



**Implementation of
Underground Storage Tank Cleanup Fund
Performance Audit
Corrective Action**

**Prepared In Accordance with
The Supplemental Report of the 2010-11 Budget**

January 2011 Update



STATE WATER RESOURCES CONTROL BOARD
REGIONAL WATER QUALITY CONTROL BOARDS



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Executive Summary

This report, which has been prepared pursuant to the requirements of the Supplemental Report to the 2010 Budget Act, provides an update on the State Water Resources Control Board's (State Water Board) progress in carrying out a corrective action plan to address issues raised by a February 2010 audit of the Underground Storage Tank (UST) Cleanup Fund (Cleanup Fund). The State Water Board continues to make significant progress in improving (a) financial management and cost containment, (b) processing efficiency, and (c) internal controls for the Cleanup Fund. Since it's June 2010 update to the Assembly Budget Subcommittee #3 on this issue, the State Water Board has completed several additional actions that were previously identified as "planned" or "underway" in the June 2010 report, and has begun to implement additional steps towards improving management and oversight of the Cleanup Fund.

Introduction

The Supplemental Report to the 2010 Budget Act, Item 3940-001-0439, requires the State Water Board to submit a report to the Joint Legislative Budget Committee by January 10, 2011, detailing the progress to-date in carrying out a corrective action plan in response to the "Underground Storage Tank Cleanup Fund Performance Audit" dated February 22, 2010. The report must contain a brief narrative description of the circumstances that required the audit, followed by a summary of actions implemented and actions to be implemented in response to the audit recommendations in the following areas: (a) Financial Management and Cost Containment, (b) Processing Efficiency, and (c) Improve Internal Controls. Additionally, the report must clearly indicate which actions reflect progress made since the last report to the Legislature (during the 2010-11 budget process), as well as the next steps to be taken and challenges to further progress.

In June 2010, the State Water Board submitted a brief report to the Assembly Budget Subcommittee #3 on the improvements that the State Water Board was making to the Cleanup Fund. The changes to the Cleanup Fund were made, in large part, in response to the February 22, 2010 "Underground Storage Tank Cleanup Fund Performance Audit." As required by the Supplemental Report to the 2010 Budget Act, the following report documents the continued improvements that the State Water Board is making to the Cleanup Fund, and its progress to date in implementing the recommendations in the audit to improve both the effectiveness and efficiency of the Cleanup Fund.

Background

The Barry Keene Underground Storage Tank Cleanup Fund Act of 1989 created the Cleanup Fund to help owners and operators of petroleum USTs satisfy federal and state financial responsibility requirements. To fulfill the federal financial requirements, the Cleanup Fund is available to assist petroleum underground storage tank owners and

operators with the costs to clean up the contamination of soil and groundwater caused by leaking tanks. The federal financial responsibility requirements also require the Cleanup Fund to provide certain coverage for third-party liability due to unauthorized releases of petroleum from underground storage tanks.

Since the Cleanup Fund program began operations in 1991, the State Water Board has paid over \$2.2 billion to thousands of individuals and small businesses to help them cover the cost of cleaning up their gas stations and other leaking tank sites. Another \$500 million has been paid to local governments and large businesses. This financial assistance program is supported by fees paid by tank owners to the Board of Equalization.

During the course of the program, over 19,000 claims have been filed. Some 11,000 claims have been paid in part or in full, of which about 7,000 have been closed and about 4,000 remain active. Another 4,600 claims filed by major corporations and government agencies are on our priority list, awaiting activation. Individual payment transactions have numbered more than 66,000, for a long-term average payment of about \$40,000/claim/year.

During the late 1990s and most of the 2000s, the program was able to accommodate all eligible claims filed by small businesses and individuals. The cost of cleanups, however, has increased over the last few years as the annual cost per claim rose to \$50,000.

In 2008, the cash reserve built up in the early years of the program fell below prudent reserves, and the program experienced a cash shortage. This shortage was made worse because of a concurrent dip in revenues due to the slow-down in the economy. Insufficient cash was available to service all of the active claims, and payments were and remain delayed by many months. This created a sudden and severe hardship for small business claimants and their consultants, who are also small businesses.

In response, the State Water Board held a public hearing on March 9, 2009, to receive testimony from stakeholders, and directed staff to develop and implement actions to remedy the problems. Through this stakeholder input and self-examination, Board staff confirmed that the problem was two pronged:

- 1) There was a need to improve the business model and processes at the Cleanup Fund to better manage cash flow; and
- 2) There was the lack of incentive to get cases cleaned up quickly and efficiently.

