California State Auditor

BUREAU OF STATE AUDITS

South Coast Air Quality Management District:

The District Should Establish a More Equitable Emission Fee Structure and Process Permits More Promptly

July 1998
97114

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July 9, 1998 97114

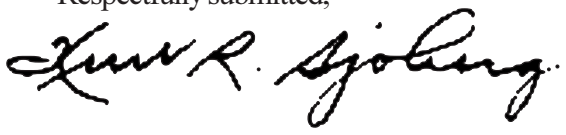
The Governor of California
President pro Tempore of the Senate
Speaker of the Assembly
State Capitol
Sacramento, California 95814

Dear Governor and Legislative Leaders:

As requested by the Joint Legislative Audit Committee, the Bureau of State Audits presents its audit report concerning the South Coast Air Quality Management District (district). This report concludes that the district's current policy requiring only the largest polluters to pay emission fees is inequitable. Also, although the district generally issues permits to construct within the time set out in state law, it issues many permits to operate outside its internally-established timelines and lacks processing timelines for certain permits.

Our review of other district responsibilities disclosed that it follows procedures to ensure equal opportunity in contracting and employment. Also, we found the key functions and salaries of the district's legal office to be comparable to those of other districts. Further, the district generally complies with laws and procedures for managing the funding of research, development, and demonstration projects although it could improve its reporting of project results to the public. Finally, the district did not fully comply with guidelines against the stigmatizing or promoting of certain products.

Respectfully submitted,



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Summary

Audit Highlights . . .

Our review of the South Coast Air Quality Management District disclosed the following:

- ☑ ***The district's policy requiring only the largest polluters to pay emission fees is inequitable, resulting in 5 percent of those regulated paying 100 percent of the fees.***
- ☑ ***Generally, the district issues permits to construct within the required period; however, many permits to operate take longer than the district's internal timeline of 180 days.***
- ☑ ***The district follows procedures to ensure equal opportunity in contracting and employment; however, it did not always follow guidelines when disseminating public information about products.***

Results in Brief

The South Coast Air Quality Management District (district), which includes Orange County and parts of Los Angeles, Riverside, and San Bernardino Counties, is mandated to control air pollution using the best available and most cost-effective control technologies. To meet federal and state air quality standards, the district monitors emissions from stationary sources of pollution, such as factories and other businesses. Further, it established a permitting program for entities that construct and operate equipment that emits, or controls the emission of, air pollutants.

We found the district does not charge emission fees to all facilities that pollute. Its policy ensures that only the largest polluters pay—those facilities reporting emissions of four tons or more for most specified pollutants. For fiscal year 1995-96, only 1,400 (5 percent) of the 26,400 facilities regulated by the district paid the $21 million in emission fees it collected. Because only a small number of polluters pay emission fees, the method of charging these fees is inequitable.

The district regulates 25,000 other facilities that do not pay emission fees. Most of these facilities (22,500) do not report their emissions to the district because the district's emission billing system requires only a small percentage of facilities to report their actual emissions. Therefore, it does not know the magnitude of the actual emissions that these facilities produce, and we could not determine the full impact a proportionate-share rate structure would have on all participants. However, we believe that a proportionate-share rate structure would better ensure an equitable allocation of emission fees to those generating pollution in the district. By spreading out assessments, those who have not paid, and may collectively contribute a significant amount of emissions, would participate in the emission fee program.

Although the district lacks actual data on the emissions from the 22,500 facilities not required to report, it gathers information on their potential emissions as part of the permitting process. Based on information from the facilities, the district calculates an estimate of potential emissions. While not an exact measure, the district apparently believes this estimate is

reasonable enough to use in combination with other district data for planning and rule-making purposes. Our analysis revealed that nonreporting facilities represent 15 percent to 27 percent of the district's estimated emissions of several key pollutants.

We also found that the district generally issues permits to construct within the time period allowed in law; however, many permits to operate take longer than the district's internal timeline of 180 days. Further, the district lacks processing timelines for certain permits. Although some delays are caused by the applicant, district workload and additional permitting requirements affect its ability to promptly process permit applications. Delayed processing potentially allows some equipment to operate outside of district guidelines for longer periods of time, slowing and potentially negatively affecting air quality attainment.

In addition to falling short of its processing goals, the district does not charge enough in permit fees to recover its processing costs. In fact, the district's revenues from permit processing have fallen short of expenditures for several years. To reduce this gap, the district adopted several fee increases at its May 1998 board meeting. However, if the shortfall in fiscal year 1998-99 is similar to that in 1996-97, expenditures will exceed revenues by $4 million even after the fee increases are implemented. Thus, the district will continue to subsidize its permit processing operations with revenues from emissions and permit renewal fees.

Our review of other district responsibilities disclosed that it follows procedures to ensure equal opportunity in contracting and employment. Further, we found the key functions and salaries of the district's legal office to be comparable to those of other districts. However, although it appropriately selects research, development, and demonstration projects, the district could improve its reporting of results to the public and its documentation of monitoring efforts. Also, by not fully complying with its guidelines for publishing literature, the district leaves itself vulnerable to criticism that it provides an unfair advantage to manufacturers of certain products by implying a recommendation of the products.

Recommendations

To ensure that those facilities generating pollution in the district pay their proportionate share of emission fees, the district should take the following actions:

- Send a reporting form to all facilities in the district and assess fees based on actual emissions.

- Alternatively, the district could send each facility an annual emission bill based upon the facility's estimate of potential emissions. Each facility would have the option to pay the amount billed or provide the district with documentation on actual emissions.

To ensure that it issues permits within the time period allowed by law or its own internal timelines, the district should take the following actions:

- Continue to evaluate the permit process to reduce the time it takes to issue permits.

- Establish processing timelines for permits to operate that are currently not subject to its timelines.

- Ensure that permit fees are set to cover the costs of processing rather than depending on other revenue sources to subsidize the permitting function.

To avoid potential claims of unfair advantage from other manufacturers, the district should adhere to all its guidelines and policies when disseminating public information about products.

Finally, the district should ensure that it fully complies with reporting requirements for research, development, and demonstration projects and appropriately documents all monitoring efforts.

Agency Comments

Overall, the district disagrees with our characterization that it does not equitably charge emission fees. However, the district generally agrees with our recommendations regarding its permitting process. Additionally, it agrees with our recommendations related to the district's dissemination of public information about products and reporting on research, development, and demonstration projects. Moreover, while the district believes that it equitably charges emission fees and comments that our recommendations in this area may be administratively impracticable, it states that its fiscal year 1998-99 fee study will examine the issues presented.

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Introduction

The South Coast Air Quality Management District (district) is the regional air pollution control agency for all of Orange County and parts of Los Angeles, Riverside, and San Bernardino Counties. This area of 12,000 square miles is home to more than 14 million people and is the second most populous urban area in the United States.

The district, which began operations in 1977, is mandated to achieve and maintain federal and state air quality standards at the earliest possible date using the best available and most cost-effective control technologies. In fiscal year 1997-98, approximately 28,000 businesses and other entities operated under district permits. A governing board of 12 members oversees the district. The boards of supervisors of the counties appoint 4 members; the cities appoint 5 members; and the governor, speaker of the State Assembly, and rules committee of the State Senate each appoint a member.

Generally, the district monitors emissions related to stationary sources of pollution, which include factories and other businesses. The State Air Resources Board is primarily responsible for monitoring emissions from mobile sources such as automobiles and buses. Some estimates indicate that mobile sources generate at least 60 percent of the pollutants within the district while other estimates place the percentage even higher.

To regulate stationary emission sources, the district established a permitting program that applies to businesses and other entities. These facilities must obtain permits before constructing, installing, or operating equipment that emits, or controls the emission of, air pollutants, unless exempted. The permitting process helps ensure that emission controls meet the need for the district to make steady progress toward achieving and maintaining federal and state air quality standards.

With a fiscal year 1997-98 budget of $93.7 million, the district employs staff to conduct air quality analyses, promulgate rules, issue permits, and monitor compliance of a variety of stationary sources. The district generates approximately 70 percent of its revenue from stationary source fees and various other fees. The

remaining 30 percent comes primarily from California Clean Air Act motor vehicle fees, the federal Environmental Protection Agency, and the State Air Resources Board.

The district generates its stationary source fees from three primary sources. A portion comes from processing and issuing equipment permits. Permit fees depend on the type and emission potential of the equipment. Annual renewals of operating permits add additional revenue. The third type of fee is charged to businesses that release large amounts of six specific pollutants and is based on the quantity and specific emission. Under the current emission fee structure, only the largest polluters pay emission fees for the six pollutants. While not all facilities pay emission fees, all facilities with permitted equipment pay an initial permit processing fee and annual renewal fees.

In recent years, revenues have declined steadily, particularly those generated from emission fees. This decline negatively impacts the district's expenditures as well as its staff resources. In fiscal year 1991-92, the district reached its peak with a budget of $113 million and 1,163 budgeted positions. By fiscal year 1997-98, its budget declined to $93.7 million with 741 budgeted positions. Because of stricter air pollution standards and improved emission controls, facilities emit less pollutants, thus producing less in revenues for the district. Based on this trend, the district projects a potential budget decline to $87.6 million and a staffing reduction to 660 positions by fiscal year 2000-01.

