

**STATE OF CALIFORNIA  
CALIFORNIA STATE AUDITOR'S OFFICE  
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**TITLE 2, DIVISION 10, CALIFORNIA CODE OF REGULATIONS**

**ADOPT SECTIONS 61000 TO 61024, INCLUSIVE, REGARDING STATE HIGH-RISK  
GOVERNMENT AGENCY AUDIT PROGRAM**

**INITIAL STATEMENT OF REASONS**

**INTRODUCTION**

The California State Auditor (State Auditor) proposes to amend the California Code of Regulations at title 2, division 10 to add regulations relating to the State Auditor's authority to implement Government Code section 8546.5, authorizing the establishment of a State High-Risk Government Agency Audit Program. Prior to the enactment of Government Code section 8546.5, the State Auditor had broad authority to conduct financial and performance audits of state government agencies as prescribed by statute and as directed by the Legislature's Joint Legislative Audit Committee, but lacked express authority to perform self-initiated audits. Government Code section 8546.5 therefore was enacted by the Legislature in 2004 (Stats. 2004, ch. 251) and subsequently amended in 2011 (Stats. 2011, ch. 328) to authorize the State Auditor to establish a State High-Risk Government Agency Audit Program for the purpose of identifying, auditing, and issuing reports on any state agency or statewide issue that the State Auditor identifies as being at high risk for waste, fraud, abuse, or mismanagement, or for having major challenges associated with its economy, efficiency, or effectiveness. By authorizing the establishment of this program, the Legislature gave the State Auditor the ability to use the expertise and experience of the California State Auditor's Office (State Auditor's Office) to identify state agencies and statewide issues that are at high risk and to conduct audits regarding those agencies and issues aimed at making recommendations for their improvement.

Unfortunately, in authorizing the State Auditor to implement a State High-Risk Government Agency Audit Program, Government Code section 8546.5 provides little guidance regarding the parameters of the program, the process that should be employed to identify high-risk state agencies and statewide issues, the standards that should be used to identify high risk, and the procedures that should be followed when auditing and issuing recommendations regarding high-risk state agencies and statewide issues. To address the lack of guidance provided by the statute, the State Auditor has initiated this proposed regulatory action to provide greater structure to the program and to provide the Legislature, state agency officials, and the public with a clearer understanding of how the program will operate.

**Proposed Regulations**

To provide the greater structure and clarity needed for the State High-Risk Government Agency Audit Program, the State Auditor is proposing a set of regulations to guide the operation of the program. This Initial Statement of Reasons provides specific information regarding each

proposed regulation below. As an overview, however, the proposed regulations will implement the provisions of Government Code section 8546.5 related to the following subject areas:

- The State Auditor’s authority to declare an agency to be a high-risk state agency or a responsible state agency for a high-risk statewide issue.
- The manner in which the two-year period referenced in subdivision (d) of Government Code section 8546.5 is incorporated into the State High-Risk Government Agency Audit Program.
- The process for identifying the agencies and statewide issues that are high risk and therefore subject to the State Auditor’s audit authority.
- The process for a state agency to respond to a potential determination that the agency is high risk or is a responsible state agency for a high-risk statewide issue.
- The standards for determining which state agencies and statewide issues are high risk.
- The standards for determining which state agencies and statewide issues no longer are high risk. The process for revising or amending the list of state agencies and statewide issues identified as high risk.
- The means by which the State Auditor will notify the Joint Legislative Audit Committee that a state agency has been identified as high risk
- The powers and responsibilities of the California State Auditor’s Office when performing audit work for the State High-Risk Government Agency Audit Program.
- The manner in which audit work will be performed for the State High-Risk Government Agency Audit Program.
- The manner in which audit reports and recommendations will be issued for the State High-Risk Government Agency Audit Program.
- The process for state agencies to “periodically report” to the State Auditor regarding the status of recommendations made under the State High-Risk Government Agency Audit Program.

**SPECIFIC PURPOSE OF EACH SECTION<sup>1</sup> -- GOVERNMENT CODE SECTION 11346.2, SUBDIVISION (b)(1)**

This proposed regulatory action would adopt the following sections in California Code of Regulations, title 2, division 10.

