

STATE OF CALIFORNIA

OFFICE OF ADMINISTRATIVE LAW

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In re:	)	1999 OAL Determination No. 6
Request for Regulatory	)	
Determination filed by EYTAN	)	[Docket No. 97-011]
R. RIBNER concerning	)	
DEPARTMENT OF HEALTH	)	February 17, 1999
SERVICES Medi-Cal rules	)	
relating to submission of	)	Determination Pursuant to
amended cost reports and	)	Government Code Section 11340.5;
application of the Hospital	)	Title 1, California Code of
Cost Index <sup>1</sup>	)	Regulations, Chapter 1, Article 3
_____	)	

**Determination by: CHARLENE G. MATHIAS, Deputy Director**

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**SYNOPSIS**

The issue presented to the Office of Administrative Law ("OAL") is whether rules of the Department of Health Services relating to (1) the submission of amended cost reports and (2) the application of the hospital cost index constitute "regulations," which are void unless adopted pursuant to the Administrative Procedure Act ("APA").

OAL has concluded that (1) the rule relating to submission of amended cost reports and (2) the Department's procedure for applying increments in the hospital cost index to prior years' allowable rates are "regulations," which must be promulgated in accordance with the APA in order to be valid.

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## ISSUE

The issue presented to the Office of Administrative Law is whether a rule and a procedure utilized by the Department to:

- (1) limit opportunities for providers of health care services and supplies under the Medi-Cal program to submit amended cost reports, and
- (2) specify the method for applying increments in the hospital cost index to prior years' allowable rates

are "regulations" and are therefore without legal effect unless adopted in compliance with the APA.

The Office of Administrative Law has concluded that:

- (1) the rule which limits opportunities for providers of health care services and supplies under the Medi-Cal program to submit amended cost reports, and
- (2) the procedure which specifies the method for applying increments in the hospital cost index to prior years' allowable rates

are "regulations" required to be adopted in compliance with the APA. The interpretations are invalid and unenforceable until properly adopted as regulations.

## ANALYSIS

### **I. IS THE APA GENERALLY APPLICABLE TO THE QUASI-LEGISLATIVE ENACTMENTS OF THE DEPARTMENT OF HEALTH SERVICES?**

In 1965, the Medi-Cal program<sup>2</sup> was created by the Legislature as a response to Title XIX of the Social Security Act, which authorized federal financial support to states which adopted conforming medical assistance programs. It was the intent of the Legislature:

“to provide, to the extent practicable, through the provisions of this [Medi-Cal Act], for health care for those aged and other persons, including family persons who lack sufficient annual income to meet the costs of health care, and whose other assets are so limited that their application toward the costs of such care would jeopardize the person or family's future minimum self-maintenance and security.”<sup>3</sup>

The program was administered by the State Department of Health and the Department of Benefit Payments. In 1978, as part of an executive branch reorganization, the Department of Health Services (“DHS”) was made responsible for the administration of the Medi-Cal program. Welfare and Institutions Code section 10721 provides in part:

“The director [of DHS] shall administer [the Medi-Cal Act] . . . and any other law pertaining to the administration of health care services and medical assistance . . . .”

The Director of DHS has been granted general rulemaking authority through Welfare and Institutions Code section 10725. Section 10725 provides in part:

*“The director [of DHS] may adopt regulations, orders, or standards of general application to implement, interpret, or make specific the law enforced by [DHS], and such regulations, orders, and standards shall be adopted, amended, or repealed by the director only in accordance with the [APA] . . . .”* [Emphasis added.]

Welfare and Institutions Code section 14124.5 provides DHS with specific rulemaking authority applicable to the Medi-Cal program. Section 14124.5, subdivision (a) states, in part, that the:

*“. . . director [of DHS] may . . . adopt, amend or repeal, in accordance with [the APA], such reasonable rules and regulations as may be necessary or proper to carry out the purposes and intent of [the Medi-Cal Act] and to enable it to exercise the powers and perform the duties conferred upon it by [the Medi-Cal Act] not inconsistent with any of the provisions of any statute of this state.”*  
(Emphasis added.)

Welfare and Institutions Code sections 10725 and 14124.5, cited above, specifically state that Medi-Cal-related quasi-legislative enactments of DHS are subject to the procedural requirements of the APA.

Additionally, the APA applies to *all* state agencies, except those “in the judicial or legislative departments . . . .”<sup>4</sup> Since the Department of Health Services is in the executive branch of state government, OAL concludes that APA rulemaking requirements generally apply to the Department.<sup>5, 6</sup>

## **II. DO THE CHALLENGED RULES CONSTITUTE "REGULATIONS" WITHIN THE MEANING OF GOVERNMENT CODE SECTION 11342?**

Government Code section 11342, subdivision (g), defines "regulation" as:

“. . . *every* rule, regulation, order, or standard of general application *or* the amendment, supplement, or revision of any rule, regulation, order, or standard adopted by *any* state agency to implement, interpret, or make specific the law enforced or administered by it, or to govern its procedure . . . . (Emphasis added.)”

Government Code section 11340.5, authorizing OAL to determine whether agency rules are "regulations," and thus subject to APA adoption requirements, provides in part:

“(a) *No* state agency shall issue, utilize, enforce, or attempt to enforce *any* guideline, criterion, bulletin, manual, instruction, order, standard of general application, or other rule, which is a [“]regulation[“] as defined in subdivision (g) of Section 11342, *unless* the guideline, criterion, bulletin, manual, instruction, order, standard of general application or other rule has been adopted as a regulation and filed with the Secretary of State pursuant to [the APA]. (Emphasis added.)”

In *Grier v. Kizer*,<sup>7</sup> the California Court of Appeal upheld OAL's two-part test<sup>8</sup> as to whether a challenged agency rule is a "regulation" as defined in the key provision of Government Code section 11342, subdivision (g):

First, is the challenged rule either:

- a rule or standard of general application, *or*
- a modification or supplement to such a rule?

Second, has the challenged rule been adopted by the agency to either:

- implement, interpret, or make specific the law enforced or administered by the agency, *or*
- govern the agency's procedure?

