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Transmitted via e-mail

May 31, 2012

Ms. Linda Whitney, Executive Director
Medical Board of California
2005 Evergreen Street, Suite 1200
Sacramento, CA 95815

Dear Ms. Whitney:

Final Report—Medical Board of California Financial Status

The Department of Finance, Office of State Audits and Evaluations, has completed its audit of the Medical Board of California's (Board) financial status as of June 30, 2011.

The enclosed report is for your information and use. The Board agreed with our results and its response is incorporated into this final report. This report will be placed on our website.

We appreciate the assistance and cooperation of the Board. If you have any questions regarding this report, please contact Kimberly Tarvin, Manager, or Jennifer Arbis, Supervisor, at (916) 322-2985.

Sincerely,

David Botelho, CPA
Chief, Office of State Audits and Evaluations

Enclosure

cc: Ms. Kimberly Kirchmeyer, Deputy Director, Medical Board of California
Ms. Pam Wortman, Deputy Director, Administrative and Information Services, Department of Consumer Affairs
Ms. Janice Shintaku, Fiscal Officer, Department of Consumer Affairs

Audit Report

Medical Board of California
Financial Status
as of June 30, 2011

Prepared By:
Office of State Audits and Evaluations
Department of Finance

121390099 SCN

April 2012

MEMBERS OF THE TEAM

Kimberly Tarvin, CPA
Manager

Jennifer Arbis
Supervisor

Staff
Wrenna Finche
Toni Silva

Final reports are available on our website at http://www.dof.ca.gov

You can contact our office at:

Department of Finance
Office of State Audits and Evaluations
300 Capitol Mall, Suite 801
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(916) 322-2985

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BACKGROUND, SCOPE AND METHODOLOGY

BACKGROUND

The Medical Board of California (Board) protects health care consumers through the proper licensing and regulation of physicians and surgeons and certain allied health care professions; enforcement of the Medical Practice Act; and promoting access to quality medical care through the Board's licensing and regulatory functions.[1] The Board operates under the oversight of the Department of Consumer Affairs (DCA) and administers the Contingent Fund of the Medical Board of California (Fund). Additionally, DCA performs the accounting and budgeting functions for the Board including monitoring the Board's legal spending authority.[2] The Board's operations are funded through licensing fees paid by California physicians and surgeons. During the fiscal year ended June 30, 2009, a $6 million loan was made from the Fund to the state General Fund.

SCOPE

In accordance with California Business and Professions Code section 2435, the Department of Finance, Office of State Audits and Evaluations (Finance), reviewed the Board's financial status as of June 30, 2011 including the following:

- The Board's projections related to revenues, expenditures, and reserves.
- The impact of the $6 million loan from the Fund to the state General Fund.

Subsequent to June 30, 2011, an additional $9 million loan was made to the state General Fund. Although not required by statute, this report includes the impact of this loan on the Fund.

METHODOLOGY

To evaluate the Board's financial projections and the impact of the loans, Finance performed the following:

- Interviewed Board administrative and budget staff, former Board budget staff, and DCA budget staff regarding the following:
  - Roles and responsibilities
  - Budget development processes and policies
  - Program development process and status
- Reviewed and analyzed financial reports.
- Reviewed the fund condition statement projection methodology.
- Compared fund condition statement projections to actual year-end financial statements.

[1] From the Medical Board's website: http://mbc.ca.gov/
[2] Ibid

- Compared the appropriated and actual revenues, expenditures, and fund balances as reported in the Governor's Budgets for a ten year period ending June 30, 2011.
- Reviewed the Board's projections through June 30, 2015 to identify any significant changes in projected revenues, expenditures, or fund balance.
- Assessed the status of Board programs under development.
- Reviewed year-end fund balances and projections to analyze the months of operating expenditures in reserve.
- Evaluated the impact of the loans through June 30, 2015 by comparing the following:
  - Months of operating expenditures in reserve—with the loans
  - Months of operating expenditures in reserve—without the loans

Except as noted, this audit was conducted in accordance with generally accepted government auditing standards, issued by the Comptroller General of the United States. In connection with this audit, there are certain disclosures required by government auditing standards. Finance is not independent of the Board, as both are part of the State of California's Executive Branch. As required by various statutes within the California Government Code, Finance performs certain management and accounting functions. These activities impair independence. However, sufficient safeguards exist for readers of this report to rely on the information contained herein. This audit was conducted during the period January 2012 through April 2012.

