changes and conclusions as to the impact of those changes on maintaining compliance with FPM Protocols and resulting changes to FPM Protocols, if any. We consider this to be a *significant deficiency*.
- 3. Education is not generally aware of changes or updates to the application that are being considered or developed by WestEd. This places Education at increased risk of changes being applied to the application that may not be beneficial or may affect their ability to properly maintain records and controls in compliance with the approved FPM Protocols. Education should consider requesting that WestEd maintain an online log of planned changes to the application and their status in the development process. Additionally, Education should work to establish a service level agreement with WestEd to ensure that announcements of changes are made with enough advance notice so that Education's subrecipient users can be properly notified. We consider this to be a *significant deficiency*.
- 4. After planned changes are developed and tested within WestEd, the release is made available to Education users on PMT.WestEd.org Web site for user testing. WestEd should make greater effort to communicate the planned changes to Education and provide sufficient time for end-user acceptance testing before applying the changes to the production system. Standard test scripts should be used by Education to evaluate the release and ensure that program changes do not adversely affect the application functions. Education should work with WestEd to develop a set of test scripts that should be used whenever program changes are being made. We consider this to be a *significant deficiency*.

The overall risk to Education is that the current change controls over Tracker give rise to a higher risk of noncompliance with established FPM Protocols and therefore, to Education's ability to properly monitor subrecipients in accordance with Federal regulations.

Questioned Costs

No specific questioned costs identified.

Recommendation

Education should enhance controls over CAIS program change management such that the risks noted in the deficiencies above are reduced to an acceptable level that allows Education to properly monitor subrecipients in accordance with federal regulations.

Department's View and Corrective Action Plan

To enhance existing controls, in the spring 2011, Education created a CAIS Steering Committee to monitor and provide direction related to the use of the CAIS within WestEd's "Tracker" modules. Education also designated a single point of contact between WestEd and Education to improve overall communication by meeting regularly to discuss issues of concern to the CAIS Steering Committee. In addition, in regard to the conditions noted by the auditors, the following actions will be, or have been, taken:

- 1. Although a formal contract or Memorandum of Understanding (MOU) between Education and WestEd was not initiated specific to Tracker, the CAIS Steering Committee has engaged internal information technology resources to assist in mitigating the risk that changes made to Tracker may negatively impact CAIS. In December 2011, Education will discuss with the SWCC and CACC, the feasibility of requesting WestEd to have a Service Organization Review of its management controls over Tracker.
- 2. The CAIS Steering Committee identified the evaluation of existing and expanded functionality of the system as a critical issue and plans to resolve this matter through the establishment of a technical advisory committee. In spring 2012, the technical advisory committee will develop a process for reviewing requests for functionality and creating a tracking system to monitor such requests. The CAIS Steering Committee has engaged with internal information technology resources to assist with the issues raised relating to backup copies of the database.
- 3. The CAIS Steering Committee requested additional information from WestEd to identify pending changes and updates to Tracker. The CAIS Steering Committee also requested assistance from internal information technology resources to advise the technical advisory committee on the development of best practices to review change requests and establish a priority system for such requests by spring 2012. The designated point of contacts within WestEd and Education meet regularly to discuss these issues and Education plans to network with other states using Tracker to obtain feedback on best practices related to change requests.
- 4. The CAIS Steering Committee plans to resolve production system change issues through the establishment of a technical advisory committee to create protocols in December 2011. The CAIS Steering Committee also requested assistance from internal information technology resources to advise the technical advisory committee on the development of best practices related to user testing. The designated point of contacts with WestEd and Education meet regularly to discuss these issues and will continue to work to improve communication related to this matter.

Current Year Reference Number: 2011-14-4

Federal Catalog Number: 93.713

Federal Program Title: Child Care Development Fund Cluster:

ARRA—Child Care and Development Block

Grant

Federal Award Number and Year: G0901CACCD7; 2009

Category of Finding: Special Tests & Provisions

State Administering Department: Department of Education (Education)

Criteria

TITLE 2-GRANTS AND AGREEMENTS, CHAPTER I—OFFICE OF MANAGEMENT AND BUDGET GOVERNMENTWIDE GUIDANCE FOR GRANTS AND AGREEMENTS, PART 176—AWARD TERMS FOR ASSISTANCE AGREEMENTS THAT INCLUDE FUNDS UNDER THE AMERICAN RECOVERY AND REINVESTMENT ACT OF 2009, Subpart D—Single Audit Information for Recipients of Recovery Act Funds

Section 176.210 Award term—Recovery Act transactions listed in Schedule of Expenditures of Federal Awards and Recipient Responsibilities for Informing Subrecipients.

(c) Recipients agree to separately identify to each subrecipient, and document at the time of subaward and at the time of disbursement of funds, the Federal award number, CFDA number, and amount of Recovery Act funds. When a recipient awards Recovery Act funds for an existing program, the information furnished to subrecipients shall distinguish the subawards of incremental Recovery Act funds from regular subawards under the existing program.

Condition

During our testing of the Special Tests and Provisions compliance requirement, including discussions with program management, we noted that Education is not identifying to each of its subrecipients, and documenting at the time of subaward the federal award number. Also, at the time of disbursement of American Recovery and Reinvestment Act of 2009 (Recovery Act) funds, Education is not informing each subrecipient the federal award number, CFDA number, and amount of Recovery Act funds.

Education's fourth quarter Section 1512 reporting reflected expenditures totaling \$187,831,959 being passed-through to subrecipients, which represents 85 percent of Education's total Recovery Act award.

By not properly informing its subrecipients of the federal award number, CFDA number, and the amount of Recovery Act funds, there is a risk that subrecipients may not be identifying and properly accounting and reporting Recovery Act funds in accordance with 2 CFR, Section 176.210 requirements. This may result in reducing Education's ability to properly monitor the subrecipients expenditure of Recovery Act funds, as well as, assisting in any oversight by the federal awarding agency, Office of Inspector General and the Government Accountability Office.

Questioned Costs

No specific questioned costs identified.

Recommendations

Education should revise its current practices to conform with the requirements set-forth in 2 CFR, Section 176.210. Management should design internal controls to ensure that such controls are operating effectively to ensure ongoing compliance with the aforementioned compliance requirements.

Department's View and Corrective Action Plan

Education does not disagree with this finding. However, given the fact that all Recovery Act funds have already been distributed, Education does not consider it cost beneficial to require staff to make further changes to its Direct Service Agreements and Standard Agreements in regard to monitoring and overseeing Recovery Act funds. Education contends that existing internal controls of tracking grant award allocations separately, and the reporting of Recovery Act 1512 data using Standardized Account Code Structure resource codes to be adequate in avoiding confusion when accounting between Recovery Act and regular funds.

Auditor's Comments on Department's View

We agree that it is ineffective to modify agreements given that all Recovery Act funds have been awarded. This does not, however, preclude Education from providing the appropriate notifications given that subrecipients have one final Single Audit report for the fiscal year ending June 30, 2012, that will include expenditures of Recovery Act funds.

We would also note that this finding does not take issue with Education's method of separately tracking Recovery Act funds for Education's recordkeeping. This finding is with regard to properly notifying subrecipients at the time of award and at the time of disbursement so that subrecipient records can properly track Recovery Act funds separate from other award funds.

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

Reference Number: 2011-4-1

Federal Catalog Number: 14.258

Federal Program Title: Tax Credit Assistance Program (Recovery

Act Fund)

Federal Award Number and Year: M09-ES060100; 2009

Category of Finding: Davis-Bacon

State Administering Department: Office of the State Treasurer (Treasurer)

Criteria

TITLE 29—LABOR, PART 5—LABOR STANDARDS PROVISIONS APPLICABLE TO CONTRACTS COVERING FEDERALLY FINANCED AND ASSISTED CONSTRUCTION, Subpart A—Davis-Bacon and Related Acts Provisions and Procedures, Section 5.5—Contract provisions and related matters

- (a) The Agency head shall cause or require the contracting officer to insert in full in any contract in excess of \$2,000 which is entered into for the actual construction, alteration and/or repair, including painting and decorating, of a public building or public work, or building or work financed in whole or in part from Federal funds or in accordance with guarantees of a Federal agency or financed from funds obtained by pledge of any contract of a Federal agency to make a loan, grant or annual contribution (except where a different meaning is expressly indicated), and which is subject to the labor standards provisions of any of the acts listed in Section 5.1, the following clauses (or any modifications thereof to meet the particular needs of the agency, provided that such modifications are first approved by the Department of Labor):
 - (3) Payrolls and basic records.
 - (ii)(A) The contractor shall submit weekly for each week in which any contract work is performed a copy of all payrolls to the agency if the agency is a party to the contract, but if the agency is not such a party, the contractor will submit the payrolls to the applicant, sponsor, or owner, as the case may be, for transmission to the agency. The payrolls submitted shall set out accurately and completely all of the information required to be maintained under 29 CFR 5.5(a)(3)(i), except that full social security numbers and home addresses shall not be included on weekly transmittals. Instead the payrolls shall only need to include an individually identifying number for each employee (e.g., the last four digits of the employee's social security number). The required weekly payroll information may be submitted in any form desired. Optional Form WH-347 is available for this purpose from the Wage and Hour Division Web site at http://www.dol.gov/esa/whd/ forms/wh347instr.htm or its successor site. The prime contractor is responsible for the submission of copies of payrolls by all subcontractors. Contractors and subcontractors shall maintain the full social security number and current address of each covered worker, and shall provide them upon request to the (write in name of appropriate federal agency) if the agency is a party to the contract, but if the agency is not such a party, the contractor will submit them to the applicant, sponsor, or owner, as the case may be, for transmission to the (write in name of agency), the contractor, or the Wage and Hour Division of the Department of Labor for purposes of an investigation or audit of compliance with prevailing wage requirements. It is not a violation of this section for a prime contractor to require a subcontractor to provide addresses and social security numbers to the prime contractor for its own records, without weekly submission to the sponsoring government agency (or the applicant, sponsor, or owner).
 - (B) Each payroll submitted shall be accompanied by a "Statement of Compliance," signed by the contractor or subcontractor or his or her agent who pays or supervises the payment of the persons employed under the contract and shall certify the following:

- (1) That the payroll for the payroll period contains the information required to be provided under Sec. 5.5 (a)(3)(ii) of Regulations, 29 CFR part 5, the appropriate information is being maintained under Sec. 5.5 (a)(3)(i) of Regulations, 29 CFR part 5, and that such information is correct and complete;
- (2) That each laborer or mechanic (including each helper, apprentice, and trainee) employed on the contract during the payroll period has been paid the full weekly wages earned, without rebate, either directly or indirectly, and that no deductions have been made either directly or indirectly from the full wages earned, other than permissible deductions as set forth in Regulations, 29 CFR part 3;
- (3) That each laborer or mechanic has been paid not less than the applicable wage rates and fringe benefits or cash equivalents for the classification of work performed, as specified in the applicable wage determination incorporated into the contract.

Condition

During our review of the Treasurer's compliance with Davis—Bacon, we noted that the Treasurer does not require the participants to submit certified payrolls, but rather to keep them on file for on-site monitoring. While the Treasurer has contracted with a Davis—Bacon expert to review those certified payrolls, the requirement expressly states that the certified payrolls are to be submitted to the agency on a weekly basis. The Treasurer was unaware that the requirement expressly stated that they must receive the certified payrolls.

Questioned Costs

No specific questioned costs identified.

Recommendation

The Treasurer should revise its current practice to require that certified payrolls be submitted to them on a weekly basis per the Davis–Bacon requirement.

Department's View and Corrective Action Plan

The Tax Credit Allocation Committee (TCAC) was awarded the Tax Credit Assistance Program (TCAP) grant in July of 2009 through the American Recovery and Reinvestment Act of 2009. The TCAP funds are subject to Davis Bacon federal prevailing wage requirements. To ensure proper oversight and monitoring of the prevailing wage requirements, TCAC entered into a contract with an outside firm with expertise in Davis Bacon laws. TCAC developed and discussed the monitoring and oversight strategy for Davis Bacon prevailing wage compliance with the Department of Housing and Urban Development (HUD). HUD agreed that the monitoring strategy was acceptable. TCAC required each project owner to maintain copies of the weekly certified payroll reports for three years, however, TCAC did not require each owner to send copies of the payroll reports to TCAC weekly. TCAC agrees that the reports should have been collected from the project owners weekly and that TCAC must also maintain copies of the reports for three years. TCAC awarded 52 TCAP loans, of which 49 were subject to Davis Bacon laws. To date TCAC has collected all payrolls for 44 of the 49 projects and anticipates the remaining five will be collected the week of November 7, 2011. TCAC will keep the payroll reports on file for a period of three years. In addition, TCAC has revised its current practice and is now collecting the payroll reports on a weekly basis for the 21 TCAP projects that are currently in the construction phase.

State Controller's Office

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U.S. ENVIRONMENTAL PROTECTION AGENCY

Reference Number: 2011-2-2

Federal Catalog Number: 66.468

Federal Program Title: Capitalization Grants for Safe Drinking Water

State Revolving Fund and ARRA-Capitalization

Grants for Safe Drinking Water State

Revolving Fund

Federal Award Number and Year: FS98934910; 2010

FS98934909; 2009

Category of Finding: Allowable Costs/Costs Principles

State Administering Department: California Department of Public Health

Criteria

Title 2, *Code of Federal Regulations*, Part 225 (2 CFR 225) requires CDPH to reduce the SDWSRF federal grant reimbursements by the amounts received from the water systems. Appendix A, Subpart (C)(l)(i), states, "To be allowable under Federal awards, costs must ... be the net of all applicable credits." Appendix A, Subpart (C)(4)(a), states, "Applicable credits refer to those receipts or reduction of expenditure-type transactions that offset or reduce expense items allocable to Federal awards..."

Condition

The Safe Drinking Water Program provides water system supports and engineering services to various water systems throughout California. The program is funded by state appropriations, federal grants, and water systems that are charged a fee for the services rendered by the program. Program employees account for the time they spend providing services to each water system using timesheets. The program then enters the time into the California Department of Public Health (CDPH) time accounting system. CDPH's time accounting system is used to report expenses for the SDWSRF grant and to capture billable hours for services rendered to the water systems. During our audit, we noted that CDPH had used two different time accounting output reports in the preparation of local water system invoices and federal grant requests, as a result some of the employee hours charged to the SDWSRF federal grant were also billed to the water systems. By receiving reimbursement from both the federal grant and the water systems, CDPH received revenue twice for the same expenditure.

A sample of 40 employee timesheets were tested, totaling 6,288 hours. Twenty-four of the timesheets tested contained an estimate of 775 hours that were expensed to the SDWSRF federal program and also billed to the water systems, resulting in a projected error rate of 12.33 percent (775/6,288). The total known questioned direct labor costs are approximately \$43,600.

CDPH was not aware that it was expensing payroll costs that were also being billed to the water systems. The error was partially due to CDPH improperly programming its time accounting system. The SDWSRF program has a process in place to review payroll expenditures of the program to ensure that only allowable payroll expenditures are being charged to the program. During our audit, we noted that the last review by CDPH was performed in September 2010. Had this process been in place, CDPH may have discovered and corrected the error.

Questioned Costs

The total known questioned direct labor costs are approximately \$43,600.

Recommendation

CDPH should ensure that payroll hours billed to the water systems are not included as SDWSRF payroll expenditures. Correction of this problem will likely require reprogramming the time accounting system. Although timesheets are properly reviewed by supervisors, CDPH should reinstitute the internal control procedures of reviewing payroll expenditures charged to the SDWSRF program.

Department's View and Corrective Action Plan

CDPH agrees that payroll hours billed to the water system should not be included as SDWSRF payroll expenditures. Correcting the problem will require reprogramming the Time Accounting System (TAS) and CDPH has started correcting the TAS Database to ensure payroll expenditures are applied correctly. CDPH expects to complete the correction by March 30, 2012.

CDPH agrees that the internal control procedures should be reinstituted. Effective March I, 2012, SDWSRF will reinstitute reviewing payroll expenditures charged to the program on a monthly basis followed by supervisory review. We have trained additional staff to help review the monthly payroll expenditures.

Auditor's Comments on Department's View

CDPH concurs with our finding and recommendation. We acknowledge CDPH's intent to implement our recommendation.

AUDITEE'S SECTION

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Schedule of Expenditures of Federal Awards

Prepared by Department of Finance

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STATE OF CALIFORNIA SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS FISCAL YEAR ENDED JUNE 30, 2011

Federal Agency/Program Title/Pass-Through Entity or Program	Federal Catalog Number	Pass-Through Entity Identifying Number	Non-ARRA Expenditures	ARRA Expenditures
epartment of Agriculture				
lant and Animal Disease, Pest Control, and Animal Care	10.025		\$ 68,982	
ildlife Services	10.028		16,405	
RRA-Aquaculture Grants Program (AGP), Recovery Act Funded	10.086			\$ 59
009 Aquaculture Grant Program	10.103		454,218	
arket Protection and Promotion	10.163		501,404	
arm Labor Housing Loans and Grants	10.405		4,201,173	
od Safety Cooperative Agreements	10.479		988,692	
pecial Supplemental Nutrition Program for Women, Infants, and Children	10.557		1,178,079,566	
nild and Adult Care Food Program	10.558		263,753,033	
ate Administrative Expenses for Child Nutrition	10.560		25,109,172	
ommodity Supplemental Food Program	10.565		5,120,286 *	
IC Farmers' Market Nutrition Program (FMNP)	10.572		2,257,611	
eam Nutrition Grants	10.574		(1,328)	
enior Farmers Market Nutrition Program	10.576		686,269	
RRA-WIC Grants To States (WGS)	10.578			3,392,301
nild Nutrition Discretionary Grants Limited Availability	10.579		1,008,907	
RRA-Child Nutrition Discretionary Grants Limited Availability,	40.550			// AD ====
Recovery Act Funded	10.579			(449,703)
resh Fruit and Vegetable Program	10.582		6,864,115	
ooperative Forestry Assistance	10.664		4,861,000	
ational Forest-Dependent Rural Communities	10.670		(503)	
ural Development, Forestry, and Communitites	10.672		200 500	
rban and Community Forestry Program	10.675		966,539	
orest Legacy Program	10.676		2,418,069	
prest Stewardship Program	10.678		1,971,314	
prest Health Protection	10.680		185,076	44.004
RRA-Capital Improvement and Maintenance, Recovery Act	10.687			44,881
RRA-Wildland Fire Management, Recovery Act Funded	10.688		44.040	4,689,777
nvironmental Quality Incentives Program	10.912		44,242	
ong Term Standing Agreements for Storage, Transportation And Lease Total Excluding Clusters	10.999		76,100,231 1,575,654,473	7,677,315
NAP Cluster				
upplemental Nutrition Assistance Program	10.551		*	See Note 4
ate Administrative Matching Grants for the Supplemental Nutrition Assistance Program	10.561		674,138,043	
RRA-State Administrative Matching Grants for the Supplemental			0. 1,100,010	
Nutrition Assistance Program, Recovery Act Funded	10.561			10,706,323
Total SNAP Cluster			674,138,043	10,706,323
hild Nutrition Cluster				
chool Breakfast Program	10.553		369,183,196	
ational School Lunch Program	10.555		1,405,751,990 *	
pecial Milk Program for Children	10.556		430,788	
ummer Food Service Program for Children	10.559		22,881,156	
Total Child Nutrition Cluster			1,798,247,130	-
mergency Food Assistance Cluster				
mergency Food Assistance Program (Administrative Costs)	10.568		9,722,457	
RRA-Emergency Food Assistance Program (Administrative				
Costs), Recovery Act Funded	10.568			6,733,097
mergency Food Assistance Program (Food Commodities)	10.569		*	
RRA-Emergency Food Assistance Program (Food Commodities),				
ecovery Act Funded	10.569		9,722,457	6.733.097
Total Emergency Food Assistance Cluster			3,122,431	0,733,097
chools and Roads Cluster chools and Roads - Grants to States	10.665		47,872,286	
	10.000		-1,012,200	
esearch & Development Cluster				
lant and Animal Disease, Pest Control, and Animal Care	10.025		289,342	
Total Department of Agriculture			4 405 000 704	05 440 705
Total Department of Agriculture			4,105,923,731	25,116,735

Department of Commerce

Anadromous Fish Conservation Act Program	11.405		8,539	
Interjurisdictional Fisheries Act of 1986	11.407		141,093	
•			,	
Coastal Zone Management Administration Awards	11.419		2,603,425	
Coastal Zone Management Estuarine Research Reserves	11.420		1,014,363	
Marine Sanctuary Program	11.429		60,084	
Pacific Coast Salmon Recovery-Pacific Salmon Treaty Program	11.438		12,098,174	
Regional Fisheries Management Councils	11.441			
ů		R0970004	102.041	
Pass-Through from Pacific Fisheries Management Councils		R0970004	192,941	
Unallied Management Projects	11.454		1,796,891	
Habitat Conservation	11.463		6,275,608	
Meteorologic and Hydrologic Modernization Development	11.467		1,251,388	
Applied Meteorological Research	11.468		183,327	
Unallied Science Program	11.472		98,000	
Public Safety Interoperable Communications Grant Program	11.555		25,362,686	
ARRA-State Broadband Data and Development Grant Program,				
Recovery Act Funded	11.558			1,075,395
Other - U.S. Department of Commerce	11.999		128,614	1,010,000
·	11.555			1 07E 30E
Total Excluding Cluster			51,215,133	1,075,395
December 9 Development Cluster				
Research & Development Cluster				
Geodetic Surveys and Services (Geodesy and Applications of the				
National Geodetic Reference System)	11.400		293,998	
Coastal Zone Management Estuarine Research Reserves	11.420		84,924	
Unallied Science Program	11.472		8,925	
· ·	11.472			-
Total Research & Development Cluster			387,847	-
Total Department of Commerce			51,602,980	1,075,395
Department of Defense				
Department of Defense				
Planning Assistance to States	12.110		2,113,908	
•			2,1.0,000	
State Memorandum of Agreement Program for the Reimbursement				
of Technical Services	12.113		15,357,647	
Basic and Applied Scientific Research	12.300		5,218	
National Guard Military Operations and Maintenance (O&M)				
• • • • • • • • • • • • • • • • • • • •	40 404		C4 702 FC4	
Projects	12.401		61,703,564	
ARRA-National Guard Military Operations and Maintenance (O&M)				
Projects, Recovery Act Funded	12.401			1,652,237
			9 521 026	1,002,207
National Guard ChalleNGe Program	12.404		8,531,036	
Other - U.S. Department of Defense	12.999		1,759,162	
Total Excluding Cluster			89,470,535	1,652,237
Research & Development Cluster				
Planning Assistance to States	12.110		1,674,135	
Air Force Defense Research Sciences Program	12.800		27,575	
Total Research & Development Cluster			1,701,710	
Total Research & Development Glaster			1,701,710	
Total Department of Defense			91,172,245	1,652,237
Total Department of Defense			91,172,245	1,032,237
Department of Housing and Urban Development				
Manufactured Home Dispute Resolution	14.171		49,075	
Emergency Shelter Grants Program	14.231		6,194,254	
• •			0,194,254	
Supportive Housing Program	14.235			
Home Investment Partnerships Program	14.239		38,492,472 **	
Housing Opportunities for Persons with AIDS	14.241		2,927,151	
ARRA-Homelessness Prevention and Rapid Re-Housing Program,				
	14.057			47 700 070
Recovery Act Funded	14.257			17,738,378
ARRA-Tax Credit Assistance Program, Recovery Act Funded				224,390,882
	14.258			
Equal Opportunity in Housing			2,219,359	
	14.258		2,219,359 15	
Equal Opportunity in Housing Lead-Based Paint Hazard Control in Privately-Owned Housing Total Excluding Cluster	14.258 14.400			242,129,260
Lead-Based Paint Hazard Control in Privately-Owned Housing	14.258 14.400		15	242,129,260
Lead-Based Paint Hazard Control in Privately-Owned Housing	14.258 14.400		15	242,129,260
Lead-Based Paint Hazard Control in Privately-Owned Housing Total Excluding Cluster CDBG - State-Administered CDBG Cluster	14.258 14.400		15	242,129,260
Lead-Based Paint Hazard Control in Privately-Owned Housing Total Excluding Cluster CDBG - State-Administered CDBG Cluster Community Development Block Grants/State's program and Non-	14.258 14.400 14.900		<u>15</u> 49,882,326	242,129,260
Lead-Based Paint Hazard Control in Privately-Owned Housing Total Excluding Cluster CDBG - State-Administered CDBG Cluster Community Development Block Grants/State's program and Non- Entitlement Grants in Hawaii	14.258 14.400		<u>15</u> 49,882,326	242,129,260
Lead-Based Paint Hazard Control in Privately-Owned Housing Total Excluding Cluster CDBG - State-Administered CDBG Cluster Community Development Block Grants/State's program and Non-Entitlement Grants in Hawaii ARRA-Community Development Block Grants/State's program and	14.258 14.400 14.900		<u>15</u> 49,882,326	
Lead-Based Paint Hazard Control in Privately-Owned Housing Total Excluding Cluster CDBG - State-Administered CDBG Cluster Community Development Block Grants/State's program and Non-Entitlement Grants in Hawaii ARRA-Community Development Block Grants/State's program and Non-Entitlement Grants in Hawaii, Recovery Act Funded	14.258 14.400 14.900		<u>15</u> 49,882,326	242,129,260 5,574,943
Lead-Based Paint Hazard Control in Privately-Owned Housing Total Excluding Cluster CDBG - State-Administered CDBG Cluster Community Development Block Grants/State's program and Non-Entitlement Grants in Hawaii ARRA-Community Development Block Grants/State's program and	14.258 14.400 14.900		<u>15</u> 49,882,326	

