

California State Auditor

B U R E A U O F S T A T E A U D I T S

Federal Funds:

California's Share of Grant Funding Is Close to Its Share of the Population, but State Spending Cuts May Result in Reduced Federal Funds



May 2003
2002-123.1

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CALIFORNIA STATE AUDITOR

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May 21, 2003

2002-123.1

The Governor of California
President pro Tempore of the Senate
Speaker of the Assembly
State Capitol
Sacramento, California 95814

Dear Governor and Legislative Leaders:

As requested by the Joint Legislative Audit Committee, the Bureau of State Audits presents the first of two audit reports concerning whether California is maximizing the amount of federal funds it is entitled to receive for appropriation via the Budget Act.

This report concludes that California receives a share of federal grant funding that is near its share of the United States' population. For eight large grants, the difference between California's share of the federal grant and its share of the country's population is attributable to allocation formulas based on factors, such as poverty rates or per capita income, that are favorable or unfavorable to California. Because funding formulas are established at the federal level, the State has little control over the share it receives of these grants. Nevertheless, many federal grants include cost-sharing provisions, and the level of federal funding may drop if the State cuts its contribution to grant activities.

We will issue a second report on federal funding in the summer of 2003 that will examine the way state agencies identify and manage federal funds, and discuss other factors that constrain the State's maximization of federal funding.

Respectfully submitted,

A handwritten signature in black ink that reads "Elaine M. Howle". The signature is written in a cursive style.

ELAINE M. HOWLE
State Auditor

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SUMMARY

Audit Highlights . . .

Our review of federal funding received by California found that:

- ☑ *California received \$188.5 billion, or 10.6 percent, of federal funding in federal fiscal year 2001, \$24.9 billion below the level it would have received if funding were allocated according to its 12 percent share of the U.S. population.*
 - ☑ *Factors beyond the State's control, such as demographics, explain much of California's relatively low share of federal funding.*
 - ☑ *California's share of grant funding, at 11.6 percent, was only slightly below its population share, or \$1.5 billion lower than a share based on population.*
 - ☑ *Eight grants accounted for the majority of award amounts diverging from California's population share. Funding formulas for these grants generally explain the discrepancy.*
 - ☑ *The fiscal year 2003–04 Governor's Budget included cuts in state spending that will reduce federal funding because of federal cost-sharing requirements.*
-

RESULTS IN BRIEF

In the federal fiscal year ending September 30, 2001, the federal government provided \$1.8 trillion to U.S. states and territories for activities ranging from Social Security retirement payments to military wages to highway construction grants. California, including individuals, private organizations, and state and local governments, received \$188.5 billion, or 10.6 percent, of this amount. This percentage was significantly below California's 12 percent share of the nation's population (population share), the benchmark we used as a starting point for analyzing federal funding. If California had received federal funds according to its population share, it would have received \$24.9 billion more in federal fiscal year 2001. Nevertheless, most of the difference between California's population share and its actual funding share relate to factors beyond the state government's control. For example, the average age of California's population is the sixth youngest among the states, and its elderly population is a relatively small percentage of its total population. Consequently, it receives only 9.5 percent of the nation's Social Security retirement and survivors insurance payments.

California's share of grant funding was also below its population share, although the difference was much smaller. Grant funding is the only component of federal funding that flows primarily through the State of California's (State) accounts, so it is the focus of this report. California's awards for formula grants (ongoing grants made according to a formula, such as Temporary Assistance for Needy Families) and project grants (fixed-term grants made to fund specific projects, such as those for research) in state fiscal year 2001–02 totaled \$40.4 billion, or 11.6 percent of such awards nationwide. This amount is \$1.5 billion below an allocation based on population share alone. For 84 grants making up 90 percent of federal grant funding nationwide, California's award share exceeded its population share in 46 cases and fell below its population share in 38 cases.

Eight formula grants accounted for the large majority of the award amounts that diverged from California's population share. Of these, six grants were above the population share and two were below it. California's above-average poverty and urbanization

rates, its youthfulness, and its large undocumented immigrant populations are important factors in explaining its large award share for six grants—Temporary Assistance for Needy Families; Special Supplemental Nutrition Program for Women, Infants, and Children; State Children’s Insurance; Foster Care Title IV-E; Federal Transit; and State Criminal Alien Assistance. On the other hand, California’s above-average per capita income, its comparatively low costs per beneficiary for medical assistance, and its high degree of urbanization largely explain its relatively small award share for two grants—the Medical Assistance Program and Highway Planning and Construction. We will discuss the remaining grants that fell below California’s population share in our next report, to be completed in late summer, along with issues related to how the State identifies and manages federal grants.

Although California’s share of federal grant awards is close to its population share, federal cost-sharing requirements may cause the amount of these awards to fall as state spending is cut. Many grants include provisions requiring recipients to match federal spending at an established rate or to maintain a historic level of nonfederal spending. For example, in fiscal year 2003–04, the federal government will match the State’s spending for medical benefits under the Medical Assistance Program on a one-for-one basis. Thus, if the State reduces its spending for medical benefits, federal funding will drop by an equal amount. In the fiscal year 2003–04 Governor’s Budget, federal expenditures for the State are expected to decrease by nearly \$4 billion, or 7.3 percent, from fiscal year 2002–03. A significant portion of this decline is related to cuts in state spending that will trigger reductions in federal funding. Any further budget discussions regarding reductions in or restorations of state funding should continue to consider the effect of these cost-sharing requirements on federal funding.

AGENCY COMMENTS

The Department of Finance generally agrees with the report’s approach, description of matching requirements, and conclusions. ■

INTRODUCTION

BACKGROUND

According to the U.S. Census Bureau's annual Consolidated Federal Funds Report, the federal government provided \$1.8 trillion to U.S. states and territories in federal fiscal year 2001, from October 1, 2000, to September 30, 2001. The types of federal funding ranged from direct payments to individuals through the Social Security Administration, such as Social Security retirement payments, to employee compensation such as military salaries, to grants such as highway planning and construction.

A number of research organizations have analyzed California's federal funding by comparing it with the amount California pays in taxes to the federal government. The difference between the two, funding and taxes, is referred to as a state's balance of payments. According to the Tax Foundation, a nonprofit, nonpartisan research organization, California paid 13.5 percent of the country's federal taxes in 2001. Based on this percentage, California's actual 10.6 percent share of federal funding was relatively low. If federal funding were based on the share of taxes paid, California would have received \$240.1 billion of the total \$1.8 trillion in federal funds paid to the states and territories in federal fiscal year 2001, rather than the \$188.5 billion that it actually received. As a result, California had a negative balance of payments of \$51.6 billion.

The federal government's progressive income tax policy generally requires individuals and entities with higher incomes to pay taxes at increasing rates. California's above-average per capita income and large population explain the high level of federal taxes paid. This situation, coupled with California's below-average per capita share of federal funding, results in the negative balance of payments. In 2001, California's per capita income exceeded the U.S. average by \$2,230, or 7.3 percent, and it ranked 11th highest among the states.

Types of Federal Funding and Related Major Programs

Direct Payments Other Than to Individuals

- Farm production flexibility payments and loan deficiency payments
- Crop insurance premium subsidies and claims payments

Federal Employment Salaries and Benefits

- Military and civilian salaries and wages
- Federal retirement and benefit payments
- Veterans' benefits

Social Security

- Retirement Insurance
- Survivors Insurance
- Disability Insurance
- Supplemental Security Income

Direct Assistance Payments to Individuals

- Food stamps
- Section 8 housing assistance
- Medicare
- Unemployment compensation benefits payments
- Excess earned income tax credits

Grants

- Highway Planning and Construction
- Medical Assistance Program
- Temporary Assistance for Needy Families

Procurement

- Military and civilian contracts

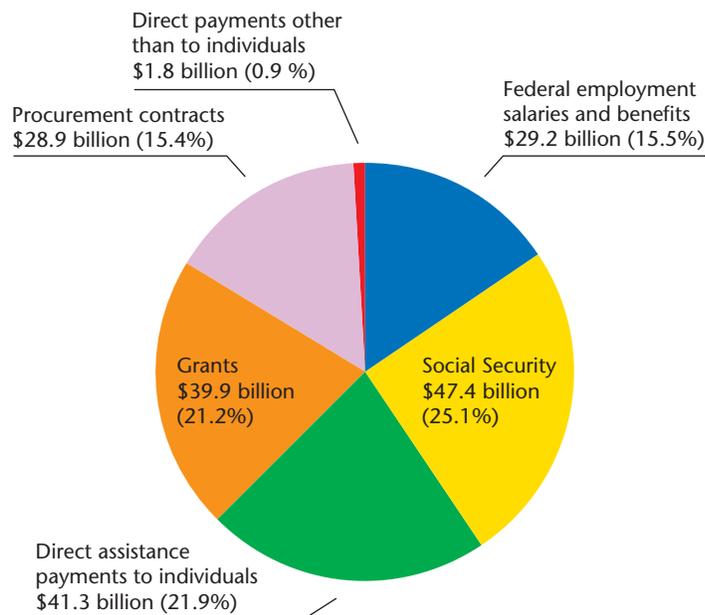
For this report, we have used a population-based, rather than a tax-based, benchmark as a starting point for analyzing federal funding. A population-based benchmark assumes equal federal funding per person across the nation. We have used this benchmark because the distribution of federal funds often depends on the size of the population a program serves but is infrequently tied to increasing levels of income. In fact, income levels and federal funding may be negatively correlated.