Scope and Methodology

At the request of the Joint Legislative Audit Committee, we reviewed the management and fiscal affairs of the district. Specifically, we evaluated the revenue programs managed by the district and determined if the relationship between facilities' emissions and the fees they pay is reasonable. Also, we determined the length of time it takes for the district to issue permits. In addition, we assessed the district's allocation of funding to research, development, and demonstration projects and determined the relevance of such projects to programs or emission sources in the district. Finally, we assessed the district's policies to ensure equal opportunity with respect to contracting and employment, evaluated the function of the district's public affairs office and determined whether it promotes or stigmatizes certain products or services in a manner that limits competition, and evaluated the functions of the district's legal office.

To gain an understanding of the district and the programs it operates, we reviewed pertinent laws, regulations, and other background information.

To evaluate the district's revenue programs and to determine if the relationship between fees and emissions is reasonable and equitable, we identified fees assessed on the basis of emissions. We analyzed the district's data on actual emissions reported by facilities and compared them to the emission fees paid. Additionally, we considered the magnitude of unreported emissions by reviewing district estimates of potential emissions.

To determine how long it takes the district to issue permits, we reviewed the time it takes to issue permits to construct and permits to operate. To determine reasons for delays, we interviewed engineers and reviewed permit application files.

As part of assessing the district's allocation of funding to research, development, and demonstration projects, we reviewed several projects to determine the extent to which such projects relate to the district's programs or emission sources. Additionally, we determined if the district followed appropriate procedures for selecting, monitoring, and reporting on projects.

We also reviewed the district's contracting policies and equal opportunity procedures. We evaluated the district's outreach program and criteria it uses in reviewing and selecting competitively bid contracts and reviewed contracts exempted from the competitive bid process for reasonable justification.

Further, we reviewed the district's policies and procedures for equal opportunity in employment. Because the district hired few employees during the period we reviewed, we did not focus on specific hiring procedures. Rather, we analyzed the district's workforce before it downsized to determine whether changes affected staff demographics or demonstrated patterns of inequity. We also reviewed the procedures the district followed during downsizing to determine if they were fair.

Additionally, we reviewed the functions of the district's public affairs office by determining if they are authorized by state law or consistent with the district's mission. To determine whether it promotes or stigmatizes certain products or services, we reviewed the policies and procedures that the public affairs office follows, as well as selected brochures and newsletters that it issues.

We reviewed the functions of the district's legal office to assess if they are authorized by law and reasonable. We also compared its key functions, salaries, and budgets with those of

other air quality management districts within the State, such as the Bay Area Air Quality Management District, San Diego County Air Pollution Control District, San Joaquin Valley Unified Air Pollution Control District, and Santa Barbara County Air Pollution Control District.

Chapter 1

The South Coast Air Quality Management District Does Not Charge Emission Fees Equitably

Chapter Summary

The South Coast Air Quality Management District (district) charges emission fees to only the largest polluters. Our audit shows that for fiscal year 1995-96, only 1,400, or 5 percent, of the 26,400 facilities regulated by the district paid all of the $21 million in emission fees collected. The 1,400 paid because they were the only ones reporting emissions at or above the established threshold—four tons for most of the specified pollutants. However, the district regulates 25,000 other facilities that do not pay emission fees, and most of these facilities (22,500) do not report their emissions to the district. Because the district's policy results in only a small number of polluters paying emission fees, the method of charging these fees is inequitable.

If the district charged facilities based on their proportionate share of emitted pollutants, the responsibility for payment of emission fees would be distributed to more facilities. By spreading out assessments, the fees charged to current payers would decrease and those who have not paid would now participate in the emission fee program. However, because the current process requires only a small percentage of facilities to report their actual emissions, the district does not know the magnitude of the actual emissions the 22,500 nonreporting facilities produce. We used district estimates rather than actual emissions as a measure of the potential pollution generated by these nonreporting facilities. This analysis reveals that the nonreporting facilities represent 15 percent to 27 percent of the district's estimated emissions of several key pollutants. Because we could not determine the actual amount of pollutants per facility, we could not determine the full impact a proportionate-share rate structure would have on all participants. Nevertheless, the district is able to obtain information that would allow it to implement such a structure. We believe that a proportionate rate structure would better ensure an equitable allocation of emission fees to those generating pollution in the district.

The District's Fee Structure Results in a Few Large Polluters Paying All the Emission Fees

For fiscal year 1995-96, the district's emission fee structure resulted in only 5 percent of all facilities paying 100 percent of the fees collected. Although these 1,400 facilities emit the majority of the reported pollutants, the district regulates 25,000 other facilities that do not pay emission fees. Further, most of the 25,000 facilities do not report their emissions to the district.

Only a small percentage of the facilities pay because the district only charges fees to facilities that produce above a specified threshold of emissions. Furthermore, the magnitude of pollutants drives the fee level assessed to large polluters. Specifically, the more a facility pollutes, the higher the fee per ton. As a result, 100 top polluters paid 82 percent of the fees for fiscal year 1995-96, or $17.3 million of the $21 million collected. Additionally, the top 8 polluters paid $10.8 million, or 51 percent, of the fees.

Of the 26,400 facilities regulated, 100 pay 82 percent of the fees and, of those, 8 pay 51 percent.

The district's fee structure differs from the fee structure of the San Diego County Air Pollution Control District (San Diego)—one of the larger collectors of emission fees among other air quality districts. Because of the district's size and level of air pollution, it is difficult to compare it to other air quality districts. However, it is important to note that San Diego employs a type of proportionate-share rate structure that allocates fees to all permitted facilities by grouping them into various categories. It allocates emission fees to all permitted facilities based on either an actual emissions inventory of the facility or estimated emissions for a category. Further, the fee per ton is the same regardless of the amount of pollution emitted. Although the amount of fees generated by San Diego is significantly lower, $900,000 for fiscal year 1996-97, spreading the cost among the regulated population is still a valid concept. We estimate that if the district used some type of proportionate-share methodology for the six primary pollutants measured, from 1.6 percent to 36.4 percent of the fee assessments would shift from the top 1,400 polluters to the other 2,500 reporting facilities. In fact, if the fees were spread proportionately to all facilities in the district that emitted the six pollutants, we would expect the fees to be spread to even more of the 25,000 facilities that are not currently paying.

State law allows the district to establish its own emission fee structure. The district established its fee schedule in 1977 and set the current threshold for paying in 1991. It charges fees for six specified pollutants based upon tons emitted per year.

It charges a fee per ton to those facilities reporting 4 tons or more per year of any one of the six pollutants. An exception to this threshold is carbon monoxide, which the district charges on emissions of more than 100 tons. It assesses a fee per ton beginning with the fourth ton, and each ton over 100 for carbon monoxide. Thus, all facilities are exempted from any emission fee for up to 4 tons of five of the six specified pollutants and the first 100 tons of carbon monoxide. Further, the district uses a graduated fee schedule with a different base fee for each pollutant to reflect the relative health impact of each. Therefore, facilities that emit more pollution, or pollutants with higher health impacts, pay higher fees.

In addition to the six specific air pollutants, the district collects emission fees from any facility emitting toxic air contaminants, based on each pound emitted. Toxic air contaminants are pollutants that may produce adverse health effects, even at very low levels. We focused our review of emission fees on the equity of the rate structure for the six air pollutants only, because fees for the toxic air contaminants are already assessed proportionately.

The Current Fee Structure Charges Emission Fees Disproportionately

When we attempted to illustrate the extent to which the district disproportionately charged emission fees, we were constrained by the district's lack of information regarding the actual amount of pollutants emitted by facilities. We analyzed the emission information for fiscal year 1995-96 because that was the latest and most complete data available at the time of our review. However, for that year, the district only had actual emission data for 3,900 of its 26,400 regulated facilities. This is because the district only requests facilities to report under certain conditions—primarily if the facilities have the potential to emit three or more tons of pollutants. Despite this incomplete information, based upon the 15 percent of facilities providing emission data, we can demonstrate that measurable amounts of pollutants are emitted by facilities that do not pay fees.

Measurable amounts of pollutants are emitted by facilities that pay no emission fees.

For example, the 1,007 facilities paying organic gas emission fees emitted only 87.4 percent of the reported emissions. Conversely, 2,552 facilities generated 12.6 percent of these emissions but paid nothing. For each of the six pollutants, we determined the total amount of emissions reported, including facilities reporting four tons or more, as well as those with emissions of less than four tons. Table 1 details this data.

Table 1

Nonpaying Facilities Emit Measurable Amounts of Pollution Based on Emissions Reported by 3,900 Facilities for Fiscal Year 1995-96[1]

Pollutants	Facilities Reporting		Amount Reported	
	Actual	Percentage	Tons	Percentage
Organic gases				
Facilities reporting 4 tons or more	1,007	28.3	20,820	87.4
Facilities reporting less than 4 tons	2,552	71.7	2,998	12.6
Total	**3,559**	**100.0**	**23,818**	**100.0**
Nitrogen oxides				
Facilities reporting 4 tons or more	475	21.4	28,257	94.9
Facilities reporting less than 4 tons	1,743	78.6	1,520	5.1
Total	**2,218**	**100.0**	**29,777**	**100.0**
Sulfur oxides				
Facilities reporting 4 tons or more	51	4.4	9,210	98.4
Facilities reporting less than 4 tons	1,112	95.6	145	1.6
Total	**1,163**	**100.0**	**9,355**	**100.0**
Particulate matter				
Facilities reporting 4 tons or more	173	10.0	4,382	87.5
Facilities reporting less than 4 tons	1,564	90.0	627	12.5
Total	**1,737**	**100.0**	**5,009**	**100.0**
Specific organics				
Facilities reporting 4 tons or more	12	17.6	343	91.0
Facilities reporting less than 4 tons	56	82.4	34	9.0
Total	**68**	**100.0**	**377**	**100.0**
Carbon monoxide				
Facilities reporting more than 100 tons	30	1.5	8,900	63.6
Facilities reporting 100 tons or less	2,033	98.5	5,093	36.4
Total	**2,063**	**100.0**	**13,993**	**100.0**

[1]This table only includes reported emissions. Since the district does not require all emissions to be reported, the total emissions are unknown.