Housing Voucher Cluster			
Section 8 Housing Choice Vouchers	14.871	4,791,681	
Lead Hazard Control Cluster			
ARRA-Lead-Based Paint Hazard Control in Privately-Owned Housing, Recovery Act Funded	14.907		1,814,375
	14.907		1,614,375
Total Department of Housing and Urban Development		122,902,423	249,518,578
Department of Interior			
Distribution of Receipts to State and Local Governments	15.227	70,925,767	
Environmental Quality and Protection Resource Management	15.236	318,651	
ARRA-Environmental Quality and Protection Resource Management, Recovery Act Funded	15.236		664,960
Coastal Impact Assistance Program (CIAP)	15.426	4,720,938	•
Providing Water to At-Risk Natural Desert Terminal Lakes	15.508	182,036	
Central Valley Project Improvement Act, Title XXXIV Fish and Wildlife Management Assistance	15.512 15.517	4,517,737 73,678	
ARRA-Fish and Wildlife Coordination Act, Recovery Act Funded	15.517	73,076	560,848
Central Valley Project, Trinity River Division, Trinity River Fish and			222,212
Wildlife Management	15.532	121,942	
California Water Security and Environmental Enhancement	15.533	221,162	
Fish and Wildlife Management Assistance	15.608	216,504	
Coastal Wetlands Planning, Protection and Restoration Act	15.614 15.615	968,243 27,992,789	
Cooperative Endangered Species Conservation Fund Clean Vessel Act	15.616	1,873,454	
Sportfishing and Boating Safety Act	15.622	264,682	
Wildlife Conservation and Restoration	15.625	775	
Coastal Program	15.630	489	
Landowner Incentive Program	15.633 15.642	179,620 75.000	
Challenge Cost Share Migratory Bird Conservation	15.647	132,834	
Central Valley Project Improvement (CVPI) Anadromous Fish Restoration Program (AFRP)			
Earthquake Hazards Reduction Program	15.648	198,359	
U.S. Geological Survey-Research and Data Collection National Spatial Data Infrastructure Cooperative Agreements	15.807 15.808	13,766 166,609	
Program	15.809	150	
National Cooperative Geologic Mapping Program	15.810	224,793	
National Geological and Geophysical Data Preservation Program	15.814	23,253	
Historic Preservation Fund Grants-In-Aid Outdoor Recreation-Acquisition, Development and Planning	15.904 15.916	1,297,038 2,666,021	
ARRA-Abandoned Mine Hazard Mitigation, Recovery Act Funded ARRA-Redwood National Park Cooperative Management with the	15.934	2,000,021	404,191
State of California, Recovery Act Funded	15.937		371,212
Other - U.S. Department of the Interior Total Excluding Clusters	15.999	7,213,206 124,589,496	2,001,211
-		124,369,490	2,001,211
Research & Development Cluster	45.000	24.057	
Challenge Cost Share Sport Fish Restoration Program	15.238 15.605	21,057 13,149,607	
Wildlife Restoration and Basic Hunter Education	15.611	12,240,160	
Cooperative Endangered Species Conservation Fund	15.615	2,445,551	
State Wildlife Grants	15.634	3,093,527	
Research Grants (Generic) Total Research & Development Cluster	15.650	20,966 30,970,868	-
Total Department of Interior		155,560,364	2,001,211
Department of Justice			
Law Enforcement Assistance-Narcotics and Dangerous Drugs			
Laboratory Analysis	16.001	40,993	
Sexual Assault Services Formula Program Prisoner Reentry Initiative Demonstration (Offender Reentry)	16.017 16.202	428,357 1,057,835	
Juvenile Accountability Block Grants	16.523	3,152,926	
Juvenile Justice and Delinquency Prevention-Allocation to States	16.540	2,356,505	
Title V - Delinquency Prevention Program	16.548	91,219	
National Institute of Justice Research, Evaluation, and Development Project Grants	16.560	468,866	
= 1. Jopinson . Tojost oranto	. 5.500	400,000	

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March 2012

Crime Victim Assistance Crime Victim Compensation	16.575 16.576		42,424,070 32,479,611		
Edward Byrne Memorial State and Local Law Enforcement	10.570		02,470,011		
Assistance Discretionary Grants Program	16.580		439,845		
Drug Court Discretionary Grant Program	16.585		101,922		
Violence Against Women Formula Grants	16.588		11,686,521		
ARRA-Violence Against Women Formula Grants, Recovery Act Funded	16.588		, , .	6,041,528	
Grants to Encourage Arrest Policies and Enforcement of Protection				2,2 11,2=2	
Orders Program	16.590				
Pass-Through from Contra Costa County (GTEA)		49002-02	23,035		
Pass-Through from Contra Costa County (GTEA)		19-662-0	5,140		
Pass-Through from Contra Costa County (CDS)		19-641-0	30,149		
Pass-Through from Contra Costa County (CDCSS)		C4539900	32,435		
Residential Substance Abuse Treatment for State Prisoners	16.593		776,740		
State Criminal Alien Assistance Program	16.606		88,106,548		
Bulletproof Vest Partnership Program	16.607		1,730,298		
Project Safe Neighborhoods	16.609		885,603		
Regional Information Sharing Systems Public Sofety Partnership and Community Policing Creats	16.610		130,087		
Public Safety Partnership and Community Policing Grants Enforcing Underage Drinking Laws Program	16.710 16.727		2,106,412 535,542		
Statewide Automated Victim Information Notification (SAVIN) Program	16.740		416,650		
Forensic DNA Backlog Reduction Program	16.741		3,435,661		
Paul Coverdell Forensic Sciences Improvement Grant Program	16.742		2,037,916		
Anti-Gang Initiative	16.744		1,116,891		
Convicted Offender and/or Arrestee DNA Backlog Reduction			, -,		
Program	16.748		52,752		
Edward Byrne Memorial Competitive Grant Program	16.751		4,357		
Congressionally Recommended Awards	16.753		454,299		
Harold Rogers Prescription Drug Monitoring Program	16.754		31,968		
ARRA-State Victim Assistance Formula Grant Program, Recovery					
Act Funded	16.801			834,648	
ARRA-Edward Byrne Memorial Competitive Grant Program,					
Recovery Act Funded	16.808			515,878	
ARRA-Assistance to Rural Law Enforcement to Combat Crime and					
Drugs Competitive Grant Program, Recovery Act Funded	16.810			597,949	
John R. Justice Prosecutors and Defenders Incentive Act	16.816		51,627		
Total Excluding Clusters			196,692,780	7,990,003	
JAG Program Cluster					
Edward Byrne Memorial Justice Assistance Grant Program	16.738		33,074,057		
•	10.700		00,014,001		
ARRA-Edward Byrne Memorial Justice Assistance Grant (JAG) Program/ Grants to States and Territories, Recovery Act Funded	16.803			59,431,658	
Total JAG Program Cluster	10.000		33,074,057	59,431,658	
•					
Total Department of Justice			229,766,837	67,421,661	_
Department of Labor					
Department of Education					
Labor Force Statistics	17.002		8,363,689		
Compensation and Working Conditions	17.005		831,537		
Unemployment Insurance	17.225		20,410,960,823		See Note 3
ARRA-Unemployment Insurance, Recovery Act Funded	17.225			599,511,599	See Note 3
Senior Community Service Employment Program	17.235		13,324,180		
ARRA-Senior Community Service Employment Program, Recovery					
Act Funded	17.235			284,366	
Trade Adjustment Assistance	17.245		20,233,809		
Work Incentives Grant Work Opportunity Tax Credit Program (WOTC)	17.266 17.271		16,144 1,814,663		
Temporary Labor Certification for Foreign Workers	17.271		1,259,491		
ARRA-Program of Competitive Grants for Worker Training and	270		.,=00,101		
Placement in High Growth and Emerging Industry Sectors,					
Recovery Act Funded	17.275			1,907,151	
Occupational Safety and Health-State Program	17.503		31,994,265	,,,,,,,,,,	
ARRA-Occupational Safety and Health-State Program, Recovery					
Act Funded					
Actiunded	17.503			152,601	
Consultation Agreements	17.504		5,452,246	152,601	
			5,452,246 297,390 20,494,548,237	152,601 601,855,717	

Employment Service Cluster Funded Activities 17.207 82.938.488 Funded Activities Funded Activities 17.207 82.938.488 Funded Activities 17.207 17.801 17.801 17.802 1					
ARRA-Employment Service/Wagner-Preyer Funded Activities, Recovery Act Funded Culteract Program (PVCP) 17,001 17,00	Employment Service Cluster				
Recovery Act Funded	Employment Service/Wagner-Peyser Funded Activities	17.207		82,936,498	
Deable Program Current Program CVOP 17.801 13.748.770 10.366.522 10.367.388 11.686.622 10.367.388 11.686.622 10.367.388 11.686.622 10.367.388 11.686.622 10.367.388 11.686.622 10.367.388 11.686.622 10.367.388 11.686.622 10.367.388 11.686.622 10.367.388 11.686.622 10.367.388 11.686.622 10.367.388 11.686.622 10.367.388 10.367.388 11.686.622 10.367.388					
Contained Cont				12 740 770	11,686,622
Total Employment Service Cluster	• ,			-, -, -	
MA Adul Program, Recovery Act Funded 17.288 127.290.414 1.512.982 MA Youth Activities 17.259 132.902.279 1.512.982 MA Youth Activities 17.259 132.902.279 1.512.982 MA Youth Activities 17.259 132.902.279 1.512.982 MA Youth Activities 17.259 11.683.994 1.680.994 1.6					11,686,622
MA Auth Program, Recovery Act Funded 17.288 127.290.411 1.512.982 MA Youth Activities 17.259 12.902.279 1.512.982 MA Youth Activities 17.259 12.902.279 1.505.123 MA Youth Activities 17.259 12.902.279 1.505.123 MA Youth Activities 17.259 1.505.994 1.505.9					
ARRA-WAN Adult Program, Recovery Act Funded 17.258 132.902.279 132		47.050		107.000.111	
MIX Youth Activities 17.299 132.902.279				127,290,441	1 512 982
MRA Discloated Workers 17.260				132,902,279	1,012,002
ARRA-WAI Dislocated Workers, Recovery Act Funded workers from the Care State Planning and Research Rat (WAI) National Emergency Grants 17.277 10.147,661 17.289 17.2894.779 17.284.779 17.2	ARRA-WIA Youth Activities, Recovery Act Funded	17.259			5,051,223
Workforce Investment Act (WIA) National Emergency Grants 17.277				11,683,994	4 0 4 0 5 0 4
Total WA Cluster				10 147 661	1,840,561
Total Department of Labor	` ,				
Department of Transportation	Total WIA Cluster				8,404,766
Department of Transportation					
Alport Improvement Program	lotal Department of Labor			21,053,450,879	621,947,105
Alport Improvement Program	Department of Transportation				
National Motor Carrier Safety 20.218 1.12,71,38 Performance and Registration Information Systems Management 20.231 101,184 Performance and Registration Information Systems Management 20.232 458,336 Fuel Tax Evisolon-Intergovernmental Enforcement Effort 20.308 1,199,249 Local Rail Freight Assistance 20.308 1,199,249 Capital Assistance Grants, Recovery Act Funded 20.317 2,659,102 ARRA-High-Speed Rail Corridors and Intercity Passenger Rail 20.505 75,053,927 Service — Capital Assistance Grants, Recovery Act Funded 20.509 27,843,656 Metropolitan Transportation Planning 20.509 27,843,656 ARRA-Formula Grants for Other Than Urbanized Areas, Recovery 20.509 369,848 At Funded 20.509 369,848 Minimum Penaltes for Repeat Offenders for Driving While Introxicated 20.608 23,931,839 E-911 Grant Porgram 20.608 23,931,839 F-911 Grant Porgram 20.608 21,99,955 Planning Grants 20.703 21,99,955 Tile Steuturing Cluster 20.703 2,443,130,054					
Performance and Registration Information Systems Management				•	
Commercial Driver's License Program Improvement Grant 20.230 12.93.61 1.99.240 1.29.361 1.29.361	*				
Fuel Tax Evasion-Intergovermmental Enforcement Effort 20.240 129.361					
Capital Assistance to States, Intercity Passenger Rail Services 20.317 2,659,102 ARRA-High-Speed Rail Corridors and Intercity Passenger Rail Service — Capital Assistance Grants, Recovery Act Funded 20.505 75,053,327 Metropolitian Transporation Planning 20.509 27,643,656 ARRA-Formula Grants for Other Than Urbanized Areas 20.509 27,643,656 ARRA-Formula Grants for Other Than Urbanized Areas, Recovery Act Funded 20.509 369,848 ARRA-Formula Grants for Other Than Urbanized Areas, Recovery Act Funded 20.515 369,848 Minimum Penalties for Repeat Offenders for Driving While Intoxicated 20.601 23,931,839 8-911 Grant Program 20.615 25,081 Interagency Hazardous Materials Public Sector Training and Leragency Hazardous Materials Public Sector Training and Construction Public Sector Training and Construction Cluster 20.700 25,081 Highway Planning and Construction Cluster 42,220 2443,130,0054 963,001,718 Highway Planning and Construction Recovery Act Funded 20.205 \$FBC 10-04 26,509 963,001,718 Federal Transit Cluster Federal Transit Cluster Capital Assistance Program for Elderly Persons and Per	· ·				
ARRA-High-Speed Rail Corridors and Intercity Passenger Rail Service - Capital Assistance Grants. Recovery Act Funded 20.319 20.505 75.053,927 Pormula Grants for Other Than Urbanized Areas 20.509 27.643,656 Pormula Grants for Other Than Urbanized Areas, Recovery Act Funded 20.505 369,848 Pormula Grants for Other Than Urbanized Areas, Recovery Act Funded 20.515 369,848 Pormula Grants for Other Than Urbanized Areas, Recovery Act Funded 20.515 369,848 Pormula Grants for Other Than Urbanized Areas, Recovery Act Funded 20.515 369,848 Pormula Grants for Other Than Urbanized Areas, Recovery Act Funded 20.506 23,931,839 Pormula Grants for Driving While Intoxicated 20.608 23,931,839 Pormula Grants Program 20.615 251,231 Pipeline Safety Program Base Grants 20.700 25,081 Pormula Grants Program 20.700 25,081 Pormula Grants Program Pormula Grants 20.700 21,99,955 Pormula Grants Program Formula Grants Program Pormula Grants Program Formula G	Local Rail Freight Assistance				
Service		20.317		2,659,102	
Metropolitan Transportation Planning 20.505 75,053,927 Formula Grants for Other Than Urbanized Areas 20.509 27,643,656	, ,	20.240			40 700 705
Formula Grants for Other Than Urbanized Areas 20.509 27,643,656 ARRA-Formula Grants for Other Than Urbanized Areas, Recovery Act Funded 20.509 369,848 16,566,590 369,848 ARRA-Formula Grants for Other Than Urbanized Areas, Recovery Act Funded 20.608 23,931,839 25,931,				75 053 927	42,723,785
Act Funded 20.509 16,566,590 16,566,590 State Planning and Research 20.515 369,848 Minimum Penaltiles for Repeat Offenders for Driving While Intoxicated 20.608 23,931,839 2.911,839 2.911,6371 2.911,63				, ,	
State Planning and Research 20.515 369,848 Minimum Penalties for Repeat Offenders for Driving While Intoxicated 20.608 23.931,839 2.911 Carnel Program 20.615 251,231 25.081 25.0	ARRA-Formula Grants for Other Than Urbanized Areas, Recovery				
Minimum Penalties for Repeat Offenders for Driving While					16,566,590
Intoxicated	•	20.515		369,848	
E-911 Grant Program 20.615 251.231 Pipeline Safety Program Base Grants 20.700 25.081 Interagency Hazardous Materials Public Sector Training and Planning Grants 20.703 2,139.955 Total Excluding Clusters 146,542,433 59,290,375 Highway Planning and Construction Cluster Highway Planning and Construction Commission 20.205 2,443,130,054 Pass-Through from Metropolitan Transportation Commission 20.205 2,443,130,054 Pass-Through Irom Metropolitan Transportation Commission 20.205 4,192,539 Recreational Trails Program 20.219 4,192,539 963,001,718 Federal Transit Cluster 20.500 252,827 Federal Transit Custer 20.500 252,827 Transit Services Programs Cluster 20.500 252,827 Transit Services Program for Elderly Persons and Persons with Disabilities 20.513 2,085,490 Highway Safety Cluster 20.600 66,273,798 Alcohol Impaired Driving Countermeasures Incentive Grants 20.601 4,740,291 Alcohol Impaired Driving Countermeasures Incentive Grants 20.602 616,380 Safety Belt Performance Grants 20.609 855,891 State Traffic Safety Information System Improvement Grants 20.610 1,881,342 Incentive Grant Program to Increase Motorcyclist Safety 20.612 3,5228 Total Highway Safety Cluster 20.205 12,191,000 Research & Development Cluster 12,454,795 -104,404,705 Total Research & Development Cluster 12,454,795 -104,404,705	· · ·	20 608		23 931 839	
Interagency Hazardous Materials Public Sector Training and Planning Grants Planning Grants Total Excluding Clusters Highway Planning and Construction Cluster Highway Planning and Construction Pass-Through from Metropolitan Transportation Commission ARRA-Highway Planning and Construction, Recovery Act Funded Pass-Through Iron Metropolitan Transportation, Recovery Act Funded Pass-Through Iron Metropolitan Transportation Pass-Through Iron Metropolitan Transportation, Recovery Act Funded Pass-Through Iron Metropolitan Transportation, Recovery Act Funded Pass-Through Iron Metropolitan Transportation, Recovery Act Funded Pass-Through Iron Metropolitan Transportation Pass-Through Iron Metropolitan Pass-Through Iron Metropolitan Iron					
Planning Grants 20.703 2.139.955 Total Excluding Clusters 146,542,433 59,290,375 Total Excluding Clusters 146,542,433 59,290,375 Total Excluding Clusters 146,542,433 59,290,375 Total Highway Planning and Construction Cluster Plass-Through from Metropolitan Transportation Commission SFBC 10-04 205,500	Pipeline Safety Program Base Grants	20.700		25,081	
Total Excluding Clusters		00.700		0.400.055	
Highway Planning and Construction Cluster Highway Planning and Construction 20.205 SFBC 10-04 206,500 ARRA-Highway Planning and Construction, Recovery Act Funded 20.205 4.192,539 963,001,718 Recreational Trails Program 20.219 4.192,539 2.447,529,093 963,001,718 Recreational Trails Program 20.219 2.447,529,093 963,001,718 Recreational Trails Program 20.219 2.447,529,093 963,001,718 Recreational Trails Program 20.219 2.447,529,093 963,001,718 Recreational Trails Program 20.500 252,827 Recreational Trails Program 20.501 20.513 2.085,490 Recreational Trails Program 20.513 2.085,490 Recreational Trails Program 20.513 2.085,490 Recreational Trails Program 20.600 20.513 2.085,490 Recreational Trails Program 20.600		20.703			59 290 375
Highway Planning and Construction	. otal Excitating officials			. 10,0 12, 100	00,200,0.0
Pass-Through from Metropolitan Transportation Commission ARRA-Highway Planning and Construction, Recovery Act Funded Recreational Trails Program Total Highway Planning and Construction Cluster Federal Transit Cluster Federal Transit - Capital Investment Grants 20.500 252,827 Transit Services Program for Elderly Persons and Persons with Disabilities 20.513 2,085,490 Highway Safety Cluster State and Community Highway Safety Alcohol Impaired Driving Countermeasures Incentive Grants 1 Alcohol Impaired Driving Countermeasures Incentive Grants 2 Safety Belt Performance Grants Safety Belt Performation System Improvement Grants 2 Safety Belt Performation System Improvement Grants 2 Safety Royal From Program to Increase Motorcyclist Safety Total Highway Safety Cluster Research & Development Cluster Highway Planning and Construction 20.205 Total Research & Development Cluster					
ARRA-Highway Planning and Construction, Recovery Act Funded Recreational Trails Program 20.219 4.192.539 2.447.529.093 963,001,718	0 , 0	20.205			
Recreational Trails Program 20.219 4,192,539 2,447,529,093 963,001,718		20.205	SFBC 10-04	206,500	063 001 718
Total Highway Planning and Construction Cluster Federal Transit Cluster Federal Transit - Capital Investment Grants 20.500 252,827 Transit Services Programs Cluster Capital Assistance Program for Elderly Persons and Persons with Disabilities 20.513 2,085,490 Highway Safety Cluster State and Community Highway Safety Alcohol Impaired Driving Countermeasures Incentive Grants I 20.601 A;740,291 Occupant Protection Incentive Grants 20.602 Safety Belt Performance Grants 20.609 Safety Belt Performance Grants 20.610 State Traffic Safety Information System Improvement Grants 20.610 Incentive Grant Program to Increase Motorcyclist Safety 20.612 Total Highway Safety Cluster Research & Development Cluster Highway Planning and Construction 20.205 Total Research & Development Cluster				4.192.539	903,001,710
Pederal Transit - Capital Investment Grants 20.500 252,827	•				963,001,718
Pederal Transit - Capital Investment Grants 20.500 252,827	Endovel Transit Cluster				
Transit Services Programs Cluster Capital Assistance Program for Elderly Persons and Persons with Disabilities 20.513 2,085,490 Highway Safety Cluster State and Community Highway Safety 20.600 66,273,798 Alcohol Impaired Driving Countermeasures Incentive Grants I 20.601 4,740,291 Occupant Protection Incentive Grants 20.602 616,380 Safety Belt Performance Grants 20.609 855,891 State Traffic Safety Information System Improvement Grants 20.610 1,681,342 Incentive Grant Program to Increase Motorcyclist Safety 20.612 35,228 Total Highway Safety Cluster 74,202,930 - Research & Development Cluster Highway Planning and Construction 20.205 12,191,000 Formula Grants for Other Than Urbanized Areas 20.509 263,795 Total Research & Development Cluster 12,454,795 -		20 500		252 827	
Capital Assistance Program for Elderly Persons and Persons with Disabilities 20.513 2,085,490	rousial marion suprial invocation status	20.000		202,027	
Disabilities 20.513 2,085,490 Highway Safety Cluster State and Community Highway Safety 20.600 66,273,798 Alcohol Impaired Driving Countermeasures Incentive Grants I 20.601 4,740,291 Occupant Protection Incentive Grants 20.602 616,380 Safety Belt Performance Grants 20.609 855,891 State Traffic Safety Information System Improvement Grants 20.610 1,681,342 Incentive Grant Program to Increase Motorcyclist Safety 20.612 35,228 Total Highway Safety Cluster 74,202,930 - Research & Development Cluster 20.205 12,191,000 Formula Grants for Other Than Urbanized Areas 20.509 263,795 Total Research & Development Cluster 12,454,795 -	-				
Highway Safety Cluster State and Community Highway Safety 20.600 66,273,798 Alcohol Impaired Driving Countermeasures Incentive Grants 20.601 4,740,291 Occupant Protection Incentive Grants 20.602 616,380 Safety Belt Performance Grants 20.609 855,891 State Traffic Safety Information System Improvement Grants 20.610 1,881,342 Incentive Grant Program to Increase Motorcyclist Safety 20.612 35,228 Total Highway Safety Cluster 74,202,930 - Research & Development Cluster Highway Planning and Construction 20.205 12,191,000 Formula Grants for Other Than Urbanized Areas 20.509 263,795 Total Research & Development Cluster 12,454,795 -		20.542		2 005 400	
State and Community Highway Safety 20.600 66,273,798 Alcohol Impaired Driving Countermeasures Incentive Grants 20.601 4,740,291 Occupant Protection Incentive Grants 20.602 616,380 Safety Belt Performance Grants 20.609 855,891 State Traffic Safety Information System Improvement Grants 20.610 1,681,342 Incentive Grant Program to Increase Motorcyclist Safety 20.612 35,228 Total Highway Safety Cluster 74,202,930 - Research & Development Cluster Highway Planning and Construction 20.205 12,191,000 Formula Grants for Other Than Urbanized Areas 20.509 263,795 Total Research & Development Cluster 12,454,795 -	Disabilities	20.513		2,005,490	
Alcohol Impaired Driving Countermeasures Incentive Grants I 20.601 4,740,291 Occupant Protection Incentive Grants 20.602 616,380 Safety Belt Performance Grants 20.609 855,891 State Traffic Safety Information System Improvement Grants 20.610 1,681,342 Incentive Grant Program to Increase Motorcyclist Safety 20.612 35,228 Total Highway Safety Cluster 74,202,930 - Research & Development Cluster Highway Planning and Construction 20.205 12,191,000 Formula Grants for Other Than Urbanized Areas 20.509 263,795 Total Research & Development Cluster 12,454,795 -					
Occupant Protection Incentive Grants 20.602 616,380 Safety Belt Performance Grants 20.609 855,891 State Traffic Safety Information System Improvement Grants 20.610 1,681,342 Incentive Grant Program to Increase Motorcyclist Safety 20.612 35,228 Total Highway Safety Cluster 74,202,930 - Research & Development Cluster Highway Planning and Construction 20.205 12,191,000 Formula Grants for Other Than Urbanized Areas 20.509 263,795 Total Research & Development Cluster 12,454,795 -	, , ,				
Safety Belt Performance Grants 20.609 855,891 State Traffic Safety Information System Improvement Grants 20.610 1,681,342 Incentive Grant Program to Increase Motorcyclist Safety 20.612 35,228 Total Highway Safety Cluster 74,202,930 - Research & Development Cluster Highway Planning and Construction 20.205 12,191,000 Formula Grants for Other Than Urbanized Areas 20.509 263,795 Total Research & Development Cluster 12,454,795 -					
State Traffic Safety Information System Improvement Grants 20.610 1,681,342 Incentive Grant Program to Increase Motorcyclist Safety 20.612 35,228 Total Highway Safety Cluster 74,202,930 - Research & Development Cluster Highway Planning and Construction 20.205 12,191,000 Formula Grants for Other Than Urbanized Areas 20.509 263,795 Total Research & Development Cluster 12,454,795 -					
Research & Development Cluster 20.205 12,191,000 Highway Planning and Construction 20.509 263,795 Formula Grants for Other Than Urbanized Areas 20.509 12,454,795 Total Research & Development Cluster 12,454,795 -	State Traffic Safety Information System Improvement Grants			1,681,342	
Research & Development Cluster 20.205 12,191,000 Highway Planning and Construction 20.509 263,795 Formula Grants for Other Than Urbanized Areas 20.509 263,795 Total Research & Development Cluster 12,454,795 -		20.612			
Highway Planning and Construction 20.205 12,191,000 Formula Grants for Other Than Urbanized Areas 20.509 263,795 Total Research & Development Cluster 12,454,795 -	Total Highway Safety Cluster			74,202,930	-
Highway Planning and Construction 20.205 12,191,000 Formula Grants for Other Than Urbanized Areas 20.509 263,795 Total Research & Development Cluster 12,454,795 -	Research & Development Cluster				
Total Research & Development Cluster 12,454,795 -		20.205		12,191,000	
<u> </u>		20.509			
Total Department of Transportation 2,683,067,568 1,022,292,093	iotai kesearch & Development Cluster			12,454,795	-
	Total Department of Transportation			2,683,067,568	1,022,292,093