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<sup>1</sup> Unless otherwise indicated, (such as by an express reference to the California Government Code) any use of the term “section” in this statement is a reference to a section or proposed section of the California Code of Regulations.

The specific purpose of each adoption, and the rationale for the determination that each adoption is reasonably necessary to carry out the purpose for which it is proposed, together with a description of the public problem, administrative requirement, or other condition or circumstance that each adoption or amendment is intended to address, is as follows:

**Proposed section 61000** sets forth a general statement of the purpose of Government Code section 8546.5 and declares the intention of the proposed regulations in California Code of Regulations, title 2, division 10, chapter 2 as being to interpret the provisions of Government Code section 8546.5 consistent with that purpose.

**Proposed section 61001** defines the term “agency of the state” as used in Government Code section 8546.5. Government Code section 8546.5 authorizes the State Auditor’s Office to audit any “agency of the state, whether created by the California Constitution or otherwise” that the State Auditor identifies as being high risk. However, this Government Code section does not define that phrase and leaves unanswered whether the term “agency of the state” includes any state agency outside the executive branch of state government. This proposed regulation interprets the term consistent with Government Code section 8547.2, subdivision (f), which includes within the State Auditor’s authority to investigate state agencies the authority to investigate any state agency in the executive or judicial branch of state government, including, the University of California, the California State University, the Supreme Court, the courts of appeal, the superior courts, and the Administrative Office of the Courts. This proposed regulation also clarifies that the State Auditor has discretion to identify only a particular program or mission area within a state agency as high risk rather than declaring an entire agency to be high risk when only a specific part or function of the agency is high risk.

**Proposed section 61002** defines the term “audited state agency,” as used in the proposed regulations. By establishing this term and giving it a particular meaning, the proposed regulation allows easy reference to a state agency that has been the subject of an audit under the State High-Risk Government Agency Audit Program and helps to avoid ambiguity in the proposed regulations.

**Proposed section 61003** defines the term “responsible state agency” as used in the proposed regulations. By establishing this term and giving it a particular meaning, the proposed regulation allows easy reference to a state agency “responsible for all or a portion of a statewide issue identified as high risk” as described in Government Code section 8546.5, subdivision (e) and helps to avoid ambiguity in the proposed regulations. In the way the term is defined by the proposed regulation, the proposed regulation also makes clear that a state agency may be considered a responsible state agency if it either is responsible for a statewide issue or could be given responsibility for resolving a portion of a statewide issue.

**Proposed section 61004** defines the term “state agency” as used in Government Code section 8546.5 and the proposed regulations. By establishing this term and giving it the same meaning as the term “agency of the state,” the proposed regulation allows easy reference to “agency of the state” as defined in proposed section 61001. It also avoids any ambiguity that may arise from the two different terms, “agency of the state” and “state agency,” both appearing in Government Code section 8546.5 while not appearing to have been intended to convey two different meanings.

**Proposed section 61005** defines the term “state high risk audit” as used in the proposed regulations. By establishing this term and giving it a particular meaning, the proposed regulation allows easy reference to a report issued regarding an audit performed under the State High-Risk Government Agency Audit Program and helps to avoid ambiguity in the proposed regulations.

**Proposed section 61006** defines the term “state high risk audit report” as used in the proposed regulations. By establishing this term and giving it a particular meaning, the proposed regulation allows easy reference to an audit report issued under the State High-Risk Government Agency Audit Program and helps to avoid ambiguity in the proposed regulations.

**Proposed section 61007** defines the term “state high risk list” as used in the proposed regulations. By establishing this term and giving it a particular meaning, the proposed regulation allows easy reference to the list of state agencies and statewide issues that the State Auditor has identified as being high risk and helps to avoid ambiguity in the proposed regulations.

**Proposed section 61008** defines the term “statewide issue” as used in Government Code section 8546.5. Government Code section 8546.5 authorizes the State Auditor to identify, audit, and issue reports on any statewide issue that the State Auditor identifies as being at high risk for waste, fraud, abuse, or mismanagement or for having major challenges associated with its economy, efficiency, or effectiveness. However, this Government Code section does not specify what constitutes a statewide issue. By defining the term in a manner that relates it to the operation of state government but also distinguishes it from the operation of a single state government agency, which the State Auditor’s Office has been given the authority to audit by other provisions of the statute, this proposed regulation gives particular meaning to the term and furthers the purpose of the statute to authorize the State Auditor to perform audit work regarding significant problems of waste, fraud, abuse and mismanagement that reach beyond a single state agency.