Knowing that facilities, other than those currently assessed fees, emit pollutants, we analyzed the fees collected for fiscal year 1995-96 to determine the impact the district's policy has on fee payers. Table 1 above shows the amount of emissions for facilities reporting emissions above the threshold, as well as for those facilities reporting below the threshold and thus not paying emission fees. We calculated the percentage of tons reported for the two groups to ascertain the level of fees each group would pay using a proportionate share method. For example, we applied 12.6 percent to the total $7.3 million collected for emissions of organic gases to determine the

amount of fees attributable to those facilities that report but do not pay. We calculated that nonpaying facilities would owe $923,000 of this fee assessment. Table 2 shows how applying a proportionate share method, even on the 3,900 reporting facilities, changes the distribution of emission fees. Overall, with nonpaying facilities emitting from 1.6 percent to 36.4 percent of pollutants, $1.6 million of the $21 million collected is attributable to facilities reporting emissions but not meeting the current payment threshold.

Table 2

Emission Fees Estimated for Fiscal Year 1995-96 Based on a Proportionate Share of Reported Emissions[1]

Pollutants	Fees Currently Collected	Percentage of Emissions	If a Proportionate Share Were Used
Organic gases			
Facilities reporting 4 tons or more	$7,322,000	87.4	$ 6,399,000
Facilities reporting less than 4 tons	--	12.6	923,000
Total	**$7,322,000**	**100.0**	**$ 7,322,000**
Nitrogen oxides			
Facilities reporting 4 tons or more	$8,561,000	94.9	$ 8,124,000
Facilities reporting less than 4 tons	--	5.1	437,000
Total	**$8,561,000**	**100.0**	**$ 8,561,000**
Sulfur oxides			
Facilities reporting 4 tons or more	$3,824,000	98.4	$ 3,763,000
Facilities reporting less than 4 tons	--	1.6	61,000
Total	**$3,824,000**	**100.0**	**$ 3,824,000**
Particulate matter			
Facilities reporting 4 tons or more	$1,349,000	87.5	$ 1,180,000
Facilities reporting less than 4 tons	--	12.5	169,000
Total	**$1,349,000**	**100.0**	**$ 1,349,000**
Specific organics			
Facilities reporting 4 tons or more	$ 24,000	91.0	$ 22,000
Facilities reporting less than 4 tons	--	9.0	2,000
Total	**$ 24,000**	**100.0**	**$ 24,000**
Carbon monoxide			
Facilities reporting more than 100 tons	$ 20,000	63.6	$ 13,000
Facilities reporting 100 tons or less	--	36.4	7,000
Total	**$ 20,000**	**100.0**	**$ 20,000**
All pollutants			
Facilities currently reporting and paying			$ 19,501,000
Facilities currently reporting but not paying			1,599,000
Total			**$ 21,100,000**

[1]This table only reflects reported emissions. Since the district does not require all emissions to be reported, the total emissions are unknown.

It is important to note that currently the district only requests facilities to report under certain conditions—primarily if they have the potential to emit three or more tons of pollutants. It is reasonable to expect that the facilities currently not reporting could collectively emit sizable amounts of pollutants.

District Estimates Indicate That Nonreporting Facilities May Emit Significant Pollution

When one considers the amount of pollution that nonreporting facilities may emit, the district's current rate structure seems even more inequitable. For fiscal year 1995-96, approximately 22,500, or 85 percent, of the facilities it regulates were not requested to report emissions under the current process. Because the district does not request these 22,500 facilities to report, it does not know the magnitude of actual emissions they may produce; however, the district has estimated data indicating that these facilities may collectively emit significant amounts of pollutants.

Because only 15 percent of the facilities report their actual emissions, the district does not know the magnitude of actual emissions the remaining 85 percent produce.

Although the district lacks actual data on the emissions from nonreporting facilities, it gathers information on their potential emissions as part of the permitting process. The facilities' permit applications provide information regarding the types of equipment, pollution control devices, and level of operations to be used by the facility. This information enables the district to estimate how much pollution a piece of equipment with specific pollution control devices, operated at a specified level, will produce during a year. The district calls this estimate of potential emissions the R2 value. While not an exact measure of emissions, the district apparently believes the R2 value is a reasonable estimate because it uses it in combination with other district data for planning and rule-making purposes.

The facilities that reported emissions for the three highest revenue-producing pollutants—organic gases, nitrogen oxides, and sulfur oxides—had R2 values representing between 73 percent and 85 percent of the total estimated emissions. Therefore, the facilities not reporting actual emissions had R2 values between 15 percent and 27 percent of the total estimated emissions. Although the emissions from each of these nonreporting facilities may be small, collectively they may comprise a significant amount of emissions. Additionally, our estimate of potential emissions from nonreporting facilities may be conservative. The district's database indicates that many facilities have R2 values of zero for specific pollutants. Certain facilities may appropriately have a zero R2 value.

However, to the extent that these nonreporting facilities incorrectly have R2 values of zero, the total potential emissions could be even greater. Thus, we believe nonreporting facilities should pay at least some emission fees.

The district indicates that under its current system of collecting emission fees, assessing these fees on small polluters would reach a point of diminishing returns. Based on data from fiscal year 1993-94, the district estimated that it would collect an additional $1.2 million in emission fees if it lowered the threshold from four tons to two tons. It estimated that $1.1 million would come from facilities that currently pay and $134,000 would come from 675 facilities that currently do not pay emission fees. Further, the district estimates additional administrative costs, if it lowered the threshold to two tons, of $685,000 for each of the first three years and $575,000 each additional year, assuming it uses its current emission fee system. In addition, the district believes that the smaller polluters will require greater assistance, and that it has insufficient resources to cover these additional costs.

We believe the district based its position on incomplete data. Specifically, its estimate of revenue is understated because the district did not consider the revenue potential of facilities that emitted less than two tons in fiscal year 1993-94. Additionally, the district does not know that the amount of emissions from facilities in the two-ton to four-ton range in fiscal year 1993-94 is representative of the current emissions from facilities in this range. Also, the district's cost analysis assumes that it would use its current reporting system to collect the emission fees. However, a simplified reporting process would minimize the additional administrative costs. The district could tailor its reporting process in proportion to the level of emissions and revenue expected from each facility. For example, the district could create a reporting form for small polluters designed to simplify its review, as it has done for automobile dealers. Also, the added administrative costs of reviewing and monitoring these additional facilities' reporting forms need not be as extensive as for the large facilities. In addition, the district could continue to focus most of its reviews on the large polluters, where errors could significantly affect the amount of emissions reported and, therefore, the amount of fees collected. Furthermore, the more accurate information on emissions would be advantageous in other management applications such as planning and rule making.

Simplified reports tailored to the type of business or equipment could minimize administrative costs of requiring all facilities to report.

Conclusion and Recommendations

Although we agree with one of the premises underlying the South Coast Air Quality Management District's (district) emission fee policy, which is that large polluters bear the majority of regulatory costs because they pollute the most, we disagree with its methodology. Because 95 percent of regulated facilities do not pay any emission fees, the current practice of requiring only the largest polluters to pay fees is inequitable. A proportionate assessment policy would effectively ensure that large polluters bear the majority of the regulatory attention as well as the costs, and still assure other regulated facilities share these costs. Therefore, we recommend the district take the following actions:

- Send a reporting form to all facilities in the district and assess the facilities a fee based on actual emissions. This is the same method the district currently uses for the facilities that now report. The district could tailor each reporting form to the type of facility reporting. For example, a small restaurant would have a simple form, while a large manufacturer would have a more complex form. Again, this would be similar to the district's current method, where automobile dealers' reporting forms are much simpler than those for oil refineries. Using reporting forms tailored to the type of facility would simplify the district's monitoring and review process and minimize any additional administrative costs.

- Alternatively, the district could send each facility an annual emission bill based upon the facility's R2 value, an estimate of emissions based upon equipment and operation information provided by the facility. Each facility would have the option to pay the amount billed or provide the district with documentation on actual emissions. For example, in its application, a facility may indicate it will operate six days per week, and its R2 will reflect this level of operation; however, if the facility only operated five days per week, the fee would be reduced accordingly. In the absence of actual reported data, we believe the R2 value may be a reasonable starting point for measuring emissions from and collecting fees from facilities. This method is consistent with the district's current practice of using the R2 value in combination with other data for planning and rule making.

- Assure that its June 1998 contract to study the structure and equity of its fees includes an assessment of the issues identified in this report to address fairness and equity in its emission fee program. The district anticipates that the study will be completed by January 1999.