Equal Employment Opportunity Commission

Employment Discrimination-State and Local Fair Employment Practices Agency Contracts	30.002		2,810,325	
General Services Administration				
Donation of Federal Surplus Personal Propery Election Reform Payments	39.003 39.011		407,743	
National Aeronautics and Space Administration				
Aeronautics	43.002		104,052	
National Endowment for the Arts				
Promotion of the Arts-Partnership Agreements	45.025		1,154,651	
ARRA-Promotion of the Arts-Partnership Agreements, Recovery Act	45.005			204.020
Funded Total National Endowment for the Arts	45.025		1,154,651	204,628 204,628
Total National Endownient for the Arts			1,104,001	204,020
Institute of Museum and Library Services				
Grants to States	45.310		18,518,019	
Department of Veterans Affairs				
0 0	0.4.00=		7.500.500	
Grants to States for Construction of State Home Facilities	64.005		7,502,563	
Veterans State Nursing Home Care	64.015 64.101		5,425 99,200	
Burial Expenses Allowance for Veterans Veterans Housing - Guaranteed and Insured Loans	64.114		99,200	
All-Volunteer Force Educational Assistance	64.124		1,322,279	
Total Department of Veterans Affairs			8,929,467	-
Environmental Protection Agency				
Air Pollution Control Program Support State Indoor Radon Grants	66.001 66.032		2,537,775 132,059	
Surveys, Studies, Research, Investigations, Demonstrations, and Special Purpose Activities Relating to the Clean Air Act	66.034		586,827	
ARRA-National Clean Diesel Emissions Reduction Program, Recovery Act Funded	66.039			3,896,904
ARRA-State Clean Diesel Grant Program	66.040			352,941
State Environmental Justice Cooperative Agreement Program	66.312		62,664	
Water Pollution Control State, Interstate, and Tribal Program	00.440		44 744 700	
Support Pass-Through from San Jose State University Foundation	66.419	R0975005	11,744,738 1,006,692	
State Public Water System Supervision	66.432	10070000	7,828,247	
State Underground Water Source Protection	66.433		426,640	
Surveys, Studies, Investigations, Demonstrations, and Training Grants				
and Cooperative Agreements - Section 104(b)(3) of the Clean Water Act	66.436			
Pass-Through from Association of Bay Area Governments		SFBC 09-02	36,343	
Water Quality Management Planning	66.454		505,711	0.007.045
ARRA-Water Quality Management Planning, Recovery Act Funded	66.454		42 529 770	2,067,015
Capitalization Grants for Clean Water State Revolving Funds	66.458		42,528,779	
ARRA-Capitalization Grants for Clean Water State Revolving Funds, Recovery Act Funded	66.458			139,835,977
Nonpoint Source Implementation Grants	66.460		10,018,142	100,000,011
Regional Wetland Program Development Grants	66.461		74,404	
Capitalization Grants for Drinking Water State Revolving Funds	66.468		82,343,037	
ARRA-Capitalization Grants for Drinking Water State Revolving Funds, Recovery Act Funded	66.468			64,464,646
State Grants to Reimburse Operators of Small Water Systems for				
Training and Certification Costs	66.471		3,120,103	
Beach Monitoring and Notification Program Implementation Grants	66.472		441,988	
Water Protection Grants to the States	66.474		200,214	
Environmental Information Exchange Network Grant Program and Related Assistance	66.608		387,717	

Consolidated Pesticide Enforcement Cooperative Agreements	66.700	1,150,557	
TSCA Title IV State Lead Grants Certification of Lead-Based Paint			
Professionals	66.707	688,608	
Pollution Prevention Grants Program	66.708	9,184	
Hazardous Waste Management State Program Support	66.801	7,878,670	
Superfund State, Political Subdivision, and Indian Tribe Site- Specific Cooperative Agreements	66.802	1,043,893	
Underground Storage Tank Prevention, Detection and Compliance	00.002	1,040,090	
Program	66.804	344,563	
Leaking Underground Storage Tank Trust Fund Corrective Action			
Program	66.805	2,638,259	
ARRA-Leaking Underground Storage Tank Trust Fund Corrective			
Action Program, Recovery Act Funded	66.805		10,936,430
Brownfields Training, Research, and Technical Assistance Grants and Cooperative Agreements	66.814	105,311	
State and Tribal Response Program Grants	66.817	(1,565)	
Brownfields Assessment and Cleanup Cooperative Agreements	66.818	849,440	
ARRA-Brownfields Assessment and Cleanup Cooperative			
Agreements, Recovery Act Funded	66.818	470,000,000	5,494
Total Excluding Cluster		178,689,000	221,559,407
Research & Development Cluster			
Pollution Prevention Grants Program	66.708	67,027	
Research, Development, Monitoring, Public Education, Training,			
Demonstrations, and Studies	66.716	127,161	
Total Research & Development Cluster		194,188	-
Total Environmental Protection Agency		470,000,400	204 550 407
Total Environmental Protection Agency		178,883,188	221,559,407
Department of Energy			
State Energy Program	81.041	1,681,532	
ARRA-State Energy Program, Recovery Act Funded	81.041	40,000,042	66,714,256
Weatherization Assistance for Low-Income Persons	81.042	10,836,813	
ARRA-Weatherization Assistance for Low-Income Persons, Recovery Act Funded	81.042		77,305,312
Office of Science Financial Assistance Program	81.049	(1,204)	77,000,012
ARRA-Conservation Research and Development, Recovery Act Funded	81.086	, ,	2,005,972
Renewable Energy Research and Development	81.087	419,398	
Office of Environmental Waste Processing	81.104	167,624	
State Energy Program Special Projects	81.119	533,098	
ARRA-Electricity Delivery and Energy Reliability, Research, Development and Analysis, Recovery Act Funded	81.122		296,686
ARRA-Energy Efficient Appliance Rebate Program (EEARP),	01.122		200,000
Recovery Act Funded	81.127		750,844
ARRA-Energy Efficiency and Conservation Block Grant Program			
(EECBG), Recovery Act Funded	81.128		5,204,177
Long Term Surveillance and Maintenance	81.136	10,309 13,647,570	152,277,247
Total Excluding Cluster		13,047,570	152,277,247
Research & Development Cluster			
Fossil Energy Research and Development	81.089	1,889,754	-
Total Department of Energy		15,537,324	152,277,247
Department of Education			
Department of Education			
Adult Education - Basic Grants to State	84.002	90,800,896	
Migrant Education_State Grant Program	84.011	144,430,960	
Title I Program for Neglected and Delinquent Children and Youth	84.013	1,783,995	
International Research and Studies Career and Technical Education Basic Grants to States	84.017 84.048	363,951	
Leveraging Educational Assistance Partnership	84.069	126,652,409 11,197,021	
Fund for the Improvement of Postsecondary Education	84.116	6,189	
Migrant Education - Coordination Program	84.144	150,118	
Rehabilitation Services-Client Assistance Program	84.161	50,060	
Safe and Drug-Free Schools and Communities-National Programs	84.184	349,283	
Byrd Honors Scholarships Safe and Drug-Free Schools and Communities-State Grants	84.185 84.186	4,902,222 5,109,669	
Supported Employment Services for Individuals with Significant	07.100	5,109,009	
Disabilities	84.187	5,388,347	
Even Start-State Educational Agencies			
· · · · · · · · · · · · · · · · · · ·	84.213	6,582,745	
Assistive Technology	84.224	858,393	
Assistive Technology Tech-Prep Education			

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Rehabilitation Training-State Vocational Rehabilitation Unit In-	0.4.005	40.4.000	
Service Training Charter Schools	84.265 84.282	194,862 45,170,411	
Twenty-First Century Community Learning Centers	84.287	172,379,397	
Special Education-State Personnel Development	84.323	2,546,163	
Advanced Placement Program (Advanced Placement Test Fee;	01.020	2,010,100	
Advanced Placement Incentive Program Grants)	84.330	4,377,974	
Grants to States for Workplace and Community Transition Training			
for Incarcerated Individuals	84.331	2,440,965	
Reading First State Grants	84.357	9,678,026	
Rural Education	84.358	1,247,945	
English Language Acquisition Grants	84.365	173,115,276	
Mathematics and Science Partnerships Improving Teacher Quality State Grants	84.366 84.367	26,665,816 320,454,396	
Grants for State Assessments and Related Activities	84.369	35,899,215	
Striving Readers	84.371	216,191	
College Access Challenge Grant Program	84.378	15,484,106	
Education Jobs Fund	84.410	1,075,228,907	
Total Excluding Cluster		2,294,635,998	-
Title I, Part A Cluster			
Title I Grants to Local Educational Agencies	84.010	1,693,860,107	
ARRA-Title I Grants to Local Educational Agencies, Recovery Act		,,,	
Funded	84.389		8,817,635
Total Title I, Part A Cluster		1,693,860,107	8,817,635
Out that Education Object on (IDEA)			
Special Education Cluster (IDEA)	04.007	4 400 500 000	
Special Education_Grants to States	84.027	1,199,596,203	
Special EducationPreschool Grants	84.173	37,687,867	070 007 400
ARRA-Special Education Grants to States, Recovery Act Funded	84.391		270,937,432
ARRA-Special Education-Preschool Grants, Recovery Act Funded Total Special Education Cluster (IDEA)	84.392	1,237,284,070	15,253,284 286,190,716
Total Special Education Gluster (IDEA)		1,237,204,070	200,190,710
Vocational Rehabilitation Cluster			
Rehabilitation Services_Vocational Rehabilitation Grants to States	84.126	167,811,876	
ARRA-Rehabilitation Services-Vocational Rehabilitation Grants to			
States, Recovery Act Funded	84.390		24,124,496
Total Vocational Rehabilitation Cluster		167,811,876	24,124,496
Early Intervention Services (IDEA) Cluster			
Special Education-Grants for Infants and Families	84.181	46,926,928	(0.7.1)
ARRA-Special Education - Grants for Infants and Families, Recovery Act	84.393	40,000,000	(654)
Total Early Intervention Services (IDEA) Cluster		46,926,928	(654)
Educational Technology State Grants Cluster			
Education Technology State Grants	84.318	10,010,923	
ARRA-Education Technology State Grants, Recovery Act Funded	84.386	-,,-	33,525,847
Total Educational Technology State Grants Cluster		10,010,923	33,525,847
School Improvement Grants Cluster			
School Improvement Grants	84.377	31,939,722	
ARRA-School Improvement Grants, Recovery Act Funded	84.388		97,304,668
Total School Improvement Grants Cluster		31,939,722	97,304,668
State Fiscal Stabilization Fund Cluster			
ARRA-State Fiscal Stabilization Fund (SFSF)-Education State			
Grants, Recovery Act Funded (Education Stabilization Fund)	84.394		763,946,004
			•
Independent Living State Grants Cluster	04.400	,,,,,	
Independent Living-State Grants	84.169	(412,926)	(440.440)
ARRA-Independent Living State Grants, Recovery Act Funded	84.398	(442.020)	(449,112)
Total Independent Living State Grants Cluster		(412,926)	(449,112)
Independent Living Services for Older Individuals Who Are Blind Clust	er		
Rehabilitation Services-Independent Living Services for Older			
Individuals Who are Blind	84.177	1,498,888	
ARRA-Independent Living Services for Older Individuals Who are			
Blind, Recovery Act Funded	84.399		(1,068,908)
Total Independent Living Services for Older Individuals Who		1,498,888	(1,068,908)
Education of Homeless Children and Vouth Cluster			
Education of Homeless Children and Youth Cluster Education for Homeless Children and Youth	84.196	8 013 773	
Education for Homeless Children and Youth	84.196	8,013,773	
Education for Homeless Children and Youth ARRA-Education for Homeless Children and Youth, Recovery Act		8,013,773	6 424 524
Education for Homeless Children and Youth	84.196 84.387	8,013,773	6,424,524 6,424,524

Statewide Data Systems Cluster Statewide Data Systems	84.372		14,711	<u>-</u>
Total Department of Education			5,491,584,070	1,218,815,216
Total Department of Education			3,431,304,070	1,210,013,210
U.S. Election Assistance Commission				
Help America Vote Act Requirements Payments	90.401		4,757,625	
Department of Health and Human Services				
State and Territorial and Technical Assistance Capacity				
Development Minority HIV/AIDS Demonstration Program Strengthening Public Health Services at the Outreach Offices	93.006		203,136	
of the U.S Mexico Border Health Commission Special Programs for the Aging - Title VII, Chapter 3, Programs	93.018		236,702	
for Prevention of Elder Abuse, Neglect, and Exploitation Special Programs for the Aging - Title VII, Chapter 2-Long Term	93.041		542,762	
Care Ombudsman Services for Older Individuals	93.042		1,670,818	
Special Programs for the Aging - Title III, Part D-Disease Prevention and Health Promotion Services	93.043		2,041,189	
Special Programs for the Aging - Title IV-and Title II-Discretionary				
Projects National Family Corogiver Support Title III. Bort F	93.048		845,238	
National Family Caregiver Support, Title III, Part E Public Health Emergency Preparedness	93.052 93.069		16,644,665 12,665,729 *	
Medicare Enrollment Assistance Program	93.003		405,169	
Emergency System for Advance Registration of Volunteer Health			,	
Professionals	93.089		56,476	
Maternal and Child Health Federal Consolidated Programs	93.110		1,109,294	
Project Grants and Cooperative Agreements for Tuberculosis	00.440		0.005.757 *	
Control Programs Emergency Medical Services for Children	93.116 93.127		8,365,757 * 73,859	
Cooperative Agreements to States/Territories for the Coordination and Development of Primary Care Offices	93.130		236,756	
Centers for Research and Demonstration for Health Promotion and				
Disease Prevention	93.135		454,940	
Injury Prevention and Control Research and State and Community Based Programs	93.136		5,108,149	
Projects for Assistance in Transition from Homelessness (PATH)	93.150		6,785,226	
Health Program for Toxic Substances and Disease Registry	93.161		522,633	
Grants to States for Loan Repayment Program	93.165		773,999	
Disabilities Prevention	93.184		230,901	
Consolidated Knowledge Development and Application (KD&A) Program	93.230		(358,217)	
Traumatic Brain Injury State Demonstration Grant Program	93.234		13,896	
Grants to States to Support Oral Health Workforce Activities	93.236		46,498	
State Rural Hospital Flexibility Program	93.241		367,715	
Substance Abuse and Mental Health Services - Projects of				
Regional and National Significance	93.243		372,581	
Universal Newborn Hearing Screening	93.251		279,277	
Substance Abuse and Mental Health Services - Access to Recovery	93.275		5,889,699	
Centers for Disease Control and Prevention - Investigations and			2,222,222	
Technical Assistance	93.283		68,175,248	
Pass-Through from Association of State and Territorial Health Officials (ASTHO)		5U38HM000454-02	22,856	
Small Rural Hospital Improvement Grant Program	93.301	30301 IW000434-02	448,702	
ARRA-State Loan Repayment Program, Recovery Act Funded	93.402			403,050
ARRA-State Primary Care Offices, Recovery Act Funded	93.414			109,429
Food Safety and Security Monitoring Project	93.448		480,320	
ARRA-Pregnancy Assistance Fund Program, Recovery Act Funded	93.500			118,658
Affordable Care Act (ACA) Maternal, Infant, and Early Childhood Home Visiting Program	93.505		1,434,621	
Strengthening Public Health Infrastructure for Improved Health	22.000		.,,	
Outcomes	93.507		183,253	
Affordable Care Act (ACA) State Health Care Workforce Development Grants	93.509		133,969	
Affordable Care Act (ACA) Personal and Home Care Aide State	55.555		.50,000	
Training Program (PHCAST)	93.512		97,634	
Affordable Care Act - Medicare Improvements for Patients and Providers	93.518		24,634	
The Affordable Care Act: Human Immunodeficiency Virus (HIV)			,00 .	
Prevention and Public Health Fund Activities	93.523		223,502	

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State Planning and Establishment Grants for the Affordable Care	93.525	25,000	1
Act (ACA)'s Exchanges Pro existing Condition Incurance Program (PCIP)	93.525	6,082,720	
Pre-existing Condition Insurance Program (PCIP) Promoting Safe and Stable Families	93.556	35,993,885	
Child Support Enforcement	93.563	629,263,036	
ARRA-Child Support Enforcement, Recovery Act Funded	93.563	029,203,030	18,533,865
Child Support Enforcement Research	93.564	3,225	
Refugee and Entrant Assistance - State Administered Programs	93.566	36,466,912	
Low-Income Home Energy Assistance	93.568	188,348,065	
Refugee and Entrant Assistance - Discretionary Grants	93.576	1,769,153	
U.S. Repatriation	93.579	51,264	
Refugee and Entrant Assistance - Targeted Assistance Grants	93.584	4.253.583	
State Court Improvement Program	93.586	3,130,762	2
Community-Based Child Abuse Prevention Grants	93.590	3,095,138	3
Grants to States for Access and Visitation Programs	93.597	196,299	9
Chafee Education and Training Vouchers Program (ETV)	93.599	5,632,205	5
Adoption Incentive Payments	93.603	62,670)
Voting Access for Individuals with Disabilities - Grants to States	93.617	1,486,295	5
Developmental Disabilities Basic Support and Advocacy Grants	93.630	10,784,162	2
Children's Justice Grants to States	93.643	1,872,783	3
Stephanie Tubbs Jones Child Welfare Services Program	93.645	34,473,623	3
Child Welfare Research Training or Demonstration	93.648	315,632	2
Foster Care - Title IV-E	93.658	1,134,720,043	
ARRA-Foster Care - Title IV-E, Recovery Act Funded	93.658		39,972,409
Adoption Assistance	93.659	415,469,414	
ARRA-Adoption Assistance, Recovery Act Funded	93.659		33,595,945
Social Services Block Grant	93.667	551,323,500	
Child Abuse and Neglect State Grants	93.669	4,136,252	2
Family Violence Prevention and Services/Grants for Battered			
Women's Shelters - Grants to States and Indian Tribes	93.671	8,539,527	
Chafee Foster Care Independence Program	93.674	20,421,277	7
ARRA-State Grants to Promote Health Information Technology,			
Recovery Act Funded	93.719		1,456,167
ARRA-Prevention and Wellness-State, Territories			
and Pacific Islands, Recovery Act Funded	93.723		1,980,345
ARRA-Prevention and Wellness - Communities Putting Prevention to			
Work Funding Opportunities Announcement (FOA)	93.724		3,732
ARRA-Communities Putting Prevention to Work: Chronic Disease			
Self-Management Program, Recovery Act Funded	93.725		612,228
Children's Health Insurance Program	93.767	1,284,857,563	3
Centers for Medicare and Medicaid Services (CMS) Research,			
Demonstrations and Evaluations	93.779	5,179,453	3
Money Follows the Person Rebalancing Demonstration	93.791	4,046,764	1
Specially Selected Health Projects	93.888	470,527	7
National Bioterrorism Hospital Preparedness Program	93.889	39,522,552	2
Grants to States for Operation of Offices of Rural Health	93.913	153,902	2
HIV Care Formula Grants	93.917	145,915,347	7
Cooperative Agreements to Support Comprehensive School Health			
Programs to Prevent the Spread of HIV and Other Important			
Health Problems	93.938	767,557	
HIV Prevention Activities - Health Department Based	93.940	15,511,840)
HIV Demonstration, Research, Public and Professional Education			
Projects	93.941	377,842	2
Epidemiologic Research Studies of Acquired Immunodeficiency			
Syndrome (AIDS) and Human Immunodeficiency Virus (HIV)			
Infection in Selected Population Groups	93.943	16,791	I
Human Immunodeficiency Virus (HIV) / Acquired Immunodeficiency			
Virus Syndrome (AIDS) Surveillance	93.944	2,667,862	2
Tuberculosis Demonstration, Research, Public and Professional			
Education	93.947	11,382	2
Block Grants for Community Mental Health Services	93.958	46,010,088	
Block Grants for Prevention and Treatment of Substance Abuse	93.959	303,602,234	
National All Schedules Prescription Electronic Reporting Grant	93.975	327,590)
Preventive Health Services - Sexually Transmitted Diseases			
Control Grants	93.977	5,003,127	7 *
Preventive Health Services - Sexually Transmitted Diseases	-	.,,	
Research, Demonstrations and Public Education Grants	93.978	658,045	5
Mental Health Disaster Assistance and Emergency Mental Health	93.982	25	
Preventive Health and Health Services Block Grant	93.991	6,269,82	
Maternal and Child Health Services Block Grant to the States	93.994	51,087,460	
Other-Department of Health and Human Services	93.999	22,810,712	
Pass-Through from National Association of Chronic Disease Directors		1045000368110 221,063	
ARRA-Other-Department of Health and Human Services, Recovery			
Act Funded	93.999		124,503
Total Excluding Clusters		5,170,215,560	96,910,331