If an uncodified rule satisfies the above two parts of the test, OAL must conclude that it is a "regulation" and is subject to the APA. In applying the two-part test, however, OAL is mindful of the admonition of the *Grier* court:

“. . . because the Legislature adopted the APA to give interested persons the opportunity to provide input on proposed regulatory action (*Armistead* . . . 22 Cal.3d at p. 204, 149 Cal. Rptr. 1, 583 P.2d 744), we are of the view that *any doubt as to the applicability of the APA's requirements should be resolved in favor of the APA.* [Emphasis added.]”

Three California Court of Appeal cases provide additional guidance on the proper approach to take when assessing claims that agency rules are *not* subject to the APA.

According to *Engelmann v. State Board of Education* (1991), agencies need not adopt as regulations those rules contained in "a statutory scheme which the Legislature has already established. . . ." <sup>10</sup> But "to the extent that any of the [agency rules] depart from, or embellish upon express statutory authorization and language, the [agency] will need to promulgate regulations. . . ." <sup>11</sup>

Similarly, agency rules properly promulgated *as regulations* (i.e., California Code of Regulations ("CCR") provisions) cannot legally be "embellished upon" in administrative bulletins. For example, *Union of American Physicians and Dentists v. Kizer* (1990) <sup>12</sup> held that a terse 24-word definition of "intermediate physician service" in a Medi-Cal regulation could not legally be supplemented by a lengthy seven-paragraph passage in an administrative bulletin that went "far

beyond" the text of the duly adopted regulation.<sup>13</sup> Statutes may legally be amended only through the legislative process; duly adopted regulations--generally speaking--may legally be amended only through the APA rulemaking process.

The third case, *State Water Resources Control Board v. Office of Administrative Law (Bay Planning Commission)* (1993), made clear that reviewing authorities focus on the *content* of the challenged agency rule, not the *label* placed on the rule by the agency:

" . . . the . . . Government Code [is] careful to provide OAL authority over regulatory measures whether or not they are designated 'regulations' by the relevant agency. In other words, *if it looks like a regulation, reads like a regulation, and acts like a regulation, it will be treated as a regulation whether or not the agency in question so labeled it. . . .*" [Emphasis added.]<sup>14</sup>

Thus, we will first analyze whether the challenged rules are standards of general application or modifications or supplements to such a rule or standard; and secondly, whether the challenged rules (1) interpret, implement, or make specific the law enforced or administered by the agency, or (2) governs the agency's procedure.

#### **A. ARE THE CHALLENGED RULES "STANDARDS OF GENERAL APPLICATION?"**

The requester asserts, and the Department apparently agrees,<sup>15</sup> that the Department changed its interpretation of a codified regulation. CCR, Title 22, section 51019, subsection (a), unchanged since 1980, provides, in part, as follows:

"An amended cost report may be submitted by a provider and accepted by the Department for the fiscal period or periods for which proceedings are pending under this article."

According to the requester, the Department currently interprets the CCR language relating to the submission and acceptance of amended cost reports to mean that an amended report may *only* be filed while an appeal is pending.

An agency standard applies generally if the rule applies to all members of a class, kind, or order.<sup>16</sup> The CCR provision, entitled "Amended Cost Reports," and

Article 1.5, "Provider Audit Appeals," of which it is a part, apply to both institutional and non-institutional entities that provide services or supplies under the Medi-Cal program.<sup>17</sup> Consequently, it is reasonable to assume that the challenged rule (the changed interpretation of section 51019 relating to submission of amended cost reports) also applies statewide to all such providers of Medi-Cal services.

The second challenged rule is the procedure for applying increments in the hospital cost index to prior years' allowable rates when determining the maximum allowable reimbursement. The index applies to all providers of Medi-Cal services or supplies, and operates to limit the annual increment in the maximum amount of reimbursement. The method of computation utilized by the Department to determine the maximum allowable reimbursement, likewise, applies generally.

For these reasons, OAL concludes that both of the challenged rules are standards of general application.

**B. DO THE CHALLENGED RULES INTERPRET, IMPLEMENT, OR MAKE SPECIFIC THE LAW ENFORCED OR ADMINISTERED BY THE AGENCY OR GOVERN THE AGENCY'S PROCEDURE?**

Under the Medi-Cal program, a provider of health care services or supplies receives payment from the program. CCR, Title 22, section 51536, subsection (a) provides:

"Reimbursement for hospital inpatient services provided to Medi-Cal program beneficiaries shall be the lesser of the following for each hospital:

- (1) Customary charges.
- (2) *Allowable costs* determined in accordance with applicable Medi-care standards and principles of reimbursement.
- (3) All-inclusive rate per discharge." [Emphasis added.]

- (1) FIRST CHALLENGED RULE - SUBMISSION OF AMENDED COST REPORTS (concerning "allowable costs" under Title 22, section 51536(a)(2))

The cost-based method of limiting payment (established in Title 22, CCR, section 51536 (a)(2)), makes it necessary for hospitals providing inpatient services under the program to report their costs to the Department. The Department, in turn, is obliged to audit amounts paid for services provided to Medi-Cal beneficiaries.<sup>18</sup> CCR, Title 22, sections 51016 through 51048 set forth the standards and procedures for appeals of the Department's audit findings. In this regard, and as noted above, Section 51019, subsection (a) provides as follows:

“An amended cost report may be submitted by a provider and accepted by the Department for the fiscal period or periods for which proceedings are pending under this article.”

Section 51019, subsection (a) has not been amended since 1980. The Department's interpretation of this provision is the first challenged rule.

#### Original Interpretation of CCR, Title 22, section 51019

The requester alleges that until mid-1989, the Department followed an interpretation of section 51019 which tracked 42 CFR §405.1885 and federal Provider Reimbursement Manual - 1 (“PRM-1”) section 2931.2. Requester provided a description of this interpretation quoted from a DHS decision on an administrative appeal.<sup>19</sup> The description, quoted below, indicates that section 51019:

“... simply serves as a notice to both the Department and providers that the existence of a pending proceeding *does not preclude* a provider from filing an amended cost report, having that amended cost report accepted by the Department, and having any new issues raised by that amended report considered at that proceeding or a subsequent proceeding. *This section only confirms the provider's right to file an amended cost report even if proceedings are currently then pending.*” [Emphasis added by requester.]