**Proposed section 61009** specifies the manner in which the State Auditor will identify the state agencies and statewide issues that are determined to be high risk, as authorized by Government Code section 8546.5. While subdivision (a) of Government Code section 8546.5 calls on the State Auditor to identify state agencies and statewide issues that are at high risk for waste, fraud, abuse, or mismanagement or for having major challenges associated with their economy, efficiency, or effectiveness, this Government Code section does not specify the manner in which that identification will be performed. Further, while subdivision (d) of Government Code section 8546.5 makes reference to the State Auditor issuing audit reports and recommendations regarding state agencies and statewide issues “identified as at high risk not less than once every two years,” this reference is ambiguous in its linking audit work and the identification of high-risk agencies and statewide issues to a two-year cycle. The proposed regulation resolves these issues by specifying that the State Auditor will identify high-risk state agencies and statewide issues through the establishment, at least once every two years, of a state high risk list that identifies the state agencies and statewide issues the State Auditor has determined to be at high risk for waste, fraud, abuse, or mismanagement or for having major challenges associated with their economy, efficiency, or effectiveness.

In furtherance of the purpose for which Government Code section 8546.5 was enacted, this proposed regulation also declares it to be the purpose of the State Auditor, when placing a state

agency or statewide issue on the state high risk list, to bring improvements to the agency or issue that will help ensure state government functions more economically, efficiently, and effectively. Moreover, the proposed regulation clarifies that it will be the objective of the State Auditor, when placing a state agency or statewide issue on the state high risk list, to promote sufficient improvement in the operation and functioning of the agency or the State's response to the issue that the agency or issue no longer will be considered high risk.

**Proposed section 61010** specifies the process that the State Auditor will employ to establish a state high risk list. While subdivision (a) of Government Code section 8546.5 calls on the State Auditor to identify state agencies and statewide issues that are at high risk for waste, fraud, abuse, or mismanagement or for having major challenges associated with their economy, efficiency, or effectiveness, section 8546.5 does not specify the process that the State Auditor will employ to perform this identification. Section 8546.5 also does not address the manner in which the State Auditor should modify the list of state agencies and statewide issues identified as high risk because of changes in circumstances that cause the previously identified agencies and issues no longer to be high risk while other agencies and issues become high risk.

This proposed regulation responds to that lack of specificity in the statute by outlining the process the State Auditor shall use, at least once every two years, to establish a new state high risk list. In outlining this process, the proposed regulation provides that the list will be established based on an assessment of the agencies and issues that are placed on the list. Agencies and issues previously identified as high risk will be re-assessed prior to the issuance of a new list to determine whether they remain high risk. Agencies and issues appearing on a state high risk list will carry forward to the succeeding list unless they satisfy specified criteria for finding they no longer are high risk. The description of a high-risk state agency or statewide issue may be modified when the agency or issue is carried forward to a new list to ensure that the description accurately reflects the assessment of risk. Finally, state agencies and statewide issues may be added to a new state high risk list provided they satisfy specified criteria for a determination they are high risk.

**Proposed section 61011** specifies the process that the State Auditor's Office will employ to perform an assessment to determine which state agencies and statewide issues should be placed on the state high risk list. Although subdivision (b) of Government Code section 8546.5 is very specific in declaring that the State Auditor should look at past audit and investigative reports and may consult with various state oversight agencies when identifying high-risk state agencies and statewide issues, Government Code section 8546.5 provides no other guidance regarding the information the State Auditor's Office should gather and the process it should follow in determining which state agencies and statewide issues to designate as high risk. Moreover, the statute does not mention providing the state agencies that are being considered for designation as high-risk state agencies or responsible state agencies for high-risk statewide issues with an opportunity to provide information relevant to the State Auditor's determination.