Aging Cluster Special Programs for the Aging Title III. Part P. Crants for			
Special Programs for the Aging - Title III, Part B - Grants for Supportive Services and Senior Centers	93.044	39.993.537	
Special Programs for the Aging - Title III, Part C - Nutrition Services	93.045	68,329,736	
Nutrition Services Incentive Program	93.053	12,962,627	
ARRA-Aging Home-Delivered Nutrition Services for States, Recovery Act Funded	93.705		444,615
ARRA-Aging Congregate Nutrition Services for States, Recovery	30 33		,
Act Funded	93.707	·	1,210,740
Total Aging Cluster		121,285,900	1,655,355
Immunization Cluster			
Immunization Grants	93.268	26,608,054 *	
ARRA-Immunization, Recovery Act Funded Total Immunization Cluster	93.712	26,608,054	6,619,050 * 6,619,050
Total Illimunization Cluster		20,000,004	0,019,050
TANF Cluster			
Temporary Assistance for Needy Families	93.558	3,390,046,831	
ARRA-Emergency Contingency Fund for Temporary Assistance for Needy Families (TANF) State Programs, Recovery Act Funded	93.714		613,268,598
Total TANF Cluster	30.7 14	3,390,046,831	613,268,598
CSBG Cluster Community Services Block Grant	93.569	64,661,782	
ARRA-Community Services Block Grant, Recovery Act Funded	93.710	04,001,762	52,540,914
Total CSBG Cluster		64,661,782	52,540,914
CODE Cluster			
CCDF Cluster Child Care and Development Block Grant	93.575	292,210,540	
Child Care Mandatory and Matching Funds of the Child Care and			
Development Fund	93.596	290,583,473	
ARRA-Child Care and Development Block Grant, Recovery Act	02.742		440 400 400
Funded Total CCDF Cluster	93.713	582,794,013	110,109,406 110,109,406
		55_,,	, ,
Head Start Cluster	02.000	220 502	
Head Start ARRA-Head Start, Recovery Act Funded	93.600 93.708	220,503	250,666
Total Head Start Cluster		220,503	250,666
Madiasid Olysten			
Medicaid Cluster			
ARRA-Survey and Certification Ambulatory Surgical Center Healthcare- Associated Infection (ASC-HAI) Prevention Initiative, Recovery Act			
Funded	93.720		719,625
State Medicaid Fraud Control Units	93.775	21,026,194	
State Survey and Certification of Health Care Providers and Suppliers (Title XVIII) Medicare	93.777	37,682,152	
Medical Assistance Program	93.778	29,356,782,672	
ARRA-Medical Assistance Program, Recovery Act Funded	93.778	00.445.404.040	5,032,334,326
Total Medicaid Cluster		29,415,491,018	5,033,053,951
Research & Development Cluster			
Food and Drug Administration-Research	93.103	443,798	
Project Grants and Cooperative Agreements for Tuberculosis Control Programs	93.116	160,332	
Substance Abuse and Mental Health Services-Projects of	90.110	100,332	
Regional and National Significance	93.243	15,000	
Affordable Care Act (ACA) Grants to States for Health Insurance Premium			
Review Affordable Care Act (ACA) – Consumer Assistance Program Grants	93.511 93.519	471,782 38,689	
Total Research & Development Cluster	00.010	1,129,600	-
Total Department of Health and Human Services		38,772,453,261	5,914,408,272
Corporation for National and Community Service			
State Commissions Learn and Serve America - School and Community Based Programs	94.003 94.004	1,357,647 2,485,538	
AmeriCorps	94.004	2,485,538 24,525,106	
ARRA-AmeriCorps, Recovery Act Funded	94.006	,,,,,,,	5,858
Volunteers in Service to America	94.013	* 06.404	
Volunteer Generation Fund Total Excluding Clusters	94.021	26,421 28,394,712	5,858
		· · -	- ,

Foster Grandparent/Senior Companion Cluster Foster Grandparent Program	94.011		1,333,473	
Total Corporation for National and Community Service		-	29,728,185	5,858
Executive Office of the President				
High Intensity Drug Trafficking Areas Program	95.001			
Pass-Through from LA Clear/LA Police Chief's Association/City of Monrovia		G09LA0006A	105,282	
Pass-Through from LA Clear/LA Police Chief's Association/City of Monrovia		G10LA0006A	304,887	
Pass-Through from CV HIDTA/LA Police Chief's Association/Sacramento County		I8PSCP504Z	108	
Pass-Through from CV HIDTA/LA Police Chief's Association/Sacramento County		G09CV0002A	57,710	
Pass-Through from INCH/LA Police Chief's Association/Riverside County		G09LA0007A	64,687	
Pass-Through from NV HIDTA/LA Police Chief's Association/Las Vegas Metro PD		G09NV0001A	9,839	
Pass-Through from NV HIDTA/LA Police Chief's Association/Las Vegas Metro PD		G10NV0001A	48,481	
Pass-Through from CA Border Alliance Group/City of San Diego/San		G09SC0001A	2,033	
Diego Police Dept (SDNIN) Pass-Through from CA Border Alliance Group/City of San Diego/San				
Diego Police Dept (SDNIN)		G10SC0001A	551,665	
Total Executive Office of the President		=	1,144,692	<u>-</u>
Social Security Administration				
Disability Insurance/SSI Cluster Social Security_Disability Insurance	96.001		215,985,809	
Total Social Security Administration		-	215,985,809	-
Department of Homeland Security				
Non-Profit Security Program Boating Safety Financial Assistance	97.008 97.012		850,171 6,884,126	
Community Assistance Program-State Support Services Element (CAP-SSSE)	97.023		395,248	
Flood Mitigation Assistance	97.029		649,814	
Disaster Grants - Public Assistance (Presidentially Declared				
Disasters) Hazard Mitigation Grant	97.036 97.039		348,319,231 13,186,229	
National Dam Safety Program	97.039		159,272	
Emergency Management Performance Grants	97.042		23,230,777	
Assistance to Firefighters Grant	97.044		(457,811)	
Cooperating Technical Partners	97.045		151,809	
Fire Management Assistance Grant	97.046		92,208,595	
Pre-Disaster Mitigation	97.047		6,304,383	
Emergency Operations Centers	97.052		(5,331)	
Interoperable Emergency Communications Map Modernization Management Support	97.055 97.070		6,534,453 157,084	
Rail and Transit Security Grant Program	97.075		17,600,491	
Buffer Zone Protection Program (BZPP)	97.078		4,685,449	
Earthquake Consortium	97.082		520,293	
Severe Loss Repetitive Program	97.110		223,038	
Regional Catastrophic Preparedness Grant Program (RCPGP)	97.111		3,024,090	
Radiological/Nuclear Detection Pilot Evaluations Program	97.121		255,313	
Gulf of Mexico US Coast Guard PRFA Total Excluding Cluster	97.999	-	34,248 524,910,972	-
Homeland Security Cluster				
Homeland Security Grant Program	97.067		230,827,709	
Pass-Through from Sacramento County Sherriff's Department		08.I8PCVP502Z	13,923	
Pass-Through from San Diego County Sherriff's Department		2010-1085	1,131,192	
Pass-Through from San Diego County Sherriff's Department		R0995008	62,200	
Pass-Through from Imperial County		CAPELC 08-001	549,387	
Total Homeland Security Cluster			232,584,411	-
Total Department of Homeland Security		-	757,495,383	-

Miscellaneous Grants and Contracts

Total Expenditures of Federal Awards			\$ 74,093,821,975	\$ 9,498,308,973
Total Miscellaneous Grants and Contracts			100,881,154	13,330
Pass-Through from Miscellaneous Entities		Unknown	1,358,970	10,000
Miscellaneous Expenditures of Federal Awards ARRA-Miscellaneous Expenditures of Federal Awards	99.999		94,215,890	** 13.330
Miscellaneous Expenditures of Federal Awards	99.099		(12,877)	
U.S. Department of Agriculture and Various Other U.S. Department- Fire Prevention/Suppression	99.016		4,857,750	
U.S. Department of the Interior-Fire Prevention/Suppression Agreement	99.014		134,000	
Shared Revenue-Grazing Land	99.004		65,233	
Shared Revenue-Flood Control Lands	99.002		262.188	

Note: OMB Circular A-133 requires that the State include, in either its Schedule of Expenditures of Federal Awards (schedule) or related notes, the value of federal awards expended in the form of non-cash assistance—such as commodities and vaccines received—the amount of insurance in effect during the year, and loan and loan guarantees outstanding at year end. Although the schedule does not include these amounts, the State did receive this assistance for certain federal programs—as noted with the symbols shown below—and further described in Notes 5 and 6.

^{*} This program has non-cash federal assistance, which may include a variety of items, such as commodites, food stamps, vaccines, or federal excess property. For the value of this assistance, see Note 5.

^{**} This program has loans and/or loan guarantees outstanding as of June 30, 2011. See Note 6.

^{***} This program has insurance in force as of June 30, 2011. See Note 6.

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STATE OF CALIFORNIA

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

FISCAL YEAR ENDED JUNE 30, 2011

1. GENERAL

The accompanying State of California Schedule of Expenditures of Federal Awards presents the expenditures for all federal award programs for the fiscal year ended June 30, 2011. Except for \$213 million passed through to the University of California and the California State University systems from the State Fiscal Stabilization Fund—Education State Grants, Recovery Act (federal catalog number 84.394), this schedule generally does not include federal awards expended by these systems, and the California Housing Finance Agency, a component unit of the State. These entities engaged other auditors to perform an audit in accordance with the U.S. Office of Management and Budget, Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations* (OMB Circular A-133).

2. BASIS OF ACCOUNTING

The federal award expenditures reported in the schedule are prepared from records maintained by each state department for federal funds. Except for the Medical Assistance Program (federal catalog number 93.778), the expenditures included on the schedule are reported on the cash basis of accounting with certain accruals. The State of California accounts for the Medical Assistance Program's expenditures on a cash basis. The departments' records are periodically reconciled to State Controller's records for federal receipts and department expenditures processed. Negative amounts shown on the schedule represent adjustments or credits made in the normal course of business to amounts reported as expenditures in prior years.

3. UNEMPLOYMENT INSURANCE

The Employment Development Department (EDD) administers the Unemployment Insurance program (federal catalog number 17.225). EDD was not able to differentiate all federal funds received and expended under the American Recovery and Reinvestment Act of 2009 (Recovery Act) for this program. Thus, the Recovery Act amount of \$599,511,599 shown on the Schedule of Expenditures of Federal Awards is an estimate of what EDD believes it expended from the Recovery Act for Emergency Unemployment Compensation, Federal Additional Compensation, Federal-State Extended Benefits, and administrative costs.

Additionally, the State funded \$3,754,686,505 of the \$20,410,960,823 shown on the schedule as non-Recovery Act expenditures with a loan from the federal Unemployment Trust Fund (UTF). The State owed the federal UTF a total of \$10,957,982,217 as of June 30, 2011, which includes \$7,203,295,712 of loans received in fiscal year 2009-10 and fiscal year 2008-09.

4. RECOVERY ACT FUNDING OF SUPPLEMENTAL NUTRITION ASSISTANCE PROGRAM BENEFITS

The reported expenditures for benefits under the Supplemental Nutrition Assistance Program (SNAP) (CFDA No. 10.551) are supported by both regularly appropriated funds and incremental funding made available under section 101 of the Recovery Act. The portion of total expenditures for SNAP benefits that is supported by Recovery Act funds varies according to fluctuations in the cost of the Thrifty Food Plan, and to changes in participating households' income, deductions, and assets. This condition prevents USDA from obtaining the regular and Recovery Act components of SNAP benefits expenditures through normal program reporting processes. As an alternative, USDA has computed a weighted average percentage to be applied to the national aggregate SNAP benefits provided to households in order to allocate an appropriate portion thereof to Recovery Act funds. This methodology generates valid results at the national aggregate level but not at the individual State level. Therefore, we cannot validly disaggregate the regular and Recovery Act components of our reported expenditures for SNAP benefits. At the national aggregate level, however, Recovery Act funds account for approximately 16.38 percent of USDA's total expenditures for SNAP benefits in the Federal fiscal year ended September 30, 2010.

5. NON-CASH FEDERAL AWARDS

The State is the recipient of federal award programs that do not result in cash receipts or disbursements. These non-cash federal awards include a variety of items, such as commodities, SNAP benefits (i.e. food stamps), vaccines, or federal excess property. Non-cash awards distributed for fiscal year ending June 30, 2011 are as follows:

Program Name	Non-Cash Awards for fiscal year 2010-11
Supplemental Nutrition Assistance Program	\$6,284,729,871
National School Lunch Program	142,384,462
Commodity Supplemental Food Program	13,463,308
Emergency Food Assistance Program (Food Commodities)	77,978,927
ARRA - Emergency Food Assistance Program (Food Commodities), Recovery Act Funded	15,532
Rural Development, Forestry, and Communities	265,650
Donation of Federal Surplus Personal Property	40,033,759
Public Health Emergency Preparedness	184,535
Project Grants and Cooperative Agreements for Tuberculosis Control Programs	311,125
Immunization Grants	465,869,765
ARRA - Immunization Grants, Recovery Act Funded	4,056,633
	Supplemental Nutrition Assistance Program National School Lunch Program Commodity Supplemental Food Program Emergency Food Assistance Program (Food Commodities) ARRA - Emergency Food Assistance Program (Food Commodities), Recovery Act Funded Rural Development, Forestry, and Communities Donation of Federal Surplus Personal Property Public Health Emergency Preparedness Project Grants and Cooperative Agreements for Tuberculosis Control Programs Immunization Grants

93.977	Preventive Health Services - Sexually Transmitted Diseases Control Grants	414,376
94.013	Volunteers in Service to America	499,242
	Total	\$7,030,207,185

6. LOANS, LOAN GUARANTEES OUTSTANDING, AND INSURANCE IN EFFECT

Loans, loan guarantees outstanding, and insurance in effect at June 30, 2011, are summarized below:

CEDA		Loans/Loan Guarantees	Insurance In Effect at
CFDA Number	Program Name	Outstanding at June 30, 2011	June 30,2011
14.228	Community Development Block Grants/ State's Program and Non-Entitlement Grants in Hawaii	\$7,727,287	
14.235	Supportive Housing Program	1,302,405	
14.239	Home Investment Partnerships Program	110,727,946*	
64.114	Veterans Housing - Guaranteed and Insured Loans		100,193,371
99.999	State Small Business Credit Initiative	3,971,401**	
	Total	\$123,729,039	\$100,193,371
		. , ., .,	. , ,

^{*} As indicated in the finding on page 59, reference number 2011-12-4, the amount reported here may not be accurate.

7. PASS-THROUGH

Federal awards received by the State from a pass-through entity are included in the Schedule of Expenditures of Federal Awards and italicized.

^{**} The amount includes \$3,626,800 from the Business, Transportation and Housing Agency and \$344,601 from the California Pollution Control Financing Authority.

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Summary Schedule of Prior Audit Findings

Prepared by Department of Finance

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SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

Reference Number: 2010-12-8

Federal Program: All programs

State Administering Department: Department of Finance (Finance)

Fiscal Year Initially Reported: 1995-96

Reporting. Because of limitations in its automated Audit Finding:

> accounting systems, the State has not complied with the provisions of U.S. Office of Management and Budget Circular A-133 requiring auditees to prepare a Schedule of Expenditures of Federal Awards that includes the total federal awards expended for each individual federal

program.

Status of Corrective Action: Fully corrected. Finance has implemented a solution that

> brings California into compliance with the requirement of reporting federal expenditures beginning with fiscal year 2010-11. As previously reported, this solution will be utilized until the long term automated solution is

operational.

Solution Implemented

In a cooperative effort with State agencies, a solution was implemented as of fiscal year 2010-2011. Finance directed departments via an August 2010 Budget Letter to manually track and report expenditures separately for each federal program. The federal expenditures will be reported on a year-end financial report that has been modified for that purpose – Report of Expenditures of Federal Funds (Report No. 13). Furthermore, the State Administrative Manual (SAM) Section 7974 was revised in March 2011 to provide further instructions on how to prepare the Report No. 13. Each department will submit a Report No. 13 to Finance by August 20, 2011 and these reports will be consolidated to create the Schedule of Expenditures of Federal Awards. As of June 30, 2011, Finance auditors consulted and trained all departments who received federal awards in fiscal year 2009-10 to ensure the success of this interim solution. Also, Finance auditors will consult with departments who received

federal awards for the first time in 2010-11 to ensure they are aware of the new reporting requirements.

Long Term Plan

The State has received legislative approval for a new automated/integrated statewide financial management system-- the Financial Information System for California (FI\$Cal Project). The FI\$Cal Project is a comprehensive Statewide initiative costing over \$1 billion and is anticipated to be completed by fiscal year 2017-2018. Wave 1 implementation is planned for 2012-13. The FI\$Cal Project's requirements related to federal funding include the capability to record grants by Catalog of Federal Domestic Assistance (CFDA) number, and to track and record transactions for individual grants at all levels of the account classification structure by time period and by CFDA number. Finance is confident the new system, upon full implementation to all State departments (planned for 2017-2018) will provide an automated solution to capture total expenditures for each federal program as required by OMB Circular A-133.

Reference Number: 2010-7-11

Federal Program: 94.006

State Administering Department: CaliforniaVolunteers

Fiscal Year Initially Reported: 2003-04

Audit Finding: Matching. California Volunteers has not ensured its

established policies and procedures for fiscal desk reviews are followed. Specifically, CaliforniaVolunteers,

did not verify the allowability of grantee match contributions for the fiscal desk reviews tested where requirements to verify match contributions existed. In addition, CaliforniaVolunteers has yet to eliminate its

backlog of fiscal desk reviews.

Status of Corrective Action: Partially corrected. Staff are now in place and have been

trained to conduct fiscal desk reviews. Since the audit findings, closing letters for the 2007-08 fiscal desk review

process have been sent to 8 sub-grantees and

CaliforniaVolunteers continues to work on the backlog. CaliforniaVolunteers has been plagued by staffing changes, complicated by the change in Administration in January 2011. It is expected that the backlog of fiscal desk reviews (those from 2007-08 and 2008-09) will be complete by December 31, 2011. In addition, beginning

with the 2009-10 grant year, the letters to sub-grantees requesting information for the fiscal desk reviews will

included. It is anticipated that these letters will be sent by September 30, 2011.¹

Reference Number: 2010-13-8

Federal Program: 94.006

State Administering Department: CaliforniaVolunteers

Fiscal Year Initially Reported: 2006-07

Audit Finding: <u>Subrecipient Monitoring</u>. CaliforniaVolunteers did not

implement its updated site-visit policy and procedures. Specifically, CaliforniaVolunteers is still in the process of reviewing and evaluating its interim policy and procedures

specify that documents verifying source of match must be

related to the review and documentation of fiscal

information on site visits.

Status of Corrective Action: Fully corrected. Site visits are regularly completed by

program staff.

Reference Number: 2010-1-2

Federal Program: 12.401

State Administering Department: Military Department (Military)

Fiscal Year Initially Reported: 2007-08

Audit Finding: Activities Allowed/Allowable Costs. Military lacks internal

controls that would allow it to prevent and/or detect instances when personnel costs are being inappropriately charged to this federal program. Specifically, the Military lacked a process to identify when personnel may no longer be working on allowable activities. Furthermore, Military did not have adequate documentation to support personnel costs charged to the federal fiscal years' 2009

and 2010 awards.

Status of Corrective Action: Partially corrected. Certifications have been completed,

during fiscal year 2010-11, for employees who work under a single federal appendix of the master cooperative

agreement (MCR). A tracking system has been

developed for employees who work under multiple federal appendix of the MCR. This process is expected to be

approved by the Federal Awarding Agency Director and implemented by July 1, 2011 for fiscal year 2010-11.²

Reference Number: 2010-5-2

Federal Program: 84.126

84.390

State Administering Department: Department of Rehabilitation (Rehabilitation)

Fiscal Year Initially Reported: 2008-09

Audit Finding: <u>Eligibility</u>. Rehabilitation did not always determine

applicant eligibility for services within the required period and did not properly document extensions to eligibility periods for six of the 40 applicant cases reviewed. Rehabilitation has processes in place to monitor the timeliness of its eligibility decisions; however, these tools and instructions were not effective in identifying and

correcting these six exceptions.

Status of Corrective Action: Partially corrected. Rehabilitation's current Field

Computer System (FCS) lacks the functionality necessary

to effectively track and monitor extensions of an

applicant's eligibility determination.

Rehabilitation implemented a short term solution in September 2010 for local level monitoring of eligibility determinations. Rehabilitation counselors and supervisors receive automated reminder notices on the FCS before the expiration of the 60 days allowed for eligibility determination. Rehabilitation will continue to remind counselors and managers of the most effective tracking tools available and emphasize the importance of manually tracking eligibility timelines and extensions using available reports. To ensure appropriateness and compliance with federal regulations, Rehabilitation supervisors continue to conduct reviews of eligibility determinations and extensions.