The lack of closure incentive applied to all three major parties:

- 1) the responsible party or claimant, whose site cleanup bills are paid by the Cleanup Fund;
- 2) the consultant, who can continue to bill hours as long as the case is active; and
- 3) the regulator, who generally prefers to close only cases that have minimal or no risk associated with the site closure.

Due, in part, to these disincentives, over 43 percent of the active claims have been open for ten years or more.

The State Water Board has taken numerous actions in response to the cash shortage situation. The State Water Board directed staff to undertake specific steps to attack both parts of the problem – making the Cleanup Fund work better and getting cases to closure more quickly and efficiently. As part of the solution, the State Water Board established two stakeholder task forces to review both the regulatory side and the payment side of the UST Program, and make suggestions for improvements or changes. The State Water Board also directed staff to commission an independent audit of the program.

The work of the audit and task forces began in July 2009 and wrapped up in early 2010. The findings and recommendations of these efforts were consistent and can be organized around four topics: 1) financial management, 2) cost containment, 3) processing efficiency, and 4) internal controls.

The audit found that the Cleanup Fund program has been, and remains, too reactive to reimbursements for UST cleanup work. The program could not adequately plan expenditures, contain costs or work efficiently because it could not forecast how many payment requests would be received in a given time period, when these requests would be received, or the amount of funding that would be requested. The auditors recommended that the program convert to a more traditional grant-like program, by putting our small business claimants on a fixed budget and establishing standard invoicing formats and regular invoicing periods. The audit also recommended that the program become more active in determining the activities that are to be undertaken at funded sites. The ongoing and proposed actions by the program will be organized with the goal of implementing this core set of recommendations.

The following summarizes actions implemented and to be implemented to address these findings and recommendations. This report uses the June 2010 report to the Assembly Budget Subcommittee #3 as a foundation, and provides updated information which is reflected in *italics*.

I. Financial Management and Cost Containment

The Cleanup Fund needs to reduce the number of active claims and/or reduce the average cost per claim to bring long term demand into balance with revenue. The reduction in active claims will be accomplished by a continuous review of older cases with the aim of quickly moving them to closure when site conditions warrant. Cost savings for active sites will be achieved by having the Cleanup Fund participate in the development of budgets for our small business claims.

1. **Monitoring.** To immediately save an estimated \$30 million annually, the State Water Board directed that groundwater monitoring at sites be reduced to twice

yearly instead of four times yearly, unless site conditions warrant otherwise.
(Completed)

2. **Case Review and Closure.** The State Water Board directed all Regional Water Quality Control Boards (Regional Water Boards) and Local Oversight Program agencies to complete reviews of all their cases by June 2010 and either close the case if warranted by site conditions, or determine what needs to be done to obtain case closure.

Update: This effort was completed in June 2010. As a result of this caseload review, approximately 1300 UST sites were closed by the various Regional Water Boards and Local Oversight Program Agencies between May 19, 2009 and June 30, 2010. (Completed)

3. **State Water Board Case Review and Closure.** State Water Board staff accelerated the review of older Cleanup Fund cases under existing Health and Safety Code authority. Staff will bring cases before the Board for consideration of closure where appropriate. The first sets of cases were heard by the State Water Board in January and April of 2010 and additional cases will be heard by the State Water Board every few months. The intent is to use this process to encourage regulators to close cases by demonstrating consistent application of the State Water Board's cleanup policy on UST cleanups. All of this work is done with full consideration of the protection of water quality and the environment, and human health and safety.

Update. This process is ongoing. State Water Board Cleanup Fund staff took additional sets of cases to the State Water Board in June and October 2010 and the Board approved closure of the majority of these cases. The next set of cases to be heard by the Board is scheduled for February 2011. The State Water Board uses a public process in which interested parties can provide comments directly to the State Water Board regarding these cases. (Underway)

4. **Cash Flow Projections.** The Cleanup Fund is implementing a systematic and rigorous cash flow projection/reporting process and has created and filled a Cleanup Fund Financial Manager position. This person has the responsibility of conducting regular cash flow projections for the Cleanup Fund and will provide reports to the State Water Board, program staff, stakeholders and our claimants on these projections. This person is also responsible for determining the number of active claims the program can support.