Overall, the Board's revenue projections have generally reflected the actual revenues. However, the authorized appropriations have exceeded actual expenditures an average of $3.7 million per year over the last 10 years. As a result, excess funds accumulated in the Board's fund balance. The Board anticipates that expenditures will exceed revenues in the near future due to the BreEZe information technology system, permanent establishment of the Operation Safe Medicine Unit, and the current recruitment effort to fill vacancies. Descriptions of these anticipated expenditures are included below.

Based on the Board's projections, the Board's operations would not be affected by the $6 million and $9 million loans made from the Fund to the State General Fund until fiscal year 2013-14, at which time it would be below its mandated reserve level.

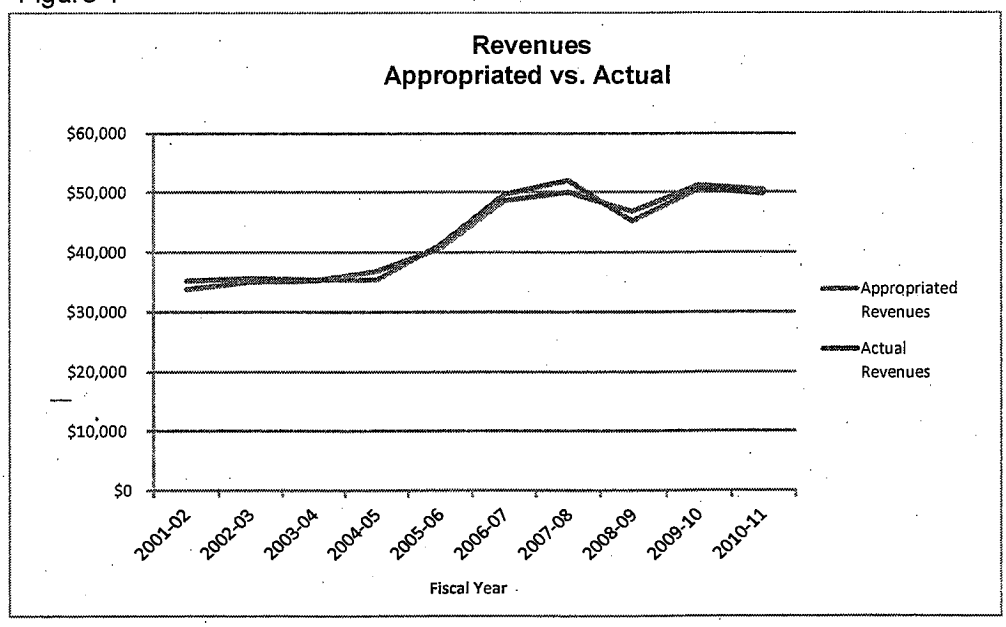
FUND STATUS

Finance compared the appropriated and actual revenues and expenditures during the 10-year period ending June 30, 2011 to determine whether the revenues and expenditures generally reflected the projections. See Appendix A for more information regarding the budget development process.

Revenues

With input from the Board, DCA develops the revenue projections reflected in the Governor's Budget. Over the last 10 years the revenue projections have generally reflected the actual revenues. See Figure 1 below for comparison of the appropriated and actual revenues.