Long term solution is the implementation of an electronic records system. Rehabilitation has committed considerable resources to replace the FCS with a new electronic records system, Accessible Web-based Activity Reporting Environment (AWARE), now in pilot implementation. Rehabilitation expects that eligibility extensions will be more effectively tracked and monitored by staff through the AWARE system. The system is expected to be fully implemented Statewide by October

2011. Rehabilitation has completed the Meet and Confer process with the American Federation of State, County and Municipal Employees union regarding the change in Information Technology systems. Rehabilitation continues to identify strategies to streamline procedures that will ensure the timeliness of eligibility decisions and extensions. Examples include streamlining of processes. forms, and signature requirements, and combining eligibility and priority for services. Issue Memo 2011.03 for this purpose was approved in January 2011. The AWARE system has been adapted to daily display a list of consumers with activities due and their respective required completion dates, including eligibility decisions and extensions. The AWARE system is configured to automatically update an approved eligibility extension expiration date upon staff entry within the Record of Services (ROS). The AWARE system also contains ad hoc reporting features that allow easily attainable reports produced by each user, facilitating increased monitoring at the local level.3

Reference Number: 2010-7-1

Federal Program: 84.126

State Administering Department: Department of Rehabilitation (Rehabilitation)

Fiscal Year Initially Reported: 2008-09

Audit Finding: <u>Matching, Reporting</u>. Rehabilitation lacks adequate

internal controls to ensure compliance with the matching requirement. In response to our prior year finding, Rehabilitation implemented a new process for reviewing spreadsheets that staff prepared to track certified expenditure information submitted by its vendors. Although Rehabilitation's new process requires the accounting officer-specialist's supervisor to review these spreadsheets each month, Rehabilitation did not always ensure that the spreadsheet contained accurate amounts. The summary spreadsheet created to support the

amounts in Rehabilitations' final financial status report for the 2008 grant included errors that over reported the

nonfederal match share by \$111,189.

Status of Corrective Action: Fully corrected. The Certified Expenditure Report

procedures were revised after the most recent Bureau of State Audits audit and then finalized. Additional controls include: (1) preparation and retention of calculator tapes for verification, (2) procedures for identifying whether a report has been received, (3) process for recording

quarterly reporting, (4) verification of final submission for each provider, (5) review of file by member of second unit, (6) identification of areas to be included in the supervisor review, and (7) periodic reconciliation of the Certified Expenditure report with the match tracking reports maintained by the Rehabilitation Collaborative Services Unit.

Reference Number: 2010-1-3

Federal Program: 93.958

State Administering Department: Department of Mental Health (Mental Health)

Fiscal Year Initially Reported: 2006-07

Audit Finding: <u>Activities Allowed/Allowable Costs.</u> Mental Health has not

yet developed a process to verify whether the

subgrantees' actual expenditures of federal grant funds

are for allowable activities and costs.

Status of Corrective Action: Partially corrected. Mental Health established a

workgroup in March 2010 to determine the feasibility of having its Program Compliance Division conduct audits of the counties in accordance with Mental Health's risk analysis procedures and federal requirements. Mental Health had anticipated that this finding would be fully addressed by September 2010. However, due to extensive discussions and issues raised, Mental Health revised its implementation date to December 2010.

In March 2011, the workgroup prepared and distributed a draft recommendation to Mental Health's management. The recommendation included three possible solutions to meet the allowability of costs requirement for fiscal year 2011-12. This new process will ensure that only allowable activities and costs are paid for with the block grant funds. If Mental Health is still responsible for administering the grant for fiscal year 2012-13, then the workgroup recommends that Mental Health consider expanding the process developed in the prior fiscal year. The expansion of the process would further ensure that only allowable activities and costs are paid for with block grant funds.⁴

Reference Number: 2010-3-6

Federal Program: 93.563

State Administering Department: Department of Child Support Services (Child Support

Services)

Fiscal Year Initially Reported: 2005-06

Audit Finding: <u>Cash Management, Special Tests and Provisions</u>. Child

Support Services did not always adhere to cash

management requirements for drawing federal funds for the Child Support Enforcement program. The Child Support Services sometimes exceeded the Treasury-State Agreement three-day limit in disbursing payments for local assistance. In addition, Child Support Services did not properly report all the \$113.1 million Recovery Act funds received in fiscal year 2009-10 to the State

Controller's Office. Also, Child Support Services did not correctly report all Recovery Act draws that took place after the creation of the new account code totaling \$13.5

million.

Status of Corrective Action: Fully corrected. Child Support Services has taken steps

to ensure that staff is included in State control agency distribution lists for policy and procedure notifications. Child Support Services has also verified that Recovery Act funds for fiscal year 2010-11 have been correctly

recorded in the State's accounting records.

Reference Number: 2010-5-1

Federal Program: 93.659

State Administering Department: Department of Social Services (Social Services)

Fiscal Year Initially Reported: 2007-08

Audit Finding: <u>Eligibility</u>. Social Services continues to need to improve

its controls over its eligibility determinations. We found that adoption case files reviewed at two district offices did not contain completed documents that demonstrate compliance with federal regulations. At one district office, nine out of 10 case files we reviewed contained a copy of the agreement but the agreement was not signed or dated by the adoptive parents. Further, one agreement was signed after the final adoptive decree and did not include

the amount of nonrecurring expenses to be paid.

Status of Corrective Action: Fully corrected. Social Services establishes Adoption

Assistance Program (AAP) requirements under statute, regulations, and all county letters to counties and adoption district offices. Counties are audited under the single audit standards that include review of the AAP Claims for

AAP administrative and assistance costs are "desk

audited" by Social Services and certified correct and accurate by county welfare directors. The State has a Federally-approved AAP Program Improvement Plan (PIP) which guides Federal compliance. Pending completion of the PIP, an All County Letter was released September 29, 2009, that provided interim direction in the following areas: AAP Eligibility; AAP Agreements and Payment Amounts; AAP Reassessments and Nonrecurring Adoption Expenses. All proposed statute language was achieved via Assembly Bill (AB) X4 4 effective July 28, 2009, and Senate Bill (SB) 597 signed October 11, 2009, effective January 1, 2010. The outstanding items to be completed per the PIP are revisions of the regulations and the forms specific to AAP. In addition, Social Services submitted a Budget Change Proposal (BCP) requesting two fulltime Social Service Consultant III to provide more comprehensive oversight and monitoring of the counties and adoption district offices policies and procedures. The BCP was denied by the Legislature. Training was provided at the January and March 2010 District Office Managers meetings. A peer review between the seven District Offices was conducted at the District Office Managers meeting November 2010. The monitoring reviews did include an analysis of all supporting AAP documentation to ensure district office eligibility determinations and related payments are correct and in compliance with federal laws and regulations. The seven district offices are responsible for the administration of AAP for twenty-eight counties.

Reference Number: 2010-7-2

Federal Program: 93.958

State Administering Department: Department of Mental Health (Mental Health)

Fiscal Year Initially Reported: 2006-07

Audit Finding: Earmarking. Mental Health did not have official written

policy or procedures in place to ensure administrative costs were charged appropriately to the Substance Abuse and Mental Health Services Administration's Block Grants

for Community Mental Health Services.

Status of Corrective Action: Partially corrected. Mental Health established a

workgroup in February 2010 to establish a written policy, as well as processes and procedures, to ensure that only allowable costs are used to meet the earmarking requirement. Mental Health had anticipated that this finding would be fully addressed by September 2010.

However, due to extensive discussions and issues raised, Mental Health revised its implementation date to December 2010.

In January 2011, the workgroup prepared and distributed a draft policy and procedures to Mental Health's management. The draft policy and procedures are in the process of being revised and will be redistributed to Mental Health's management for review and approval. Prior to full implementation of the policy and procedures, the revision of processes, forms, and reports may be required. In addition, a draft desk manual for the grants management program has been developed.⁵

Reference Number: 2010-7-3

Federal Program: 93.958

State Administering Department: Department of Mental Health (Mental Health)

Fiscal Year Initially Reported: 2006-07

Audit Finding: <u>Level of Effort – Maintenance of Effort</u>. Mental Health still

needs to make further refinements to its process for complying with the maintenance of effort (MOE)

requirements. Specifically, Mental Health did not provide documentation to support the percentages it applied against the total of managed care and realignment dollars to arrive at the amount it reported as expenditures for children with serious emotional disturbance (SED). Additionally, Mental Health was unable to provide documentation that showed the components and expenditures used to generate the fiscal year 1994-95 threshold of \$160 million. For the MOE requirement related to the State's expenditures for community mental health services, we found that Mental Health did not include any expenditures from the Mental Health Services Act, and it could not positively state whether other State agencies fund community mental health programs for adults with serious mental illness (SMI) or children with

SED.

Status of Corrective Action: Partially corrected. Mental Health established a

workgroup in February 2010 to research the percentages used to support the managed care and realignment dollars used in its calculation of MOE for children with SED, and examine for revision its methodology for the MOE calculation for community mental health services. Mental Health had anticipated that this finding would be fully addressed by September 2010. However, due to

extensive discussions and issues raised, Mental Health revised its implementation date to December 2010.

Initially, Mental Health researched legislation on Managed Care and Realignment, as well as internal documents, which explained the MOE requirements.

In addition, Mental Health attempted to locate the fiscal year 1994-95 financial statement used to establish the baseline for SED expenditure, but they could not be found.

In March 2011, the workgroup developed a methodology, which will enable Mental Health to determine the dollar amount expended on approved actual claims for managed care. After the dollar amount is determined, Mental Health will recalculate the managed care percentage for each fiscal year. Mental Health is researching alternatives to determine the percentage used to support the realignment dollars used in its MOE calculation. If Mental Health is not successful in its efforts to reevaluate the percentages used to support the managed care and realignment dollars, then Mental Health will seek guidance from its federal awarding agency to determine how it can adequately determine the threshold.

Also, the workgroup has developed procedures to capture actual expenditure date based on the Governor's Budget for calculating the community mental health services MOE requirement.⁶

Reference Number: 2010-7-4

Federal Program: 93.568

State Administering Department: Department of Community Services and Development

(CSD)

Fiscal Year Initially Reported: 2008-09

Audit Finding: <u>Earmarking</u>. CSD lacks sufficient internal controls to

ensure that it meets earmarking requirements. CSD does not have a mechanism in place to track final expenditures

related to earmarking requirements.

Status of Corrective Action: Partially corrected. Contracts and Accounting will set up

the line-item budget detail in the Expenditure Activity Reporting System/Program Audit Report Contracts (EARS/PARC) and those dollars will be assigned an object code and tracked separately. The budget line item

March 2012

detail in EARS/PARC has yet to be modified by the Information Technology Department. Once it is modified, Accounting will be able to track and reconcile final expenditures.⁷

Reference Number: 2010-8-1

Federal Program: 93.959

State Administering Department: Department of Alcohol and Drug Programs (ADP)

Fiscal Year Initially Reported: 2008-09

Audit Finding: <u>Period of Availability</u>. ADP charged expenditures totaling

\$7,640 to the federal fiscal year 2008 grant after the period of availability. Our review of a sample of five transactions charged after the period of availability found that two of the five transactions were for expenditures obligated in October 2010, after the grant's period of

availability ended.

Status of Corrective Action: Fully corrected. ADP has corrected the errors in its

accounting records and has initiated a refund to the federal government to cover the amount of the questioned costs. As indicated in the Bureau of State Audit's finding, ADP has provided additional training and implemented procedures to ensure staff avoid charging expenditures

outside the period of availability in the future.

Reference Number: 2010-9-1

Federal Program: 93.568

State Administering Department: Department of Community Services and Development

(CSD)

Fiscal Year Initially Reported: 2008-09

Audit Finding: Procurement and Suspension and Debarment. CSD did

not comply with the suspension and debarment requirements in the Administration for Children and Families grants' terms and conditions. CSD developed and implemented a process to consult the federal Excluded Parties List System (EPLA) to ensure the subrecipients are not suspended or debarred; because of the timing of its implementation, this control was not in

effect before CSD issued its fiscal year 2009-10

subawards or contracts.

Status of Corrective Action: Fully Corrected. CSD was credited by the Bureau of

State Audits (BSA) for developing and implementing a new process; however, credit was not given for the 2009 year since the control was not in effect during the year

BSA was testing.

Reference Number: 2010-12-1

Federal Program: 93.044

93.045

State Administering Department: Department of Aging (Aging)

Fiscal Year Initially Reported: 2006-07

Audit Finding: Reporting. Aging needs to refine its procedures to ensure

that the financial status reports it submits to the federal government reflect accurate information. Our review of the revised financial status report for the fiscal year 2006 grant concerning the Title III portion of the Aging Cluster found that Aging overreported its in-kind contributions by \$7.1 million as well as the other recipient outlays by \$31.4 million. This error caused Aging to also overreport total program outlays less program income - it reported \$239

million when it should have reported \$200 million.

Status of Corrective Action: Fully corrected. A corrected 2006 Financial Status Report

SF-269 (FSR) that removed the non-match cash and inkind expenditures was sent to the Administration on Aging on September 13, 2010. To ensure the accuracy of future FSRs, Aging is revising the desk procedures to detail the process for reviewing the accounting report that is used to isolate expenditures for FSR preparation. The procedure will include a list of checkpoints for accuracy. Aging anticipates the revision of the desk procedures to be

completed by December 2010.

Reference Number: 2010-12-2

Federal Program: 93.568

State Administering Department: Department of Community Services and Development

(CSD)

Fiscal Year Initially Reported: 2006-07

Audit Finding: Reporting. CSD lacks sufficient internal controls to

ensure it meets proper federal reporting requirements. Specifically, CSD's written procedures do not include

steps to reconcile the federal share of program outlays shown in its internally developed spreadsheets to its accounting records.

Status of Corrective Action:

Partially corrected. Procedures have been updated to reconcile CALSTARS and accounting spreadsheets. Procedures for the Community Services Block Grant and Low Income Home Energy Assistance Program have been written and adequately document this process. U.S. Department of Energy (DOE) procedures have been updated, but the written procedures are still in process of being revised. DOE written procedures are anticipated to be completed by mid-July 2011.⁸

Reference Number: 2010-13-2

Federal Program: 93.659

State Administering Department: Department of Social Services (Social Services)

Fiscal Year Initially Reported: 2007-08

Audit Finding: <u>Subrecipient Monitoring</u>. Social Services lack formal

processes to ensure it fulfills its pass-through

responsibility to monitor the counties during the award period. Specifically, Social Services does not perform monitoring procedures such as on-site visits or desk reviews of the counties' activities to ensure they are administering the program in compliance with federal laws

and regulations.

Status of Corrective Action: Fully corrected. Social Services has completed review of

six counties (San Joaquin, San Diego, Los Angeles, Orange, Riverside, and San Bernardino). Social Services will implement a progress report procedure to ensure compliance with the corrective action plan. This report will include what corrective actions were taken to resolve the reported findings. If counties are not in compliance, Social Services will implement ongoing monitoring procedures to eventually bring the County into compliance. Additionally, all claims will be adjusted

accordingly for the ineligible costs.

Reference Number: 2010-13-3

Federal Program: 93.044

93.045

93.053

93.705

93.707

State Administering Department: Department of Aging (Aging)

Fiscal Year Initially Reported: 2007-08

Audit Finding:

Subrecipient Monitoring. Aging lacks internal controls to ensure it identifies all the required federal award information at the time it awarded Recovery Act funds to its subgrantees. Aging also did not always fully comply with its policies and procedures for monitoring subgrantees' use of funds. Aging's policy requires its program staff to conduct on-site comprehensive assessments of each subgrantee every four years, which includes issuing final reports and corrective action plans to the subgrantees 75 working days after the exit conference it holds at the conclusion of the on-site assessment. Specifically, Aging did not meet its 75-day working day requirement for three out of six comprehensive assessments completed in fiscal year 2009-10.

Status of Corrective Action:

Fully corrected. Aging concurs it did not identify some of the federal award information to the Recovery Act grantees. This was because the finding came well after the contracts and subsequent amendments had already been issued to the grantees. Since the award period was one-time, ending June 30, 2010, and the finding was after-the-fact, Aging did not send out anything additional to the existing Recovery Act contractors. However, in response to the original audit finding, internal procedures were issued via Administrative Memo 10-01, to ensure that any future contracts include this information. Further, this information has been provided to our new Recovery Act grantee by including it in Exhibit D, Special Terms and Conditions, Article X, Audits section of their contract package for 2010-11. In addition, this information is included in the program memos that transmit all of the contracts and amendments to our grantees for our other regular federal grants.

Aging will modify its policies and procedures for monitoring sub-recipient activities to specify that Aging has 75 working days from the date of the on-site exit conference to issue its final monitoring report and that sub-grantees have 30 working days from the date the final monitoring report is issued to submit their Corrective Action Plan (CAP). All due dates will be calculated and included in applicable communications to sub-grantees. In addition, these policies and procedures will be modified to specify action steps and dates to ensure sub-recipient

CAPs are received timely. Aging anticipates this to be completed by November 2010.9

Reference Number: 2010-13-4

Federal Program: 93.568

State Administering Department: Department of Community Services and Development

(CSD)

Fiscal Year Initially Reported: 2006-07

Audit Finding: Subrecipient Monitoring. CSD's audit services unit (ASU)

did not always ensure it issued management decisions on audit findings within six months of receipt of subrecipients' U.S. Office of Management and Budget Circular A-133 reports. In our review of eight subrecipients' audit reports, in one case CSD did not issue a management decision

within the required six-month deadline.

Status of Corrective Action: Fully corrected. All audit reports have been reviewed and

a management decision issued within six months.

Reference Number: 2010-13-5

Federal Program: 93.563

State Administering Department: Department of Child Support Services (Child Support

Services)

Fiscal Year Initially Reported: 2006-07

Audit Finding: <u>Subrecipient Monitoring</u>. Child Support Services

continues to have problems fulfilling its subrecipient monitoring responsibilities for the Child Support

Enforcement program. Although Child Support Services indicated that it held entrance conferences to begin audits with nine local child support agencies (LCSAs) during fiscal year 2009-10, it was unable to complete any of

these audits by the end of the fiscal year. Further, Child

Support Services did not provide all required federal award information to LCSAs such as the federal award number and amount of Recovery Act funds. Child Support Services took steps to resolve these concerns; however, letter sent to LCSAs in January 2010 identifying amount of Recovery Act funds awarded did not include the award number for the federal fiscal year 2009 award.

Status of Corrective Action: Fully corrected. Child Support Services has fulfilled its

monitoring responsibilities by completing all nine plus three additional fiscal audits of the LCSAs. The required federal award information was provided to the LCSAs in the December 2010 allocation letter.

Reference Number: 2010-13-20

Federal Program: 93.959

State Administering Department: Department of Alcohol and Drug Programs (ADP)

Fiscal Year Initially Reported: 2007-08

Audit Finding:

Subrecipient Monitoring. ADP's county monitoring unit (CMU) did not follow written policies and procedures requiring supervisory review and approval of all desk and site review reports completed by its staff. Specifically, CMU temporarily assigned senior staff to finalize and sign off on desk and site-visit reports. During our review of a sample of six desk and site review files, we found staff did not always follow the temporary process. Specifically, we found peer reviews were not completed for four reviews. ADP also did not track the resolution of all corrective actions identified in its site and desk reviews to ensure subrecipients are addressing corrective actions promptly. Based on our testing of six county reviews completed by CMU, we found that for five of the reviews, CMU did not formally track resolution of all corrective actions it identified. Furthermore, we found that ADP did not issue one of five management decisions within six months as required. Finally, ADP's audit services branch did not complete and issue a final report for the one county it selected as part of its annual audit plan for fiscal year 2009-10.

Status of Corrective Action:

Partially corrected/remains uncorrected. This finding as it relates to the audit services branch remains uncorrected. We have been working with Alameda County and they in turn have been working with the County Board of Supervisors to approve/make the necessary changes. ADP is in the process of imposing monetary sanctions. As of this date, we have not received the county's corrective action and have now referred this to our accounting branch. They will proceed with monetary sanctions (withholding a percentage of the federal award). Our audit procedures state that management decisions will be issued within six months and we will adhere to that in future years.

CMU temporarily modified the report review process in

March 2010 to manage the workload due to staff shortages. The modified process received management approval verbally and was communicated to staff verbally. In the future, any temporary modifications to the review process will be appropriately documented. Also, the County Monitoring Operations Manual, County Monitoring and Negotiated Net Amount (NNA) compliance procedures, PMB-1 are updated annually to reflect ongoing process improvements. The policy and procedures related to the review and approval of desk and site reviews reports have been reviewed. CMU procedures manual has been updated to reflect the supervisor or designated lead analyst will be required to review and approve three county reports per CMU monitoring analyst. After three reports have been reviewed the supervisor or designated lead analyst will determine if the monitoring analyst possess the knowledge to review and finalize their own reports. This determination will be made on a case by case basis. Peer reviews will be required for every report.

ADP has taken several measures to ensure that CMU's staff track and maintain documentation to demonstrate that its subrecipients promptly address corrective actions identified during desk and site reviews completed by CMU. In particular, CMU has updated its corrective action tracking spreadsheet and revised the procedures manual to include a step-by-step process for proper documentation and tracking throughout the course of the review. In addition, CMU management will provide training and follow-up at regularly scheduled staff meetings to ensure staff maintains an understanding of the process and appropriately carries out the new process and procedures.

The final report was issued for the county. The Audit Services Branch has assigned dedicated staff to ensure that this does not happen in the future.¹⁰

Reference Number: 2010-14-1

Federal Program: 93.958

State Administering Department: Department of Mental Health (Mental Health)

Fiscal Year Initially Reported: 2006-07

Audit Finding: Special Tests and Provisions. Mental Health has not

facilitated peer reviews, but has made progress toward

correcting this finding. Specifically, Mental Health

executed a memorandum of understanding to perform peer reviews with the California Mental Health Planning Council (Council) in April 2010. However, the Council did not complete its first peer review report until July 2010, after the end of fiscal year 2009-10.

Status of Corrective Action:

Partially corrected. Council has finalized the process for conducting the independent peer reviews, and a Memorandum of Understanding between the Council and Mental Health.

In July 2010, the Council completed its first peer review. The Council plans to issue three reports in fiscal year 2010-11, including the report issued in July 2010.

The Council completed its second peer review in December 2010. The third peer review was conducted in April 2011; however, the report was not completed by June 30, 2011.¹¹

Reference Number: 2010-13-1

Federal Program: 10.561

93.558 93.658 93.659 93.667 93.714

State Administering Department: Department of Social Services (Social Services)

Fiscal Year Initially Reported: 2006-07

Audit Finding: <u>Subrecipient Monitoring</u>. Social Services cannot ensure

that federal funds are expended only for allowable activities, that federal funds are expended only in accordance with approved cost-allocation plan for local agencies, and that adjustments included on the county claims are for expenditures made within the two-year limit

for claiming payment.

Status of Corrective Action: Fully corrected. Per discussions with the Administration

for Children and Families (ACF), Social Services submitted a revised Corrective Action Implementation Plan (CAIP) on December 7, 2010. The ACF accepted Social Services' final CAIP on February 8, 2011. The reviews conducted by Social Services were fiscal monitoring evaluations of county fiscal controls and processes, and were not formal audits. The reviews were

conducted between December 2010 and June 2011. The

scope of the reviews was limited to selected cost pools for only one guarter (December 2009). These reviews were conducted in five counties in fiscal year 2010-11, and included a review of the Caseworker Salary and Benefits. Support Staff Salary and Benefits, Support Operating, and Direct Cost pools in the Social Services and California Work Opportunity and Responsibility to Kids (CalWORKs) functions. The review also included an evaluation of county processes to report the federal and nonfederal foster care caseload that was used to develop the nonfederal discount rate for the County Expense Claim (CEC) costs. The county assistance claim back-up for the same period was also reviewed for the Foster Care, Adoptions, and CalWORKs programs. Reviews of Yolo, Alameda, Butte, Los Angeles and San Francisco counties were completed by June 17, 2011. During the site visit, Social Services reviewed assistance payments claimed on the CA 800 Foster Care assistance claim form, as well as associated administration and services costs reported on the CEC. A random sampling methodology was used to determine the number of assistance payments that were reviewed. All back-up summaries, time studies, and payment documentation were reviewed for the administration and services costs reported on the CEC. There was only one situation where a county was required to submit an adjustment claim, which was necessary due to a claim submitted in error with transposed numbers. There were no other monetary findings associated with the assistance, administration, and services costs. There were some minor findings related to the time study documents such as missing identifying information, the use of white out, missing signatures/dates, etc., for which the monitoring team provided technical assistance to county staff to ensure that time studies are filled out correctly in the future. Summary letters of the on-site reviews were provided to ACF.