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Chapter 2

The South Coast Air Quality Management District's Permitting Operation Continues to Face Challenges

Chapter Summary

Although the South Coast Air Quality Management District (district) generally issues permits to construct within the time period allowed by law, many permits to operate take longer than the district's internal timeline of 180 days to issue. In addition, the district has not established processing timelines for certain permits. Although some delays are caused by the applicant, district workload and additional permitting requirements affect its ability to promptly process permit applications. Delayed processing potentially allows some equipment to operate outside of district guidelines for longer periods of time, slowing and potentially negatively affecting air quality attainment. In addition to falling short of its processing goals, the district does not charge enough in permit fees to recover processing costs. With new permitting requirements taxing resources, the district will continue to face the challenge of meeting statutory and internal timelines.

Although the District Generally Issues Permits to Construct According to Law, It Does Not Always Comply With Internal Timelines for Issuing Permits to Operate

The district generally issues permits to construct within the 180 days required by law. For example, for the fourth quarter of 1997, the district issued 91 percent of its permits to construct within the 180-day time frame. However, 49 percent of the permits to operate issued during the same time period took longer than the internally established 180-day timeline.

Any equipment that may cause or control air pollution requires a permit from the district, unless specifically exempted. The permit is a written authorization to construct, install, or operate the equipment. The district also requires a permit when a business using such equipment changes ownership, moves equipment to another location, or proposes a change in operating conditions. Businesses applying for permits could be

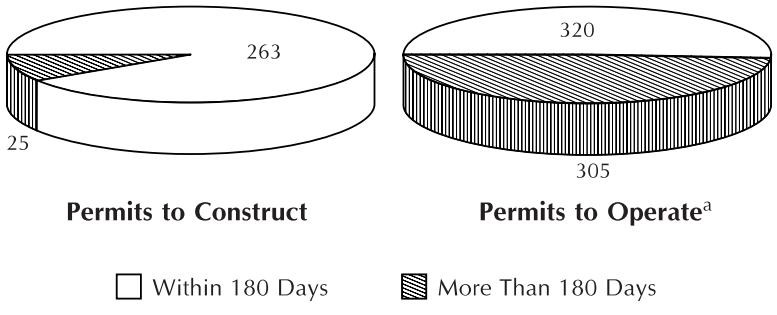
a neighborhood dry cleaner or a large oil refinery. Annually, the district processes about 12,000 applications for permits to construct and permits to operate. The district does not approve all permit requests; some applications are canceled or denied, or they expire.

The California Government Code, beginning with Section 65920, known as the Permit Streamlining Act (act), requires a public agency to approve or disapprove a development project within 180 days of accepting the application. The act applies only to permits to construct and not to permits to operate. The California Health and Safety Code, beginning with Section 42320, titled the Air Pollution Permit Streamlining Act of 1992, requires districts to designate projects as minor, moderate, or major and to establish a permit action schedule for each designation. The district developed the following internal processing guidelines: 7 days for minor projects, 30 days for moderate projects, and 180 days for major projects. The guidelines are intended to apply to all permit applications except for permits to operate that result from previously-issued permits to construct. The district no longer considers this type of transaction an open application pending its action since the facility must complete construction and related testing, which may take several months or years.

During the fourth quarter of 1997, the district issued 288 permits to construct and 1,623 permits to operate. We focused our review of permits to operate on the 625 classified as major projects and subject to the internal 180-day guideline. Figure 1 displays the district's performance at meeting the 180-day deadline.

Figure 1

South Coast Air Quality Management District
Permits Issued Within 180 Days
Fourth Quarter 1997



[a] This figure does not include permits for major projects not subject to internal guidelines and minor or moderate projects the district expected to complete within 7 or 30 days.

As shown by Figure 1, the district issued 263, or 91 percent, of the 288 permits to construct within 180 days. However, it was not as successful in issuing permits to operate promptly. For the 625 permits designated for 180-day processing, the district issued 305, or 49 percent, after the deadline. It took from 181 to 3,259 days to issue these delayed permits.

The district places a high priority on processing permits to construct to minimize the effect that delays might have on a business's operations. Delaying the construction, installation, or modification of equipment could postpone the start-up of a business or the use of equipment, resulting in potential revenue loss to the business. Because a permit to construct serves as a temporary permit to operate, the facility can use the equipment once it is constructed while waiting for the district to issue the permit to operate. Similarly, an application for a permit to operate, with some exceptions, serves as a temporary permit to operate, so business operations are likewise not halted during the processing period.

We reviewed five of the permits to construct that took more than 180 days to issue. The number of days to issue these permits ranged from 225 to 600. The reasons these five took more than 180 days varied. For example, the permit that took 600 days, or more than one and a half years, to process required public notice to be sent to nearby residences. The applicant took nearly a year of that period to complete the 30-day public notice requirement.

Permit processing priorities or a backlog of applications partially contributed to some significant delays caused by the district.

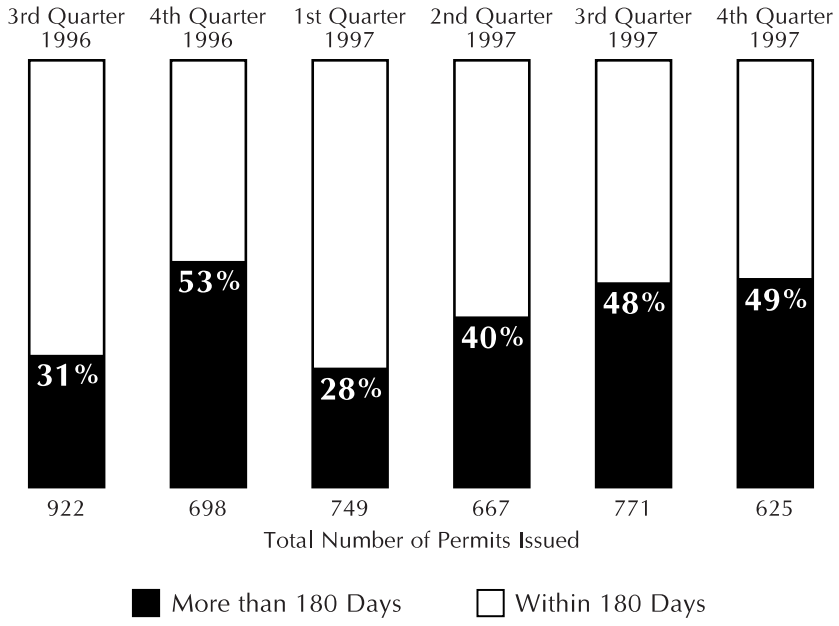
We also selected for review ten of the applications for permits to operate for which the internal guidelines applied and which took longer than 180 days to issue. We found that the district caused delays in seven cases, and both the district and the applicant contributed to delays in three applications. One of the seven permits where the district caused delays took 3,222 days, or almost nine years, to issue. The long delay was a result of several factors that included negotiations with the industry to develop emission factors and applicable rules for the affected equipment. Six of the seven applications were delayed at least partially because of a backlog of applications or district policy placing a lower priority on processing permits to operate. One of these six applications, which took 693 days to process, documented contact with the applicant in which its lower priority was cited as the reason the application had not yet been processed. Further, the district's backlog, coupled with the applicants' nonpayment of fees or slow responses to district requests for information, contributed to the delays in the three applications in which delays were both district- and applicant-caused.

The District Has Consistently Experienced Delays in Issuing Permits to Operate

In addition to our review of the fourth-quarter 1997 data, we looked at the permitting data for the previous five quarters and determined that the district issued 4,432 permits to operate that it classified as major projects and that were subject to the internal 180-day guideline. We found that the district took more than 180 days to issue 1,807, or 41 percent, of these permits. Further, the district issued a significant percentage of permits later than the 180-day timeline in each of the six quarters we reviewed. The portion of late permits ranged from 28 percent to 53 percent. Figure 2 below depicts the issuance patterns of 180-day permits to operate over an 18-month period beginning in July 1996.

Figure 2

The District Experienced Delays in Issuing Permits to Operate in Each of the Six Quarters We Reviewed[a]



[a] This figure does not include permits for major projects not subject to internal guidelines and minor or moderate projects the district expected to complete within 7 or 30 days.

Delays in permit processing may potentially affect the district's air quality. The longer equipment is operating without evaluation, the longer it could potentially be polluting at levels outside district-imposed thresholds. The threat of additional emissions due to processing delays may be reduced by the district's policy of placing a higher priority on certain applications. Because the district organizes engineers and inspectors into teams that monitor like industries, inspectors can alert reviewing engineers to potential problems with pending applications. Although the effect of delays on air quality may not be significant, the district should continue to consider air quality goals when establishing processing priorities.

The District Needs Guidelines for All Permits

Nearly 13 percent of the permits to operate that the district designated as major projects, issued over the six quarters we reviewed, were not subject to any processing goals. As discussed previously, the district does not establish internal processing timelines for permits to operate that result from previously-issued permits to construct. The district issues these permits to operate once the equipment is constructed and the applicant has demonstrated it can comply with all applicable rules and regulations. The district states that it has not established internal guidelines because the transition from a permit to construct to a permit to operate is dependent on action by the facility applying for the permit. However, once the facility fulfills its part of the process, the permit to operate is once again dependent upon district action. Thus, we believe that the district should establish processing goals for these permits as well.