To address this lack of guidance in the statute, this proposed regulation describes a multi-step assessment process that the State Auditor's Office will execute, with the participation of the state agencies affected by the assessment, aimed at providing the State Auditor's Office with as much relevant information as possible for the purpose of determining which state agencies and statewide issues to place on the state high risk list. Specifically, the proposed regulation suggests

sources of information that the State Auditor's Office may consult in addition to those listed in the statute. It encourages communication between the State Auditor's Office and relevant state agency staff during the assessment process. It also calls for the State Auditor to provide an agency with notification, whenever the State Auditor preliminarily determines that the agency is high risk or should be designated a responsible state agency for a high-risk statewide issue, so that the agency may respond with information bearing on whether the determination should become final. In this way, the proposed regulation seeks to ensure that the State Auditor's determination of which state agencies and statewide issues to place on the state high risk list is as well-informed, transparent, and fair as possible.

**Proposed section 61012** specifies the criteria the State Auditor will use in determining when a state agency or statewide issue previously designated as high risk no longer should appear on the state high risk list when a new list is established. In authorizing the State Auditor to identify the state agencies and statewide issues that are at high risk for waste, fraud, abuse, or mismanagement or for having major challenges associated with their economy, efficiency, or effectiveness, Government Code section 8546.5 does not establish any criteria on which the State Auditor should base this determination. Similarly, it does not establish any criteria on which the State Auditor should base a determination that a state agency or statewide issue no longer is high risk. As a result, there is no rule of general application in place governing this determination without the adoption of a regulation.

This proposed regulation remedies the gap in the statute with respect to the criteria that will be used for determining a state agency or statewide issue no longer is high risk by establishing criteria for measuring when sufficient progress has been made, either through a change of circumstances or the implementation of corrective actions, toward eliminating the basis on which the state agency or statewide issue was found to be high risk.

The proposed regulation also provides for the State Auditor removing a state agency or statewide issue from the state high risk list in unusual cases, even when the agency or issue still should be considered high risk, if the State Auditor determines that performing additional audit work regarding the agency or issue is not likely to reduce the risk. In this way, the State Auditor may redirect resources to other audit activities that would be more beneficial to the state.

Finally, the proposed regulation provides that even after the State Auditor removes a state agency or statewide issue from the state high risk list, the State Auditor's Office will stay alert to the agency or issue with an eye toward returning the agency or issue to the list if the agency or issue again becomes high risk.

**Proposed section 61013** specifies the criteria the State Auditor will use in determining when a state agency or statewide issue is high risk and therefore should appear on the state high risk list. As noted in the discussion of section 61012, in authorizing the State Auditor to identify the state agencies and statewide issues that are at high risk for waste, fraud, abuse, or mismanagement or for having major challenges associated with their economy, efficiency, or effectiveness, Government Code section 8546.5 does not establish any criteria on which the State Auditor should base this determination. As a result, there is no rule of general application in place governing this determination without the adoption of a regulation. This proposed regulation remedies that gap in the statute by establishing criteria for measuring when a state agency or

statewide issue is at high risk for waste, fraud, abuse, or mismanagement or for having major challenges associated with their economy, efficiency, or effectiveness.

In establishing the criteria for determining when a state agency or statewide issue is high risk, the proposed regulation sets forth separate but conceptually consistent criteria for determining when a state agency is high risk and when a statewide issue is high risk. Both sets of criteria focus on the same three requirements: (1) serious detriment to the State or its residents may result from the waste, fraud, abuse, or mismanagement or impaired economy, efficiency, or effectiveness being risked; (2) the likelihood of serious detriment occurring is great enough, when compared with the level of serious detriment that may result, that there is substantial risk of serious detriment; and (3) there are not adequate corrective actions in place to keep the risk of serious detriment from being substantial. Both sets of criteria also provide, however, that for a state agency or statewide issue to be found to be high risk and then to be placed on the state high risk list, the State Auditor must believe that the substantial risk of serious detriment associated with the state agency or statewide issue may be reduced significantly by the State Auditor's Office performing audit work regarding the agency or issue, making recommendations aimed at reducing the risk, and the recommendations of the State Auditor's Office being implemented.

Mirroring the definition contained in section 61003, this proposed regulation also specifies that in determining which state agencies the State Auditor will identify as responsible state agencies for a statewide issue, the State Auditor will identify those agencies which, in the State Auditor's professional judgment, either are responsible for a portion of a statewide issue or could be tasked with responsibility for resolving a portion of a statewide issue. In performing audit work to address a statewide issue, the State Auditor will perform work at the agencies that already have some responsibility for the issue and may not have managed their responsibility adequately and at those agencies that have not been given any responsibility for the issue but perhaps should be given some responsibility because of their expertise or other abilities.