Update. This process is ongoing. The Cleanup Fund Financial Manager has been setting up monitoring and reporting mechanisms to more accurately project and track revenues for the Cleanup Fund, as well as Cleanup Fund expenditures. The Manager has set up a budget and expenditure tracking system for the individual claim budgets that are discussed in more detail

below. This financial tracking and monitoring infrastructure will be critical to the successful implementation of the individual claim budget process. (Underway)

5. **Budgets for Small Business Claims.** The Cleanup Fund will require budgets be developed for all small business claims. This will enable development of program cash flow demand projections and establish cost limits for individual claims. Setting budgets for each of our claimants will also lead to faster and more efficient cleanups by focusing all work to be evaluated against the ultimate goal of case closure. We are implementing a pilot project now to develop and test this claim budget process.

Update. The development of individual site budgets, one of the key components of the Cleanup Fund's new approach, has begun, and will be fully implemented starting in July 2011. Approximately 25 claims were included in the pilot project. The initial phases of the pilot project are completed, with each of these sites now having an individual claim budget for the work currently being implemented. Cleanup Fund staff is still in the process of developing invoicing and payment forms and processes for this new claim budget method.

Cleanup Fund staff established new processes when they introduced the new claim budget method to Priority A, B, C, and D claimants (approximately 3,500 claims). As a first step, Cleanup Fund staff performed a comprehensive examination of all Priority A, B, and C claims in the Cleanup Fund to determine the stage of the cleanup process that each claim was in. The budget for each claim will be dependent on the phase of site cleanup for each individual claim, as some phases of cleanup, remedial system installation for example, are more cost-intensive than other phases. Cleanup Fund staff devised an expedited appeal process to provide claimants an opportunity to ensure that their site was placed in the proper category. This initial step was completed in November 2010. Subsequent on-going steps include the negotiation of individual site scopes of work and budgets for these claims. Cleanup Fund staff anticipate that all Priority A, B, and C claims will complete this process and have an individual claim budget by the end of June 2011. (Underway)

6. **Long Term Cash Flow Planning.** The Cleanup Fund will analyze expenditures by types of costs and project phases to help develop better long-term cash-flow planning. Budgeted claims will request payments organized around budget categories.

Update. Cleanup Fund staff also analyzed the expenditures for the last several years at each claim and cross-referenced this with the phase of cleanup. This has provided the staff with a better understanding of the average costs of each phase of cleanup, and will help the Cleanup Fund

better analyze budget proposals for each claim. Also, by better understanding the costs of each phase of cleanup, staff can help prevent shortfalls in the Cleanup Fund caused by over-allocation of resources. Cleanup Fund staff will continue to evaluate and analyze expenditures by types of costs and project phases as the individual claim budgets are built in the coming months, and each year thereafter. This information gathered on an ongoing basis will be used to help Cleanup Fund staff better project the needs for each forthcoming fiscal year. (Completed)

7. **Suspension of Additional Payments for Select Cases.** The Cleanup Fund will begin imposing a stay on any additional payments for claims determined ready for closure under the Five Year Review process, while the case is elevated to the State Water Board for formal consideration of closure.

Update. One of the phases of cleanup identified during the categorization process is "No Further Action". This category is populated both by sites that State Water Board Cleanup Fund staff, through the Five Year Review process, has identified as ready for closure and sites that the Regional Water Boards or the local regulatory agency staff has already granted closure. Claims in this category will receive a minimal budget for site work, but will be given an opportunity to negotiate increases in the budget for costs directly related to site closure, such as monitoring well abandonment and waste disposal. In the meantime, Cleanup Fund staff will continue to elevate claims from this category (those sites identified as ready for closure by the Five Year Review process) to the State Water Board for closure as described in Number 3 above. (Underway)

8. **Outreach –NEW.** Considerable outreach and education efforts are necessary to inform both claimants and regulatory staff about how the State Water Board intends to operate the Cleanup Fund in the future. State Water Board staff has started communicating this information through letters to claimants from the Fund Manager, postings on the State Water Board website, and presentations by Cleanup Fund staff to Regional Water Board and Local Oversight Program staff. Additional efforts planned include multiple teleconference/WebEx presentations specifically tailored to both the claimant and regulatory agency communities, and possible in-person presentations/trainings at various locations in the State convenient to those with Cleanup Fund interactions. (Underway)

II. Processing Efficiency

The Cleanup Fund needs to process payments more quickly through use of standardized invoices and simpler procedures. Cleanup Fund staff have already implemented numerous changes in this area, but will continue to transition to a more effective budgeted-claim approach.