#### New Interpretation of CCR, Title 22, section 51019

The requester alleges that since mid-1989, the Department has interpreted the CCR language relating to the submission and acceptance of amended cost reports to mean that an amended report may *only* be filed while an appeal is pending.<sup>20</sup>

He asks OAL to determine whether this change in policy is a “regulation” which must be adopted in accordance with the APA in order to be valid.

As noted above in section II, pp. 5-6, of this determination, *Union of American Physicians and Dentists v. Kizer* makes clear that DHS rules that interpret, implement, and make specific Medi-Cal regulations printed in the CCR are subject to the APA. The DHS argument that, in general, rules which interpret CCR provisions should be deemed exempt from APA requirements will be discussed below, in section III.C. of this determination.

Responding to requester’s specific contention, the Department points out that section 51019 is an existing regulation and contends that the new interpretation comports with its plain meaning, while the original interpretation did not. The Department argues that “the only alleged change in interpretation is to enforce the regulation.”<sup>21</sup> The Department may be arguing by implication that the Department is now enforcing the only legally tenable interpretation of the section 51019.

If the Department’s new interpretation of section 51019 is indeed the only legally tenable interpretation of existing applicable law, then the Department would be correct to turn away from any prior interpretation inconsistent with that law, and follow the lawfully adopted regulation. In such a circumstance, the practice of following the original, incorrect interpretation of the law would be the improper action, and no additional rulemaking by the agency would be required prior to using the correct and only legally tenable interpretation. The foregoing example is, of course, only hypothetical, and depends upon the very important condition that the second interpretation of the regulation utilized by the agency is the *only* one that is legally tenable. The problem with this hypothetical is that section 51019 is, without doubt, a regulation susceptible to *more than one possible interpretation*.

The fact that for years, the Department followed a different practice, despite having promulgated the language in subsection (a) of section 51019 in 1980,<sup>22</sup> certainly suggests that there may be another legally tenable interpretation of its provisions. Although the Department characterizes its change in course simply as a turning away from a mistaken decision concerning the applicability of federal Medicare law, this theory does not withstand close examination. The Court of Appeal, Second District, has already considered the new interpretation of section 51019 and found it to be unreasonable. In the case of *Mission Community Hospital v. Kizer* (1993),<sup>23</sup> the Court acknowledged that:

“California Code of Regulations section 51019 provides a reasonable regulation for the timely submission of amended cost reports and is not in conflict with Welfare and Institutions Code section 14170. Accordingly, California Code of Regulations section 51019 is entitled to our deference. [footnote 9].”

Footnote no. 9 to the opinion states:

“[Mission Community Hospital’s] assertion of an unlimited time frame for the filing of amended cost reports is an unreasonable statutory interpretation. To the extent [the Department of Health Services] contends that its regulation [section 51019] does not permit amended cost reports to be submitted unless an audit proceeding is pending, *we conclude such interpretation is also unreasonable.*”  
[Emphasis added.]

Thus, the challenged rule has already been judicially determined to be an unreasonable interpretation of a duly adopted regulation. OAL is bound by this determination. It flies in the face of logic for the Department to argue that an interpretation found to be *unreasonable* by the California Court of Appeal is the only legally tenable interpretation. Clearly, the new interpretation of section 51019 is not the *only* legally tenable interpretation, and given the finding of the Court of Appeal, it is not legally tenable at all.

OAL concludes that the Department’s new interpretation of section 51019 satisfies the definition of “regulation” as set out in the APA because it implements and interprets Welfare and Institutions Code section 14170 and CCR, Title 22, section 51019, and governs the Department’s procedure<sup>24</sup> by limiting the time period in which amended cost reports may be filed.

(2) SECOND CHALLENGED RULE - PROCEDURE FOR APPLICATION OF THE HOSPITAL COST INDEX

The requester has challenged the Department’s procedure for applying increments in the Hospital Cost Index to prior years’ allowable rates. Use of the Hospital Cost Index is required by CCR, Title 22, section 51536, subsection (f) which provides:

“A hospital cost index shall be established for each hospital. This index shall consist of an input price index and an allowance for changes in service intensity.

“(1) The hospital cost index shall be calculated to account for *actual changes in the input price index* after the close of each hospital’s accounting year.

“(2) The hospital cost index shall be applied on a cumulative basis to the hospital’s rate per discharge for the base year to determine its rate per discharge for the final settlement year. [Emphasis added.]”

Concerning the base year cost per discharge, and the rate per discharge, section 51536, subdivision (b), paragraph (6) provides:

“Rate per discharge means the hospital specific, all-inclusive rate per Medi-Cal discharge which, when multiplied by the number of Medi-Cal discharges, including deaths but excluding newborns, in the hospital’s accounting year, determines the total dollar limit on reimbursable cost for that accounting year. The Department shall adjust the base year cost per discharge from the *midpoint* of the hospital’s fiscal year to the implementation date of these regulations to ensure uniform application of the reimbursement system. *This rate shall become the rate per discharge for the base year.* [Emphasis added.]”

Pursuant to the rule above, base year rates were determined on the original effective date of section 51536, which was July 1, 1980. It appears that the rate per discharge for any subsequent year would properly be determined by adding the sum of the annual changes for all years since the base rate was determined to the rate per discharge for the base year. The annual change for a particular hospital is calculated after the close of the hospital’s accounting year. Requester argues that the Department adopted and twice changed the method of accounting utilized to adjust the base year rate by the Hospital Cost Index without following the APA.

The Department, in its reply to this request for determination, acknowledges the changes in accounting method:

“In cost settlement calculations made when the current reimbursement system was first adopted in 1980, the hospital cost index was applied to the prior year’s allowable rate per discharge only. Thus, no averaging technique was utilized. Beginning in 1981, the hospital cost index was applied to the beginning rate per discharge for each settlement year (the ending rate per discharge for the prior year) to compute the ending rate per discharge in that settlement year. The beginning and ending rates were then averaged to determine the settlement year allowable rate per discharge. Thereafter, in August, 1990, the Department began computing cost settlements by applying the hospital cost index to the prior year’s allowable rate per discharge only. Thus no averaging technique was utilized.”