Nearly 13 percent of the permits to operate for major projects were not subject to any processing goals.

A meaningful measure of processing performance for these permits could begin from the date construction is complete. However, because the district does not track that date, for lack of a better measure, we counted the days to issue the permit from the date the permit to construct was issued. Using this measure, 502, or 78 percent, of the 647 permits of this type issued during the six quarters we reviewed, took longer than 180 days to issue.

We reviewed five of the permits to operate that were not subject to district guidelines but took longer than 180 days to issue. The reasons for the long processing times varied; however, not all delays resulted solely from construction delays or other delays by the applicant. For example, one permit to operate took 1,705 days to issue. The prior permit to construct was issued in 44 days, but construction took more than 500 days to

complete. The remaining processing delay resulted from the district's permitting workload and the lower priority placed on issuing permits to operate. If it tracked the construction completion date or designated some other action as the tracking date, the district could set reasonable timelines.

Processing Permits Promptly Is a Continuing Challenge for the District

Downsizing cut permitting staff by 24 percent, but workload did not decline, threatening to increase an existing backlog.

As explained in the Introduction, due to declining revenues, the district downsized, significantly reducing staff. Staff responsible for approving permits decreased from 156 in fiscal year 1993-94 to 119 in the following fiscal year. While staff reductions took place, the number of permit applications received did not decrease, threatening to increase an already existing backlog.

The district made a major effort to reduce its backlog that had grown to nearly 30,000 by mid-1990 to under 8,000 by early 1994. The district accomplished the reduction by concentrating all available permit processing resources on trimming the backlog. After reducing the backlog, the district continued to streamline the permit process. Some of these efforts include the following:

- Simplifying permit application forms.
- Introducing over-the-counter permitting.
- Certifying over 900 models of equipment as meeting district requirements.
- Expediting large-project permitting through the Green Carpet program for eligible firms that create jobs or develop advanced air pollution control technology.
- Providing instructions, forms, and electronic permit filing through an Internet homepage.

Despite these streamlining efforts, the district is not processing many of its permits to operate promptly, as previously discussed. Additionally, the district is facing new challenges that will create more difficulties in meeting permit deadlines in the future. In particular, the district is in the first phase of implementing Title V, a federally mandated operating permit program. Beginning March 31, 1997, the district has three years to issue permits for affected facilities. A Title V permit is a

single-facility permit consolidating and replacing all of the previously issued permits for individual pieces of equipment. Title V does not include any new requirements for reducing emissions, but it does include new permitting, noticing, monitoring, record keeping, and reporting requirements. Title V permits incorporated more than 3,000 existing equipment permits into the first group of 300 facilities. Further, more than 400 facilities have submitted Title V applications for processing, while a second phase will become effective in the year 2000, encompassing additional facilities. Because Title V consumes many hours of staff time and diverts them from processing other permits, the district needs to continue focusing its efforts to ensure it appropriately allocates resources and conducts its permit processing efficiently and effectively.

The district acknowledges that it needs to process permits faster. To help address this problem, the district recently appointed a permit streamlining task force and ombudsman with the goal to improve efficiency and customer service. Additionally, the district plans to contract with an outside consultant who will conduct an evaluation of the district's permitting process and recommend steps to reduce the time for issuing permits.

The District Does Not Collect Enough Permit Processing Fees to Recover Its Costs

Permit revenues consistently fall short of expenditures, requiring the district to cover costs with other revenues.

The district faces the challenge of processing permits promptly in an environment where funding shortfalls have frequently existed. The district's permit processing fee revenues have fallen short of expenditures for several years. The California Health and Safety Code, beginning with Section 40500, establishes the district's authority to adopt rules and regulations, including fee schedules, to cover actual costs for controlling and reducing air pollution. District Rule 301 establishes permit fees, which include permit processing, annual operating permit renewal, and annual emission-based fees. Permit processing fees are tied to the complexity of compliance review required and the emission potential of the equipment to be permitted. The district bases the permit processing fee on the average costs to process a permit. Federal law requires the district to establish fees sufficient to cover all costs required to develop and administer the Title V permit program.

The district subsidizes permit processing costs with revenues from annual renewal fees and annual emission fees. The revenue and expenditure comparison in Table 3 represents direct costs for issuing permits and does not include related

costs, such as legal advice, permit risk assessment, customer service, and operational support. The district's director of finance acknowledges that permit processing fees are insufficient to cover permit processing costs. He states that, while the district attempts to cover program costs with program revenues, staff interpret state law to allow the use of all available stationary-source permit revenue to fund any permitted source programs.

Table 3

Permit Processing
Revenues and Expenditures
(In Millions)

Year	Fiscal Year 1992-93	Fiscal Year 1993-94	Fiscal Year 1994-95	Fiscal Year 1995-96	Fiscal Year 1996-97
Revenues	$10.4	$ 9.0	$ 7.1	$ 7.6	$ 5.5
Expenditures	12.8	12.6	10.7	11.0	11.7
Shortfall	**$(2.4)**	**$(3.6)**	**$(3.6)**	**$(3.4)**	**$(6.2)**

The district's director of finance states that various factors contribute to the revenue shortfall including discounts for small businesses, as well as discounts for similar or multiple equipment or equipment installed in a series. For example, some operators may install air pollution control devices in a series to improve how efficiently the equipment filters air pollutants. For several years, the district has allowed discounts for such multiple devices. However, multiple control devices operating in a system are more complex to review and approve than those same devices operating separately. District staff acknowledge that they save no labor costs in evaluating these types of permit applications, since the emission reduction contributions of each device must be evaluated separately.

Adding to the shortfall, existing Title V fees also do not recover the costs of processing these permits. When the district began administering the Title V program, it underestimated the related processing time. The application fee of $786 was based on an estimated processing time of 10 hours. However, the district found that it took an average of 28 hours to complete the review process for some of the smaller facilities. As a result, the district concluded that it undercharged each applicant by $1,400. For larger facilities, the average review time ranged from 78 hours to 471 hours, and a review of one public facility alone took 1,000 hours. In April 1998, the district reported it

The district grossly underestimated the time to process Title V permits, thus contributing $1.2 million to the shortfall in 1996-97.

collected $247,000 in permit processing fees for the first 300 Title V applications but spent more than $3.3 million to process these applications. Approximately $1.4 million of those expenditures occurred in fiscal year 1996-97, thus contributing about $1.2 million to that fiscal year's shortfall.

To better match revenues and expenditures, the district board adopted several permit processing fee increases at its May 8, 1998, meeting, including the following:

- A consumer price index increase of 2.2 percent.
- Reduction from 75 percent to 50 percent in the discount for identical equipment.
- Elimination of multiple discounts.
- Creation of a tiered Title V fee structure to include an initial fee per device and a time-and-materials charge for time exceeding hours covered by the initial fee.
- Increased fees for voluntary express application processing.

The district estimates that the permit processing fee increases and related changes will generate approximately $2.2 million in additional revenue in fiscal year 1998-99. However, if shortfalls in 1998-99 are similar to those in 1996-97, the revenues including the estimated increase will not cover expenditures, and the district will continue to subsidize permit processing costs with revenues from renewal and emission fees.

Conclusion and Recommendations

Complying with statutory and internal permit processing timelines will continue to challenge the South Coast Air Quality Management District (district) as it faces new permitting requirements. The district appropriately prioritizes processing permits to construct and issues most within 180 days, in accordance with state law. However, the district does not always process permits to operate within the 180 days prescribed in its internal guidelines. Further, the district lacks internal processing timelines for certain permits to operate. While applicants caused some delays, others were due to district workload issues and processing priority policies. Additionally, the district does not charge enough in permit fees to recover processing costs. Therefore, we recommend the district take the following actions:

- Continue to evaluate the permit process to reduce the time it takes to issue permits.

- Establish processing timelines for permits to operate that are currently not subject to its timelines.

- Ensure that permit fees are set to cover the costs of processing rather than depending on other revenue sources to subsidize the permitting function.

Chapter 3

Additional Issues Reviewed, as Requested by the Legislature

Chapter Summary

In addition to examining the emission fee structure and permitting process of the South Coast Air Quality Management District (district), the Joint Legislative Audit Committee also asked us to review the following district responsibilities:

- Allocating and managing the funding of research, development, and demonstration projects.
- Ensuring equal opportunity in contracting and employment.
- Managing the public affairs office and its publications on products or services.
- Managing the legal office.

We found the district follows procedures to ensure equal opportunity in contracting and employment. Further, we compared the key functions and salaries of the district's legal office to those of other districts and found them to be similar. However, although it appropriately selects research, development, and demonstration projects, the district could improve its reporting of results to the public and its documentation of monitoring efforts. Also, the district does not always follow its own guidelines for disseminating information on products and services for regulated sources.

Allocating and Managing the Funding of Research, Development, and Demonstration Projects

The district generally complies with laws and procedures for managing the funding of research, development, and demonstration projects and appropriately uses funds available for promoting projects that deal with mobile-source as well as

stationary-source emissions. Based on the projects we reviewed, the district follows its policies and procedures for selecting and allocating funds to projects. However, the district did not fully comply with state law in reporting the results of projects. Additionally, the district did not always retain evidence that it appropriately monitored progress reports.