CALIFORNIA'S SHARE OF FEDERAL FUNDS IS SIGNIFICANTLY LOWER THAN ITS SHARE OF THE U.S. POPULATION, BUT DEMOGRAPHICS AND FEDERAL POLICIES BEYOND THE STATE'S CONTROL EXPLAIN MOST OF THE DISPARITY

California as a whole, including individuals, private organizations, and state and local governments, receives the largest amount of federal funding of any state; however, its share of federal dollars is significantly below its share of the U.S. population (population share). For example, in federal fiscal year 2001, California received \$188.5 billion, or 10.6 percent, of the \$1.8 trillion in total federal obligations and expenditures, excluding debt and international payments as shown in Figure 1. Yet the State made up 12 percent

FIGURE 1

**Federal Funds Received by California by Type
Federal Fiscal Year 2001**

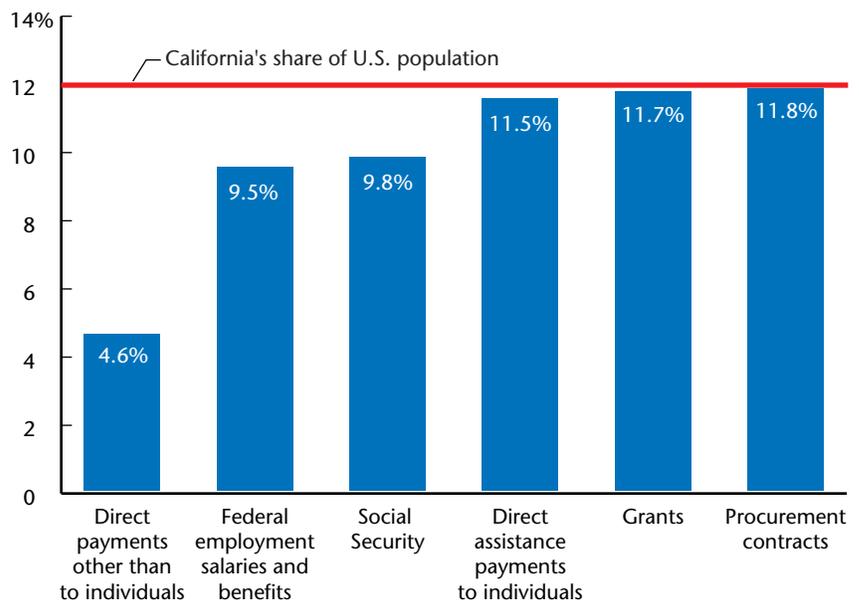


of the country's population. In fact, California's share of federal funding over the past five years has been consistently lower than its population share, never rising above 11.1 percent. If California had received federal funds in proportion to its population share in federal fiscal year 2001, federal funding for California would have been \$24.9 billion higher, for a total of \$213.4 billion. Although the focus of our report is limited to grants received by California, we believe it is important to address the other types of federal funding in this section.

Most types of federal funding do not pass through the accounts of the State of California (State). Figure 1 also shows that nearly half of the federal funding sent to California is made up of Social Security benefits and other direct assistance payments to individuals. Salaries and benefits for federal employees, both civilian and military, account for an additional 15.5 percent. The funding categories of procurements and direct payments other than to individuals make up 16.3 percent of federal funds sent to California. Only 21.2 percent of California's federal funds relate to grants, the majority of which pass through the State's own accounts.

FIGURE 2

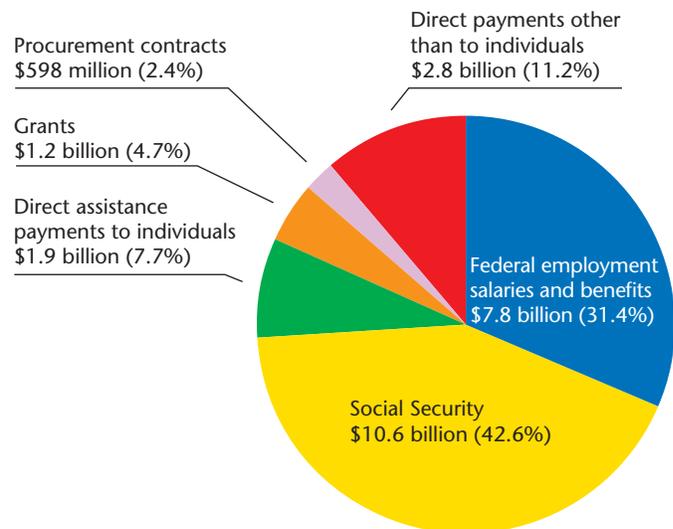
Percent of Total Federal Funding Received by California by Type Federal Fiscal Year 2001



As Figure 2 on page 5 shows, California received less than its population share across all the federal funding categories. Figure 3 shows the total amount by which California’s federal funding fell below its population share—\$24.9 billion—broken down by type of federal funding. The largest contributor was Social Security payments, which amounted to \$10.6 billion less than would be expected according to population share alone. The next largest negative positions related to federal civilian and military salaries and benefits, which were \$7.8 billion below the population share, and direct payments other than to individuals, which were \$2.8 billion lower. Procurements and direct assistance payments to individuals, such as Medicare and food stamps, were \$2.5 billion below California’s proportional share. Grants, which we will discuss in the body of the report, accounted for the remaining \$1.2 billion. As we explain later, however, California’s relatively low share of federal funding relates primarily to its demographics, although federal policies also play a part in limiting federal funding. Specifically, California’s relatively young population, its distance from the seat of national government, and its relatively small agricultural staples industry explain most of the shortfall in federal funding other than grants.

FIGURE 3

**Amount of Federal Funds Below Population Share
Federal Fiscal Year 2001**



California's Low Share of Social Security Administration Payments Can Be Attributed to Its Young Population

California received \$35.2 billion in Social Security Retirement Insurance and Survivors Insurance payments in federal fiscal year 2001. This represented only 9.5 percent of the total for these federal payments, well below California's 12 percent share of the U.S. population. California residents would have received an additional \$9 billion if payments had been based simply on population share. The comparatively small proportion of senior citizens living in California explains its low share of these federal payments. According to the 2000 U.S. census, California's median age was 33.3 years, the sixth youngest in the country. In addition, based on U.S. Census Bureau estimates, the elderly made up 12.4 percent of the nation's population in 2001, but California's elderly made up only 10.6 percent of California's population that year. In contrast, Florida, Pennsylvania, Maine, and West Virginia combined made up 11 percent of the U.S. population but received 14.1 percent of these federal payments because they had a significantly higher proportion of citizens 65 years of age and older. With comparatively fewer senior citizens, it is understandable that California would receive a lower proportion of Social Security Retirement Insurance payments. Moreover, California's share of the nation's deaths was disproportionately low. Of the estimated 2.4 million U.S. deaths in 2001, California accounted for 230,000, or 9.4 percent. California's 8.9 percent of Social Security Survivors Insurance payments is consistent with its share of U.S. deaths.

California's proportion of Social Security Disability Insurance (SSDI) payments in federal fiscal year 2001, at 8.9 percent, was also low. If the distribution of SSDI payments were based on population share alone, California residents would have received \$2.5 billion more in 2001. SSDI is paid to working-age disabled with an SSDI-defined disability who have accumulated enough work credits to qualify for benefits. According to the 2000 census, California's working-age disabled made up 12.4 percent of the U.S. total. However, according to the latest Social Security Administration statistics, California workers consistently made up only 10.6 percent of U.S. workers with earnings covered under Social Security between 1995 and 1999, although they made up 11.3 percent to 11.7 percent of the nation's civilians employed during the same period. Thus, it appears that a low level of participation in the Social Security program is one reason for the low share.