The Department points out that the method of computation of the Hospital Cost Index is specified in detail in section 51536. It also notes:

“Neither this regulation - nor any other statute or regulation - mandates any specific application of the hospital cost index. As the Department has gained experience with methods of calculating hospital costs, it has adjusted its methods to produce calculations which more closely reflect the intent of the governing State and federal regulations. These adjustments in the methodology were made because *the governing regulations had to be interpreted and applied* in a way that was equally fair to different hospitals, which had fiscal periods ending on different dates. [Emphasis added.]”<sup>25</sup>

Thus, the Department has admitted that its methodology for applying the Hospital Cost Index *interprets* section 51536. Because the challenged accounting method interprets and supplements a regulation administered by the Department and governs its procedure, OAL concludes that the Department’s uniform method of applying the hospital cost index is a “regulation.”

For the reasons described above, each of the challenged rules is a “regulation” within the meaning of Government Code section 11342, subdivision (g). The challenged rules apply generally, and were issued to interpret, supplement, implement and make specific laws enforced by the Department, or govern its procedure. These “regulations” should have been adopted pursuant to the APA.

### III. DO THE CHALLENGED RULES FOUND TO BE “REGULATIONS” FALL WITHIN ANY RECOGNIZED EXEMPTION FROM APA REQUIREMENTS?

Generally, all “regulations” issued by state agencies are required to be adopted pursuant to the APA, unless expressly exempted by statute.<sup>26</sup> In *United Systems of Arkansas v. Stamison* (1998),<sup>27</sup> the California Court of Appeal rejected an argument by the Director of the Department of General Services that language in the Public Contract Code had the effect of exempting rules governing bid protests from the APA.

According to the *Stamison* Court:

*“When the Legislature has intended to exempt regulations from the APA, it has done so by clear, unequivocal language. (See, e.g., Gov. Code, section 16487 [‘The State Controller may establish procedures for the purpose of carrying out the purposes set forth in Section 16485. These procedures are exempt from the Administrative Procedure Act.’]; Gov. Code, section 18211 [‘Regulations adopted by the State Personnel Board are exempt from the Administrative Procedure Act’]; Labor Code, section 1185 [orders of Industrial Welfare Commission ‘expressly exempted’ from the APA.] [Emphasis added.]”<sup>28</sup>*

Express statutory APA exemptions may be divided into two categories: special and general.<sup>29</sup> *Special* express statutory exemptions typically: (1) apply only to a portion of one agency’s “regulations” and (2) are found in that agency’s enabling act. *General* express statutory exemptions typically: (1) apply across the board to all state agencies and (2) are found in the APA. An example of an express *special* exemption is Penal Code section 5058, subdivision (d)(1), which exempts pilot programs of the Department of Corrections under specified conditions. An example of an express *general* exemption is Government Code section 11342, subdivision (g), part of which exempts “internal management” regulations of all state agencies from the APA.

**A. DO THE CHALLENGED RULES FOUND TO BE “REGULATIONS” FALL WITHIN ANY *SPECIAL* EXPRESS APA EXEMPTION?**

In this determination proceeding, DHS does not contend that any special statutory exemption applies. Our independent research having also disclosed no special statutory exemption, we conclude that none applies.

**B. DO THE CHALLENGED RULES FOUND TO BE “REGULATIONS” FALL WITHIN ANY *GENERAL* EXPRESS APA EXEMPTION?**

**1. Internal Management**

The APA excepts policies which pertain solely to the internal management of a state agency from the notice and hearing requirements of the Act.<sup>30</sup> Government Code section 11342, subdivision (g) states:

“Regulation” means every rule, regulation, order, or standard of general application or the amendment, supplement or revision of any such rule, regulation, order or standard adopted by any state agency to implement, interpret, or make specific the law enforced or administered by it, or to govern its procedure, *except one that relates only to the internal management of the state agency.* [Emphasis added.]”

However, as the *Grier* Court found: “. . . the definition of regulation is broad, as contrasted with the scope of the internal management exception, which is narrow.”<sup>31</sup> Internal management policies are those designed to govern the internal operations of the Department. The exception does not apply to “. . . the rules necessary to properly consider the interests of all who will seek consideration under the provisions of the statutes dealing with review and allocations.”<sup>32</sup>

In *City of San Joaquin v. State Board of Equalization* (1970),<sup>33</sup> a statistical accounting technique was held not to be a “regulation” within the meaning of the APA. The *San Joaquin* court held the pooling procedure required by the Board’s challenged rule was:

“merely a statistical accounting technique to enable the Board to allocate, as expediently and economically as possible, to each [participating city], its fair share of sales taxes collected by the Board on that city’s behalf.”

Considering *San Joaquin*, the California Court of Appeal, in *Grier v. Kizer* (1990) wrote:

“In view of the Supreme Court’s subsequent recognition in *Armistead* of the distinction between purely internal rules which merely govern an agency’s procedure and rules which have external impact so as to invoke the APA, [citations] *San Joaquin*’s holding that statistical accounting techniques are exempt from the APA appears to have lost its precedential value. After *Armistead*, it would appear an accounting procedure resulting in a possibly disproportionate allocation of tax revenues would be the appropriate subject of a regulation adopted pursuant to the APA, allowing interested parties to be heard on the merits of the proposed rule.”<sup>34</sup>

The rules at issue in this determination clearly deal with the interests of all Medi-Cal providers who desire to submit amended cost reports to the Department or are concerned about the procedure for applying the hospital cost index in order to determine the maximum allowable rate of payment. With regard to the hospital cost index, the accounting method selected by the Department could possibly affect the maximum allowable rate of payment. For these reasons, the Department’s policies are not covered by the internal management exception to the APA.