Update. The State Water Board has made, and continues to make, additional changes to improve the efficiency of processing reimbursement requests and closing or re-opening of claims. State Water Board staff have created or modified forms and documents to streamline the collection of information that the Cleanup Fund staff requires to process requests (for example, the Proof of Payment Certification form was streamlined and staff revised the Payment Summary to include a proof of payment requirement). Furthermore, Cleanup Fund staff is developing and posting to its website guidance documents for commonly encountered situations, such as what to do if a claimant is deceased, what standards are required for subcontractor invoices, etc., that will benefit claimants and consultants by allowing them to obtain accurate answers quickly and efficiently.

The backlog of reimbursement requests needing to be reviewed has been significantly reduced since June 2010. State Water Board Cleanup Fund staff has reduced the review time of a new reimbursement request to approximately 60 days (as required by Cleanup Fund Regulations). Using the revenue from the fee increase, as provided by Chapter 649/2009, the State Water Board expects to pay out the entire backlog of payments during fiscal year 2010-2011.

1. **Cleanup Fund Stakeholder Advisory Group.** The Cleanup Fund has formed a Stakeholder Advisory Group to provide feedback and suggestions for changes in the program business model.

Update. The Stakeholder Advisory Group has been meeting approximately monthly since May 2010. The members of the Stakeholder Advisory Group are claimants, regulatory agency staff, and consultants. Cleanup Fund staff worked closely with the Stakeholder Advisory Group to obtain input on the various options under consideration for changing the way the Cleanup Fund operates. (Completed)

2. **Efficiency in Payment Process.** The Cleanup Fund changed from an overall two step process to encumber and pay funds to a single step process. This has saved staff time, paper and reduced processing time by one week. (Completed)
3. **Reduced Wait Time.** Cleanup Fund staff reduced the number of steps and people involved in the review of a given payment to reduce wait time. (Completed)
4. **Data Collection Efficiency.** Cleanup Fund staff eliminated the requirement for submittal of hard-copy reports when these reports are entered into the State Water Board's online Cleanup Programs database – Geotracker – via the online Geotracker tools. (Completed)
5. **Proof of Payment** Cleanup Fund staff developed a vendor affidavit to provide proof of payment vs. requiring submittal of cancelled checks. (Completed)

6. **Signature Requirements.** Cleanup Fund staff eliminated the need for original wet signatures on some forms where legally defensible to facilitate submittal by email and FAX. (Completed)
7. **Productivity Tracking.** Cleanup Fund management staff are reviewing individual staff workloads and improving productivity tracking. Telework was canceled for all Fund staff, while the new business model is being developed. (Underway)
8. **User-Friendly Forms.** Cleanup Fund staff is creating more user-friendly forms for claimants. (Underway)
9. **Website Enhancements.** Cleanup Fund staff will continue to enhance the program website so that claimants can more easily determine the status of their payments and otherwise be better informed, thereby improving service and reducing telephone call and email response demands. (Underway)
10. **Standardized Invoice Formats.** Cleanup Fund staff will standardize invoice formats and establish regular reimbursement schedules for budgeted small business claims. This will further improve processing speed and allow for better management of cash flows and overall workloads.

Update. As part of the new business model development, Cleanup Fund staff has been working on standardized invoice forms. These forms will be fully implemented by July 2011. (Underway)

11. **Backlog Reduction.** Cleanup Fund management staff will temporarily redirect approximately ten staff from the claims processing unit to the payments processing unit to reduce the backlog of payment requests awaiting review.

Update. The backlog of reimbursement requests needing to be reviewed has been significantly reduced since June 2010. All reimbursement requests in-house are now within the 60 day review period. (Completed)

12. **Eligibility Determinations--NEW.** Cleanup Fund staff are making eligibility determinations and issuing Staff Decisions within 60 days of receipt of a claim application as required by statute. Claimants have 60 days to respond and correct any deficiencies at which time a Final Staff Decision is issued. (Completed)
13. **Regulatory Agency Compliance Reviews--NEW.** Cleanup Fund staff will use a risk-based approach for conducting regulatory agency compliance reviews. Previously Cleanup Fund staff visited local regulatory agency offices to review the case files for every claim submitted to the Fund. Staff has identified alternate means, other than travel, to verify with the regulatory agency that a claimant is in

current corrective action compliance. Cleanup Fund staff will now conduct these reviews using information available on-line and over the telephone as much as possible. This will streamline and reduce review time as well as travel costs. (Underway)

14. **Active Claims Management—NEW.** *Cleanup Fund staff will manage the number of active claims to ensure day-to-day demand is in balance with revenues. Letters of Commitment (LOC) for new claims will be issued once a year depending on available funding for that year.*