California also may have a disproportionately high number of working-age disabled who have paid in to SSDI but have not met minimum contribution standards. A disabled worker must have worked long enough, and recently enough, under Social Security to qualify for disability benefits. To receive SSDI payments, depending on the claimant's age, a disabled worker generally must have worked for five to 10 years, with five years of credits earned within the past 10 years. Some younger disabled workers can qualify with less than five years of work experience. It is possible that California's workers are not earning the minimum credits they need to be eligible for SSDI when they become disabled.

On the other hand, in federal fiscal year 2001, California received 14.9 percent of Supplemental Security Income (SSI) benefits, significantly above its population share. This share provided California with \$981 million more than a distribution based on population would have. SSI is paid to the disabled and elderly, but payments are based on need rather than on work credits. The program is designed as the assistance of last resort for the disabled or elderly because SSI applicants who are eligible for SSDI or Retirement Insurance payments must apply for those benefits first. It is likely that California's relatively high share of SSI payments is linked to its relatively low share of SSDI. In fact, California's proportion of the country's combined SSDI and SSI disabled beneficiaries was 11.5 percent, much more in line with California's 12.4 percent share of the nation's working-age disabled. However, California's relatively high portion of SSI payments is overshadowed by its low share of the much larger SSDI program.

California's Low Proportion of Federal Employee Salaries and Benefits Reflects Its Distance From the Seat of Government

California received only 9.1 percent, or \$13.1 billion, of the total spending on federal civilian employee wages and salaries, including civilians working for the Defense Department, in federal fiscal year 2001. This was \$4.2 billion less than it would have received based solely on its population share. Most of the discrepancy is explained by the fact that the capital of the United States and the headquarters of all major federal agencies are located in metropolitan Washington, D.C. In fact, Washington, D.C., and the neighboring states of Maryland and Virginia receive 19 percent of federal employee salaries and wages, far above their combined population share of 4.6 percent.

When Washington, D.C., Maryland, and Virginia are excluded, California receives 11.2 percent of the remaining federal employee salaries and wages, a figure much closer to its share of the remaining population.

Similarly, California's share of the one million military personnel stationed in the United States was only 10.8 percent in 2001, and it received 10.9 percent of the spending on military salaries. Again, California's low proportion reflects its distance from metropolitan Washington, D.C., site of the military headquarters. Washington, D.C., and the neighboring states of Maryland and Virginia receive 14.9 percent of military salaries and wages. When Washington, D.C., Maryland, and Virginia are excluded, California receives 12.8 percent of the remaining military salaries and wages, somewhat exceeding its population share.

The placement of military bases around the country has a significant impact on the distribution of military salaries, with some states having a much larger military presence than others. For example, North Carolina accounted for 6.4 percent of military salaries in federal fiscal year 2001, despite its relatively small population share of 2.8 percent. The State should be aware that the U.S. Congress plans to vote in 2005 on closing and realigning military bases around the country. These changes likely will affect California's share of military personnel and salary spending.

California's Low Proportion of Direct Payments Other Than to Individuals Reflects Federal Support of Agricultural Staples

Although California accounted for nearly 12.8 percent of the value of U.S. agriculture production in 2001, California farmers received only 4.1 percent of the funding for the three largest federal farm assistance programs. This represents \$2.2 billion less than California would have received based on its population share. California grows more than half of the nation's fruit, nuts, and vegetables, but the types of crops that receive federal assistance, such as rice, feed grains, wheat, and upland cotton, make up a relatively small part of its agricultural product. Only 1.4 percent of the planted acres for these crops in 2001 were in California. Except for rice, California produces only a fraction of the federally supported crops. Because federal assistance to farms focuses on products that are not widely grown in California, it is not surprising that the State's share is low.

Although some of the types of federal spending discussed in this section, such as military base locations and federal farm assistance policies, may be amenable to change through the national political process, none of them is subject to unilateral action by the State or its agencies. The body of this report and our second report will discuss federal funding for grants, where the State's activities are more likely to affect the level of federal funding that California receives.

SCOPE AND METHODOLOGY

The Joint Legislative Audit Committee (audit committee) requested that the Bureau of State Audits determine whether California is maximizing the amount of federal funds it is entitled to receive for appropriation via the Budget Act. Specifically, we were asked to determine if the State is applying for and receiving the federal program funds for which it is eligible.

To understand federal funding available to California, we analyzed information in the Consolidated Federal Funds Report database. This data, issued by the U.S. Census Bureau for each federal fiscal year, documents federal expenditures and obligations flowing to the states and territories. It includes all funds except those that cannot be allocated to states, such as interest payments on the federal debt, foreign assistance, and defense intelligence agency expenditures.

To understand the federal obligations for formula and project grants, we analyzed data from the Federal Assistance Award Data System. This system is the source of 98 percent of the grant award data contained in the Consolidated Federal Funds Report database just mentioned. This data is, however, available on a quarterly basis rather than for an entire federal fiscal year. We were thus able to accumulate this information for the State's fiscal year. We selected the 84 largest grants, making up 90 percent of federal awards in fiscal year 2001–02, for further review.

To determine factors affecting California's share of federal funding, we reviewed information from the Catalog of Federal Domestic Assistance, applicable federal laws and regulations, and U.S. agency publications. We compared these factors to statistics from the U.S. Census Bureau, Social Security Administration, U.S. Department of Agriculture, and other federal and state sources. We compared California's share of the different federal grants and programs to California's share of the total

U.S. population. We calculated the population share based on 2001 U.S. Census Bureau estimates for the United States, Puerto Rico, and other territories. Where California's share of federal funding diverged substantially from its population share, we determined whether the factors we had identified reasonably explained the difference.

Finally, to provide information on federal cost-sharing requirements, we determined matching and level of effort provisions for the State's major federal grants. Matching provisions require nonfederal program support for a set amount or percentage of program costs, while level of effort provisions require nonfederal entities to maintain a historical level of support for a program. We also reviewed the fiscal year 2003–04 Governor's Budget and interviewed Department of Finance personnel to determine if cuts to the General Fund or to other state funds resulted in concomitant drops in federal funding as presented in the budget.

In a separate report to be issued this summer, we will further examine the policies, procedures, and practices state agencies use to identify and apply for federal funds. We also will review whether the State is collecting all applicable federal funds or is forgoing or forfeiting federal funds for which it is eligible. ■

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AUDIT RESULTS

CALIFORNIA'S PORTION OF FEDERAL GRANTS IS CLOSE TO ITS SHARE OF THE U.S. POPULATION

California's share of federal grant awards has been relatively close to its share of the nation's population (population share) over the past five years. In state fiscal year 2001–02, it stood at 11.6 percent, slightly below the 12 percent population share for California. This overall statistic, however, masks significant variations in the share of awards from grant to grant. The largest variations generally relate to funding formulas based on demographics that favor or disfavor California. For example, grant formulas that focus on poverty rates generally result in relatively large awards for California, while those that focus on low population density do not. In this report, we focus on eight formula grants, of which six are above and two are below California's population share. These grants accounted for the large majority of award amounts that diverged from California's population share. Appendix A presents additional information on 46 large grants for which California's share of the award was above its population share. We will discuss the remaining 36 grants that fell below California's population share in our next report, to be issued in late summer, along with issues related to how the State identifies and manages federal grants.

Types of Federal Grants

Formula Grants

These grants are awarded to states or their subdivisions according to formulas prescribed by law or regulation. They fund ongoing activities that are not confined to a specific project. Examples of formula grants are grants for the Medical Assistance Program and Temporary Assistance for Needy Families.

Project Grants

These grants are awarded to private as well as governmental entities for specific projects of a fixed duration. Project grants include fellowships, scholarships, and research grants. Examples of project grants California receives are ones for Cancer Cause and Prevention Research and Lung Diseases Research.