Reference Number: 2010-2-6

Federal Program: 14.239

State Administering Department: Department of Housing and Community Development

(Housing)

Fiscal Year Initially Reported: 2008-09

Audit Finding: Allowable Costs; Subrecipient Monitoring. Housing could

not demonstrate that the Home Investment Partnerships Program (HOME) funds it disbursed to State recipients were necessary and reasonable in accordance with the U.S. Office of Management and Budget Circular A-87. In response to the prior year's finding, Housing indicated that it would follow a risk-based approach for selecting and reviewing State recipients and conduct reviews of 40 highest-risk recipients. Housing fell short of its goal to monitor 40 State recipients, and in selecting which State recipients it monitored, it did not consistently choose those that it had determined to be at greater risk for noncompliance. Specifically, Housing performed reviews of 10 projects and 10 programs administered by State recipients, for a total of 20 projects reviewed during fiscal year 2009-10. However, of the 10 projects reviewed, only five were in Housing's "top ten" listing of projects with the highest risk. Furthermore, Housing had not issued letters notifying State recipients of the results of the reviews that were performed.

Status of Corrective Action:

Partially corrected. Letters were sent on March 31, 2011 to all jurisdictions monitored in calendar year 2010.

The Risk Assessment is nearly done and will be completely done by June 30, 2011.

Monitoring visits will be conducted on site for the 20 highest-risk State recipient programs and projects by December 31, 2011. Monitoring letters will be sent to the jurisdictions within 30 days of the visit.¹²

Reference Number: 2010-7-12

Federal Program: 14.239

State Administering Department: Department of Housing and Community Development

(Housing)

Fiscal Year Initially Reported: 2007-08

Audit Finding: <u>Matching; Reporting</u>. Housing's overstatements of match

amounts from prior fiscal years accumulates and

contributes to an overstated excess match balance on its report to Housing and Urban Development (HUD). Although Housing has corrected the double-counting issue with its match amounts, it has not resolved the uncertainty surrounding the accuracy of its excess match

balances that carry forward from prior years.

Status of Corrective Action: Fully corrected. The State has finished reviewing and

adjusting its excess match balance, and the 2009-10 match report was sent to HUD by June 15, 2011.

Reference Number: 2010-12-9

Federal Program: 14.228

State Administering Department: Department of Housing and Community Development

(Housing)

Fiscal Year Initially Reported: 2007-08

Audit Finding: Reporting. Housing still lacks adequate internal controls

to ensure the completeness of the Section 3 Summary Report that it submits to the U.S. Department of Housing and Urban Development. Housing began using a

computer system to identify and report on those

subrecipients that should provide Section 3 data based on the amounts of their subawards. However, Housing did not establish the correct parameters when programming

the report, which resulted in excluding certain

subrecipients that were required to submit Section 3 data. As a result, Housing's computer-based report did not identify 24 subrecipients out of 130 subrecipients required

to submit Section 3 data.

Status of Corrective Action: Fully corrected. The Community Development Block

Grant (CDBG) program analyzed all reports submitted that were not on the tracking list to determine why they reported no Section 3 activity. While the majority did not need to report, some were incorrectly excluded from the list, which could result in approximately 20 contracts. The CDBG program has incorporated the missing activity into the report for next year. The Consolidated Automated Program Enterprise System report for the upcoming reporting period has incorporated the additional codes so that all possible contracts that require reporting will be

captured.

Reference Number: 2010-12-10

Federal Program: 14.239

State Administering Department: Department of Housing and Community Development

(Housing)

Fiscal Year Initially Reported: 2007-08

Audit Finding: Reporting. Housing reported to the Department of

Finance that it had more than \$93 million in outstanding loans under the Home Investment Partnerships Program

(HOME). However, Housing had not yet completed its reconciliation at the time it reported this information. As a result, the amount included on the Schedule of Federal Assistance has been potentially understated.

Status of Corrective Action: Partially corrected. Although significant progress has

been made, the reconciliation has not yet been completed. The reconciliation work continues to be a high-priority task and the target completion date is estimated for May 31, 2012 to obtain, review, and reconcile six years of CALSTARS microfiche data.¹³

Reference Number: 2010-12-11

Federal Program: 14.239

State Administering Department: Department of Housing and Community Development

(Housing)

Fiscal Year Initially Reported: 2007-08

Audit Finding: Reporting. Housing lacks adequate internal controls over

the accuracy and completeness of the data it includes in

its Section 3 Summary Report.

Status of Corrective Action: Fully corrected. Housing has developed a report of all

subrecipients that received funding for activities subject to Section 3 requirements, and ensured that Section 3 reports were received for all such subrecipients. Housing also contacted a 10 percent sample of those reporting zero Section 3 activity to ensure that their report is

accurate.

Reference Number: 2010-13-17

Federal Program: 14.228

State Administering Department: Department of Housing and Community Development

(Housing)

Fiscal Year Initially Reported: 2007-08

Audit Finding: <u>Subrecipient Monitoring</u>. Housing did not comply with the

requirement to issue management decisions on audit findings within six months after the State's receipt of a local agency's audit report. Housing was late in issuing management decisions for four of the seven subrecipients reviewed, ranging between 16 days and six months late.

Status of Corrective Action:

Fully corrected. Housing has implemented a revised process to ensure management decision letters are issued within the six-month timeframe required by the U.S. Office of Management and Budget A-133. The sixmonth timeframe begins when the State Controller's Office (SCO) receives the audit reports from the jurisdiction for review and distribution to the various departments. Housing's Audit Division receives the audit report from SCO and distributes the audit information to the program staff for action. Using a Findings Tracking Excel spreadsheet, the Audits Division tracks the date the A-133 audits are sent to program staff, the dates the findings are sent to recipients, and the date the findings are resolved and plan of correction approved. On December 22, 2010, program management began providing the Audit Division with the name of the program staff assigned to issue each management decision letter and the date each management decision letter is expected to be issued. The Audit Division closely monitors the due dates for the management decision letters so these letters will be issued in a timely manner. The Audits Division has established a tracking time period of three months to issue management decision letters from the date received by the SCO. As a result, management decision letters are being issued on a timely basis.

Reference Number: 2010-13-18

14.228 Federal Program:

State Administering Department: Department of Housing and Community Development

(Housing)

2007-08 Fiscal Year Initially Reported:

Audit Finding:

Subrecipient Monitoring. Housing has taken partial corrective action to address the prior year's finding and did not complete an adequate number of monitoring site visits. Housing indicated that it would complete 16 site visits for Economic Development projects and another 24 site visits for general projects during 2010. We reviewed Housing's site-visit tracking log, we noted that it had completed three site visits of general projects and 13 site visits of Economic Development projects. We also noted that these site visits were not always focused on projects identified by Housing as having the highest risk. For example, of the four general Community Development Block Grant (CDBG) projects with the highest risk score,

Housing did not complete any site visits.

Status of Corrective Action:

Partially corrected. The CDBG Section has created a Monitoring Unit, which has begun the process of creating a risk assessment tool, a monitoring procedure, and a monitoring plan. The Monitoring Unit has begun addressing the backlog of reports that have either not gone out or are not cleared.

However, the Monitoring Unit has been unable to hire any staff to complete CDBG required monitoring visits due to State's hiring freeze. Even so, it is still impossible to complete his correction action on schedule.

Staff in the Monitoring Unit have been trained to enter data into Consolidated Automated Program Enterprise System (CAPES) correctly and have addressed all past entry problems.¹⁴

Reference Number: 2010-13-19

Federal Program: 14.239

State Administering Department: Department of Housing and Community Development

(Housing)

Fiscal Year Initially Reported: 2007-08

Audit Finding: <u>Subrecipient Monitoring</u>. Housing did not issue

management decisions on audit findings within six months after the State's receipt of local agency's audit report. We reviewed one audit finding the State Controller's Office (SCO) provided Housing. Housing did not issue its management decision nearly nine months after it was

received.

Status of Corrective Action: Fully corrected. Housing has implemented a revised

process to ensure management decision letters are issued within the six-month timeframe required by the U.S. Office of Management and Budget (OMB) A-133. The six-month timeframe begins when the SCO receives the audit reports from the jurisdiction for review and distribution to the various departments. Housing's Audit Division receives the audit report from SCO and distributes the audit information to the program staff for action. Using a Single Audit Information System Data Base and a Findings Tracking Excel spreadsheet, the Audits Division tracks the date the OMB A-133 audits are sent to program staff, the date the findings are sent to recipients, and the date the findings are resolved and plan of correction approved. On December 22, 2010, program

management began providing the Audit Division with the name of the program staff assigned to issue each management decision letter and the date each management decision letter is expected to be issued. The Audit Division closely monitors the due dates for the management decision letters so these letters will be issued in a timely manner. The Audits Division has established a tracking time period of three months to issue management decision letters from the date received by SCO. As a result, management decision letters are being issued timely.

Reference Number: 2010-1-7

Federal Program: 16.606

State Administering Department: Department of Corrections and Rehabilitation

(Corrections)

Fiscal Year Initially Reported: 2007-08

Audit Finding: <u>Activities Allowed/Allowable Costs.</u> Corrections submitted

ineligible inmate data in its federal fiscal year 2009 application for the State Criminal Alien Assistance Program funding. Specifically, Corrections' application included nearly 2,000 additional records in instances where an inmate had more than one Alien Registration Number for the same incarceration period. In addition, we reviewed a sample of 29 records to determine the

inmates' citizenship status. For 10 inmates, Corrections had information in its files that these inmates were either

U.S. citizens or permanent residents.

Status of Corrective Action: Partially corrected. In an ongoing effort to comply with the

Bureau State Audits' (BSA) recommendation to seek the guidance from the federal government, staff of

guidance from the federal government, staff of Correction's Office of Legislation (OOL) and Offender

Information Services Branch has attended training provided by the Department of Homeland Security (DHS). The training familiarized staff with the DHS Secured Communities Program- a program created by DHS to assist law enforcement agencies in obtaining immediate

citizenship status of offenders.

Corrections is also working with the DHS/Immigration and Customs Enforcement (ICE) to develop an electronic process for obtaining information pertaining to the findings of ICE investigations. These findings would be provided to Corrections on a routine basis and would assist Corrections in validating alien numbers and citizenship

status.

The BSA findings that characterized Corrections of falsely submitting the 2,000 additional records are misleading. After several discussions with DHS/ICE, it has been confirmed that the 2,000 additional records are a valid representation of the California alien population. The DHS/ICE has informed Corrections that there are individuals with multiple alien numbers. For those individuals whose alien numbers can be consolidated, the DHS/ICE is in the process of consolidating these multiple alien registration numbers into one master alien number.

The DHS has not yet completed this process. 15

2010-1-1 Reference Number:

Federal Program: 17.245

State Administering Department: Employment Development Department (EDD)

Fiscal Year Initially Reported: 2006-07

Audit Finding: Activities Allowed/ Allowable Costs; Eligibility. EDD lacks

> adequate controls to ensure its field offices made appropriate eligibility determinations for the Trade Adjustment Assistance (TAA) program. Although EDD had policies and procedures in place for the entire 2009-

10 fiscal year, it only recently implemented them.

Because EDD had not completed full implementation of its policies and procedures until after our period of review, the finding remains uncorrected for fiscal year 2009-10.

Status of Corrective Action: Fully corrected. EDD revised its TAA Training Plan in

September 2008. The TAA Training Plan serves as a control document and is published on EDD's Intranet, which allows specialist day-to-day access to current program policies and procedures. In addition, EDD developed new TAA monitoring guidelines in July 2009. EDD has proper monitoring procedures in place for TAA

and is continuing this practice.

2010-9-2 Reference Number:

17.207 Federal Program:

> 17.801 17.804

State Administering Department: Employment Development Department (EDD) Fiscal Year Initially Reported: 2007-08

Audit Finding: <u>Procurement, Suspension and Debarment</u>. EDD's

procedures related to suspension and debarment were in place for the entirety of fiscal year 2009-10; however,

EDD did not fully implement those procedures.

Specifically, EDD's updated desk procedures require that every contract over \$25,000 have either a suspension and debarment certificate included in the file or an Excluded Parties List System (EPLS) printout verifying that the proposed vendor is not excluded or disqualified. For one of the 12 contracts reviewed, EDD checked the vendor against the EPLS nearly five months after the contract

was awarded.

Status of Corrective Action: Fully corrected. In January 2011, EDD implemented a

revised Procurement Checklist along with a review and approval process that resolved this finding. The checklist provides detailed information on what documents shall be included in the procurement file, including the Excluded Parties List System (EPLS) printout. The revised process includes multiple levels of management reviews and

approvals.

Reference Number: 2010-13-7

Federal Program: 17.258

17.259 17.260

State Administering Department: Employment Development Department (EDD)

Fiscal Year Initially Reported: 2007-08

Audit Finding: Subrecipient Monitoring. EDD does not monitor all of its

non-Local Workforce Investment Areas (LWIA) to ensure

that non-LWIAs are complying with federal laws, regulations, and provisions of contracts or grant

agreements and that performance goals are achieved. Specifically, EDD's Compliance Monitoring Section only monitored 13 of the 48 non-LWIAs that received funding

in fiscal year 2009-10.

Status of Corrective Action: Fully corrected. EDD has hired additional staff to conduct

monitoring of the non-LWIAs and completed monitoring of

all non-LWIAs in January 2011.

Reference Number: 2010-14-2

Federal Program: 17.225

State Administering Department: Employment Development Department (EDD)

Fiscal Year Initially Reported: 2008-09

Audit Finding: Special Tests and Provisions. EDD's financial

management systems did not allow it to separately identify and report on American Recovery and Reinvestment Act of 2009 (Recovery Act) funds.

Specifically, the Unemployment Insurance (UI) program expended \$24.8 billion, which included both Recovery Act and non-Recovery Act funds. However, EDD was not able to identify what portion of the total expenditures was

paid with Recovery Act funds.

Status of Corrective Action: Partially corrected. EDD has partially completed

programming changes to revise the 58 different financial reports needed to correct this finding. EDD can and has been reporting all the benefits paid by each federal extension. This finding only pertains to the current inability to identify which federal extension payments should be charged to the different federal accounts.

Because of the complexity of the reports and the other extension-related work, the programming is not yet complete. In addition, the federal Department of Labor's clarification of the reporting requirements for Federal Additional Compensation (FAC) funds required additional programming to separate Recovery Act funds and "post-Recovery Act" funds. The FAC funds were initially identified as 100 percent Recovery Act funds.

Half of the reports went into production in December 2010 with plans to complete the remainder by mid-2012. The completion date for all programming was changed due to the additional programming required to accurately report on FAC funds/expenditures, the need to share Information Technology Branch resources with other priority UI automation projects, and project schedules that require a "code freeze" to ensure the proper deployment of EDD's new systems.

After release, the remaining financial reports will be rerun beginning with State fiscal year 2008-09 and reviewed to identify proper adjusting entries to the accounting records. EDD expects this effort will take an additional few months to complete.¹⁶

Reference Number: 2010-2-1

Federal Program: 96.001

State Administering Department: Department of Social Services (Social Services)

Fiscal Year Initially Reported: 2008-09

Audit Finding: Allowable Costs/Cost Principles. Social Services could

not substantiate some of the payroll expenditures it charged to the Disability Insurance program. Specifically, Social Services did not distribute the payroll expenditures using the actual time spent working on activities related to the program. Instead, Social Services used percentages to distribute the payroll expenditures that were based on a time study occurring before January 2009, which Social

Services was unable to provide.

Status of Corrective Action: Fully corrected. As of October 25, 2010, staff in the

Financial Services Bureau began completing monthly employee time study reports which reflect the actual activities being performed and for which the employees are being compensated. Current staff have been trained on the correct procedures for completing time study

reports.

Reference Number: 2010-3-4

Federal Program: 20.205

State Administering Department: California Department of Transportation (Caltrans)

Fiscal Year Initially Reported: 2009-10

Audit Finding: <u>Cash Management</u>. Caltrans lacks adequate internal

controls to ensure that it consistently adhered to the funding techniques specified in the Treasury-State Agreement (TSA) for the Highway Planning and Construction program. Specifically Caltrans did not comply with the "pre-issuance" funding technique. Also, for fiscal year 2009-10 TSA was not amended to reflect any changes in the funding techniques or how Caltrans was actually drawing down federal funds for the program. Furthermore, we noted an inconsistency regarding how Caltrans calculates how long it holds onto federal funds

when preparing its interest calculation.

Status of Corrective Action: Partially corrected. Caltrans has policies and controls in

place to ensure compliance with the current TSA. However, the TSA could be more explicit in terms of methodology. On January 31, 2011, Caltrans requested

the Department of Finance to process an amendment to the TSA to be more explicit about (1) the calculation of the clearance patterns, and (2) the funding techniques used for federal reimbursement under the Federal Highway Administration's Advance Construction Program.¹⁷

Reference Number: 2010-7-10

Federal Program: 20.205

State Administering Department: California Department of Transportation (Caltrans)

Fiscal Year Initially Reported: 2009-10

Audit Finding: Matching. Caltrans lacks adequate internal controls to

ensure noncompliance with the matching requirement would be prevented or detected in a timely manner. Specifically, Caltrans lacks procedures to ensure its staff enters the correct federal reimbursement rates into the

Current Billing and Reporting System.

Status of Corrective Action: Fully corrected. Caltrans has policies and procedures in

place that result in accurate reporting of data, but those procedures did not require verification by a supervisor. It is important to note the Single Audit Report did not identify any instances where the federal reimbursement rate was

entered incorrectly. Caltrans has implemented

procedures to address this issue. Currently, Caltrans is performing periodic random sampling of projects to ensure that the federal reimbursement rate is accurate.

Documentation of these reviews is maintained.

Reference Number: 2010-13-6

Federal Program: 20.205

State Administering Department: California Department of Transportation (Caltrans)

Fiscal Year Initially Reported: 2009-10

Audit Finding: <u>Subrecipient Monitoring</u>. Caltrans lacks internal controls

to ensure subrecipients who spent more than \$500,000 during fiscal year 2008-09 submitted audit reports to the federal government as required under the U.S. Office of Management and Budget (OMB) Circular A-133. We identified 24 subrecipients that had no record of an audit submission on the federal audit clearinghouse's website for fiscal year 2008-09. Caltrans also lacks internal controls to impose sanctions on subrecipients that failed

to meet OMB Circular A-133 audit requirements. The lack of audit reports by the subrecipients previously described also limits Caltrans' ability to review and issue management decisions on potential findings and exercise effective oversight of the Highway Planning and

Construction program.

Status of Corrective Action: Fully corrected. Caltrans has implemented procedures to

address this issue. Caltrans monitors the State

Controller's Office website for subrecipients that have not vet submitted Single Audit Reports. Lists of noncompliant

subrecipients are compiled and forwarded to the appropriate Caltrans Divisions for follow-up and

resolution. Noncompliant subrecipients are required to submit their audits. The respective Caltrans divisions will sanction noncompliant subrecipients, if necessary.¹⁸

Reference Number: 2010-1-4

Federal Program: 64.005

State Administering Department: California Department of Veterans Affairs (Veterans

Affairs)

Fiscal Year Initially Reported: 2008-09

Audit Finding: Activities Allowed/ Allowable Costs, Matching, Suspension

<u>and Debarment</u>. Veterans Affairs continued to lack written policies and procedures throughout fiscal year 2009-10 regarding the Department of General Services'

(General Services) payments to contractors and verification that contractors are not suspended or

debarred.

Status of Corrective Action: Fully corrected. Veterans Affairs Capital Assets Policies

and Procedures were placed into effect in October of 2010. Procedures for suspension and debarment verification are currently being followed by General

Services.

Reference Number: 2010-4-1

Federal Program: 64.005

State Administering Department: California Department of Veterans Affairs (Veterans

Affairs)

Fiscal Year Initially Reported: 2008-09

Audit Finding: Davis-Bacon Act. The Department of General Services

(General Services), under the supervision of Veterans Affairs, did not always obtain an appropriate payroll certification, known as a statement of compliance, from the all of its contractors. We reviewed three of the 26 weekly payrolls that were submitted from January 2010 through June 2010 and found that at least one contractor submitted a certification with its payrolls that did not meet the federal requirement. Further, Veterans Affairs continued to lack written policies and procedures to communicate formally to General Services all applicable Davis-Bacon requirements throughout fiscal year 2009-

Status of Corrective Action: Fully corrected. Veterans Affairs Capital Assets Policies

and Procedures were placed into effect in October 2010. Procedures for obtaining all applicable Davis-Bacon requirements are currently being met by General

Services.

10.

Reference Number: 2010-12-3

Federal Program: 64.005

State Administering Department: California Department of Veterans Affairs (Veterans

Affairs)

Fiscal Year Initially Reported: 2008-09

Audit Finding: Reporting. The Department of General Services (General

Services), under the supervision of Veterans Affairs, does not have a sufficient process for reporting the amounts spent by category on the request for reimbursement. Also, Veterans Affairs lacked policies and procedures to improve General Services' reporting of expenditures and Veterans Affairs oversight of the reporting process

throughout fiscal year 2009-10.

Status of Corrective Action: Fully corrected. Veterans Affairs Capital Assets Policies

and Procedures were placed into effect in October of 2010. Procedures for improvement of expenditures are

currently be followed by General Services.

Reference Number: 2010-12-4

Federal Program: 64.114

State Administering Department: California Department of Veterans Affairs (Veterans

Affairs)

Fiscal Year Initially Reported: 2008-09

Audit Finding: Reporting. Veterans Affairs did not always report the

required events to the U.S. Department of Veterans Affairs within the applicable reporting deadlines. Further, Veterans Affairs lacks a process to use the information in its systems to determine which borrowers no longer have delinquent payments. Finally, for the first eight months of fiscal year 2009-10, delinquent loans reported to the credit bureau were not always reported to the U.S. Department

of Veterans Affairs.

Status of Corrective Action: Fully corrected. Automated reporting has been created

and is being tested in the live environment. This will resolve the reporting deadline issue as stated in the "findings". Included in the automated process is the capturing and reporting of accounts that are no longer delinquent. None of these previous findings have or will have any negative impact on the department's ability to

file claims. 19

Reference Number: 2010-3-2

Federal Program: 10.557

State Administering Department: Department of Public Health (Public Health)

Fiscal Year Initially Reported: 2007-08

Audit Finding: Cash Management. Public Health did not comply with the

three-day requirement in the Cash Management Improvement Act. In our sample of 65 drawdowns, we noted 2 drawdowns were issued five and nine days after

the drawdown request.

Status of Corrective Action: Fully corrected. On September 7, 2010, Public Health's

Accounting Payables Management team met with State Controller's Office (SCO) Claims Audit Unit. The SCO agreed in this meeting to notify Public Health of the expected claim cut of an invoice payment schedule involving federal funds. Public Health's Accounting Federal Reporting Unit will then adjust the federal draw as

needed to account for this cut in expenditures.

In addition, on October 18, 2010, the Public Health's Accounting Payables and Federal Unit met to verify timing of federal draws with claim schedule payments. The Federal Reporting Unit will be notified when a claim schedule is going to be held for corrections or additional

processing before going to SCO.

As of October 19, 2010, Public Health's Accounting has updated written procedures to document the enhanced procedures with SCO and between the Public Health's Accounting Units to ensure payments to subrecipients are issued as close as is administratively feasible to the State's actual cash outlay.