The district's Technology Advancement Office expedites the future implementation of advanced technologies and clean-burning fuels in Southern California to help achieve air quality standards. It meets this goal by entering into contracts with companies that do research and development to increase the use of clean fuels and clean air technologies. For example, the district partially funded a project to build and demonstrate a transit bus powered by a zero-emissions, fuel-cell engine. The success of this project has enabled the contractor to begin testing the fuel-cell bus with various transit authorities.

We reviewed 10 of the 65 research, development, and demonstration contracts completed during the 18-month period ending December 31, 1997. The 10 contracts we reviewed made up $4.5 million of the total $9.7 million the district spent on these contracts for that period. We determined that the district followed its key selection criteria, such as targeting projects with the potential to reduce emissions or the cost of emission control, or projects that displayed technological innovation. We also reviewed projects to determine if they related to the goals of the district, such as establishing technical feasibility, demonstrating current or potential State Air Resources Board standards or district rules, or enhancing emission databases. In addition, we reviewed the district's monitoring process of the projects to determine if it followed the appropriate procedures. In the contracts we reviewed, the district generally followed its procedures in using funds for their intended purpose, relating projects to the stated goals, and monitoring the progress of the various projects. However, the district did not retain progress reports for 1 of 10 contracts we reviewed, and we were unable to determine if it was properly reviewed by the project supervisor.

The district generally followed its procedures in using funds, relating projects to the stated goals, and monitoring the progress of the various projects.

Additionally, although state law requires a public report setting forth the project cost, results achieved, and assessment of actual to expected costs and benefits, the district does not always provide this information. Specifically, in our sample of 10 projects, 1 had no report, and 1 report did not compare the actual to expected costs of the project. When the district does not issue a public report or it does not include complete

information in its reports, the public is not appropriately informed of the results of the projects and how it spends money.

After we brought these matters to its attention, the district took action to strengthen its reporting procedures. In a memorandum issued April 22, 1998, the district's assistant deputy executive officer for the Technology Advancement Office introduced a new reporting policy. Together with the new policy, the district created a guide for project supervisors to follow that should, if used, ensure that the district obtains the information it needs to prepare the reports.

Ensuring Equal Opportunity in Contracting

The district follows contracting procedures designed to ensure equal opportunity. Specifically, we found that it has appropriate procedures to notify the community about upcoming contracts. Additionally, based on the contracts we reviewed, the district complies with its policies and procedures for competitively bidding contracts, evaluating bids, and awarding contracts based on its scoring process. Further, we found that the district has proper justification when it awards sole-source contracts, which do not require a competitive bidding process but must meet certain conditions.

We found the district has appropriate procedures for notification, competitive bidding, evaluation, and awarding contracts.

Within the past year, the district changed its contracting policies and procedures to comply with Proposition 209 by no longer awarding additional points to minority- and women-owned businesses in the competitive bidding process. This proposition approved by California voters prohibits discrimination against, or granting preferential treatment to, any individual or group on the basis of race, sex, color, ethnicity, or national origin in the operation of public employment, education, or contracts. Further, the district's contracting policy complies with Proposition 209 by not prohibiting action to maintain eligibility for any federal programs. For example, the federal Environmental Protection Agency (EPA) requires that a recipient of EPA funds make a good faith effort to use minority- and women-owned businesses when possible. The district has appropriate procedures to ensure that a good faith effort occurs for its EPA-funded contracts.

The district also has appropriate outreach efforts informing the community of the opportunities to contract with the district. The outreach process includes a list of contracts on its website,

a bidder hotline, public service announcements, newspaper advertisements, mailings to targeted organizations, and listings of contracts in the California state contracts register.

Further, for the 18-month period ending December 1997, the district awarded 52 contracts totaling $9.2 million that it competitively bid. We reviewed 10 contracts totaling $2.7 million and found that the district followed its policies and procedures for competitively bidding the contracts, evaluating the bids, and awarding contracts based on its scoring process.

The district's policy for contracts that are competitively bid consists of an evaluation of each proposal received. A panel of three to five district staff familiar with the subject matter evaluates the proposals according to specified criteria and assigns a numerical score to each evaluation factor. If deemed desirable by the executive officer, the panel may include outside public sector or academic community expertise. District staff recommend to the executive officer that the proposer with the highest score receive the contract. The executive officer or the board may award the contract to a proposer other than the one receiving the highest score if they determine that another proposer from among those technically qualified would provide the best value to the district considering cost and technical factors. Supporting rationale for such a determination must be provided. All contracts for $50,000 or more require board approval.

For the 18-month period ending December 1997, the district issued 65 contracts totaling $4.1 million that it awarded by sole source rather than through a competitive bid.

For the 18-month period ending December 1997, the district issued 65 contracts totaling $4.1 million that it awarded by sole source rather than through a competitive bid. The district's policy is to award a sole-source contract if it meets any of the following four justifications:

- Cost to prepare documents to obtain bids exceeds the savings that could be derived from such documents.
- Delay would endanger public health or property.
- Services are only available from one source.
- Other circumstances exist identifying sole source to be in the best interests of the district.

Most of the high-dollar, sole-source contracts we reviewed related to technology projects. Because of the new technology involved with such projects, many of the contracts are approved by the board with the justification that other circumstances exist identifying sole source to be in the best interests of the district. Specifically, the district justifies these contracts on such factors as the contractor's expertise, experience, and involvement in the particular field. Further, for technology projects, the district specifies a minimum level of cost sharing from outside sources as a requirement for the contract. We reviewed the sole-source justification for 10 contracts totaling $1.4 million and found that the district followed its policies and procedures.

Ensuring Equal Opportunity in Employment

The district followed policies and procedures to ensure equal opportunity in employment. We reviewed the district's recent annual reports for its affirmative action program that address the hiring goals for the district. A primary purpose of the program is to achieve a workforce that is balanced for minorities and females based on their representation in the district's relevant labor market. However, the district began a significant downsizing of its staff in fiscal year 1993-94 and has hired few staff in recent years. In fact, the district hired only seven people from July 1, 1996, through January 22, 1998. Therefore, we focused our review on the results of the downsizing rather than on specific hiring procedures. We found that the district followed proper procedures during the downsizing and that no one group was unfairly treated.

Due to declining revenues from emission fees, the district reduced its budget, so in fiscal year 1993-94 it began downsizing its workforce. Between July 1, 1993, and July 1, 1994, the district reduced its workforce from 967 to 797 employees. In subsequent years, the district has not replaced most of the employees, and additional employees have left. As a result, the district had 724 employees as of January 1998. During downsizing, through its agreement with its labor unions, the district followed certain procedures that required it to lay off all temporary employees first, followed by probationary employees, and then permanent employees. For permanent employees, within each job class, the lay-offs were in the order of performance evaluations, with the first group made up of people ranked "improvement needed." The next group laid off was the "satisfactory or commendable" group. The last to be laid off were the permanent employees rated as "outstanding."

Despite downsizing during the 1990s, the district's workforce demographics did not significantly change.

The downsizing did not significantly change the demographics of the district's workforce. We analyzed the downsizing several different ways to determine if any apparent trends existed. For example, we compared the total number and percentage of the district workforce by ethnic group for June 1993, before the downsizing occurred, to January 1998. Table 4 details the total number of district workforce by ethnic group and the percentage of workforce within the respective groups. The number of employees represents actual staff rather than budgeted positions. As the table shows, the percentage of workforce by ethnic group did not significantly change for the period we reviewed.

Table 4

South Coast Air Quality Management District
Workforce by Ethnic Group

	Number		Percent	
Workforce[1]	**June 1993**	**January 1998**	**June 1993**	**January 1998**
White	460	324	47%	45%
Asian or Pacific Islander	238	203	25	28
Hispanic	144	109	15	15
Black	117	82	12	11
American Indian or Alaskan Native	8	6	1	1
Totals	**967**	**724**	**100%**	**100%**

[1]Ethnic group classifications are those used by the U.S. Equal Employment Opportunity Commission.

In addition to the overall workforce analysis, we further evaluated the data by individual job category. Table 5 compares the percentage of workforce by ethnic group for June 1993 to January 1998 for three job categories: professionals, office/clerical, and technicians. Because there were less than 45 total employees in the officials/administrators, skilled craft, and service/maintenance categories, we did not include them in this analysis. As the table shows, within the individual job categories, there was no significant change in demographics of the workforce.

Table 5

South Coast Air Quality Management District
Percentage of Workforce by Ethnic Group
for Selected Job Categories

	Professionals		Office/Clerical		Technicians	
Workforce[1]	**June 1993**	**January 1998**	**June 1993**	**January 1998**	**June 1993**	**January 1998**
White	50%	48%	35%	35%	53%	49%
Asian or Pacific Islander	31	35	20	20	21	26
Hispanic	10	8	28	29	12	13
Black	9	9	17	16	13	12
American Indian or Alaskan Native	--*	--*	--*	--*	1	--*
Total percent	**100%**	**100%**	**100%**	**100%**	**100%**	**100%**
Total employees[2]	**430**	**328**	**227**	**178**	**266**	**186**

[1] Ethnic group classifications are those used by the U.S. Equal Employment Opportunity Commission.

[2] The combined total employees of the individual job categories shown in this table do not agree with the total workforce shown in Table 4 because this table does not include three job categories that totaled less than 45 employees.

*This group accounts for less than 1 percent of the workforce.