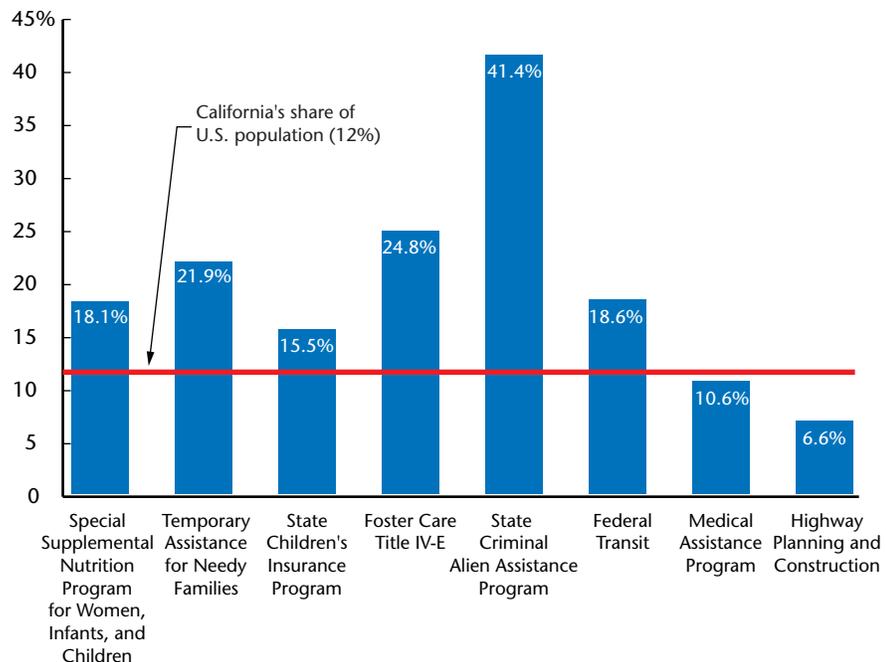
Based on information from the Federal Assistance Award Data System, California's portion of federal awards was 11.6 percent, or \$40.4 billion, in fiscal year 2001–02. This share was in line with awards for the past five years, which never exceeded 12.5 percent, according to the California Institute for Federal Policy Research. Though proportionally only slightly below California's population share, grant awards were still about \$1.5 billion less in fiscal year 2001–02 than they would have been if based on population alone. Federal grants come in two forms—formula grants and project grants—with most grant funding provided to state governments rather than to individuals, private entities, or local governments. In fiscal year 2001–02, the State of California (State) and its university systems received 86 percent of the federal grant awards made to California.

The number of large federal grants received by California was split evenly between those above and those that fell below California’s population share. We reviewed 84 grants that accounted for 90 percent of the total nationwide federal grant awards in fiscal year 2001–02. California’s share of these selected grants, at 11.6 percent, mirrored its 11.6 percent share for all federal grants that year. According to our preliminary analysis, for 46 of the 84 grants, California’s awards exceeded its 12 percent population share, providing \$4.7 billion more than an allocation based on population share alone. California’s portion for these grants was as high as 41 percent of the total grants awarded nationwide. California’s share for the remaining 38 grants fell below its population share and provided \$5.8 billion less than an allocation based on population share alone.

The funding formulas for the eight grants we focused on explain the majority of California’s high and low positions. Six grants, shown in Figure 4, accounted for more than 72 percent of the \$4.7 billion in grant funding that exceeded California’s population

FIGURE 4

**California’s Percentage of Federal Awards for the Eight Grants With the Largest Dollar Difference Between Award and Population Share
Fiscal Year 2001–02**



share, and two grants shown there accounted for 67 percent of the \$5.8 billion in grant funding that fell below California's population share. In the following sections, we discuss the factors related to these grants that favor or disfavor California.

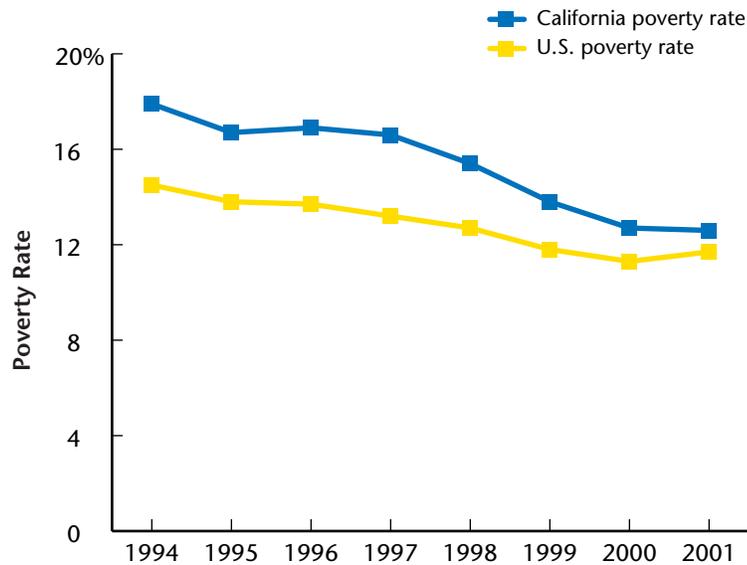
California's Above-Average Poverty and Urbanization Rates, Its Youthfulness, and Its Large Undocumented Immigrant Population Are Important Factors in Explaining Its Large Share of Some Grants

During fiscal year 2001–02, funding formulas helped California garner a sizable share, ranging from 15.5 percent to 41.4 percent, of six large grants. Three of these grants allocate funds based primarily on poverty rates: Temporary Assistance for Needy Families (Temporary Assistance); Special Supplemental Nutrition Program for Women, Infants, and Children (WIC); and State Children's Insurance Program (Children's Insurance). Meanwhile, California's population of low-income children and the State's efforts to include eligible children drive awards for the Foster Care Title IV-E (Foster Care) grant; urbanization rates and mass transit revenues determine allocations for the Federal Transit formula grant; and a state's share of incarcerated illegal aliens and its costs per prisoner affect awards under the State Criminal Alien Assistance Program (Criminal Alien).

Formula grants based on poverty rates have been favorable to California. These rates show the percentage of a population that falls below a specified income level. As shown in Figure 5 on the following page, California's poverty rate has been consistently higher than that of the nation, and it remains quite high, even with recent declines. In fact, California's poverty rate was the 19th highest among the states in 2001. In that year California accounted for 12.6 percent of U.S. residents living below the poverty line. Although the type of poverty rate used for a particular program may vary, the basic rate is a good indicator of how a state will fare with poverty-related funding.

FIGURE 5

California Versus National Poverty Rates From 1994 to 2001



The first of three poverty-based grants, the WIC program, provides free supplemental food, nutrition education, and health care referrals. The program aims to improve the health and nutritional status of low-income pregnant, breastfeeding, and postpartum women and their infants and young children. WIC's food benefit funds are granted to states based on the number of people residing in the State whose income is at or below 185 percent of the poverty level. The population figures include undocumented immigrants who receive services through the program, as well as citizens and legal aliens. This is significant for California, which has the largest share of the nation's undocumented immigrant population, at 32 percent. The federal government awarded the State \$781 million, or 18.1 percent, of the WIC grant in fiscal year 2001–02.

The second poverty-based program, the Temporary Assistance grant, helps reduce dependency on assistance by promoting job preparation, work, and marriage. The establishment of the Temporary Assistance grant in 1996 marked the end of entitlement to federal assistance and the termination of past entitlement programs—Aid to Families with Dependent Children, Job Opportunities and Basic Skills Training, and Emergency Assistance. Each state's Temporary Assistance grant is, however, linked to the amount it received under the old programs in federal fiscal year 1994, fiscal year 1995, or the

The award for the Temporary Assistance grant is linked to the amount the State received for predecessor grants in the early 1990s, a period when California's poverty rate was relatively high.

three-year period from 1992 through 1994. Awards under the old programs were linked to the number of beneficiaries falling below a set income level. Because California's poverty rate was a relatively high 17.9 percent in 1994, California had many eligible participants, and its share of awards was high. In 2003, Congress is considering renewing the legislation governing the Temporary Assistance grant for an additional five years; if this occurs, California will likely benefit from the same favorable funding formula until 2008. In fiscal year 2001–02, the federal government awarded California \$3.8 billion, or 21.9 percent of the Temporary Assistance grant.

The third poverty-based grant, the Children's Insurance program, helps states provide health care to low-income children who do not have health insurance. The program allows states to provide these children with health insurance coverage that meets minimum standards or with health care eligibility under the Medical Assistance Program (Medicaid). In 2001, the U.S. Department of Health and Human Services began allotting funds to states according to a formula that places equal weight on a state's proportion of uninsured, low-income children and its low-income children. Thus, the formula has a poverty component, an uninsured component, and a youth component. According to the U.S. Census Bureau, California's rate for children who were both uninsured and in poverty averaged 10.4 percent for 1999 through 2001, significantly higher than the national average of 7.9 percent. In addition, California's rate for children in poverty averaged 43.1 percent in 1999 through 2001 compared with the national average of 38.1 percent.

Similarly, California's population of low-income children contributes to large awards under the Foster Care program. This open-ended entitlement program reimburses states for the cost of providing 24-hour substitute care to eligible children who are under the jurisdiction of the administering state agency and need temporary placement and care outside their homes. In federal fiscal year 2001, California's average monthly number of children in foster care was 66,000, making up 25 percent of the national total. This percentage may be attributable in part to the State's efforts in identifying children who are eligible for this program. According to the Department of Social Services, in the early 1990s it began emphasizing the importance of obtaining documentation showing the household income level of children entering the foster care system. The department uses this information to place eligible children in the federal Foster Care program.