**C. Argument that *interpretations* of codified regulations should be deemed exempt from the APA**

The Department does not argue that the challenged rules are exempt from the APA under any express *statutory* exemption.<sup>35</sup> Rather, relying on *case law*,<sup>36</sup> the Department appears to argue that state agency interpretations of regulations codified in the CCR are generally *not* subject to the APA.

First, the Department states:

“An interpretation of an existing regulation does not constitute a new regulation for purposes of compliance with APA procedures. The California Supreme Court has recently found that, in a variety of situations, the interpretation of a regulation by the agency charged with its

administration does not itself constitute a regulation for the purposes of the APA. (*Tidewater Marine Western, Inc. v. Bradshaw* (1996) 14 Cal.4th 557, 571-572.)”<sup>37</sup>

We are not sure precisely what legal argument is being made in the passage just quoted.<sup>38</sup> It is clear, however, that the argument (whatever its precise parameters) is at odds with the primary APA holdings in *Tidewater*.<sup>39</sup> The two primary APA issues in *Tidewater* were (1) whether the APA applied to the state agency in question, the Division of Labor Standards Enforcement (“DLSE”) and (2) whether the particular DLSE policy at issue (*a policy which interpreted a CCR provision*) constituted a “regulation” as defined in the APA. The first issue is not relevant here; DHS does not argue that it as an agency is wholly exempt from the APA. Concerning the second issue, the *Tidewater* court, quoting Government Code section 11342, subdivision (g), stated that the APA defines “regulation” “*very broadly.*” (Emphasis added.)<sup>40</sup> The court concluded that DLSE policy interpreting the CCR provision was a “regulation” within the meaning of the APA and thus “void.”<sup>41</sup>

The court went on to overrule two appellate cases which had held that specific DLSE policies (that had also interpreted CCR provisions) were not “regulations” within the meaning of the APA: *Bono Enterprises, Inc. v. Bradshaw* (1995) (policy for calculating overtime pay)<sup>42</sup> and *Skyline Homes, Inc. v. Department of Industrial Relations* (1985) (policy requiring employer to pay employees if they have to remain on its premises during lunch hour).<sup>43</sup> Both of these previously litigated DLSE policies were, the *Tidewater* court concluded, “regulations” within the meaning of the APA, and the lower courts had been in error in holding to the contrary.

In analyzing the second APA issue, the *Tidewater* court also clearly rejected an imaginative argument put forward by Professor Michael Asimow in a friend of the court brief. Professor Asimow had urged the court to issue a sweeping declaration that “interpretive regulations” were not subject to the APA. The court rejected this suggestion, noting that:

“Government Code section 11340.5 makes clear that the rulemaking procedures of the APA apply to any ‘regulation,’ and the definition of regulation includes ‘every rule . . . adopted . . . to . . . *interpret* . . . the law . . . (i.e., interpretive regulations). (Gov. Code, sec. 11342, subd. (g), [“interpret” italicized by the court]. *If the Legislature did not intend the*

*APA to apply to interpretive regulations, we do not think it would have expressly included interpretive regulations in this definition. . . .*

Furthermore, when the Legislature wanted to create exceptions to the formal rulemaking requirements of the APA, it did so expressly and in separate sections. (Gov. Code, secs. 11346.1, subd. (a), 11343, subds. (a), (b); see also Gov. Code sec. 11351; Lab. Code, sec. 1185.) [Emphasis added.]”<sup>44</sup>

From the above, it is clear that, based upon unambiguous statutory language, the Supreme Court has definitively rejected the thesis that “interpretive regulations” or, in other words, interpretations of codified regulations, are categorically exempt from the APA.

In addition, three Court of Appeal decisions make it clear that agency rules interpreting CCR provisions are subject to the APA. The first, *Union of American Physicians and Dentists v. Kizer* (1990),<sup>45</sup> is discussed above in section II of this determination. The second, *Goleta Valley Community Hospital v. State Department of Health Services* (1984),<sup>46</sup> held that a DHS rule interpreting a Medi-Cal reimbursement regulation (Title 22, CCR, section 51537) violated the APA. The *Goleta Valley* court noted that “. . . the power to overrule an earlier interpretation of an agency’s regulations does not necessarily render the act of reinterpretation procedurally valid.”<sup>47</sup> The *Goleta Valley* court agreed that DHS could elect to abandon an earlier interpretation of the CCR provision in question, but that the new interpretation was procedurally “invalid” due to failure to comply with the APA. The third Court of Appeal decision, *Motion Picture Studio Teachers v. Milan* (1996),<sup>48</sup> struck down a state agency rule interpreting a CCR provision, stating:

“An agency may not alter a regulation except by the APA process (*Goleta Valley Community Hospital v. State Department of Health Services* (1983) 149 Cal.App.3d 1124, 1129, 197 Cal.Rptr. 294), which is similar to the procedures that govern its adoption. The procedure for adoption, amendment and repeal of a regulation parallel the law applicable to statutory changes. If a state agency believes that a regulation it adopted ought to be changed, it may only accomplish that result through the APA procedure, a process that ordinarily requires advance publication and an opportunity for public comment. (See Gov. Code, secs. 11346.4, 11346.5, 11346.8.) . . .”

Second, the Department argues that its method of applying the Hospital Cost

Index is exempt from the APA. Citing *Aguilar v. Association of Retarded Citizens* (1991),<sup>49</sup> the Department contends:

“. . . an agency charged with enforcing a regulation is permitted to interpret that regulation, and in doing so it need not comply with the APA. The different application of the cost index in the calculation of Medi-Cal reimbursement is an exercise of this agency’s permissible discretion to interpret its regulations. Moreover, the interpretation of the regulation under discussion here is the type of interpretation which the Supreme Court has held *not* to be a regulation (*Tidewater Marine Western, Inc. v. Bradshaw* [(1996)]. [Emphasis in original.]”<sup>50</sup>

We cannot agree with this argument for three reasons.

*One:* the argument stated in the first quoted sentence (“permitted to interpret . . . and in so doing need not comply with the APA”) has been dealt with just above, in the discussion of the Department’s first contention (pages 16-17). This argument is expressly rejected in *Tidewater* and other appellate opinions. In addition, the precedential authority of *Aguilar* (the only case cited by DHS) has been gravely weakened by the *Tidewater* court’s decision to overrule *Skyline*--the case so heavily relied upon by *Aguilar*.