**Proposed section 61014** specifies the criteria the State Auditor will use when determining whether the waste, fraud, abuse, or mismanagement or impaired economy, efficiency, or effectiveness being risked by a state agency or statewide issue may result in serious detriment to the State or its residents. As stated in section 61013, the State Auditor may find that a state agency or statewide issue is high risk when, in the State Auditor's professional judgment, the agency or issue is at substantial risk of causing serious detriment to the State or its residents and adequate corrective actions are not being taken to prevent the risk of serious detriment from being substantial. However, neither section 61013 nor Government Code section 8546.5 specifies any criteria for determining what constitutes serious detriment. As a result, there is no rule of general application in place governing this determination without the adoption of an additional regulation to provide guidance.

This proposed regulation provides that guidance by listing particular circumstances which, if any of them is a potential outcome of the waste, fraud, abuse, or mismanagement or impaired economy, efficiency, or effectiveness being risked by the state agency or statewide issue, may serve as the basis for a finding by the State Auditor that serious detriment to the State or its residents is being risked.

**Proposed section 61015** specifies the criteria the State Auditor will use when determining whether there is substantial risk that the waste, fraud, abuse, or mismanagement or impaired economy, efficiency, or effectiveness being risked by a state agency or a statewide issue may result in serious detriment to the State or its residents. As stated in section 61013, the State Auditor may find that a state agency or statewide issue is high risk when, in the State Auditor's professional judgment, the agency or issue is at substantial risk of causing serious detriment to the State or its residents and adequate corrective actions are not being taken to prevent the risk of serious detriment from being substantial. However, neither section 61013 nor Government Code section 8546.5 specifies any criteria for determining what constitutes substantial risk. As a result, there is no rule of general application in place governing this determination without the adoption of an additional regulation to provide guidance.

This proposed regulation provides that guidance by listing a series of factors, any one of which may serve as the basis for a finding by the State Auditor that the waste, fraud, abuse, or mismanagement or impaired economy, efficiency, or effectiveness being risked by a state agency or a statewide issue is great enough, when compared with the level of serious detriment that may result, for there to be substantial risk of serious detriment to the State or its residents.

**Proposed section 61016** specifies the criteria the State Auditor will use when determining whether a state agency or the responsible state agencies for a statewide issue have taken adequate corrective actions to prevent the risk of waste, fraud, abuse, or mismanagement or impaired economy, efficiency, or effectiveness associated with the agency or issue from presenting a substantial risk of serious detriment to the State or its residents. As stated in section 61013, the State Auditor may find that a state agency or statewide issue is high risk when, in the State Auditor's professional judgment, the agency or issue is at substantial risk of causing serious detriment to the State or its residents and adequate corrective actions are not being taken to prevent the risk of serious detriment from being substantial. However, neither section 61013 nor Government Code section 8546.5 specifies any criteria for determining what constitutes adequate corrective actions. As a result, there is no rule of general application in place governing this determination without the adoption of an additional regulation to provide guidance.

This proposed regulation provides that guidance by listing four criteria a state agency or the responsible state agencies for a statewide issue must satisfy to be found by the State Auditor to have taken adequate corrective actions to prevent a risk of serious detriment to the State or its residents from being substantial.

**Proposed section 61017** specifies the process that the State Auditor's Office will employ to issue a new state high risk list once it is established in accordance with the provisions of section 61010. Section 61010 provides that at least once every two years the State Auditor will establish a new state high risk list consisting of the state agencies and statewide issues that the State Auditor has identified as high risk pursuant to Government Code section 8546.5. However, section 61010 does not specify the process by which the State Auditor's Office will issue the state high risk list after it is established. Specifically, section 61010 does not provide any guidance regarding the information that should be included on the list, the extent to which the content of the list should be explained or supported by any other documentation, the publication of the list, the distribution of the list within state government, or the distribution of the list to the public.

This proposed regulation addresses the lack of guidance provided by section 61010 regarding the process for issuing a new state high risk list. It does this by establishing rules for issuing the list that will bring greater clarity, predictability, and transparency to this process for the Legislature, state agency officials, and the public. In particular, the proposed regulation establishes minimum requirements for the content of the list, requires that the list be supported by an accompanying report, requires publication of both the list and the report, expressly calls for delivery of the list and report to particular state officials, and mandates making the list and report available to the public.