The federal Criminal Alien program partly defrays California's cost of incarcerating undocumented criminal aliens. Funds are available to state and local governments that incarcerate undocumented criminal aliens for 72 hours or more. The awards are made on a pro rata share of the average costs of incarceration, based on four factors: (1) total days for all inmates housed in the facility, (2) total days that qualifying undocumented criminal aliens were incarcerated, (3) the total salary cost for the jurisdiction applying for the award, and (4) a nationwide payment ratio calculated annually by the Bureau of Justice Assistance. In fiscal year 2001–02, California's share of federal awards for the Criminal Alien program at the state and local level was 41.4 percent of the program's allocated funds. California's large undocumented immigrant population, totaling 32 percent of the nation's undocumented immigrant population, is the primary reason for its large award for the grant.

Finally, California has fared well with a grant based on the level of urbanization. The Federal Transit grant, available only to urban areas, provides funds for building mass transit systems, such as purchasing buses, as well as for operating the systems. More than 90 percent of grant funds are set aside for urban areas with populations exceeding 200,000, with these funds then allocated across the nation based on population, population density, and measures of mass transit usage. The U.S. Census Bureau reported that 94.5 percent of Californians resided in urban areas in 2000, compared with a nationwide rate of 79.2 percent. In addition, California made up a substantial portion of mass transit usage. For example, according to data from the American Public Transportation Association, California accounted for 16 percent of the nation's bus revenue miles in the fiscal year ending in 2001. In fiscal year 2001–02, the federal government awarded nearly \$1 billion, or 18.1 percent, of the Federal Transit grant to local governments in California.

Formulas for Medicaid and Highway Grants Have Been Less Favorable to California

California's comparatively low costs per Medicaid beneficiary, as well as the federal government's low reimbursement rate to the State for these costs, explain much of the State's low proportion (10.6 percent) of the total federal Medicaid grant. This formula grant provides funds to states to cover payments for medical assistance for their indigent residents. States have the flexibility to establish their own eligibility standards, scope of services, and payment rates, but they also must meet minimum federal

guidelines. For example, all state Medicaid programs must provide for inpatient hospital services, laboratory services, and X-ray services. The Medicaid grant represents by far the largest federal grant, making up more than 41 percent of all federal grants funding in fiscal year 2001–02. The formulas for this grant are thus very significant to a state’s total share of grant funds.

One factor causing a low share of Medicaid for California is that the State spends less per enrollee for medical assistance payments than any other state.

Federal Medicaid grant payments reimburse states for a portion of their Medicaid costs and are not capped; thus, the level of resources a state puts into the program is critical to its level of federal payments under the grant. Although California has a significant proportion of the nation’s eligible population—at 18 percent in 2000—it winds up with a much lower percentage of funding, largely because it spends less on medical assistance payments per enrollee than any other state spends. To gain some perspective, consider that in federal fiscal year 2000, New York spent \$30.2 billion on medical assistance payments, or an average of \$8,900 for each of its 3.4 million enrollees; meanwhile, California spent \$21.2 billion on medical assistance payments, or an average of \$2,600 for each of its 8.1 million enrollees. Because California spends less on medical assistance payments per Medicaid enrollee than the national average, it receives less federal funding per enrollee than the national average. A publication by the Kaiser Commission on Medicaid and the Uninsured (Kaiser Commission) suggests that the demographics of a state’s enrollee population, regional health care costs, and state policy choices on which optional benefits to provide play a role in creating the disparity in per enrollee spending. That said, it also should be noted that, according to data provided by the Kaiser Commission, California spent 16 percent of its state budget on Medicaid in state fiscal year 1999–2000. New York spent 32 percent of its state budget on Medicaid in that same fiscal year.

Another factor reducing California’s share of the Medicaid grant is the sliding reimbursement rate, called the Federal Medical Assistance Percentage (matching percentage). The matching percentage is updated each year according to the relative per capita income of each state. For most of state fiscal year 2002–03 and all of fiscal year 2003–04, California will receive the lowest matching percentage possible, 50 percent, because its per capita income is slightly above the national average. The reduction in the matching percentage from 51.4 percent to 50 percent in federal fiscal year 2003 is expected to cause the State to lose more than \$206 million in federal funds that year. In designing the formula for the matching percentage, federal policy makers attempted to reduce differences likely to result between the

Beginning in fiscal year 2002–03, California will receive the lowest Medicaid matching share possible.

Medicaid programs of wealthier and poorer states. Thus, a state with an above-average per capita income will have a relatively low matching percentage, and vice versa. California, however, has a high proportion of needy residents, even though it also has an above-average per capita income.

The method for determining the matching percentage has its critics. The federal General Accounting Office has testified several times since 1983 that the use of per capita income is not the best method for determining the size of a state's poverty population or the extent of its financial resources for use with the Medicaid program. The General Accounting Office has suggested modifying the formula to take into account poverty rates, total taxable resources, and geographic adjusters of health care costs. We also note that the nation's progressive tax system already requires states with high per capita incomes to pay relatively more to the federal government to support all federal programs. Using income measures to then reduce program payments appears to penalize higher-income states, including California, at both the beginning and end of the process.

Most of the federal formulas for the Highway Planning and Construction (Highways) grant also do not favor California. This grant is made up of numerous components, such as the National Highway System, Surface Transportation, and Interstate Maintenance, each of which has its own funding formula. These formulas, however, generally are weighted most heavily toward factors in which California is weak. For example, the National Highway System program allocates funds based 25 percent on a state's share of miles of principal arterial routes, 30 percent on the proportion of diesel fuel consumed, and 10 percent on the sparseness of population compared with lane mileage on principal arterials. Only 35 percent of the formula is based on a state's share of vehicle miles traveled. In federal fiscal year 2001, California accounted for only 9 percent of the nation's noninterstate arterial lane mileage and 8 percent of diesel fuel usage, but it made up 14 percent of the nation's vehicle miles traveled. Because California is highly urban, with relatively few but very well-traveled roads and a comparatively low proportion of freight traffic, the allocation produced by this and similar formulas is comparatively low.

Despite the unfavorable formulas, another aspect of the Highways grant keeps California's share from being even lower. The grant is funded through fuel taxes and fees, and each state is guaranteed a return of 90.5 percent of the taxes and fees it pays

Despite formulas that disfavor California, a guaranteed return on taxes and fees paid into the Highway Account keeps California's share of the Highways grant from being even lower.

into the Highway Account of the Highway Trust Fund for certain components of the grant. These components, including the National Highway System, made up 87 percent of the program's obligated funds in federal fiscal years 1998 through 2001. During this period, California paid an average of 10.1 percent of total taxes and fees. Based on the guarantee, California could thus expect to receive back about 9.1 percent of funding for the majority of the Highways grant. Nevertheless, our preliminary analysis shows that California's share of obligated funds in federal fiscal years 1998 through 2001 was 8.2 percent, and its share in federal fiscal year 2002 was 6.6 percent. Obligated funds represent awards for this grant in the federal awards database. We will more fully explore other factors explaining an apparent share of funding lower than the guarantee in our next report on federal funding.

PROPOSED CUTS IN STATE SPENDING WILL REDUCE FEDERAL FUNDING

Although California is receiving a proportion of federal grants that is close to its population share, proposed cuts in state funding will result in reduced funding because of federal cost-sharing requirements. Some of the largest federal grants to California are administered by the State and have cost-sharing requirements that make state and/or local governments bear part of the program costs. Reductions in state spending for these programs generally can be expected to result in decreases in federal funding in the year the cuts take effect. In addition, state reductions may affect future federal funding if state participation falls below specified levels and subsequent grant awards are reduced in kind.

The State's Largest Federal Programs Require State Financial Participation

In fiscal year 2001–02, the State received more than \$38 billion in federal cash to administer federal programs. This amount does not include cash received by local agencies, private recipients, or California's state-run universities. Of the 52 state-administered programs accounting for more than 95 percent of these funds, 33 programs have cost-sharing requirements, including some of the largest programs such as Medicaid and the Temporary Assistance program. The Table on the following page shows the applicable requirements for the six federal programs for which the State had the largest cash receipts. See Appendix B for a complete list of the 52 programs and applicable requirements.