Figure 1

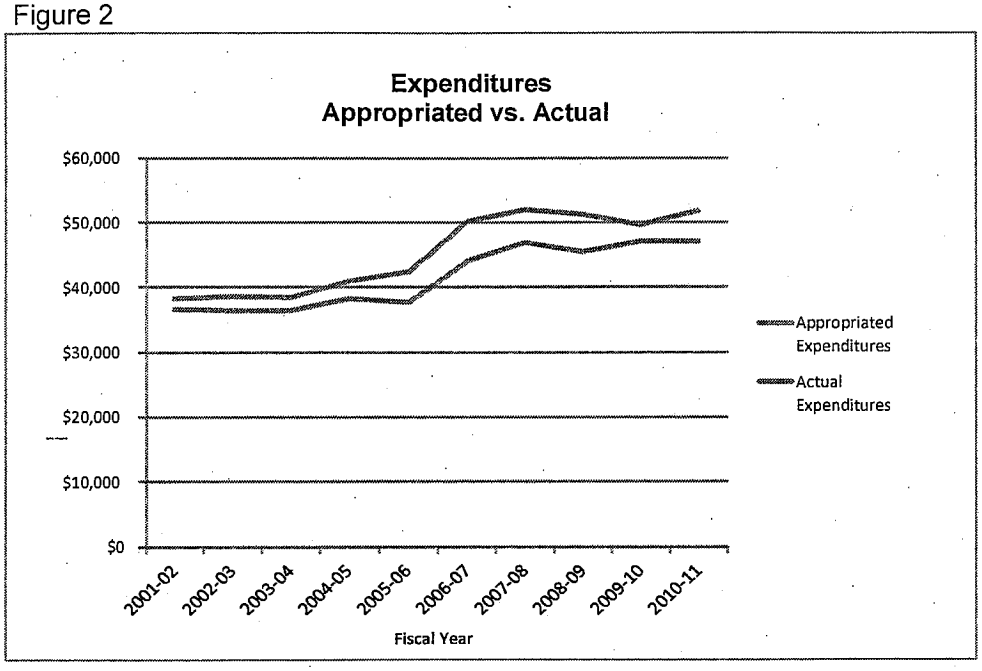


Source: Governor's Budget for fiscal years 2002-03 through 2012-13

Expenditures

The Board's expenditure projection process begins with DCA adjusting the annual Budget Act for Budget Change Proposals, Budget Letters, and other changes authorized by the Department of Finance. For each subsequent year, expenditures have been projected to increase by two percent each year. Over the last 10 years, the Board's actual expenditures were an average of $3.7 million less than the appropriated expenditures each year. The Board indicated that recent statewide hiring freezes combined with a high turnover rate of enforcement staff resulted in a high number of vacant positions, resulting in lower than anticipated expenditures. See Figure 2 for comparison of the appropriated and actual expenditures.

Figure 2



Source: Governor's Budget for fiscal years 2002-03 through 2012-13.

Anticipated Expenditure Increases

The Board expects expenditures to increase due to the following:

- DCA's BreEZe information system.
- Operation Safe Medicine Unit.
- Current recruitment efforts.

BreEZe Information System
DCA is in the process of implementing the BreEZe information system to be used by all of DCA's boards and bureaus for tracking licensing and enforcement activities. Subsequent to June 30, 2011, DCA obtained authorizations for the Board's portion of these costs of $200,000 and $1.3 million for fiscal years 2011-12 and 2012-13, respectively. DCA will seek to obtain approval of the ongoing BreEZe costs estimated to be $1.3 million.

Operation Safe Medicine Unit
Operation Safe Medicine enables the Board to fulfill its enforcement mandate through the investigation of complaints of unlicensed medical activity. The Board received authorization from the Department of Finance to permanently establish the Operation Safe Medicine Unit

effective July 1, 2012. The Board will redirect current resources to fund the six approved positions. Beginning 2012-13, the Board projects yearly costs of approximately $583,000.

Recruitment Efforts
The Board indicated that it is actively recruiting and in the process of filling all vacant positions.

If costs related to BreEZe and Operation Safe Medicine are incurred as projected and the Board fills its vacancies, the Board's expenditures will likely reflect the projected expenditures through 2014-15.