In *Aguilar*, the Division of Labor Standards Enforcement’s interpretation of Industrial Welfare Commission Wage Order 5-80, section 2(H) was challenged as an improper regulation. The court in *Aguilar* relied on an earlier case, *Skyline Homes, Inc. v. Department of Industrial Relations* (1985), which had presented a comparable situation. Both cases arose from the Division of Labor Standards Enforcement’s efforts to enforce wage orders, which had been properly adopted as regulations of the Industrial Welfare Commission. The Court of Appeal, in *Skyline* wrote:

“The DLSE is charged with enforcing the wage orders, and to do so, it must first interpret them. The enforcement policy is precisely that--an interpretation--and need not comply with the APA.”<sup>51</sup>

Following the rationale of *Skyline*, the court in *Aguilar* wrote:

“*In this case as well* the IWC Wage Order was properly applied. DLSE’s action here amounted to no more than an interpretation of

that Wage Order and its application to a specific situation. DLSE's interpretation did not create a new rule or policy; it construed the words of the IWC Wage Order. The fact DLSE did not adopt ARC's [Defendant's] interpretation does not mean that DLSE must have engaged in rule-making rather than interpretation. Adoption of an interpretation consistent with the language and intention of the Wage Order as a prelude to enforcement does not require compliance with the APA. [Emphasis added.]”<sup>52</sup>

The court in *Tidewater* disapproved of the decision in *Skyline*, stating:

“The policy for calculating overtime pay at issue in *Skyline Homes* was a regulation within the meaning of the APA because it was a standard of general application interpreting the law the DLSE enforced and because it was not merely a restatement of prior agency decisions [<sup>53</sup>] or advice letters.<sup>[54]</sup> We acknowledge that the employer challenged the policy in the context of a particular adjudication, but this fact *does not alter its character as a policy of general application and thus a regulation*. [Emphasis added.]”<sup>55</sup>

Similarly, the *Tidewater* court also noted:

“A written statement of policy that an agency intends to apply generally, that is unrelated to a specific case, and that predicts how the agency will decide future cases is *essentially legislative in nature* even if it merely interprets applicable law. [Emphasis added.]”<sup>56</sup>

The various procedures for applying the hospital cost index utilized by the Department have applied *generally*, not simply to one particular hospital. They are not interpretations made necessary in order to properly adjust one *particular* hospital's maximum allowable rate. Like the policy for calculating overtime pay in *Skyline*, the Department's authoritative selection of the accounting procedure is essentially quasi-legislative in nature, and thus a “regulation.”

*Two*: the issue is not whether DHS has “discretion” to interpret its regulations (duly adopted and printed in the CCR). It clearly has that discretion. To paraphrase the *Tidewater* court: the issue, rather, is DHS's “power to interpret [its] regulation[s] in an enforcement policy of general application *without following the APA*.” (Emphasis added.)<sup>57</sup>

*Three:* in a one-sentence passage, DHS argues that the interpretation of the CCR provision under discussion here is “the type of interpretation” which the Supreme Court has held *not* to be a regulation in *Tidewater*. DHS does not specify the legal theory under which it would argue that its interpretation of Title 22, CCR, section 51536 is not a “regulation.” Absent more details, we must reject this argument.

### CONCLUSION

For the reasons set forth above, OAL concludes that the challenged rules, which:

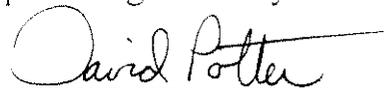
- 1) Limit opportunities for providers of health care services and supplies under the Medi-Cal program to submit amended cost reports, and
- 2) Set forth the procedure for applying increments in the hospital cost index to prior years’ allowable rates when determining the maximum allowable reimbursement

are “regulations” that are without legal effect unless adopted in compliance with the APA. No exceptions to APA requirements are applicable.

DATE: February 17, 1999



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## ENDNOTES

1. This determination was requested by Eytan Ribner, "requester," of Blumberg Ribner, Inc. 315 South Beverly Drive, Suite 505, Beverly Hills, California 90212 (310) 551-1925, represented by Mitchell R. Miller, Attorney At Law, same address, (310) 277-1848. The State Department of Health Services was represented by John R. Pierson, Deputy Director and Chief Counsel, Department of Health Services, 714/744 P Street, P.O. Box 942732, Sacramento, CA 94234-7320, (916) 657-0742.

On October 2, 1998, OAL published a summary of this Request for Determination in the California Regulatory Notice Register ("CRNR") 98, No. 40-Z, p. 1977, along with a notice inviting public comment. No public comments were received. The Department of Health Services filed a response to the request for determination.

2. Medi-Cal Act (chapter 7, part 3, division 9, of the Welfare and Institutions Code, sections 14000 - 14196.1).
3. Welfare and Institutions Code section 14000.
4. Government Code section 11342, subdivision (a). See Government Code sections 11343 and 11346. See also 27 Ops.Cal.Atty.Gen. 56, 59 (1956).
5. See *Poschman v. Dumke* (1973) 31 Cal.App.3d 932, 943, 107 Cal.Rptr. 596, 609.
6. Cases holding that DHS is subject to the APA are listed in 1987 OAL Determination No. 10, note 7; California Regulatory Notice Register 98, No. 8-Z, February 23, 1996, p. 292, note 7 (determination concluding certain DHS Medi-Cal rules violated the APA).
7. (1990) 219 Cal.App.3d 422, 440, 268 Cal.Rptr. 244, 251. We note that a 1996 California Supreme Court case stated that it "disapproved" of *Grier* in part. *Tidewater Marine Western, Inc. v. Bradshaw* (1996) 14 Cal.4th 557, 577. *Grier*, however, is still good law, except as specified by the *Tidewater* court. Courts may cite cases which have been disapproved on other grounds. For instance, in *Doe v. Wilson* (1997) 57 Cal.App.4th 296, 67 Cal.Rptr.2d 187, 197, the California Court of Appeal, First District, Division 5, cited *Poschman v. Dumke* (1973) 31 Cal.App.3d 932, 107 Cal.Rptr. 596, on one point, even though *Poschman* had been expressly disapproved on another point nineteen years earlier by the California Supreme Court in *Armistead v. State Personnel Board* (1978) 22 Cal.3d 198, 204 n. 3, 149 Cal.Rptr. 1, 3 n. 3. Similarly, in *Economic Empowerment Foundation v. Quackenbush* (1997) 57 Cal.App.4th 677, 67 Cal.Rptr.2d 323, 332, the California Court of Appeal, First District, Division 4, nine months after *Tidewater*, cited *Grier v. Kizer* as a distinguishable case on the issue of the futility exception to the exhaustion of administrative remedies requirement. Finally, the California Court of Appeal, Third District, citing *Grier* for the proposition that any doubt as the applicability of the APA's requirements should be resolved in favor of the APA, noted that *Grier* had been "disapproved on another point" in *Tidewater*. *United Systems of Arkansas v. Stamison*