TABLE

Cost-Sharing Requirements of the State’s Largest Federal Programs

Federal Program	State Administering Department	Federal Cash Receipts in Fiscal Year 2001–02 (in Billions)	Matching Requirement?	Level of Effort Requirement?
Medical Assistance Program	Health Services	\$14.9	50 percent state share of total medical benefits in fiscal year 2003–04.	No
Unemployment Insurance	Employment Development	5.2	State pays 50 percent of the unemployment compensation for extended benefits from its unemployment insurance tax revenues.	No
Temporary Assistance for Needy Families	Social Services	3.2	No	Yes
Highway Planning and Construction	Transportation	2.5	States pay a portion of project costs—generally 10 percent for interstate system projects and 20 percent for most other projects. These portions are reduced for states with sizable nontaxable Indian and public lands, but not below 5 percent. For example, California’s portion of interstate system projects is 8.4 percent.	No
Title I Grants to Local Educational Agencies	Education	1.2	No	Yes
Foster Care—Title IV-E	Social Services	1.0	50 percent nonfederal share of total maintenance payments in fiscal year 2003–04; 25 percent nonfederal share of training expenditures, and 50 percent nonfederal share of other administrative expenditures.	No

As shown in the Table, cost-sharing requirements can vary greatly by program, in type and complexity. There are two types of cost-sharing requirements—matching requirements and level of effort requirements. Under matching requirements, the State must provide contributions of a specified amount or percentage to match federal awards. As we mentioned previously, Medicaid, which received nearly \$14.9 billion in federal funds in fiscal year 2001–02, will have a state matching contribution of 50 percent in fiscal year 2003–04 for total medical benefits expenditures. The Foster Care program will have a similar 50 percent matching contribution. Any reductions in available state funding for these programs thus will double the impact of state reductions because federal funding will drop proportionately.

The State must continue to spend \$2.9 billion of its own money each year for the Temporary Assistance program in order to receive maximum federal funding.

Level of effort requirements are designed to prevent the State from obtaining federal funds for a program and then reducing its own expenditures on the program. They include requirements that the State maintain a set level of expenditures from nonfederal sources for specified activities from period to period, or that it use federal funds to supplement, but not supplant or replace, nonfederal funding of services. The Temporary Assistance program, which received \$3.2 billion in fiscal year 2001–02, has detailed level of effort requirements. For example, the State must continue to spend \$2.9 billion a year (80 percent of the amount of nonfederal funds it spent in federal fiscal year 1994 on the Aid to Families with Dependent Children program) in order to receive the maximum federal grant. If the State meets required levels of program beneficiaries who participate in work-related activities, determined after the end of each fiscal year, it need spend only \$2.7 billion (75 percent of the federal fiscal year 1994 amount). Penalties may result if the State does not maintain its effort at the established level. For example, if the State spends less than the \$2.9 billion required, the federal government could reduce the Temporary Assistance grant in the following year by the amount of the difference between the \$2.9 billion and the actual nonfederal expenditures.

Similarly, some programs administered by the Department of Education, such as the Title I Grants to Local Educational Agencies, specify that the State may use federal program funds only to supplement, or increase, the level of funds available from nonfederal sources for the education of participating students. This means the State cannot gain federal funds and subsequently cut its own spending. In other words, supplement but not supplant provisions require the State to maintain past spending levels in order to maximize federal funding.

California’s Proposed Budget Identifies Federal Funding Decreases in Fiscal Year 2003–04

In the fiscal year 2003–04 Governor’s Budget, proposed federal expenditures on grants to the State are expected to decrease by nearly \$4 billion, or 7.3 percent, from their estimated actual levels in fiscal year 2002–03. This net decline in federal spending includes reductions related to cuts in state spending, reductions related to changes in federal formulas and programs, and increases in federal funding for some programs.

Some large reductions in federal funding are unrelated to decreases in General Fund support. For example, state spending of federal funds for the Temporary Assistance program is set to decrease by \$900 million in fiscal year 2003–04, mainly due to California’s use in fiscal year 2002–03 of sizable county performance incentives that had been carried over to fiscal year 2002–03 from an earlier year. This extra source of cash will not be available in fiscal year 2003–04. The fiscal year 2003–04 Governor’s Budget proposes to reduce the maximum monthly aid payments and suspend cost-of-living adjustments for program recipients. Other savings in program expenditures will occur from an estimated decline in caseload resulting from recipients reaching their 60-month time limit in the program. Despite the drop in program expenditures, however, the actual federal award for fiscal year 2003–04 will not fall because the State plans to maintain the required level of effort for this program.

Other federal funding decreases relate to state spending reductions caused by efforts to close the gap between planned expenditures and estimated revenues. In November 2002, the governor issued an executive order for state agencies and departments to identify General Fund savings by reducing expenditures in fiscal year 2002–03. This entailed freezing spending where possible and reducing nonessential functions. The Department of Finance (Finance) was responsible for ensuring compliance with the order, which is to remain in effect until June 30, 2004. As a result, in December 2002, Finance and the departments identified General Fund savings totaling \$10.2 billion—\$3.4 billion in fiscal year 2002–03 and \$6.8 billion in fiscal year 2003–04. The savings were, however, not expected to close the entire gap in funding for fiscal year 2003–04. To balance the budget, Finance and the departments then proposed additional state cuts. Combined, these reductions are presented within the fiscal year 2003–04 Governor’s Budget. Cost-sharing requirements add to the impact of cuts in state funding by causing cuts in federal funding as well.

A proposed reduction in rates paid to Medicaid providers would cut state spending by \$721 million and federal funding by \$707 million in fiscal year 2003–04.

The fiscal year 2003–04 Governor’s Budget appears to consider the effect that these cuts in state spending will have on federal funding of programs with cost-sharing requirements. For example, proposed cuts in federal funding related to cost-sharing requirements include a nearly \$645 million net decrease in federal Medicaid funding from fiscal years 2002–03 to 2003–04, consisting of increases of \$755 million, mostly from estimated increased caseload, and decreases of nearly \$1.4 billion related

to proposed cuts in state spending. Of this latter amount, the State's planned 15 percent rate reduction for Medicaid providers, which is expected to cut General Fund spending by nearly \$721 million in fiscal year 2003-04, would lead to a similar federal funding decrease of more than \$707 million. According to Finance, its primary focus in the fiscal year 2003-04 Governor's Budget was on reducing state expenditures from the General Fund, resulting in a secondary consideration of the special funds, including federal funds. Our review indicates that Finance appropriately reduced federal funding as a result of state funding cuts. However, any further budget discussions regarding reductions or restorations in state funding should continue to consider the effect of matching and level of effort requirements on federal funding.

We conducted this review under the authority vested in the California State Auditor by Section 8543 et seq. of the California Government Code and according to generally accepted government auditing standards. We limited our review to those areas specified in the audit scope section of this report.

Respectfully submitted,



ELAINE M. HOWLE
State Auditor

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APPENDIX A

Grants for Which California Received More Than Its Population Share in State Fiscal Year 2001–02

In the audit results, we state that for 46 of 84 grants making up 90 percent of total federal grant funding in fiscal year 2001–02, California received a share of the grant that exceeded its 12 percent share of the U.S. population (population share). Table A.1 presents California’s share of the total national grant during that period, the amount of California’s actual award, and the amount by which its actual award exceeded an allocation based solely on population share. In addition, for formula grants, the table indicates the factors, established by law or regulation, which drive the level of grant funding. In total, California’s awards for these grants exceeded an allocation based solely on population share by \$4.7 billion.