**Proposed section 61018** specifies a process the State Auditor's Office may employ to amend a state high risk list when the need arises. In specifying the process that the State Auditor's Office will follow to establish a new state high risk list at least once every two years, section 61010 implements the provisions of Government Code section 8546.5, subdivision (a) regarding identification by the State Auditor of high risk state agencies and statewide issues not less than once every two years. However, neither section 61010 nor Government Code section 8546.5 provide any guidance regarding what the State Auditor should do when a need arises to add a state agency or statewide issue to the state high risk list when it has been less than two years since the list was established and the list otherwise does not require any modification. Although the State Auditor could establish a new list solely for the purpose of adding the agency or issue, performing all of the steps required for issuing a new list, as provided by sections 61011 and 61017, would be very burdensome and require an unnecessary expenditure of resources when there is no indication the entire list needs to be reassessed and revised. Meanwhile, failing to act to add the agency or issue to the state high risk list until a complete reassessment of the list is called for would constitute a disservice to the State and its residents if the agency or issue currently presents a substantial risk of serious detriment and the State Auditor could reduce the risk significantly by performing audit work and making recommendations regarding the agency or issue.

This proposed regulation resolves that dilemma by establishing a process that the State Auditor's Office may follow to amend an existing state high risk list, in lieu of establishing an entirely new list, to add a high risk state agency or statewide issue. In establishing this process, the proposed regulation requires all of the same actions be undertaken as when establishing a new state high risk list, except that those actions only need to relate to the agency or issue being added to the list. So the State Auditor may add the agency or issue to the list only on the basis of an assessment that demonstrates the agency or issue is high risk and urgently in need of attention and transformation prior to the establishment of a new list, the amendment of the list must be supported by a report that explains and justifies the amendment, and the amended list with its accompanying report must be published and distributed in the same manner as a new state high risk list. However, the State Auditor's Office need not reassess or address in its report the risk associated with any of the agencies or issues already appearing on the list as it would need to do when establishing a new state high risk list.

**Proposed section 61019** specifies a planning component for the State High-Risk Government Agency Audit Program designed to keep the Legislature, government officials, and the public informed about the valuable work the State Auditor intends to perform regarding high risk state agencies and statewide issues. In authorizing the State Auditor to establish and execute the State High-Risk Government Agency Audit Program, Government Code section 8546.5 does not

mandate any particular allocation of the State Auditor’s resources for the program. Accordingly, the resources that the State Auditor may use for the program are only those resources remaining after the State Auditor has allocated resources for other auditing obligations, particularly financial and performance audits required by statute, as described in Government Code section 8546.1, subdivision (a), and audits requested by the Joint Legislative Audit Committee, as described in Government Code section 8546.1, subdivision (b). As a result, unless the State Auditor has a mechanism in place, as part of the State High-Risk Government Agency Audit Program, for describing the valuable work the State Auditor envisions performing under the program, government decision-makers and members of the public cannot keep informed about the state high risk audit work that could be affected by the assignment of additional audit projects.

To remedy that situation, this proposed regulation provides for the State High-Risk Government Agency Audit Program to include a planning component in which the State Auditor’s Office will establish a plan for the audit work it intends to perform under the program, update the plan regularly after every meeting of the Joint Legislative Audit Committee at which new audit work is assigned to the State Auditor’s Office, and maintain the updated plan on the State Auditor’s website.

**Proposed section 61020** specifies the standards that must be satisfied for the audit work performed under the State High-Risk Government Agency Audit Program. Government Code section 8546.1, subdivision (c) is very clear in stating that both the financial and performance audits required by statute and the audits requested by the Joint Legislative Audit Committee must be performed by the State Auditor’s Office “pursuant to the ‘Government Auditing Standards’ published by the Comptroller General of the United States.” However, while this subdivision may be interpreted as declaring that all other audits performed by the State Auditor’s Office also must comply with these standards, that point is less clear. Therefore, to bring greater clarity to the applicability of this subdivision to the audits performed under the State High-Risk Government Agency Audit Program, this proposed regulation expressly declares that such audits shall be performed under the “Government Auditing Standards.”