(1998) 63 Cal.App.4th 1001, \_\_\_\_, 74 Cal.Rptr.2d 407, 412, review denied.

*Tidewater* itself, in discussing which agency rules are subject to the APA, referred to "the two-part test of the Office of Administrative Law," citing *Union of American Physicians & Dentists v. Kizer* (1990) 223 Cal.App.3d 490, 497, 272 Cal.Rptr. 886, a case which quotes the test from *Grier v. Kizer*.

8. The *Grier* Court stated:

"The OAL's analysis set forth a two-part test: 'First, is the informal rule either a rule or standard of general application or a modification or supplement to such a rule? [Para.] Second, does the informal rule either implement, interpret, or make specific the law enforced by the agency or govern the agency's procedure?' (1987 OAL Determination No. 10, *supra*, slip op'n., at p. 8.)

OAL's wording of the two-part test, drawn from Government Code section 11342, has been modified slightly over the years. The cited OAL opinion--1987 OAL Determination No. 10--was published in California Regulatory Notice Register 98, No. 8-Z, February 23, 1996, p. 292.

9. (1990) 219 Cal.App.3d 422, 438, 268 Cal.Rptr. 244, 253, review denied.

9. 2 Cal.App.4th 47, 62, 3 Cal.Rptr.2d 264, 275-75, review denied.

11. *Id.*

12. 223 Cal.App.3d 490, 501, 272 Cal.Rptr. 886, 891.

13. *Id.*

14. (1993) 12 Cal.App.4th 697, 702, 16 Cal. Rptr.2d 25, 28.

15. Agency response to this request for determination, page 2, paragraphs 2 and 3.

16. *Roth v. Department of Veteran Affairs* (1980) 110 Cal.App.3d 622, 167 Cal.Rptr.552. See *Faulkner v. California Toll Bridge Authority* (1953) 40 Cal.2d 317, 323-324 (standard of general application applies to all members of any open class.)

17. See CCR, Title 22, section 51016, subsections (a)(13), (14).

18. Welfare and Institutions Code section 14170.

19. *In the Matter of St. Joseph's Hospital of Orange*, DHS Audit Appeal No. HA1-0687-057, adopted as final 2/11/92, at p. 6.
20. Request for determination, page 2.
21. Agency response to request for determination, dated November 13, 1998, page 2, paragraph 3.
22. The language of CCR, Title 22, section 51019, subsection (a) was filed with the Secretary of State on May 8, 1980, effective June 4, 1980, (Register 80, No. 19) and has not been amended since.
23. (1993) 13 Cal.App.4th 1683, 1691, 17 Cal.Rptr.2d 303, 310.
24. Government Code section 11342, subdivision (g), clearly provides that "every rule . . . adopted by any state agency . . . to govern its *procedure*" (emphasis added) is a "regulation" subject to the APA. See *City of San Marcos v. California Highway Commission* (1976) 60 Cal.App.3d 383, 131 Cal.Rptr. 804 (deadline for receipt of grant applications violated APA).  
  
A comment on page two of the DHS response may be read to suggest that interpretations of CCR provisions which concern "procedural matter[s]" are somehow less significant or less subject to the APA. This is incorrect. Uncodified agency rules which amend, supplement, or revise procedural regulations printed in the CCR are, following the plain language of section 11342, subdivision (g), fully subject to the APA. In addition, agency procedural rules often have a significant impact on the regulated public, as was the case in the *City of San Marcos* case, cited just above.
25. Agency response to request for determination, p.3.
26. Government Code section 11346.
27. 63 Cal.App.4th 1001, \_\_\_, 74 Cal.Rptr.2d 407, 411-12, review denied.
28. 63 Cal.App.4th at \_\_\_, 74 Cal.Rptr.2d at 411.
29. Cf. *Winzler & Kelly v. Department of Industrial Relations* (1981) 121 Cal.App.3d 120,126, 174 Cal.Rptr. 744, 747 (exemptions found either in prevailing wage statute or in the APA itself).
30. Government Code section 11342, subdivision (g).
31. *Grier v. Kizer*, *supra*, 219 Cal.App.3d 422, 438, 268 Cal.Rptr. 244, 251, disapproved on another point, *Tidewater Marine Western, Inc. v. Bradshaw* (1996) 14 Cal.4th 557, 577, 59 Cal.Rptr.2d 186, 198.