Managing the Public Affairs Office and Its Publications on Products or Services

We found that certain functions within the district's public affairs office are authorized by state law while other functions are in line with the district's mission. We also found that the district issued guidelines against the stigmatizing or promoting of certain products. However, in two issues of its newsletter, we found articles in which the district displayed particular products in a manner that did not fully comply with its guidelines.

The mission of the public affairs office is to promote the understanding of air quality issues and provide information regarding the district's regulatory and planning activities to the general public, businesses, local governments, minority groups, and environmental organizations. The public affairs office consists of the public advisor, two local government units, media communications, and a legislative office. The public advisor provides community outreach services and small-business assistance. The two local government units administer funding of local projects designed to reduce air

pollution from mobile sources and act as a liaison between the district and state and local governments. Media communications educates the public about the district's clean air programs and enlists public support for those activities. The legislative office promotes the district's clean air goals in the Legislature. We found that the goals of the public advisor complied with requirements in the California Health and Safety Code, Section 40448. We also found that the goals of the two local government units, media communications, and the legislative office meet the district's mission. We focused our review of the public affairs office on the production and distribution of information to the public.

The public affairs office educates the public about the district's mission and purpose through literature it publishes. The Health and Safety Code, Section 40730(b), allows the district to publish any factual, nonconfidential information on the air emissions of a product or service that complies with district regulations. However, that information cannot recommend any product or service.

The district's legal counsel interprets this law to mean that the district shall not endorse any particular product or service. The legal counsel issued guidelines to assist district staff when developing public information. However, the district did not fully comply with these guidelines in the information we reviewed. We reviewed 22 brochures issued by the public affairs office between 1990 and 1997 and eight newsletters issued between January 1997 and March 1998, which provide general information on how individuals within the region can help improve air quality. For example, the literature contained information on water-based cleaners and low-volatile organic-compound paints, and promoted public transportation.

Two district newsletters displayed products in a manner that did not fully comply with district guidelines that prohibit stigmatizing or promoting certain products.

Although the public affairs office followed its procedures for the 22 brochures we reviewed, two of the eight district newsletters we reviewed presented products in a manner that did not fully comply with its guidelines. Specifically, one article displayed a prominent picture of particular products, and the other article included the name of a particular product as an example. Neither article contained a disclaimer indicating that the district was not warranting the products' suitability for any particular purpose, as required. In addition, in neither instance could the district demonstrate that the products represented all those available within the mentioned category. Further, one of the articles displayed the district's trademarked logo with the particular product, which is against its guidelines. By not following its guidelines, the district may provide an unfair advantage to manufacturers of certain products.

Its legal counsel stated that the guidelines are intended to keep the district well within the boundaries of the law and thereby avoid any suggestion of impropriety. Moreover, the legal counsel believes one should not assume that any perceived violation of the guidelines constitutes an improper recommendation of any product or service. Further, the legal counsel stated that the two articles cited above either were not subject to the guidelines or generally met the guidelines, except for not including a disclaimer. For example, for the first article, the legal counsel stated that the article met the guidelines because it displayed all known products within the particular category; however, the district did not retain documentation of this. Additionally, the legal counsel stated that the placement of its trademark in the second article may have violated the letter of its guidelines but did not violate the spirit. Further, the legal counsel believes the caption in the second article clearly dispels any implication of a recommendation by stating the item displayed was an example of a type of clean air product. However, we believe situations such as these leave the district vulnerable to criticism from other manufacturers of similar products. Although the district disagrees with our conclusions, it stated that its legal office will review all publications for compliance with its guidelines in the future.

Managing the Legal Office

Key functions and salaries of the district's legal office are similar to those in other air quality districts.

Key functions and salaries of the district's legal office are similar to those of legal offices of other air quality districts that we reviewed. Certain functions within the legal office are authorized by state law. Additionally, the law requires the district to appoint a legal counsel and authorizes the legal office to litigate on behalf of the district. Furthermore, we found the key functions of the legal office to be in line with the duties and role of the district.

Due to the differences in size between the district and the other air quality districts, and the uniqueness of each legal office, it was difficult to make overall comparisons. For example, the district's budget of $95.8 million for fiscal year 1996-97 was the largest in the State among air quality districts. The budget of the next largest district, the Bay Area Air Quality Management District, totaled $29.3 million. Therefore, for the four we reviewed, we compared each air quality district's key functions and salary levels to those of the district.

The key legal functions performed by the surveyed air quality districts are similar to the district's key functions. The Bay Area and San Joaquin Valley districts each maintain a legal office within their operation; however, the San Diego and

Santa Barbara districts perform their legal functions using county counsel. San Diego and Santa Barbara counties each dedicate one attorney full time to the legal matters of their respective air pollution control districts, with any additional legal services provided by other county counsel staff on an as-needed basis.

The following are the common key functions:

- Governing board and district staff advice
- Litigation or litigation assistance
- Rule making and interpretation
- Planning advice
- Hearing board advice
- Permitting assistance
- Interagency communication and negotiation

The district's legal office also performs investigative functions performed by the other districts' compliance divisions. The Bay Area district recently moved investigations associated with one program to its legal office.

Additionally, the salaries of the district legal staff are comparable to those of other districts. Salaries of district lead positions of general counsel, district counsel, and district prosecutor for fiscal year 1996-97 ranged from $97,700 to $107,600, compared to $104,900 and $106,400 for the lead positions of the two other surveyed districts that employ their own legal staff. The district's senior and assistant legal counsel salaries ranged from $66,200 to $89,200, less than the Bay Area district's senior and assistant counsels, whose salaries ranged from $88,000 to $98,800.

Further, we compared the legal budget for the Bay Area district with the district because they were the only two with more than one attorney dedicated to legal matters. The district's fiscal year 1996-97 budget for the legal office was $3.6 million, and the Bay Area's budget was $579,000. The district's legal office budget is 3.7 percent of its total budget, while the Bay Area's budget for the legal office was 2.0 percent. Although the district's legal office percentage of total budget is higher than the Bay Area's, it appears reasonable given the additional investigative functions performed by the district's

legal office that the Bay Area's legal office did not perform until recently, and the overall difference in size and local air quality between the two districts.

Conclusion and Recommendations

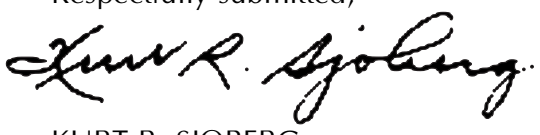
The South Coast Air Quality Management District (district) follows procedures that help ensure equal opportunity in contracting and employment. In addition, the key functions and salaries of the district's legal office are similar to the air quality districts that we surveyed. However, although it appropriately selects research, development, and demonstration projects, the district could improve its reporting of results to the public and its documentation of monitoring efforts. Also, the district needs to adhere more closely to its guidelines regarding disseminating information on products to avoid implying that certain products are being endorsed or promoted by the district. Therefore, we recommend the district take the following actions:

- Follow its new procedures for reporting on the results of its research, development, and demonstration projects and ensure that it appropriately documents all monitoring efforts.

- Adhere to all its guidelines and policies when disseminating public information about products to avoid potential claims of unfair advantage from other manufacturers.

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 governmental auditing standards. We limited our review to those areas specified in the audit scope section of this report.

Respectfully submitted,



KURT R. SJOBERG
State Auditor

Date: July 9, 1998

Staff: Karen L. McKenna, CPA, Audit Principal
Jeffrey A. Winston, CPA
Deborah M. Ciarla
Ken Cools
Brian Lewis, CPA

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Agency's response to the report provided as text only:

SOUTH COAST AIR QUALITY MANAGEMENT DISTRICT
21865 E. Copley Drive
Diamond Bar, CA 91765-4182
(909) 396-2000 • http://www.aqmd.gov

Office of the Executive Officer
909.396.2100, fax 909.396.3340

July 1, 1998

Kurt R. Sjoberg, State Auditor
Bureau of State Audits
660 J Street, Suite 300
Sacramento CA 95814

via fax to 916 327 0019, and via U. S. Mail

Attention: Mr. Jeff Winston

Dear Mr. Winston:

The South Coast Air Quality Management District appreciates the opportunity to comment and provide clarification on certain points in the draft audit report regarding this district. We suggest a few wording changes to clarify and/or correct statements, as summarized on Attachment A, and have the following response comments:

Chapter 1

The audit concludes that emission fees place an unfair burden on the largest polluting sources. The AQMD respectfully disagrees.

AQMD's emission fees are fair and equitable to large and small emitters because (1) every facility is equally exempt from fees for the first four tons of emissions; and (2) both large and small emitters pay similar total fees per ton of emissions.

No facility is charged in circumstances where another is exempt. This is somewhat analogous to the Federal and State income tax structure that provides all taxpayers, without regard to income, the same standard deduction for themselves and their dependents. Most importantly, because this audit focused on emission fees, it does not consider permit renewal fees. Both types of fees are annual operating fees, and together they cover the costs of the AQMD's programs related to permitted sources, except permit processing. When both fees are considered together, both large and small emitters pay similar total fees per ton of emissions. In 1995, the audit firm of KPMG Peat Marwick studied AQMD's emissions and renewal fees, and concluded (for the pollutant NOx) that the fees were proportionately charged and the fee structure

(1)* (2)

*California State Auditor's comments on this response begin on page 41.

was balanced.[1] AQMD staff believes that similar results would apply for the other pollutants. Therefore, the AQMD's overall fee structure is equitable. KPMG did, however, suggest that AQMD could consider extending emissions-based fees to all stationary sources of emissions.