**Proposed section 61021** specifies the powers and responsibilities of the State Auditor in connection with performing audits under the State High-Risk Government Agency Audit Program. Government Code sections 8545 through 8545.4 describe various powers and responsibilities that the State Auditor has when performing an audit. While these sections may be interpreted as applying to every audit the State Auditor performs, including audits performed under the State High-Risk Government Agency Audit Program, these statutes do not make any express reference to such audits. Therefore, to eliminate any potential ambiguity regarding the powers and responsibilities of the State Auditor in connection with performing audits under the program, this proposed regulation makes it clear that those same powers and responsibilities apply when the State Auditor performs an audit under the program.

**Proposed section 61022** specifies the process that the State Auditor’s Office should follow in preparing to issue audit reports with recommendations under the State High-Risk Government Agency Audit Program. Government Code section 8546.5, subdivision (d) provides that under the State High-Risk Government Agency Audit Program, the State Auditor “may issue audit reports with recommendations for improvement in state agencies, and for statewide issues,

identified as at high risk . . .” However, the statute provides no other guidance regarding the content of such reports or the procedures that should be followed when issuing them. Government Code section 8546.1 declares that upon completing a financial or performance audit required by statute or an audit directed by the Joint Legislative Audit Committee, the State Auditor shall transmit a copy of the report to various government officials and then make it available to the public, but it provides no other guidance regarding the content of such reports or the procedure that should be followed for issuing them, and it is unclear whether the provisions of this subdivision apply to audit reports issued under the State High-Risk Government Agency Audit Program.

This proposed regulation resolves the lack of guidance provided by Government Code sections 8546.5 and 8546.1 regarding the content of audit reports issued under the State High-Risk Government Agency Audit Program and the procedures that should be followed when preparing to issue them by instituting standards for the content of the reports and setting forth a procedure that should be followed prior to their issuance that conforms with the long-standing practices of the State Auditor’s Office regarding the issuance of audit reports. Specifically, the proposed regulation requires that an audit report issued under the program contain: (1) the objectives, scope, and methodology of the audit; (2) the audit results; (3) recommendations; and (4) a copy or summary of the response of the audited state agency. It requires the State Auditor’s Office to issue a confidential draft copy of the report to the audited state agency prior to the report’s issuance for the purpose of receiving the agency’s comments on the report. It requires the audited state agency to provide a response to the draft report within five business days of receiving the draft. It also affords the State Auditor’s Office the opportunity to revise its draft report based on the agency’s comments or include a rebuttal to the agency’s comments in the final report.

**Proposed section 61023** specifies the process that the State Auditor’s Office should follow when issuing audit reports with recommendations under the State High-Risk Government Agency Audit Program. As noted in the discussion of section 61022, aside from declaring that under the State High-Risk Government Agency Audit Program the State Auditor may issue audit reports with recommendations, Government Code section 8546.5, which authorizes the establishment and execution of the program, provides no guidance regarding the procedures that should be followed when issuing the reports. Additionally, Government Code section 8546.1, which declares that upon completing a financial or performance audit required by statute or an audit directed by the Joint Legislative Audit Committee, the State Auditor shall transmit a copy of the report to various government officials and then make it available to the public, provides no other guidance regarding the procedure that should be followed for issuing those reports, and it is unclear whether the provisions of this subdivision apply to audit reports issued under the State High-Risk Government Agency Audit Program.

To resolve this lack of guidance provided by Government Code sections 8546.5 and 8546.1, this proposed regulation sets forth a procedure that should be followed by the State Auditor’s Office when issuing an audit report under the State High-Risk Government Agency Audit Program that conforms with the long-standing practices of the State Auditor’s Office regarding the issuance of audit reports. Specifically, the proposed regulation requires that the report be issued by publication in the same manner that the State Auditor publishes audit reports directed by the Joint Legislative Audit Committee. Further, at the time of issuing the report, the State Auditor’s

Office will deliver copies of the report to each audited state agency and to the government officials designated in Government Code section 8546.1 for receiving copies of audit reports. Finally, the proposed regulation requires that after the report is delivered to the designated government officials, it will be made available to the public including by posting on the State Auditor's website.