Reference Number: 2010-1-5

Federal Program: 93.778

State Administering Department: Department of Health Care Services (Health Care

Services)

Fiscal Year Initially Reported: 2005-06

Audit Finding: <u>Activities Allowed/ Allowable Costs</u>. Findings cited in the

annual Medi-Cal Payment Error Study (2007) revealed that 6.56 percent of the total dollars paid for claims had some indication that they contained a provider payment error, 2.53 percent of paid claims were submitted by providers that disclose characteristics of potential fraud, and 46 percent of the payments for claims with errors did not have sufficient documentation to support the services claimed. Based on the error percentage related to Medi-Cal payments, the risk of noncompliance with allowable

costs and activities is considered material.

Status of Corrective Action: Partially corrected. Health Care Services will continue to implement the corrective action steps outlined in the 2007

Medi-Cal Payment Error Study (MPES).

Health Care Services has made a commitment to routine systematic measurement as part of a comprehensive antifraud strategy through the MPES process. The bi-annual MPES provides opportunities for identifying new patterns of payment errors and areas of potential fraud, waste, and

abuse in the Medi-Cal program.

Health Care Services has initiated corrective actions for all providers identified in the 2007 MPES against which actions were warranted. In addition, Health Care Services took additional actions to focus anti-fraud efforts on those areas identified by the study as most vulnerable to fraud and abuse. These additional actions included: additional on site reviews of pharmacies, Adult Day Health Centers (ADHC) and Non-Emergency Medical Transportation (NEMT); expanded use of new technology to better

identify potential fraud schemes; reform of the ADHC program; an increase in the number of investigational and routine field compliance audits; and development of a joint action plan with provider regulatory boards and provider associations to address provider claiming errors identified as potential fraud and abuse.

MPES 2007 also identified the need to increased outreach and education to improve provider documentation of medical necessity. Health Care Services has subsequently worked with the California Association for Adult Day Services, American Russian Medical Association, California Medical Association, Medical Board of Pharmacy, and the Centers for Medicare and Medicaid Services to develop outreach, education, and training for improved compliance with documentation requirements.

The 2009 MPES is complete and under review by management.²⁰

Reference Number: 2010-1-6

Federal Program: 93.778

State Administering Department: Department of Health Care Services (Health Care

Services)

Fiscal Year Initially Reported: 2006-07

Audit Finding: Activities Allowed/ Allowable Costs. Health Care Services

lacks sufficient internal controls to ensure only medically necessary claims and eligible providers are paid and the providers are observing record retention rules. Of the 50 fee-for-service claims reviewed, ten included exceptions: claims were not deemed medically necessary and the

services were not properly documented.

Status of Corrective Action: Partially corrected. Health Care Services continues to

perform pre and post-payment reviews including Random Claims Review, Self-Audits, Desk Audits, Field Audit Reviews, and Audits for Recovery. Health Care Services conducts focused reviews on provider types identified as high risk. Health Care Services also provides provider education to prevent common problems and potential

issues.

Health Care Services continues to conduct a biannual Medi-Cal Payment Error Rate Study (MPES) to identify

potential problem trends. MPES has identified

documentation and medical necessity issues with pharmacies, adult day health centers (ADHC), local educational agencies (LEA) and non-emergency medical transportation (NEMT) providers. As a result, projects such as the Pharmacy Outreach Project which reviewed over 2,000 pharmacies and the NEMT Project which reviewed approximately 200 NEMT providers were developed. Health Care Services has completed several ADHC projects, reviewing over 100 ADHCs. Also, an independent extended review of LEAs was conducted by the State Controller's Office and was part of the MPES 2007 report. The measured error rate has steadily declined since the inception of MPES.²¹

Reference Number: 2010-2-2

Federal Program: 93.778

State Administering Department: Department of Health Care Services (Health Care

Services)

Fiscal Year Initially Reported: 2006-07

Audit Finding: <u>Allowable Costs</u>. Health Care Services does not ensure

that drug utilization data are provided to drug manufacturers/labelers on a timely basis.

Status of Corrective Action: Fully corrected. Health Care Services has modified the

Rebate Accounting Information System (RAIS) on October 30, 2009, to allow the invoicing process to be more efficient and require less manual reviewing, thus allowing for timely mailing of the invoices. Health Care Services is now meeting the deadlines for submitting the Utilization reports to the drug manufacturers. However, though the Centers for Medicare and Medicaid Services (CMS) Guidelines use a sixty-day window after the quarter for submission of the utilization reports to drug manufacturers, the States continue to be penalized when CMS is late in submitting or making available the quarterly drug rebate files to the States. These factors should be considered when an audit is performed to ensure that CMS is submitting the quarterly drug rebate files within 45 days of the end of the quarter which then gives the States

15 days after receipt of the file as stated in the

guidelines.²²

Reference Number: 2010-2-3

Federal Program: 93.778

State Administering Department: Department of Health Care Services (Health Care

Services)

Fiscal Year Initially Reported: 2008-09

Audit Finding: <u>Allowable Costs</u>. Health Care Services has contracted

with California's Department of Social Services (Social Services) to implement the Personal Care Services Program (PCSP) of the Medicaid grant. Health Care Services and Social Services lack controls to ensure PCSP claim forms are properly obtained and stored. Of the 25 claim forms selected for review, one provider claim

totaling \$180 could not be located.

Status of Corrective Action: Partially corrected. Social Services has moved forward

with a new Case Management Information and Payroll System (CMIPS) to enhance controls related to the PCSP in order to ensure claim forms are properly obtained and

stored.

CMIPS II was created to award and administer a contract to design, develop, maintain, and operate a replacement for legacy CMIPS. CMIPS II will be the only State system that processes Medi-Cal claims for In-Home Supportive Services programs and provides paid claims information to Health Care Services for analysis and reporting. CMIPS II will provide enhanced automation and improve the integrity and quality of program support for the all program initiatives.

CMIPS II is in its fourth year of Design, Development, and Implementation. It is currently in the User Acceptance Testing phase, which is the last test phase to be completed before pilot activities can begin.

The first pilot counties, Merced and Yolo, are scheduled to "go live" in the fall of 2011 and San Diego, as the final pilot county, is scheduled to "go live" one month later. The implementation of the remaining counties is expected to last an additional 15 months.²³

Reference Number: 2010-2-4

Federal Program: 93.778

State Administering Department: Department of Health Care Services (Health Care

Services)

Fiscal Year Initially Reported: 2009-10

Audit Finding: <u>Allowable Costs/ Cost Principles (ADP and Risk Analysis)</u>.

The State's fiscal intermediary, Electronic Data Systems (EDS), manages Medi-Cal network systems in

accordance with EDS policies and are protected against unauthorized access, intrusion, and virus attack. The SAS 70 Audit report for EDS noted that EDS did not

consistently perform monitoring over their network security related to their firewall configuration and their

antivirus software updates.

Status of Corrective Action: Fully corrected. Health Care Services, in conjunction with

Hewlett-Packard (HP), made the following changes to improve the monitoring of network security related to firewall configuration and anti-virus updates: (1) HP updated the Medi-Cal Network Security Standards and Guidelines on July 1, 2009 to include semi-annual firewall configuration reviews (2) HP updated the Medi-Cal Network Security Standards and Guidelines manual on February 15, 2010 to state that Security Architects would

perform the reviews.

Firewall configuration reviews were performed in March and September 2010. The firewall configuration logs were reviewed by HP and Health Care Services staff. The logs were clean for March 2010. There was a finding that old user IDs were present on the September 2010 logs, but they were still within the allowable timeframe.

HP will modify the Medi-Cal Network Security Standards and Guidelines manual to include semi-annual anti-virus update reviews that will be performed every March and September by the Security Architects. The September 2010 review will be performed, this year only, in October 2010. All reviews will be stored in the Security folder in LiveLink.

Reference Number: 2010-3-1

Federal Program: 93.917

State Administering Department: Department of Public Health (Public Health)

Fiscal Year Initially Reported: 2009-10

Audit Finding: <u>Cash Management</u>. Public Health did not comply with the

three-day requirement in the Cash Management Improvement Act. In our sample of 65 drawdowns, we noted four drawdowns were issued between 16 and 55

days after the drawdown request.

Status of Corrective Action:

Fully corrected. On September 7, 2010, Public Health's Accounting Payables Management team met with State Controller's Office (SCO) Claims Audit Unit. The SCO agreed in this meeting to notify Public Health's of the expected claim cut of an invoice payment schedule involving federal funds. Public Health's Accounting Federal Reporting Unit will then adjust the federal draw as needed to account for this cut in expenditures.

In addition, on October 18, 2010, the Public Health's Accounting Payables and Federal Unit met to verify timing of federal draws with claim schedule payments. The Federal Reporting Unit will be notified when a claim schedule is going to be held for corrections or additional processing before going to SCO.

As of October 19, 2010, Public Health's Accounting has updated written procedures to document the enhanced procedures with SCO and between the Public Health's Accounting Units to ensure payments to subrecipients are issued as close as is administratively feasible to the State's actual cash outlay.

Reference Number: 2010-5-3

Federal Program: 93.917

State Administering Department: Department of Public Health (Public Health)

Fiscal Year Initially Reported: 2006-07

Audit Finding: <u>Eliqibility</u>. Public Health continues to lack sufficient

internal controls over the eligibility process to ensure payments are only made to eligible recipients and all required documentation to verify eligibility is maintained in the recipient's file. Public Health lacks controls for

following up on findings related to site visits.

Status of Corrective Action: Fully corrected. Public Health agrees with the finding that

Public Health lacked sufficient internal controls over the eligibility process to ensure payments are only made to eligible recipients and all required documentation to verify eligibility is maintained in the recipient's file. The AIDS Drug Assistance Program (ADAP) has fully implemented corrective action regarding eligibility documentation and site visits in fiscal year 2010-11. The changes included an acceleration of the ADAP enrollment site visit cycle from every five years to every three years as well as an updated site visit tool. In fiscal year 2010-11, ADAP

coordinators conducted 72 site visits and plan to conduct 60-70 in fiscal year 2011-12. Based on the current site visit plan, ADAP will meet its three year audit cycle at the end of fiscal year 2012-13. Programmatic procedural changes include tracking client files that have documentation deficiencies. These clients are placed on a 60 day eligibility grace period to receive the missing documentation or the client's eligibility is terminated at the end of the 60 days. Any site that is found deficient is required to submit a Corrective Action Plan (CAP), and a follow up site visit is conducted to ensure the CAP was implemented. Finally, ADAP is continuing to work with Medi-Cal and the Pharmacy Benefits Manager to enhance the systems for identifying clients' Medi-Cal eligibility. Corrective action was completed in August 2010 when the site visit tool was finalized and site visits began.²⁴

Reference Number: 2010-5-4

Federal Program: 93.917

State Administering Department: Department of Public Health (Public Health)

Fiscal Year Initially Reported: 2009-10

Audit Finding: Eligibility. Public Health utilizes site visits to monitor

enrollment sites to ensure payments are made to eligible recipients. In the current year, no site visits were conducted by the HIV Care Program and no other processes for monitoring eligibility were identified.

Status of Corrective Action: Remains uncorrected/disagree with finding. Public Health

disagrees with the finding that no site visits were conducted by the HIV Care Program and no other processes for monitoring eligibility were identified. The finding for fiscal year 2009-10 monitoring visits was inaccurate. At that time, Health Resources and Services Administration monitoring standards required site visits once in a three year contract period in which we were in compliance because all sites had been visited within a

three year cycle.²⁵

Reference Number: 2010-5-5

Federal Program: 93.778

State Administering Department: Department of Health Care Services (Health Care

Services)

Fiscal Year Initially Reported: 2005-06

Audit Finding: <u>Eligibility</u>. Health Care Services lacks adequate internal

controls to obtain and track the enrollment presumptive eligibility identification numbers issued to prevent unauthorized use of identification numbers. Health Care Services does not perform procedures to authenticate the existence of the recipient, prevent duplicate issuances, and reconcile the presumptive eligibility numbers with the recipient enrollment listing filed during the claims

adjudication process.

Status of Corrective Action: Remains uncorrected. Health Care Services lacks the necessary resources to develop and implement automated systems to address this finding at this time.

The Patient Protection and Affordable Care Act (PPACA) of 2010 provides an opportunity to implement a solution to this problem. As required by the PPACA and with the passage of SB 900 (Chapter 659, Statutes of 2010) and AB 1602 (Chapter 655, Statutes of 2010), California will establish the California Health Benefits Exchange (Exchange). A component the Exchange has is the ability to screen for and enroll eligible individuals into the Medi-Cal program, utilizing a web-based enrollment portal and streamlined eligibility processes. The Exchange provides an opportunity to allow Presumptive Eligibility (PE) Qualified Providers to complete the PE enrollment for eligible pregnant women using an internet-based application that will provide real-time validation with the Statewide Medi-Cal Eligibility Data System. This will result in the assignment of a Client Index Number for tracking and billing purposes; thereby eliminating the possibility of duplicate issuances of identification numbers and will provide a means of authentication of enrolled individuals.

Currently, Health Care Services is analyzing the Medicaid provisions of PPACA and is awaiting guidance from the federal Centers for Medicare and Medicaid Services and implications for modernizing current PE processes for pregnant women. Health Care Services is in the process of revising the current enrollment form to include instructions for providers to inform pregnant women of additional options available to apply for Medi-Cal by telephone or use a web-based application to remove the requirement for this population to submit the application in-person or the mail. The additional options could reduce the length of time this population is served under PE.²⁶

Reference Number: 2010-5-6

Federal Program: 93.778

State Administering Department: Department of Health Care Services (Health Care

Services)

Fiscal Year Initially Reported: 2008-09

Audit Finding: <u>Eligibility</u>. Health Care Services lacks adequate internal

controls over its redetermination requirements for Medi-Cal beneficiaries to ensure benefits are discontinued when redeterminations are not received within 12 months of the most recent redetermination date and when proper

citizenship is not obtained.

Status of Corrective Action: Partially corrected.

Redeterminations: Pursuant to State statute and federal requirements, counties must complete redeterminations within specified timeframes. Health Care Services reinforces this policy through written guidance in the form of All County Welfare Directors Letters. Additionally, Health Care Services conducts semi-annual Medi-Cal Eligibility Quality Control (MEQC) reviews and operates a County Performance Standards (CPS) program. Under CPS, counties self certify performance standards relative to the timeliness of county processing of applications and redeterminations. Counties that do not demonstrate adequate performance through either self-certifications or independent State reviews are required to document written corrective action plans (CAP) to demonstrate remedial efforts with required quarterly reports to demonstrate progress on remedial actions. Health Care Services will continue in its efforts to reinforce the expectations that counties complete redeterminations on a timely basis and assure that documentation is available for review in county case files consistent with State policies. This reinforcement will be in the form of both verbal and written communication to the counties when findings present that are not consistent with State policy.

Citizenship Documentation: Effective July 1, 2006, State Medicaid programs have been required to have citizenship and identity documentation on individuals seeking program services. Since January 2010, Health Care Services had relied on an automated system match of social security numbers (SSNs) with the federal Social Security Administration as its primary means to verify citizenship and identity. This verification matching

process has increased accuracy and improved the documentation of citizenship and identity for individuals seeking or enrolled in Medi-Cal. To date, California has experienced an approximate success rate of 94 percent of SSNs being validated by this means. To the extent the electronic SSN match process does not yield a successful result and the beneficiary or the county is unable to correct issues relative to achieving a successful SSN match, the State requires counties to rely on existing procedures whereby appropriate paper documents such as passports, drivers licenses and birth records can be used to validate citizenship and identity status.

Health Care Services has reinforced this requirement through the release of All County Welfare Director's Letters and evaluates such documentation when conducting MEQC reviews. As deficiencies are noted with citizenship documentation, this information is communicated both verbally and in writing to the counties. Health Care Services will continue to reinforce to the counties the requirements to have citizenship documentation in case records.

Health Care Services will discuss the audit findings and corrective action with the affected counties. On April 22, 2011, Health Care Services issued All County Welfare Directors Letter 11-19 which informs counties that if the county MEQC case error rate is 10 percent or higher, Health Care Services may impose a CAP requirement. If Health Care Services finds that a county is having significant problems with either redeterminations or citizenship documentation, it can require that county to develop and implement a CAP on one or both of these program areas. Health Care Services will monitor the county's progress on each CAP and will also conduct a follow-up review to evaluate the efficacy of the county's corrective action measures.²⁷

Reference Number: 2010-7-5

Federal Program: 93.917

State Administering Department: Department of Public Health (Public Health)

Fiscal Year Initially Reported: 2009-10

Audit Finding: <u>Earmarking</u>. Public Health lacks adequate record-keeping

process and policies and procedures to determine that the

use of grant funds properly reflects earmarking

requirements.

Status of Corrective Action:

Fully corrected. Public Health agrees with the finding that we lacked a sufficient record-keeping process and policies and procedures to determine that the use of grant funds properly reflected earmarking requirements. Office of AIDS (OA) has implemented procedures to more thoroughly document and support any information that is reported for this grant to ensure that the use of grant funds properly reflects earmarking requirements. Information (such as Public Health's Accounting CALSTARS Online Reporting Environment Reports) are saved electronically, in a central network file that is accessible by program staff, administrative staff, and the OA. In addition to supporting materials, the documentation process will include a summary narrative of steps taken to prepare and submit grant reports. Staff and management from OA's Age Drugs Assistance Program Branch, HIV Care Branch, Administration Section and Division Office are now included in the process of preparing and submitting reports to fulfill mandatory grant earmarking reporting requirements. OA has implemented procedures to more thoroughly document and support any information that is reported for this grant and all other grants. Corrective action was completed in August 2010. Written procedures for the OA Fiscal Management Section were updated in August 2010. Additionally, trainings were implemented for Fiscal Management Section staff on a bi-weekly basis and continue to occur as new staff are hired and/or procedures are updated.

Reference Number: 2010-12-5

Federal Program: 93.917

State Administering Department: Department of Public Health (Public Health)

Fiscal Year Initially Reported: 2008-09

Audit Finding: Reporting. Public Health lacks sufficient policies to

ensure proper completion and review of its annual financial status report. Specifically, Public Health was not able to provide adequate supporting documentation to support the amount reported in its 2010 annual financial

status report.

Status of Corrective Action: Fully corrected. Public Health agrees that it needs to

enhance current policies and procedures to ensure that supporting documents and calculations are retained to ensure compliance with specified reporting and document retention requirements. Public Health completed written desk procedures on how to calculate indirect costs when the grant budget period crosses State fiscal years and the approved Indirect Cost Rate Proposal is different for the two fiscal years on February 9, 2011. The Federal Reporting Unit desk procedures were also enhanced on February 9, 2011, to reiterate that supporting CALSTARS reports and indirect cost calculations be retained to support the Federal Financial Report. Staff were trained on February 9, 2011 on these desk procedure updates.

Reference Number: 2010-12-6

Federal Program: 93.268

State Administering Department: Department of Public Health (Public Health)

Fiscal Year Initially Reported: 2009-10

Audit Finding: Reporting. Public Health did not maintain supporting

documentation for the cumulative expenditures reported in its Federal Financial Report SF 425 (A) for June 2010.

Status of Corrective Action: Fully corrected. Public Health agrees with the

recommendation to enhance current policies and procedures to ensure that supporting documents and calculations are retained, to ensure compliance with specified reporting and document retention requirements. Immunization Branch (IZB) has implemented a more thorough procedure to document and track expenditures report monthly. Expenditure reports and copies of CALSTARS are saved electronically in a central file for easy access by admin staff and management. Program continues to reconcile expenditure report monthly and identify any discrepancies between Program records and CALSTARS. Public Health's Accounting continues to review and reconcile supporting documents monthly and collaboratively work together with Public Health's IZB to ensure that any necessary corrections are successfully completed. This includes comparing source documents held within IZB against CALSTARS expenditure reports created and updated by Accounting.

Reference Number: 2010-13-9

Federal Program: 93.069

State Administering Department: Department of Public Health (Public Health)

Fiscal Year Initially Reported: 2009-10

Audit Finding: <u>Subrecipient Monitoring</u>. Public Health lacks policies and

procedures to ensure that the identifying number of the federal program is included in each of its subgrant

agreements.

Status of Corrective Action: Partially corrected. Public Health agrees with the

recommendation to implement policies and procedures to ensure that the identifying number of federal program is included in each of its subgrant agreements. Public Health is incorporating the identifying Catalog of Federal Domestic Assistance (CFDA) number into the 2011-12 Local Guidance and Agreements. Local guidance and local agreements are in rough draft with the federal CDFA numbers. Public Health will issue the guidance at a training session on August 10, 2011. Local health departments and local hospital preparedness program entities will have 60 days to submit the application including the signed agreement with the CDFA numbers.²⁸

Reference Number: 2010-13-10

Federal Program: 93.778

State Administering Department: Department of Health Care Services (Health Care

Services)

Fiscal Year Initially Reported: 2009-10

Audit Finding: <u>Subrecipient Monitoring</u>. Health Care Services did not

conduct site visits of local government agencies (LGAs) as required. Only one LGA site visit was conducted during the current fiscal year when 22 site visits should have been performed as the previous visits were more

than four years ago.

Status of Corrective Action: Partially corrected. It was the intent of the County Based

Medi-Cal Administrative Activities (CMAA) Unit to conduct 16 LGA site visits during fiscal year 2010-11 to comply with Medicaid funding requirements which indicate LGA site visits must be conducted at least once every four years. However, due to the delayed passage of the State Budget in November 2010 and a Governor's order

restricting non-essential travel in May 2011, the CMAA Unit only had five months to work towards compliance. The CMAA Unit was able to conduct and complete 11 of the planned 16 LGA site visits in fiscal year 2010-11; however, due to the aforementioned issues, five of the LGA site visits were not conducted. Currently the CMAA

Unit staff is developing a desk review process that will meet the Medicaid funding requirements and not require travel. It is the intent of the CMAA Unit to complete the outstanding site visits in fiscal year 2011-12 through the desk review process and still achieve compliance with the LGA monitoring policy by June 30, 2012.²⁹

Reference Number: 2010-14-3

Federal Program: 93.778

Department of Health Care Services (Health Care State Administering Department:

Services)

2009-10 Fiscal Year Initially Reported:

Special Tests and Provisions – Managed Care. Health Audit Finding:

> Care Services did not ensure grievance hearings are scheduled on a timely basis. Specifically, Health Care Services should schedule a hearing 90 days from the date of request by the enrollee. We reviewed 25 State hearing

cases, and five did not appear to be scheduled or

resolved within 90 days of the initial enrollee request date.

Status of Corrective Action: Fully corrected. Through a Delegation Order, Health Care

> Services has delegated the scheduling of State Hearings to the Department of Social Services (Social Services). Health Care Services' Managed Care Ombudsman coordinates State Hearings between Social Services and the Medi-Cal Managed Care Organizations, ensuring timely communication of new State Hearings, or other

status updates.

On November 9, 2010, Health Care Services received the first Uncalendared Case Listing Report from Social Services. Social Services submits this report weekly for review by the Medi-Cal Managed Care Division (MMCD) Ombudsman. For hearings not scheduled within 60 days, Ombudsman staff checks to see if the hearings have been postponed or re-opened; they also verify that Social Services has provided an explanation for the delay. If the unscheduled hearings have not been postponed or reopened, Health Care Services staff contact Social Services for an explanation for the delay and remind Social Services to make sure the hearings are scheduled prior to the 90 day requirement. So far, for those hearings not scheduled within 60 days and for which Health Care Services have contacted Social Services, all hearings were scheduled the following week and prior to the 90 day

requirement.

Reference Number: 2010-14-4

Federal Program: 93.778

State Administering Department: Department of Health Care Services (Health Care

Services)

Fiscal Year Initially Reported: 2006-07

Audit Finding: Special Tests and Provisions – Provider Eligibility. Health

Care Services and Public Health did not retain the

federally required provider agreements for four of the 50

providers sampled.