The Cleanup Fund is also revising and streamlining the ways claims are initially reviewed and processed to determine if they are eligible for Cleanup Fund reimbursement, and to ensure that new claims are not activated until there is sufficient money in the Fund to adequately cover their costs. (Underway)

15. **Letters of Commitment—NEW.** *Claimants will be required to have an approved project budget before a LOC is issued. (Underway)*

III. Improve Internal Controls

All audit recommendations regarding internal control improvements will be implemented, including:

1. **Cleanup Fund Fraud Team.** Cleanup Fund management staff established an independent Cleanup Fund Fraud Team in the State Water Board's Enforcement Office to pursue allegations of fraud, waste and abuse. Results of this effort will be evaluated as it proceeds and consideration will be made for making this a permanent unit in the Enforcement Office. While the audit did not make any specific findings regarding fraud, it did identify weaknesses in the program that could result in waste and abuse. This effort will provide feedback to the program as it develops its new business model on how to better contain costs and reduce the risk of fraud, waste and abuse. (Completed)
2. **Audit and Review Processes.** Cleanup Fund staff will establish a real-time payment audit and review process to ensure payment reviews are accurate.

Update. Cleanup Fund staff are in the process of designing a real-time audit process that will be implemented concurrently with the implementation of the individual claim budgets in July 2011. (Underway)

3. **Quality Control Processes.** Cleanup Fund management staff will also establish management-level quality control processes to evaluate overall payment procedures. (Planned)

IV. Next Steps

Chapter 649/2009 has provided the Cleanup Fund a cash infusion that will allow the program to make payments on the more than \$100 million outstanding payment requests now in-house. It also provides the Cleanup Fund a window of opportunity to implement changes necessary to prevent the cash shortages from being repeated. The Cleanup Fund must develop and implement the changes discussed today in a relatively short period of time. Cleanup Fund staff will continue to aggressively develop, implement, and monitor these changes. Cleanup Fund staff will continue to report progress to the State Water Board at regular intervals during and after this implementation phase.

Update. The Cleanup Fund has begun to make payments on outstanding payment requests using the additional funding provided by Chapter 649/2009 and anticipates that it should be able to pay all of these outstanding payment requests as funds become available throughout the 2010-2011 fiscal year. The Cleanup Fund is making good progress in implementing improvements in Financial Management and Cost Containment, Processing Efficiency, and Internal Controls. Based on the performance of these measures in Fiscal Year 2011-2012, Cleanup Fund staff will further refine and implement any necessary corrections or revisions to the new business model to allow it to function more efficiently and effectively.

V. Challenges

With more than \$100 million in payment requests in-house and work of some type on-going at most of the 4,000 active sites, the challenge will be to accomplish the transition in the business model to a budgeted-claim approach while continuing to process payments submitted under the old model. Also, instilling change in a highly decentralized regulatory program that has been in existence for more than two decades remains a challenge.

Although these challenges will be significant and will require a major change in program and stakeholder/claimant operational procedures, the State Water Board is committed to streamlining our operations and bringing this program into a sustainable balance.

Update. The primary challenge to the program remains that demand on the Cleanup Fund still exceeds the revenues available. As a corollary to this, the challenge also remains as to how to equitably fund the existing claims with the revenues currently available. This situation is anticipated to exist until sufficient sites can be closed to alleviate the cash demand on the Cleanup Fund.

Although the State Water Board anticipates paying off the \$100 million backlog in in-house requests during the 2010-11 fiscal year, additional costs will continue to accrue as sites continue work in 2010-11. The State Water Board anticipates

that some of those costs will be paid this fiscal year, while others will need to wait for payment until next fiscal year when additional funds are available. Claimants have been informed of this possibility, and have been advised to plan site work accordingly. This carryover of existing costs into the 2011-2012 fiscal year, however, will decrease the funds available to implement the new business model in its first year.

Conclusion

The State Water Board continues to make significant progress in improving (a) financial management and cost containment, (b) processing efficiency, and (c) internal controls for the Cleanup Fund. Since it's June 2010 update to the Assembly Budget Subcommittee #3 on this issue, the State Water Board has completed several additional actions that were previously identified as "planned" or "underway" in the June 2010 report, and has begun to implement additional steps towards improving management and oversight of the Cleanup Fund. Implementation of key additional steps, including placing all small business claims on a budget, is planned to be complete by July 2011. The 2011-2012 fiscal year will be a test year for these significant changes to the Cleanup Fund, and any necessary further changes and improvements will be implemented as they are identified through continued ongoing process improvement reviews. It is anticipated that the Cleanup Fund will be operating on a "business as normal" basis incorporating all the planned changes by July 2012.