TABLE A.1

**Formula and Project Grants for Which California Received More Than Its Population Share
Fiscal Year 2001–02**

Federal Catalog Number	Program Name	Type of Assistance	Formula Driver	Total Federal Award (in Millions)	California Award (in Millions)	California’s Percent Share	Amount Over Population Share (in Millions)
10.555	National School Lunch Program	Formula	Paid lunches plus free and reduced lunches for low-income (based on poverty level) children served at schools	\$9,530	\$1,232	12.93%	\$ 89
10.557	Special Supplemental Nutrition Program for Women, Infants, and Children	Formula	Population at or below 185 percent of poverty level	4,308	781	18.12	264
10.561	State Administrative Matching Grants for Food Stamp Program	Formula	State costs for administering the Food Stamp Program	2,274	283	12.46	10
14.218	Community Development Block Grants/Entitlement Grants	Formula	For metropolitan and urban counties only: population, population in poverty, housing overcrowding, housing built before 1940, population growth lag	3,257	576	17.68	185
16.592	Local Law Enforcement Block Grant Program	Formula	Violent crimes	481	63	13.19	6
17.255	Workforce Investment Act*	Formula	Unemployment statistics	475	94	19.69	37

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Federal Catalog Number	Program Name	Type of Assistance	Formula Driver	Total Federal Award (in Millions)	California Award (in Millions)	California's Percent Share	Amount Over Population Share (in Millions)
20.507	Federal Transit: Formula Grant	Formula	Urban population and population density, bus and fixed guideway passenger and revenue miles	\$ 3,884	\$723	18.62%	\$257
84.002	Adult Education State Grant Program	Formula	Population 16 years and older without a high school degree and unenrolled in secondary school	529	74	13.91	10
84.010	Title I Grants to Local Educational Agencies (Title I)	Formula	Three separate formulas: 1) Per pupil education expenditures and number of low-income school-age children 2) Local educational agencies with 6,500 low-income children or 15 percent or greater poverty rate 3) Percentage of poor children	8,442	1,155	13.68	142
84.186	Safe and Drug-Free Schools and Communities— State Grants	Formula	School-age population and share of Title I received by a state	431	53	12.28	1
84.281	Eisenhower Professional Development State Grants	Formula	School-age population and share of Title I received by a state	480	59	12.35	2
93.558	Temporary Assistance for Needy Families	Formula	Population in poverty	17,163	3,754	21.87	1,694
93.575	Child Care and Development Block Grant	Formula	Population of children under 5 years, population of children in the National School Lunch Program, and per capita income	2,190	293	13.36	30
93.658	Foster Care Title IV-E	Formula	Federal match to state for foster care maintenance payments	4,470	1,108	24.79	571
93.659	Adoption Assistance	Formula	Federal match to state for subsidy payments that support adoption of special needs children	1,318	213	16.14	55
93.667	Social Services Block Grant	Formula	Population	1,700	204	12.00	<1
93.767	State Children's Insurance Program	Formula	Population of low-income and uninsured low-income children	6,872	1,062	15.45	237
93.917	HIV Care Formula Grants	Formula	Population of persons living with Acquired Immunodeficiency Syndrome	960	116	12.04	<1

Federal Catalog Number	Program Name	Type of Assistance	Formula Driver	Total Federal Award (in Millions)	California Award (in Millions)	California's Percent Share	Amount Over Population Share (in Millions)
93.958	Block Grants for Community Mental Health Services	Formula	Population of adults (with greater weight on younger adult age groups) and state's costs to provide mental health services (relative to the other states' costs) and the taxable resources of a state	\$ 409	\$57	13.83%	\$7
93.959	Block Grants for Prevention and Treatment of Substance Abuse	Formula	Population of adults age 18 to 64 (with weight on younger adults living in urban areas) and a state's cost to provide substance abuse treatments (relative to the other states' costs) and the taxable resources of a state	1,619	247	15.24	52
16.606	State Criminal Alien Assistance Program	Formula/Project	Ratio of criminal alien incarcerated days to total population incarcerated days, and prison salary costs	1,090	452	41.42	321
20.500	Federal Transit: Capital Improvement Grants	Formula/Project	Urban population and population density, bus and fixed guideway passenger and revenue miles	2,442	294	12.06	1
12.420	Military Medical Research and Development	Project		575	98	17.11	29
47.049	Mathematical and Physical Sciences	Project		664	92	13.92	13
47.050	Geosciences	Project		491	68	13.75	9
47.070	Computer and Information Science and Engineering	Project		406	108	26.58	59
47.074	Biological Sciences	Project		444	80	17.93	26
47.076	Education and Human Resources	Project		418	67	16.00	17
81.049	Office of Science Financial Assistance Program	Project		770	139	18.05	47
93.242	Mental Health Research Grants	Project		804	124	15.46	28
93.268	Immunization Grants	Project		501	69	13.73	9
93.393	Cancer Cause and Prevention Research	Project		563	85	15.13	18
93.395	Cancer Treatment Research	Project		729	125	17.16	38
93.396	Cancer Biology Research	Project		549	85	15.40	19
93.821	Cell Biology and Biophysics Research	Project		539	113	20.89	48
93.839	Blood Diseases and Resources Research	Project		441	74	16.68	21
93.847	Diabetes, Endocrinology, and Metabolism Research	Project		611	82	13.35	8
93.853	Extramural Research Programs in Neurosciences and Neurological Disorders	Project		1,066	148	13.91	20

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Federal Catalog Number	Program Name	Type of Assistance	Formula Driver	Total Federal Award (in Millions)	California Award (in Millions)	California's Percent Share	Amount Over Population Share (in Millions)
93.855	Allergy, Immunology, and Transplantation Research	Project		\$ 452	\$ 89	19.75%	\$ 35
93.856	Microbiology and Infectious Diseases Research	Project		1,345	171	12.75	10
93.859	Pharmacology, Physiology, and Biological Chemistry Research	Project		458	74	16.23	19
93.862	Genetics and Developmental Biology Research and Research Training	Project		435	74	17.12	22
93.866	Aging Research	Project		711	129	18.19	44
93.867	Vision Research	Project		448	79	17.71	26
93.914	HIV Emergency Relief Project Grants	Project		598	109	18.18	37
43.AAA	Research Grants for the Space Program	Project		1,078	213	19.77	84
Totals				\$89,420	\$15,388	17.21%	\$4,657

* The Workforce Investment Act grant has been replaced by the Workforce Investment Act cluster grants 17.258, 17.259, and 17.260.

APPENDIX B

Cost-Sharing Requirements for Selected Federal Programs

In the audit results, we indicate that the current budget challenges can affect federal funding received by California if the State's share of program costs drop. Table B.1 identifies 52 federal programs that accounted for more than 95 percent of the State's federal cash receipts in fiscal year 2001–02. The list does not include any noncash assistance, such as commodities, food stamps, loans, and insurance that the State receives. In addition, the list includes only federal cash that the State receives through its own accounts and does not include federal cash receipts provided directly to state-run universities, local agencies, or private recipients. We briefly describe the applicable state matching requirements for each of the programs. Also, we indicate only whether there are level of effort requirements because, as stated in the audit results, these requirements can vary greatly by program and be very detailed. These descriptions are intended to provide information for budget discussions affecting these programs and are not meant to be all-inclusive.

TABLE B.1

Cost-Sharing Requirements for Selected Federal Programs

State Administering Department	Federal Catalog Number	Federal Program	Federal Cash Receipts in Fiscal Year 2001–02 (in Millions)	Matching Requirement?	Level of Effort Requirement?
Aging	93.044	Special Programs for the Aging—Title III, Part B—Grants for Supportive Services and Senior Centers	\$ 33.8	At least 15 percent nonfederal share for all services statewide. At least 25 percent nonfederal share for cost of state plan administration.	Yes
Aging	93.045	Special Programs for the Aging—Title III, Part C—Nutrition Services	49.6	At least 15 percent nonfederal share for all services statewide. At least 25 percent nonfederal share for cost of state plan administration.	Yes
Alcohol and Drug Programs	93.959	Block Grants for Prevention and Treatment of Substance Abuse	259.4	No	Yes
Child Support Services	93.563	Child Support Enforcement	297.0	34 percent nonfederal share generally for program costs. 10 percent nonfederal share for laboratory costs to determine paternity.	No

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State Administering Department	Federal Catalog Number	Federal Program	Federal Cash Receipts in Fiscal Year 2001–02 (in Millions)	Matching Requirement?	Level of Effort Requirement?
Community Services and Development	93.568	Low-Income Home Energy Assistance	\$ 67.0	No	No
Community Services and Development	93.569	Community Services Block Grant	52.7	No	No
Corrections	16.606	State Criminal Alien Assistance Program	301.3	No	No
Education	10.553	School Breakfast Program	202.4	No	No
Education	10.555	National School Lunch Program	806.6	At least 30 percent state match of the funds received under Section 4 of the National School Lunch Act in the 1980–81 school year.	No
Education	10.556	Special Milk Program for Children	0.8	No	No
Education	10.558	Child and Adult Care Food Program	216.5	No	Yes
Education	10.559	Summer Food Service Program for Children	20.3	No	No
Education	84.010	Title I Grants to Local Educational Agencies	1,152.4	No	Yes
Education	84.011	Migrant Education—Basic State Grant Program	98.3	No	Yes
Education	84.027	Special Education—Grants to States	637.7	No	Yes*
Education	84.048	Vocational Education—Basic Grants to States	112.1	50 percent nonfederal share for administration of the state plan.	Yes
Education	84.173	Special Education—Preschool Grants	57.6	No	Yes*
Education	84.298	Innovative Education Program Strategies	45.1	No	Yes
Education	84.340	Class Size Reduction	84.6	No	Yes
Education	93.575	Child Care and Development Block Grant	622.7	No	No
Education	93.596	Child Care Mandatory and Matching Funds of the Child Care and Development Fund	326.1	Allowable costs greater than the State's level of effort requirement will be matched at 50 percent in fiscal year 2003–04.	Yes
Emergency Services	83.544	Public Assistance Grants	409.5	State and local government share of the grant is generally 25 percent or less.	No
Emergency Services	83.548	Hazard Mitigation Grant	134.3	State or project applicant must provide at least 25 percent of the eligible costs of each project.	No
Employment Development	17.207	Employment Service	83.8	No	No
Employment Development	17.225	Unemployment Insurance	5,225.8 [†]	State pays 50 percent of the unemployment compensation for extended benefits from its unemployment insurance tax revenues.	No
Employment Development	17.253	Welfare-to-Work Grants to States and Localities	89.2	State must provide \$1 nonfederal match for each \$2 of federal formula funds allotted.	No