(3) **Assessing emission fees on approximately 25,000 small sources that emit under four tons may be administratively impracticable.**

Sixty percent of these small sources have only one permit. The AQMD already goes well beyond the ten-ton threshold used by the U. S. Environmental Protection Agency to define a major source in implementing its emission fee program down to sources of emissions greater than four tons. AQMD staff believes it has sufficient information to make appropriate estimates of the emissions from small sources and is concerned that the statement that AQMD "does not know the magnitude of the actual emissions" from facilities not billed under the annual emissions billing system may be misleading. In the context of AQMP inventory, AQMD does know the magnitude of emissions from these small permitted sources. In addition, as part of planning and rule development, the emissions inventory always includes estimates for the non-reporting permitted facilities. AQMD staff would agree, however, that we do not know the actual emissions for each individual facility for billing purposes.

(4)

(5) **The fairness of AQMD's emission fee system is supported by the Legislature's judgment in establishing the State's Clean Air Act Fees program.**

State law[2] authorizes the California Air Resources Board to impose permit fees on nonvehicular sources to support costs in administering programs related to nonvehicular sources. By statute, these fees, based on actual emissions, are collected only from permitted sources that emit more than 500 tons annually.

AQMD's emission fees are based on actual emissions.

(6) California Health & Safety Code Section 40510(c)(2) — applicable only to the AQMD — limits its ability to base fees on the nature of the activities (potential emissions) at a stationary source. That law states: "The fees shall not be indexed to the potential emissions from, or to a percentage of the emissions trading units held by, any source." This may hinder basing fees on some surrogate for emissions, such as R2 factors. The law does not limit other districts, such as San Diego (to which the State Auditors compared South Coast).

As recommended by the Bureau of State Audits, the AQMD's 1998-99 fee study will examine these issues and make any appropriate recommendations.

Chapter 2

AQMD agrees that the permitting process can be further improved.

AQMD staff generally concurs with the recommendations and appreciates the State Auditors' acknowledgement of the substantial challenges faced by a downsized engineering staff con-

[1] "Emission fee liability is heavily concentrated within the RECLAIM group. . . . However, it is important to note that when NOx emissions, share allocation fees [1995 version of emission fees] and operating fees paid by the RECLAIM facilities are contrasted with the NOx emissions and [associated emission] fees, and operating fees paid by the remaining stationary source emitters, a balanced allocation of fee liability develops. Thus, the total fees paid by each group is proportionate to the total emissions of each group." (KMPG Peat Marwick 1995 Fee Study, pp. 6-2, 6-3.)

[2] Health and Safety Code Section 39612

fronted with increasing workload. Several recent actions are indicative of the agency's efforts to improve in this area: appointment of a Permitting Ombudsman, establishment of the Governing Board-level Permit Streamlining Task Force, issuance of a Request for Proposals for assistance in streamlining the permitting process, redirection of staff resources to permit processing activities, and investment in automated systems that will result in streamlined engineering analysis and permit production.

Chapter 3

Reporting Procedures Have Been Strengthened

The District staff appreciates the State Auditors' acknowledgement of the District's efforts to strengthen its reporting procedures and is committed to follow its enhanced procedures for reporting in these efforts as recommended by the State Auditor. It should be noted that, for the one Technology Advancement project found with no final report, a peer-reviewed technical paper that summarized the project was published at an international conference and was provided upon request. For the project report noted as not including project costs, that report was a compilation of a 600-page conference proceedings that acknowledged the district as a cosponsor and invoice records were provided upon request detailing the actual and contracted costs of that project.

Commitment to equal opportunity will continue.

Further, the District staff appreciates the State Auditors' recognition of the District's long-standing, strong commitment to equal opportunity, both in contracting and employment, which will be continued in the future and the State Auditors' finding that the key functions of the legal office are in line with the duties and role of the district.

Strict publications/literature review will include internal legal review in the future.

Regarding Public Affairs, as stated in the audit, published literature is one of the tools used by the District to educate the public about cleaner processes and compliant products. It is now the practice of Public Affairs to ensure legal review on brochures and newsletters as a normal course of business. AQMD has developed internal guidelines more stringent than required by law. As a result of the audit recommendations, a new policy has been implemented to require legal review of any new publication or literature prior to it being printed or distributed.

Thank you for the opportunity to respond.

Sincerely,

Barry R. Wallerstein, D.Env.
Acting Executive Officer

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Attachment A

Requested Word Changes to Correct or Clarify

1. Report Title, Table of Contents Chapter 1, and p. 1-1 title:
   The South Coast Air Quality Management District Does Not Charge Emission Fees ~~Equitably~~To All Sources

(1) (2) *The AQMD staff believes that its emission fees are charged equitably for the reasons set forth in the response to Chapter 1. The suggested edit neutrally states a fact.*

2. p. S-1, third paragraph:
   Therefore, it ~~does not know~~ can only estimate the magnitude of the actual emissions that these facilities produce, …

   p. 1-1, second paragraph, third sentence:
   However, because the current process…, the District ~~does not know~~ can only estimate the magnitude of the actual emissions…

   p. 1-4, footnote to table; p. 1-6, footnote to table:
   Since the district does not require all emissions to be reported, the total emissions are ~~unknown~~ only estimated.

(4) *The AQMD staff believes that it does know the magnitude of the actual emissions. In fact, we can and do estimate the emissions based on reliable indicators and with an acceptable degree of certainty. Such emission estimates are an important part of the agency's air quality planning effort.*

/ / /

Note: Page numbers in the report have changed.

Comments

California State Auditor's Comments on the Response From the South Coast Air Quality Management District

To provide clarity and perspective, we are commenting on the South Coast Air Quality Management District's (district) response to our audit report. The numbers correspond to the numbers we have placed in the response.

(1) The district states that emission fees are somewhat analogous to the federal and state income tax structure. However, we believe it is an inappropriate analogy to compare the tax systems and the district's emission fee structure because each has a different intent. There are numerous tax laws that do not necessarily treat all taxpayers equally.

(2) As support for its statement that both large and small emitters pay similar total fees per ton of emissions, the district cites a KPMG Peat Marwick (KPMG) 1995 study that compared facilities in the Regional Clean Air Incentives Market program with other permitted facilities. We question the extent of the conclusion that the district has drawn from the study because the comparison analyzed only one pollutant and compared estimated fee revenues for 1995 with estimated emissions for 1990.

Additionally, we believe the district should consider this conclusion in the broader context of all conclusions in the KPMG study. For example, the study also considered the option of lowering the threshold for charging emission fees and concluded that the "option would improve the fee equity among permitted sources." Although the study noted that the net return on these additional revenues may be limited due to increased administrative and audit costs, it did not provide data on these expected costs. Moreover, as we discuss on page 11 of the report, a simplified reporting process would minimize the additional administrative costs. Further, the study concluded that "a potentially more balanced basis for distribution of district costs would be to extend the fee burden among all stationary sources of emissions through an emission-based operating fee." Finally, the study suggested an alternative where the district would retain its system for monitoring the actual emissions for large sources but combine it with potential or estimated

emissions data for other sources to establish a new system. The study concluded that "by spreading costs among an expanded fee base, a more balanced recovery of air regulatory program costs can be achieved."

(3) The district asserts that assessing emission fees on all facilities may be administratively impracticable. However, its position is based on its current emission reporting system. As we state on page 11 of the report, a simplified reporting process would minimize the additional administrative costs that it would incur. We encourage the district to explore alternative cost-efficient methods to collect fees from additional facilities.

(4) The district contends our statement that it does not know the magnitude of the actual emissions that the nonreporting facilities produce may be misleading. We disagree. We recognize that the district has information for planning purposes on total estimated emissions affecting the district. In addition to estimated emissions from reporting and nonreporting facilities with permitted equipment, total estimated emissions also include emissions from nonpermitted sources. Although the district states that it knows the magnitude of emissions from nonreporting facilities, it was never able to provide us with the estimated emissions for the permitted facilities that are not required to report. Thus, to assess the magnitude of unreported emissions, we had to compile R2 (potential emission) estimates related to individual facilities from the district's database. Further, the district agrees that it does not know the actual emissions for each individual facility for billing purposes.

(5) The fairness of the district's emission fee system should not be evaluated on the basis of whether or not another entity's method is equitable. Because only a small portion of the facilities that pollute pay emission fees, we concluded the district's emission fee system is inequitable.

(6) When we questioned district staff during the audit, they were not in agreement that this code section would limit its ability to implement one of our recommended alternatives for assessing emission fees. Further, although the district expresses concern that the code section may hinder basing fees on some surrogate for emissions, such as R2 factors, we note that the district has directed its consultant to examine the feasibility of fee structures based on the emission potential of permitted devices as part of its upcoming fee study. Finally, if the district determines that the code section restricts its ability to implement appropriate changes in its emission fee process, we believe that the district should pursue legislation to modify it.

cc: Members of the Legislature
Office of the Lieutenant Governor
Attorney General
State Controller
Legislative Analyst
Assembly Office of Research
Senate Office of Research
Assembly Majority/Minority Consultants
Senate Majority/Minority Consultants
Capitol Press Corps