Fund Balance

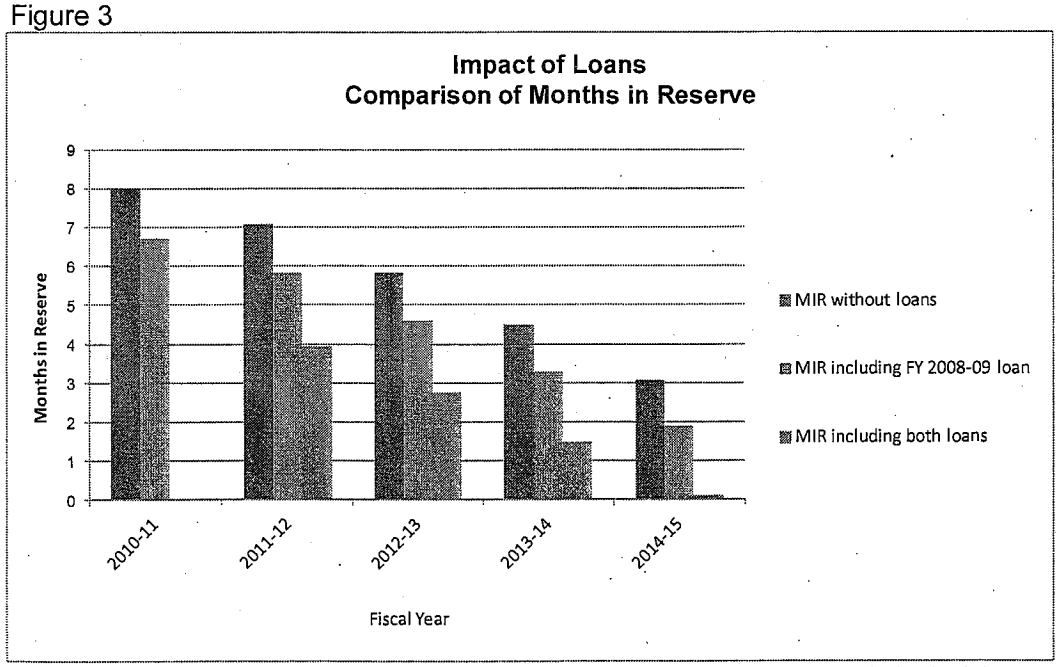
The fund balance, also referred to as the reserve, displays the resources available to sustain the Board's current operations. Per California Business and Professions Code section 2435, the Board is currently required to maintain a reserve level between two to four months of operating expenditures. Since 2001-02, the Board maintained an average of 4.7 months in reserve (MIR). The Board projects the MIR for future years by dividing the projected year-end fund balance by one-twelfth of the subsequent year's projected annual expenditures. See the Impact of the Loans section below for the projected MIRs.

IMPACT OF LOANS

Two loans of $6 million and $9 million were made from the Fund to the General Fund per the 2009 and 2011 Budget Acts, respectively. Figure 3 illustrates the actual impact of the loan for fiscal year 2010-11 and projected impact of both loans for 2011-12 through 2014-15 as follows:

- MIR without loans
- MIR with the $6 million loan
- MIR with both loans totaling $15 million