State Administering Department	Federal Catalog Number	Federal Program	Federal Cash Receipts in Fiscal Year 2001–02 (in Millions)	Matching Requirement?	Level of Effort Requirement?
Employment Development	17.255	Workforce Investment Act [‡]	\$ 300.7	No	No
Employment Development	17.258	WIA Adult Program	93.1	No	No
Employment Development	17.259	WIA Youth Activities	99.2	No	No
Employment Development	17.260	WIA Dislocated Workers	105.6	No	No
Employment Development	17.801	Disabled Veterans' Outreach Program	11.3	No	No
Employment Development	17.804	Local Veterans' Employment Representative Program	6.9	No	No
Health Services	10.557	Special Supplemental Nutrition Program for Women, Infants, and Children	761.5	No	No
Health Services	66.468	Capitalization Grants for Drinking Water State Revolving Fund	57.8	20 percent state match of each capitalization grant payment. 50 percent state share for state program management.	No
Health Services	93.268	Immunization Grants	15.7	No	No
Health Services	93.777	State Survey and Certification of Health Care Providers and Suppliers	31.2	No	No [§]
Health Services	93.778	Medical Assistance Program	14,869.8	50 percent state share of total medical benefits in fiscal year 2003–04.	No [§]
Health Services	93.917	HIV Care Formula Grants	108.9	State must provide \$1 nonfederal match for each \$2 of federal funds spent.	Yes
Housing and Community Development	14.228	Community Development Block Grant/State's Program	48.6	50 percent state share of administrative costs above \$100,000.	No
Housing and Community Development	14.239	HOME Investment Partnerships Program	35.1	Generally at least 25 percent nonfederal match of federal funds drawn.	No
Justice	93.775	State Medicaid Fraud Control Units	14.3	25 percent state share.	No [§]
Managed Risk Medical Insurance Board	93.767	State Children's Insurance Program	401.0	35 percent state share for fiscal year 2003–04.	Yes
Rehabilitation	84.126	Rehabilitation Services—Vocational Rehabilitation Grants to States	237.8	21.3 percent state share of expenditures under the state plan, except construction. At least 50 percent nonfederal share for construction of a facility for community rehabilitation program purposes.	Yes
Social Services	10.561	State Administrative Matching Grants for Food Stamp Program	287.4	Nonfederal share is generally 50 percent. No match for Employment and Training Program grants.	No

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State Administering Department	Federal Catalog Number	Federal Program	Federal Cash Receipts in Fiscal Year 2001–02 (in Millions)	Matching Requirement?	Level of Effort Requirement?
Social Services	10.568	Emergency Food Assistance Program	\$ 8.0	50 percent nonfederal share of administrative costs, except for costs related to emergency feeding organizations.	No
Social Services	93.558	Temporary Assistance for Needy Families	3,201.4	No	Yes
Social Services	93.658	Foster Care—Title IV-E	1,020.4	50 percent nonfederal share of total maintenance payments in fiscal year 2003–04. 25 percent nonfederal share of training expenditures, and 50 percent nonfederal share of other administrative expenditures.	No
Social Services	93.659	Adoption Assistance	212.7	50 percent nonfederal share of total subsidy payments in fiscal year 2003–04. 25 percent nonfederal share of training expenditures, and 50 percent nonfederal share of other administrative expenditures.	No
Social Services	93.667	Social Services Block Grant	178.1	No	No
Social Services	96.001	Social Security—Disability Insurance	177.1	No	No
Transportation	20.205	Highway Planning and Construction	2,470.0	States pay a portion of project costs—generally 10 percent for interstate system projects and 20 percent for most other projects. These portions are reduced for states with sizable nontaxable Indian and public lands, but not below 5 percent. For example, California's portion for interstate system projects is 8.4 percent.	No
Water Resources Control Board	66.458	Capitalization Grants for State Revolving Funds	108.3	At least 20 percent state match of each capitalization grant payment.	No

* Requirement applies to local educational agency expenditures only.

† Of the \$5,225.8 million in total unemployment insurance funds (federal catalog number 17.225) received by the Employment Development Department during fiscal year 2001–02, \$4,840 million was State Unemployment Insurance funds that were drawn down from the Unemployment Trust Fund in the U.S. Treasury.

‡ Funding is no longer available for this program and is instead now provided through three new programs: WIA Adult Program, WIA Dislocated Workers, and WIA Youth Activities.

§ A state waiver may contain level of effort requirements. However, the waivers in effect in fiscal year 2001–02 did not contain such requirements.

Agency's comments provided as text only.

Department of Finance
Office of the Director
State Capitol, Room 1145
Sacramento, CA 95814-4998

May 16, 2003

Ms. Elaine M. Howle
State Auditor
Bureau of State Audits
555 Capitol Mall, Suite 300
Sacramento, California 95814

Dear Ms. Howle:

Thank you for the opportunity to review and comment on the audit entitled "Federal Funds: California's Share of Grant Funding is Close to its Share of the Population, But Cuts in State Spending May Result in Reduced Federal Funds." As the Department of Finance (Finance) understands it, this is the first of two reports assessing whether California is maximizing the amount of federal funds it is entitled to receive for appropriation through the Budget Act. This initial report describes the types of federal funds available to California, assesses the degree to which funding mirrors California's share of national population, and then focuses more specifically on grant funding, because only these federal resources pass through the State's accounting and appropriation systems.

Of the federal grants available to state government, the report devotes attention to the top eight, concluding that the State has been receiving more than its proportionate share of six of these grants, and less than its share of two grants—Medicaid grant payments and Highway Planning and Construction (Highway) grants. For each of these two grants, the report examines in greater depth the potential causes for disproportionately low grant levels, noting that a primary cause is disadvantageous federal formulas.

The report concludes that California's overall share of federal grants is currently close to its population share, although proposed reductions in state funding may change that situation since the largest federal programs require state matches. The report correctly notes that not all of the anticipated decrease in federal funds for fiscal year 2003-04 is related to General Fund reductions, since a portion of the funding level changes is due to fluctuations in carry-forward funding from earlier years. Of that portion that is related to General Fund reductions, the report notes that the 2003-04 Governor's Budget has taken into consideration the effect on programs with federal cost-sharing requirements ("...Finance appropriately reduced federal funding as a result of state funding cuts"). The report closes with the counsel that budget reduction decisions should continue to factor in impacts on the State's receipt of federal funds.

In our review of the report, Finance did not verify numeric data and understood that was not your office's expectation. Finance staff did review whether the descriptions of cost-sharing requirements by grant (Appendix B) appeared correct. We have discussed and resolved with your staff any differences we had with the draft report.

Ms. Elaine M. Howle
May 16, 2003
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Staff also reviewed basic methodology and the report's conclusions. We noted that in deriving population shares, the report includes Puerto Rico data in the national population base, which results in very slightly different population shares than typically used by Finance's Demographics Research Unit. However, the difference is not significant. In the transportation area, we note that the Bureau of State Audits included a general discussion of these adjustments and hope that the second report might provide more detail on this and other transportation-related issues.

In order to assess trends, we believe it might be useful to track the change in the State's share of federal funds over a longer period of time than five years. However, overall we agree with the report's approach, its description of federal matching requirements, and conclusions. We look forward to the release of the second report in the series.

If you have any questions or need any additional information regarding this response, then please contact Shelley Mateo, Program Budget Manager, at 445-3274.

STEVE PEACE
Director
By:

(Signed by: Kathryn Radtkey-Gaither)

KATHRYN RADTKEY-GAITHER
Assistant Director, Operations

cc: Members of the Legislature
Office of the Lieutenant Governor
Milton Marks Commission on California State
Government Organization and Economy
Department of Finance
Attorney General
State Controller
State Treasurer
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