Status of Corrective Action: Partially corrected. Provider Enrollment Division (PED)

> updated its provider enrollment process to require provider agreements and continues its plan to re-enroll all Medi-Cal providers as a continuous process as resources are available. In addition, PED continues to work in conjunction with Audits and Investigations to re-enroll providers identified as high risk, including the reenrollment of identified pre-1999 providers. Re-enrolled

providers are required to submit a re-enrollment

application package updated to current federal standards to retain Medi-Cal eligibility. PED has also updated its requirements so that all providers must submit a new application package to report a new, additional, or change of service location. In addition, State law requires that a new application be submitted when there is a change in business entity. Health Care Services continually verifies

provider information to ensure compliance with State and federal requirements in its ongoing re-enrollment efforts.

Public Health's Licensing and Certification Division is responsible for determining the eligibility of facility providers. Per Interagency Agreement 07-65492 executed in fiscal year 2007-08, Public Health collects. maintains, and stores enrolled facility provider records. including provider agreements. In 2008, a new provider agreement was jointly developed for facility providers by Health Care Services and Public Health. Public Health continues to collect new provider agreements from facility providers and forwards copies of the provider agreements to PED for Health Care Services records. Since June 2010, provider agreements have been obtained from the three facility providers noted in bullet two of the audit finding; an agreement was requested from the fourth facility but they have not responded.³⁰

Reference Number: 2010-14-5

Federal Program: 93.069

93.268 93.712

State Administering Department: Department of Public Health (Public Health)

Fiscal Year Initially Reported: 2009-10

Audit Finding: <u>Special Tests and Provisions – Control, Accountability.</u>

and Safeguarding of Vaccine. A sample of Quality Assurance Reviews (QAR) were selected to determine whether Public Health provides oversight of vaccinating providers. Based on a review of QAR samples, it was noted that Public Health's QAR procedures did not include a review of inventory records to ensure vaccines are

properly accounted for.

Status of Corrective Action: Partially corrected. Public Health's Immunization Branch

has revised the internal QAR document to include a check of inventory records and to ensure that private vaccine is differentiated from public vaccine. The Centers for Disease Control and Prevention only accepts potential revisions to the Vaccines For Children provider agreement in September so Public Health was unable to submit revisions by December 2010. We will be submitting revisions outlined in our original corrective action plan by

September 1, 2011.31

Reference Number: 2010-13-11

Federal Program: 10.553

10.555

State Administering Department: Department of Education (Education)

Fiscal Year Initially Reported: 2009-10

Audit Finding: <u>Subrecipient Monitoring</u>. Nine out of 12 subrecipient

contracts with food services management companies lacked documentation within Education's Child Nutrition Information and Payment System (CNIPS) that such contracts had been approved. In addition, Education did not implement appropriate internal controls to ensure the approval of a contract is documented within CNIPS. Furthermore, adequate monitoring procedures were not performed to ensure the documentation existed prior to

reimbursements to subrecipients.

Status of Corrective Action: Partially corrected. The Nutrition Services Division (NSD)

is developing a Food Service Management Company (FSMC) registry with prototype contracts and bid

documents. Once the FSMC registry is fully developed and implemented, school nutrition program sponsors will only be allowed to contract with the registered and approved FSMCs. In addition, Education is exploring the feasibility of creating a new unit devoted solely to FSMC

bid/contract administration, technical assistance, and

training.32

Reference Number: 2010-2-5

Federal Program: 84.365

State Administering Department: Department of Education (Education)

Fiscal Year Initially Reported: 2009-10

Audit Finding: Allowable Costs/Cost Principles. Education lacks internal

controls to ensure only allowable payroll costs are charged to the program. Fiscal analyst's review and approval of payroll charges is not documented.

Status of Corrective Action: Fully corrected. To document the review and approval of

monthly payroll charges, in February 2011, Education instituted the new "ELCSD Monthly Monitor Report for Labor Distribution" form. This form is completed each month and is: (1) utilized to identify payroll discrepancies, (2) indicate the actions taken to resolve the discrepancies, and (3) document the unit analyst's and administrator's

reviews and approvals.

Reference Number: 2010-3-3

Federal Program: 84.010 84.365

State Administering Department: Department of Education (Education)

Fiscal Year Initially Reported: 2001-02

Audit Finding: <u>Cash Management</u>. Education does not have an

adequate process in place for assessing the cash needs

of its recipients.

Status of Corrective Action: Fully corrected. To effectively improve cash management

over the Title I and English Language Acquisition Grants,

Education expanded its Federal Cash Management Data Collection (CMDC) system to include Title I, Part A and Part D, Subpart 2; Title III, Part A LEP; and Title III Immigrant programs. The CMDC was established by Education to minimize the time elapsing between subrecipients' receipt and disbursement of federal program funds.

Reference Number: 2010-5-7

Federal Program: 84.048

State Administering Department: Department of Education (Education)

Fiscal Year Initially Reported: 2008-09

Audit Finding: <u>Eligibility</u>. Education does not have policies and

procedures in place that narrate the procedures performed and the source of data used to complete the calculation of grant awards. We noted an error in the poverty count totaling 2,000 that resulted in Education allocating \$57,145 less to one local educational agency

than it was entitled.

Status of Corrective Action: Fully corrected. Education strengthened existing policies

and procedures by instituting a formula driven spreadsheet that automatically calculates each local educational agencies' (LEA) Perkins Section 131 grant funding amounts; the spreadsheet will include the appropriate reviewing manager's approval. In addition.

Education developed a procedures manual which delineates the steps needed for staff to: (1) find the appropriate source data, (2) populate the spreadsheet with the appropriate data, and (3) calculate the subgrant amounts. To correct the calculation error noted by the auditors, Perkins carryover funds were used to increase the available fiscal year 2010-11 Perkins Section 131 funds, and LEAs' allocations were appropriately

recalculated.

Reference Number: 2010-7-6

Federal Program: 84.010

84.287 84.365 84.367

State Administering Department: Department of Education (Education)

Fiscal Year Initially Reported: 2005-06

Audit Finding: <u>Level of Effort – Maintenance of Effort</u>. Education's

current maintenance of effort (MOE) policies and procedures are insufficient to ensure that they are compliant with required federal guidelines. Specifically, Education was using unaudited local educational agency expenditure figures to calculate compliance with the MOE

requirements instead of using the final audited

expenditures.

Status of Corrective Action: Partially corrected. Education is working with the U.S.

Department of Education's Risk Management Service and Office of Inspector General in exploring feasible and acceptable options for enhancing Education's existing MOE calculation process, including the use of unaudited versus audited data; as part of this cooperative effort,

other States' processes will be considered.33

Reference Number: 2010-7-7

Federal Program: 84.048

State Administering Department: Department of Education (Education)

Fiscal Year Initially Reported: 2007-08

Audit Finding: Level of Effort – Maintenance of Effort. Education did not

review or approve the maintenance of effort (MOE)

calculation.

Status of Corrective Action: Fully corrected. Education has implemented a process

that includes a review of the MOE calculations and a signoff sheet by a manager to indicate his/her review and

approval.

Reference Number: 2010-7-8

Federal Program: 84.048

State Administering Department: Department of Education (Education)

Fiscal Year Initially Reported: 2007-08

Audit Finding: Level of Effort – Supplement not Supplant. Although

Education has policies and procedures for monitoring its compliance with the requirement to use program funds to supplement rather than supplant existing funds for its State activities and operations expenditures, there is no

documentation that such policies and procedures have been performed.

Status of Corrective Action:

Remains uncorrected/Disagree with finding. Education does not concur with this finding. Education's budgetary processes include built-in controls that are effective in preventing supplanting as documented and evidenced in Education's accounting and budgetary records. Furthermore, in a program determination letter dated September 30, 2010, the U.S. Department of Education's Assistant Secretary for Elementary and Secondary Education did not sustain the auditor's finding (Finding 2006-7-2) stating that, "Because Education has a process to ensure that program grant funds supplement and do not supplant other funding, we consider this finding resolved and required no further action."

Reference Number: 2010-7-9

Federal Program: 84.048

State Administering Department: Department of Education (Education)

Fiscal Year Initially Reported: 2009-10

Audit Finding: Matching. Education lacks adequate internal control

policies and procedures to ensure reported match amounts are supported by accounting records.

Status of Corrective Action: Fully corrected. To strengthen existing controls over

match, Education created a spreadsheet to serve as a template that will ensure consistency and accuracy in reporting match; documentation to support the match amounts will be maintained with the spreadsheet.

Reference Number: 2010-12-7

Federal Program: 84.391

84.392

State Administering Department: Department of Education (Education)

Fiscal Year Initially Reported: 2009-10

Audit Finding: Reporting. Education requires subrecipients of Recovery

Act funding to submit Section 1512 report data using the Education developed web-based Recovery Act Reporting and Data Collection System and to maintain the records supporting the submitted data. We noted that Education

did not monitor subrecipients' Section 1512 data for

accuracy.

Status of Corrective Action: Fully corrected. To ensure ongoing compliance with both

Individual with Disabilities Education Act (IDEA) and Recovery Act requirements, Education implemented a new application process to ensure that Recovery Act IDEA funds for construction, infrastructure projects, and

equipment purchases greater than \$5,000 are

appropriate. In addition, Education's "Special Education Self-Review" software includes a fiscal component that

includes a review of personnel time sheets.

Reference Number: 2010-12-12

Federal Program: 84.048

State Administering Department: Department of Education (Education)

Fiscal Year Initially Reported: 2008-09

Audit Finding: Reporting. Education lacks internal controls over the

Perkins data collection system used to prepare the Consolidated Annual Performance, Accountability, and Financial Status Report (CAR) submitted by local educational agencies (LEAs). Data reported by LEAs

may not be complete, accurate, and reliable.

Status of Corrective Action: Fully corrected. The controls Education has implemented

to enhance the quality of data submitted for the annual CAR are complete and operating as designed. This includes the availability of an electronic upload for data submitted by the LEAs. Once the submission period ends, the data is reviewed and verified by Education for correctness and completeness. If discrepancies are found, the LEA is contacted and required to make the necessary corrections prior to the approval of the current application. LEAs failing to submit data from the prior year and no longer participating in the grant will be contacted to either submit the required data or revert back

the granted funds. In addition, the Perkins Program Monitoring system has been implemented. LEAs failing to meet required performance targets are required to

complete a self-review, including the review of data submitted for E-1 and E-2 reporting. Education conducts on-site monitoring visits based on suspected inaccuracies in data reporting and provides technical assistance as

necessary.

Reference Number: 2010-13-12

Federal Program: 84.010

84.011 84.048 84.287 84.365 84.367

State Administering Department: Department of Education (Education)

Fiscal Year Initially Reported: 2005-06

Audit Finding: <u>Subrecipient Monitoring</u>. Education requires local

educational agencies (LEAs) to resolve all deficiencies noted during Categorical Program Monitoring site visits within 225 days. For 28 of 41 site visits tested, the LEAs were significantly late with their resolutions. In addition, Education was not prompt for an additional eight of 16 site visits tested in resolving the corrective actions once it

received the resolutions from LEAs.

Status of Corrective Action: Partially corrected. Education continuously works with

LEAs to resolve all deficiencies noted during monitoring visits with the understanding that, in some instances, complete corrective action may require time beyond the standard timeframes. However, to emphasize the importance of timely corrective action, staff are provided resolution training, and LEAs are informed and reminded

of the timeframes for resolving items following a

monitoring review.35

Reference Number: 2010-13-14

Federal Program: 84.048

State Administering Department: Department of Education (Education)

Fiscal Year Initially Reported: 2009-10

Audit Finding: <u>Subrecipient Monitoring</u>. Education does not monitor the

Board of Governors of the California Community Colleges (CCC) use of pass-through federal awards. Education considers CCC a vendor, but the interagency defines a subrecipient relationship, thus requiring Education to

monitor the federal awards.

Status of Corrective Action: Partially corrected. For the fiscal year 2011-12, Education

has added a monitoring clause to interagency contracts with the CCC. Education is currently exploring the

development of formal procedures for monitoring the

CCC.36

Reference Number: 2010-13-15

Federal Program: 84.394

State Administering Department: Department of Education (Education)

Fiscal Year Initially Reported: 2009-10

Audit Finding: <u>Subrecipient Monitoring</u>. Education needs to enhance the

timeliness and scope of its subrecipient monitoring

activities to ensure subrecipients are administering federal awards in compliance with applicable federal compliance

requirements.

Status of Corrective Action: Fully corrected. To ensure subrecipient compliance with

federal requirements, Education conducts on-site and online State Fiscal Stabilizing Fund (SFSF) monitoring reviews. To maximize SFSF fiscal monitoring coverage with limited resources, Education utilizes a risk-based methodology in consideration of local educational agencies' unresolved prior year Single Audit findings and

to capture the largest federal funding allocations.

Reference Number: 2010-13-16

Federal Program: 84.357

State Administering Department: Department of Education (Education)

Fiscal Year Initially Reported: 2007-08

Audit Finding: Subrecipient Monitoring. Education outsources its

monitoring to a contractor, California Technical Assistance Centers (C-TAC). C-TAC's monitoring procedures focus

on assisting local educational agencies (LEA) with

program implementation and do not contain procedures to ensure LEAs' compliance with federal requirements. In addition, Education has no formal process in place to follow up and resolve issues promptly and to review expenditures reports to ensure program funds are used in

accordance with authorized purposes.

Status of Corrective Action: Fully corrected. The Reading First program ended in

fiscal year 2009-10. However, Education will continue to

work with the C-TAC and with regional technical

assistance centers to effectively oversee and improve the

outstanding issues.

Reference Number: 2010-14-6

Federal Program: 84.391

84.392

State Administering Department: Department of Education (Education)

Fiscal Year Initially Reported: 2009-10

Audit Finding: Special Tests and Provisions. Education is not identifying

and documenting the federal award number to each of its subrecipients at the time of subaward. In addition, at the time of disbursement of Recovery Act funds, Education is not informing subrecipients of the federal award number, Catalog of Federal Domestic Assistance (CFDA) number.

monitoring of LEA's and to timely follow up on known

and amount of Recovery Act funds.

Status of Corrective Action: Fully corrected. Education will identify the appropriate

CFDA numbers on all future grant awards. Education identifies and treats Recovery Act funds uniquely from non-Recovery Act funds. As required under the Recovery

Act, the Recovery Act grant awards include grant

conditions informing grantees that the Recovery Act funds must be tracked separately from non-Recovery Act funds. In order for local educational agencies to track the funds separately, each Recovery Act grant award has a unique: (1) grant award name, (2) Program Cost Account (PCA), and (3) Standardized Account Code Structure (SACS) resource code. Furthermore, LEAs are required to report Recovery Act 1512 data using the unique Recovery Act

PCA and SACS resource codes.³⁷

Reference Number: 2010-3-5

Federal Program: 93.575 93.596

State Administering Department: Department of Education (Education)

Fiscal Year Initially Reported: 2006-07

Audit Finding: <u>Cash Management</u>. Education is not using the funding

technique set forth in the Cash Management Improvement Act (CMIA) Agreement as it relates to payments made to

child care providers.

Status of Corrective Action:

Fully corrected. Education's clearing account payment process involves a "Monthly Estimate/Monthly Draw" concept. In this regard, State funding is initially utilized to make child care payments based on estimated or known monthly expenditures posted to the clearing account. If payments are based on estimates, funds drawn are reconciled to actual expenditures. However, actual monthly child care expenditures, not estimates, typically are posted and timely paid through the clearing account with State funds. Consequently, plans of financial adjustments in the following months are, in essence, reimbursements to Education, not child care vendor payments; payments for State funds and reimbursement from federal funds have recently been simultaneous.

Reference Number: 2010-13-13

Federal Program: 93.575

93.596

State Administering Department: Department of Education (Education)

Fiscal Year Initially Reported: 2008-09

Audit Finding: <u>Subrecipient Monitoring</u>. Education requires local

educational agencies (LEAs) to resolve all deficiencies noted during Categorical Program Monitoring site visits within 225 days of the exit date. For 28 of the 41 site visits tested, Education received the resolutions after 225 days. In addition, Education was not prompt for an additional eight of 16 site visits tested in resolving the corrective actions once it received the resolutions from

LEAs.

Status of Corrective Action: Partially corrected. Education continuously works with

LEAs to resolve all deficiencies noted during monitoring visits with the understanding that, in some instances, complete corrective action may require time beyond the standard timeframes. However, to emphasize the importance of timely corrective action, staff are provided resolution training, and LEAs are informed and reminded

of the timeframes for resolving items following a

monitoring review.38

Reference Number: 2010-14-7

Federal Program: 93.713

State Administering Department: Department of Education (Education)

Fiscal Year Initially Reported: 2009-10

Audit Finding: Special Tests and Provisions. Education is not identifying

to each of its subrecipients the federal award number at

the time of subaward. In addition, at the time of

disbursement, Education is not informing subrecipients of the federal award number, Catalog of Federal Domestic Assistance (CFDA) number, and amount of Recovery Act

funds.

Status of Corrective Action: Remains Uncorrected. Education will identify the

appropriate CFDA numbers on all future grant awards. Education identifies and treats Recovery Act funds

uniquely from non-Recovery Act funds. As required under Recovery Act, the Recovery Act grant awards include grant conditions informing grantees that the Recovery Act funds must be tracked separately from non-Recovery Act funds. In order for local educational agencies (LEAs) to track the funds separately, each Recovery Act grant award has a unique: (1) grant award name, (2) Program Cost Account (PCA), and (3) Standardized Account Code Structure (SACS) resource code. Furthermore, LEAs are required to report Recovery Act 1512 data using the unique Recovery Act PCA and SACS resource codes. ³⁹

Endnotes – Auditor's Comments

- 1. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-7-6 for additional information.
- 2. This finding is fully corrected. Although the Department of Military plans to take additional actions to strengthen its processes, the actions it has taken sufficiently addressed our prior-year finding.
- 3. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-5-5 for additional information.
- 4. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-1-3 for additional information.
- 5. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-7-3 for additional information.
- 6. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-7-4 for additional information.
- 7. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-7-7 for additional information.
- 8. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-12-7 for additional information.
- 9. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-13-13 for additional information.
- 10. This finding is fully corrected. Our audit this year did not identify a similar finding.
- 11. This finding is fully corrected. Our audit this year did not identify a similar finding.
- 12. Our review found that the department has substantially corrected this finding.
- 13. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-12-4 for additional information.
- 14. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-13-15 for additional information
- 15. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-1-4 for additional information.
- 16. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-14-6 for additional information.
- 17. We elected not to report this as a finding because the state and federal government updated the Treasury State Agreement (TSA) for fiscal year 2011–12 to ensure that Caltrans' process complies with the TSA. Although Caltrans did not use the funding technique identified in the TSA applicable for the current fiscal year, it did use the interest neutral technique that is now approved in the TSA for use in fiscal year 2011–12. Additionally, our testing found that Caltrans' use of the incorrect funding technique during fiscal year 2010–12 had no effect on the amount of interest Caltrans calculated as owed to the federal government.
- 18. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-13-14 for additional information.
- 19. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-12-6 for additional information.
- 20. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-1-1 for additional information.
- 21. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-1-2 for additional information.

- 22. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-2-1 for additional information.
- 23. This finding is fully corrected. Our audit this year did not identify a similar finding.
- 24. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-5-1 for additional information.
- 25. This finding is fully corrected. Our audit this year did not identify a similar finding.
- 26. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-5-4 for additional information.
- 27. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-5-2 for additional information
- 28. This finding is fully corrected. Our audit this year did not identify a similar finding.
- 29. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-13-2 for additional information.
- 30. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-14-3 for additional information.
- 31. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-14-2 for additional information.
- We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-13-4 for additional information.
- 33. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-7-1 for additional information.
- 34. This finding is fully corrected. Our audit this year did not identify a similar finding.
- 35. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-13-7 for additional information. During our testing, we did not identify this same monitoring exception for the Career & Technical Education (84.048), 21st Century Community Learning Centers (84.287), Migrant Education Grants (84.011), and Improving Teacher Quality (84.367) programs. Therefore, we did not include these programs in the current year finding.
- 36. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-13-9 for additional information.
- 37. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-14-7 for additional information
- 38. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-13-5 for additional information.
- 39. We reported a similar finding in our audit of fiscal year 2010–11. Please refer to reference number 2011-14-4 for additional information.

We conducted this audit to comply with Section 8543 et seq. of the California Government Code. The Independent Auditor's Reports provide the opinions we expressed on the State of California's internal control and on compliance and other matters.

Respectfully submitted,

ELAINE M. HOWLE, CPA

State Auditor

Date: March 30, 2012

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(Agency response provided as text only.)

Department of Finance State Capitol Room 1145 Sacramento, CA 95814-4998

March 16, 2012

Ms. Elaine M. Howle, State Auditor Bureau of State Audits 555 Capitol Mall, Suite 300 Sacramento, CA 95814

Dear Ms. Howle:

Thank you for the opportunity to respond to the internal control and state and federal compliance audit report for the fiscal year ended June 30, 2011. This report was the result of your examination of the state's general purpose financial statements and administration of federal programs for the fiscal year ended June 30, 2011, and will be part of the Single Audit Report covering this period. We accept the reported findings and recommendations and recognize that the compliance findings resulted in 31 unqualified and 4 qualified opinions for the 35 major programs audited. We also recognize that there are areas where internal controls and administration of federal awards needs to be improved.

California provides its citizens with numerous state and federal programs and activities and is much more complex and vast than most economic entities in the world. Moreover, such operations must exist within a system of internal and administrative control that safeguards assets and resources and produces reliable financial information. Attaining these objectives and overseeing the financial and business practices of the state continues to be an important part of the Department of Finance's (Finance) leadership.

In meeting our responsibility for financial leadership and oversight, Finance provides internal audit related education and training to departments as well as oversight of departmental internal audit units by issuing audit guidelines and conducting quality assurance reviews. Further, we have an ongoing process of issuing audit memos to departments that establish statewide policy and provide technical advice on various audit related issues. An audit memo concerning the results of the fiscal year 2010-11 Single Audit will be issued to remind all departments of their responsibility for implementing corrective action plans for their single audit findings.

The head of each state department is responsible for establishing and maintaining a system of internal accounting and administrative control within their department. This responsibility includes documenting the system, communicating system requirements to employees, and assuring that the system is functioning as prescribed and is modified for changing conditions.

Moreover, all levels of state management must be involved in assessing and strengthening their systems of internal accounting and administrative controls to minimize fraud, errors, abuse, and waste of government funds. The Financial Integrity and State Manager's Accountability Act (FISMA) requires each agency to conduct an internal review of its controls and report on their results. Finance will continue to provide education and guidance to assist agencies in meeting the FISMA requirements. The state is committed to sound and

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effective fiscal oversight. Individual departments have separately responded to the report's findings and recommendations. Accordingly, their viewpoints and corrective action plans are included in the report. We will monitor the findings and reported corrective actions to identify potential changes in statewide fiscal procedures.

Finance is committed to ensuring the proper financial operations and business practices of the state, as well as ensuring that internal controls exist for the safeguarding and effective use of assets and resources. We will take the single audit findings into consideration during the performance of audit work in those departments that received a qualified opinion on a major program.

If you have any questions concerning this letter, please contact David Botelho, Chief, Office of State Audits and Evaluations, at (916) 322-2985.

Sincerely,

(Signed by: Ana J. Matosantos)

ANA J. MATOSANTOS Director cc: Members of the Legislature

Office of the Lieutenant Governor

Little Hoover Commission

Department of Finance

Attorney General

State Controller

State Treasurer

Legislative Analyst

Senate Office of Research

California Research Bureau

Capitol Press