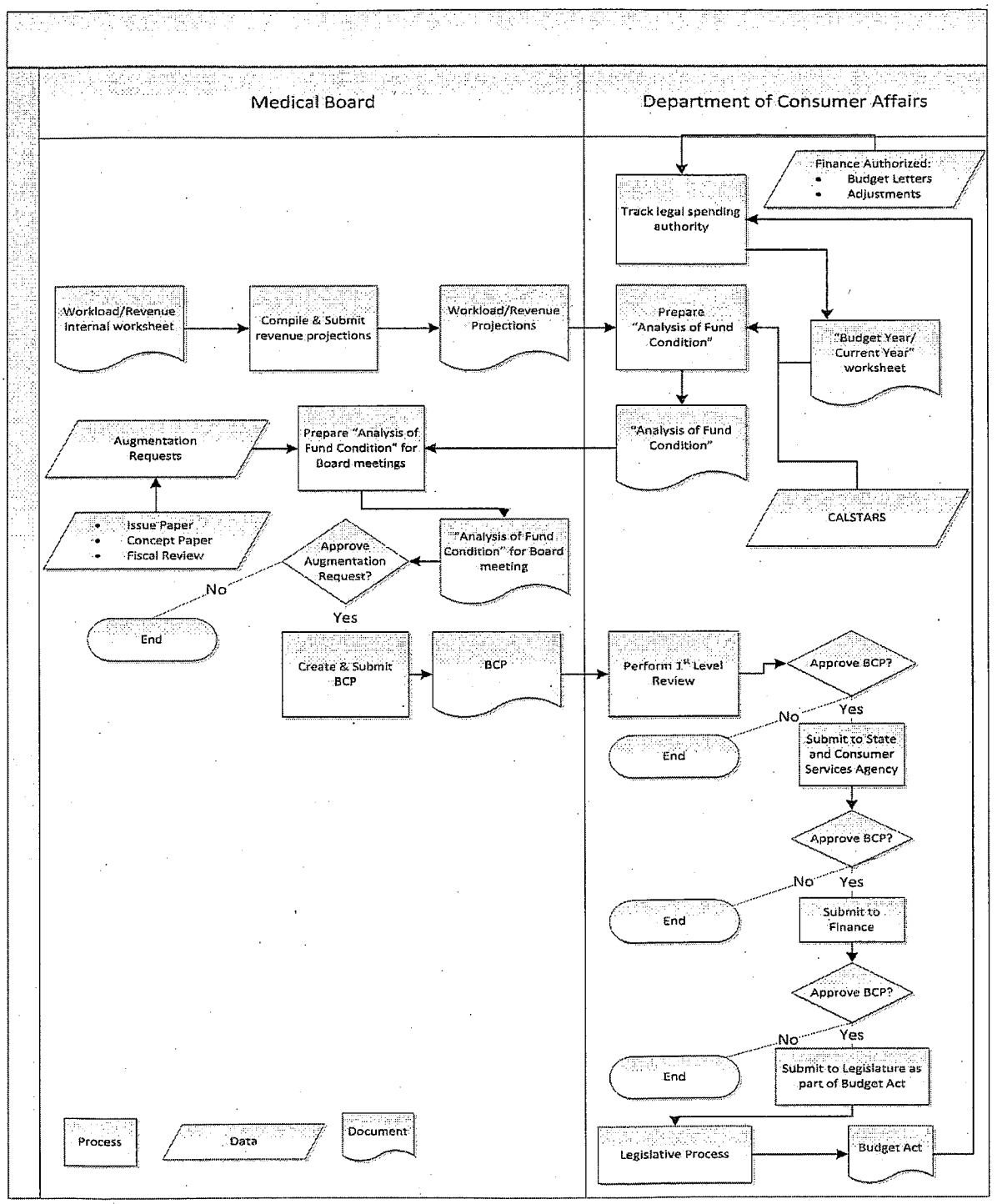
Figure 3



Source: Board Analysis of Fund Condition report, dated October 26, 2011, which includes both loans, and anticipated expenditures noted in the Anticipated Expenditure Increases section of this report.
Note: The yellow bar (between two and four months) highlights the Board's mandated level of reserve.

Currently, the loans have not impacted the Board's ability to operate. However, if the loans are not repaid and the anticipated increase in expenditures occurs, the MIR will fall below the minimum mandated reserve level of two months of operating expenditures in 2013-14. If the loans are not fully repaid, are partially repaid, or the anticipated increase in expenditures do not occur, the MIR will be impacted accordingly.

MEDICAL BOARD OF CALIFORNIA'S BUDGET PROCESS



MEDICAL BOARD OF CALIFORNIA
Executive Office

May 16, 2012

David Botelho, CPA, Chief
Office of State Audits & Evaluations
915 L Street, Suite 801
Sacramento, CA 95814

RE: Draft Report – Medical Board of California Financial Status

Dear Mr. Botelho:

The Medical Board of California (Board) is in receipt of your draft report dated April 2012 entitled "Medical Board of California Financial Status as of June 30, 2011". The Board would like to thank you for conducting this audit and for providing this report.

As stated in the report, the Board was mandated to be audited by the Department of Finance pursuant to California Business and Professions Code section 2435, which states:

> *Not later than January 1, 2012, the Office of State Audits and Evaluations within the Department of Finance shall commence preliminary review of the board's financial status, including, but not limited to, its projections related to expenses, revenues, and reserves, and the impact of the loan from the Contingent Fund of the Medical Board of California to the General Fund made pursuant to the Budget Act of 2008.*

Based upon requests from the audit team, the Board and the Department of Consumer Affairs provided the fiscal documents and information that assisted in the preparation of this draft report. The draft report has accurately captured the information provided and the mandate of the legislature.

The Board would like to thank the audit team for their professionalism during this process and appreciates the thoroughness of the team's work.