**Proposed section 61024** specifies the procedures that audited state agencies will follow when reporting to the State Auditor regarding their implementation of recommendations made to them in the audit reports issued under the State High-Risk Government Agency Audit Program. It also specifies the procedures the State Auditor's Office will follow in collecting those reports and passing along the information in the reports to state decision-makers and the public.

Government Code section 8546.5, subdivision (e) provides that the State Auditor may require state agencies and responsible state agencies for statewide issues identified as high risk to report periodically regarding the status of recommendations for improvement that were made to them. However, the statute provides no further guidance regarding the frequency of those reports, the number of reports that must be provided, or what information the State Auditor may require from the agencies to support the content of the reports. Further, the subdivision does not describe what use the State Auditor's Office should make of the information in the reports after those reports are received.

To resolve this lack of clarity in the statute, this proposed regulation specifies how frequently the audited state agencies shall report to the State Auditor, the circumstances that must be present for the State Auditor to relieve the agency of this reporting obligation, and the authority of the State Auditor to request evidence from an audited state agency to support the information and analysis provided in any such report. The proposed regulation also provides that the State Auditor's Office shall make the information in the reports available to the public through the State Auditor's website and the State Auditor's annual report regarding the implementation of State Auditor recommendations issued pursuant to Government Code section 8548.9.

#### **OTHER REQUIRED SHOWINGS – GOVERNMENT CODE SECTION 11346.2, SUBDIVISIONS (b)(2)-(5)**

**Economic Impact Assessment – Government Code section 11346.2, subdivision (b)(2):** This proposed regulatory action will not have an economic impact on California business enterprises or individuals as the regulatory action relates entirely to the auditing of state government agencies. Accordingly, the proposed regulatory action will not affect:

- The creation or elimination of jobs within the state;
- The creation of new businesses or the elimination of existing businesses within the state;  
or
- The expansion of businesses currently doing business within the state.

However, the proposed regulatory action will benefit California residents by promoting greater economy, efficiency, and effectiveness in the operation of state government by establishing rules

for identifying, auditing, and recommending improvements to state government agencies and statewide issues at high risk for waste, fraud, abuse, or mismanagement or for having major challenges associated with their economy, efficiency, or effectiveness. The specific benefits this proposed regulatory action will bring to the health and welfare of California residents, worker safety, and the state's environment will depend on the audit work the State Auditor's Office performs in accordance with the proposed regulations.

**Studies, Reports, or Documents Relied Upon - Government Code section 11346.2, subdivision (b)(3):** In proposing this regulatory action, the State Auditor was informed by past experience auditing California state government agencies and the experience of the United States Government Accountability Office (U.S. GAO) in operating a High Risk Program since 1990. Specific U.S. GAO publications considered in proposing this regulatory action were:

- Letter to Congressional Committees Identifying GAO's Original High Risk Areas (January 23, 1990).
- Determining Performance and Accountability Challenges and High Risks, GAO-01-159SP (November 1, 2000).
- High Risk Series: An Update (January 1999 through February 2015).
- High Risk Series: An Overview (February 1995 and February 1997).

**Reasonable Alternatives to the Regulations – Government Code section 11346.2, subdivision (b)(4)(A):** The State Auditor considered alternatives when drafting these proposed regulations, and was open to considering any reasonable alternatives suggested. However, no reasonable alternative were suggested or available.

**Reasonable Alternatives that Would Lessen the Impact on Small Businesses – Government Code section 11346.2, subdivision (b)(4)(B):** This proposed regulatory action will not impact small business as it relates entirely to the auditing of state government agencies. Therefore, no reasonable alternatives were suggested or available regarding lessening the impact on small businesses.

**Facts Relied On to Support an Initial Determination the Regulatory Action Will Not Have a Significant Adverse Economic Impact on Business – Government Code section 11346.2, subdivision (b)(5):** This proposed regulatory action will not have an economic impact on business, as the action relates entirely to the auditing of state government agencies.

**Public Discussions of Proposed Regulations – Government Code section 11346.45, subdivision (a):** This proposed regulatory action does not involve complex proposals or a large number of proposals that cannot easily be reviewed during the public comment period prescribed by Government Code section 11346.4. The State Auditor therefore encourages the submission of written comments to improve the quality of the proposed regulations from persons who would be subject to the proposed regulations and from the public during the comment period.