Sincerely,

Linda K. Whitney
Executive Director

STATE OF CALIFORNIA
dca
DEPARTMENT OF CONSUMER AFFAIRS

STATE AND CONSUMER SERVICES AGENCY • GOVERNOR EDMUND G. BROWN JR.
ADMINISTRATIVE AND INFORMATION SYSTEMS DIVISION
OFFICE OF ADMINISTRATION, BUDGET OFFICE
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MEMORANDUM

DATE	May 24, 2012
TO	David Botelho, CPA Chief, Office of State Audits and Evaluations
FROM	Taylor Schick, Budget Officer Department of Consumer Affairs
SUBJECT	**RESPONSE TO DOF DRAFT REPORT OF THE MEDICAL BOARD OF CALIFORNIA FINANCIAL STATUS**

The Department of Consumer Affairs (Department) Budget Office is submitting this memo in response to the Office of State Audits and Evaluations (OSAE) May 10, 2012 Draft Report of the Medical Board of California (MBC) Financial Status. The Budget Office has concerns with some of the terminology used in the report. These concerns are outlined below and are mainly focused on the use of the term "expenditure projections" where we believe different terms would be more appropriate. (headlines correspond to sections of the draft report)

Methodology

"expenditure projections have exceeded actual expenditures an average of $3.7 million per year over the last 10 years"

The term "expenditure projections" is more accurately referred to as "authorized appropriations". It is assumed the point is to address a comparison between authorized appropriations and actual expenditures.

Expenditures

"Expenditure projections are initially developed by DCA based on spending authority in the annual Budget Act with adjustments made for Budget Change Proposals, Budget Letters, and other changes authorized by the Department of Finance. For each subsequent year, expenditures have been projected to increase by two percent each year."

Again, the term "expenditure projections" is more accurately referred to as "authorized appropriations". Additionally, the "authorized appropriations" are not "initially developed" but rather "adjusted" by DCA.

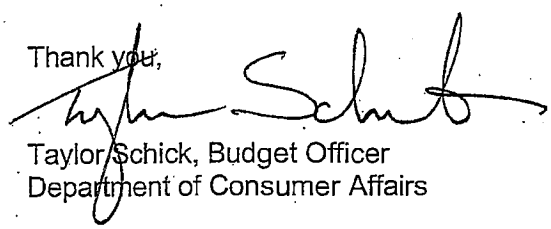
The reference to expenditures projected to increase by two percent each year refers only to internal fund condition scenarios. The only 'official' fund condition would be as it is reflected in each year's Proposed Governor's Budget, and would include only prior year actual expenditures, current year authorized, and budget year proposed.

"If costs related to BreEZe and Operation Safe Medicine are incurred as projected and the Board fills its vacancies, the Board's expenditures will likely reflect the projected expenditures through 2014-15."

The term "projected expenditures" should be replaced with "authorized appropriation".

We ask that our concerns be noted and that revisions are considered prior to public release. Please contact me at 916-574-7177 with any questions.

Thank you,



Taylor Schick, Budget Officer
Department of Consumer Affairs

cc: Jennifer Osborn, Deputy Secretary, Fiscal Operations, State and Consumer Services Agency
Kim Kirchmeyer, Deputy Director, Medical Board of California
Denise Brown, Director, Department of Consumer Affairs
Awet Kidane, Chief Deputy Director, Department of Consumer Affairs
Reichel Everhart, Deputy Director, Board and Bureau Relations, Department of Consumer Affairs
Sandra Mayorga, Deputy Director, Office of Administrative Services, Department of Consumer Affairs
Ms. Janice Shintaku, Fiscal Officer, Department of Consumer Affairs

EVALUATION OF RESPONSE

The Department of Finance, Office of State Audits and Evaluations reviewed the draft report responses from the Medical Board of California, dated May 16, 2012, and the Department of Consumer Affairs (DCA), dated May 24, 2012. In response to DCA's concern regarding some terminology, we revised the report as follows:

- Results Section - In the first paragraph, the term expenditure projections was changed to authorized appropriations.

- Expenditures Section - The expenditure projection process was clarified in the first paragraph.

For the Anticipated Expenditure Increases section, the terminology remains as projected expenditures instead of the term authorized appropriations suggested by DCA. This portion of the report discusses expenditure projections beyond the proposed budget which are not authorized appropriations.