32. *City of San Marcos v. California Highway Commission, Department of Transportation* (1976) 60 Cal.App.3d 383, 408, 131 Cal.Rptr. 804, 820.
33. (1970) 9 Cal.App.3d 365, 88 Cal.Rptr. 12, 20.
34. (1990) 219 Cal.App.3d 422, 442, 268 Cal.Rptr. 244, 253.
35. See Government Code section 11346 (APA exemptions must be expressly stated in statute).
36. According to Government Code section 11346, APA procedural requirements apply to “the exercise [by any state agency] of any quasi-legislative power conferred by any statute” except where legislation has expressly superseded or modified the procedures required by the APA (i.e., where an express statutory exemption has been enacted). Though courts will, of course, be called upon to determine (1) whether specific statutory language constitutes an express statutory exemption (e.g., *United Systems of Arkansas v. Stamison* (1998) 63 Cal.App.4th 1001, 74 Cal.Rptr.2d 407, review denied) and (2) the scope of a particular express statutory exemption (e.g., *California Coastal Commission v. Office of Administrative Law* (1989) 210 Cal.App.3d 758, 258 Cal.Rptr. 560, review denied), it seems clear that courts may not themselves create APA exemptions based solely upon public policy concerns. Pertinent principles concerning limitations on judicial power were stated in a 1987 APA case from the California Court of Appeal for the Third District: *Johnston v. Department of Personnel Administration* (1987) 191 Cal.App.3d 1218, 236 Cal.Rptr. 853, review denied. The *Johnston* court rejected a state agency’s argument that a statute be interpreted to include a criterion that reflected agency practice, a criterion that was not actually present in the statute. The Court stated:

“A court may not insert into a statute qualifying provisions not included or rewrite a statute to conform to an inferred intention that does not appear from its language. (*Mills v. Superior Court* (1986) 42 Cal.3d 951, 957, 232 Cal.Rptr. 141, 728 P.2d 211.)” (191 Cal.App.3d at 1223.)

Responding to an agency argument that failure to interpret the statute to include a criterion customarily included as a matter of agency practice would lead to a “deluge” of hearing requests, the Court also stated:

“DPA’s argument is more appropriately addressed to the Legislature. . . . The sole judicial function is to enforce statutes as written. This court is without the authority to determine the wisdom, desirability, or propriety of statutes enacted by the Legislature. (*Estate of Horman* (1971) 5 Cal.3d 62, 77, 95 Cal.Rptr. 433, 485 P.2d 785.)”

37. Agency response, p. 3.

38. It may be that the quoted passage was not intended to constitute an exemption argument. Insofar as it was intended to constitute a legal defense, however, it should be dealt with.
39. However, DHS' position is consistent with the *vacated* opinion of the Court of Appeal, Second District, Division 6, which stated:

“A regulation is a ‘*rule of general application which implements, interprets and makes specific the statute . . .*’ (citations omitted). DLSE internal policies which interpret or construe the words of a wage order [duly adopted regulation printed in the CCR] and apply the order to a specific situation are not regulations within the meaning of the Administrative Procedures [sic] Act. (*Aguilar v. Association for Retarded Citizens* (1991) 234 Cal.App.3d 21, 27, 286 Cal.Rptr. 515.) [*Tidewater v. Labor Commissioner* (1995) 43 Cal.Rptr.2d at 420; emphasis added.]”

This *vacated* opinion seemingly took the position that an agency interpretation of a regulation printed in the CCR could *never* be found to violate the APA!

40. 59 Cal.Rptr.2d at 194.
41. 59 Cal.Rptr.2d at 198.
42. 32 Cal.App.4th 968, 38 Cal.Rptr.2d 549.
43. 165 Cal.App.3d 239, 211 Cal.Rptr. 792.
44. 59 Cal. Rptr.2d. at 197.
45. 223 Cal.App.3d 490, 501, 272 Cal.Rptr. 886, 891.
46. 149 Cal.App.3d 1124, 197 Cal.Rptr. 294, review denied.
47. 197 Cal.Rptr. at 297.
48. 51 Cal.App.4th 1190, 59 Cal.Rptr.2d 608.
49. (1991) 234 Cal.App.3d 21, 25-26.
50. Agency response, p. 3.
51. *Skyline Homes v. Department of Industrial Relations* (1985) 165 Cal.App.3d 239, 253; 211 Cal.Rptr. 792, 800.
52. (1991) 234 Cal.App.3d 21, 27, 285 Cal.Rptr. 515, 518.

53. In dictum, *Tidewater* states that “[i]nterpretations that arise in the course of case-specific adjudication are not regulations, though they may be persuasive as *precedents* in similar subsequent cases.” (59 Cal.Rptr.2d at 194; emphasis added.) *OAL has serious concerns about the correctness of the statement of law contained in this quotation*, for the reasons stated in the following excerpt from 1998 OAL Determination No. 4 (Department of Fish and Game, Docket No. 90-049), May 22, 1998), endnote 1, CRNR 98, No. 26-Z, June 26, 1998, p. 1197, at p. 1203, endnote 1.

“The *Tidewater* opinion contains a significant discussion of quasi-judicial precedent decisions. Also, several months after the opinion was filed, an express statutory exemption covering precedent decisions became effective.

“OAL’s position since 1986 has been that, absent an express statutory exemption from the APA, agency precedent decision systems violate the APA. Government Code section 11346; **1993 OAL Det. No. 1** (California Energy Commission, April 6, 1993, Docket No. 90-015), CRNR 93, NO. 16-Z, April 16, 1993, p. 413), [determination] cited in official comment to Gov. Code sec. 11425.60; *California Public Agency Practice*, sec. 20.06, esp. [4]. Under the law as it existed until July 1, 1997, a general rule developed in a quasi-judicial proceeding could not be used from that point on in similar factual settings in lieu of a duly adopted regulation unless the rule had first been adopted as a regulation. The new statutory provision, Government Code section 11425.60, took effect on July 1, 1997. (The *Tidewater* opinion was filed December 19, 1996, over six months before the new provision went into effect.)

“Government Code section 11425.60 had the effect of legalizing the use of precedent decisions, if certain conditions were met. The *Tidewater* court does not cite section 11425.60. Several portions of *Tidewater* might well have been drafted differently, had the court taken enactment of section 11425.60 into account. For instance, the following passage must be read with the knowledge that it appears to have been written without considering the significance of section 11425.60:

‘[i]nterpretations that arise in the course of case-specific adjudication are not regulations, though they may be persuasive as *precedents* in similar subsequent cases. [citations] . . . Thus, if an agency prepares a policy manual that is no more than a restatement or summary, without commentary, of the agency’s prior decisions in specific cases, . . ., the agency is not adopting regulations.’ (59 Cal.Rptr.2d at 194; emphasis added.)

The quoted passage likely cannot be reconciled with Government Code section 11425.60. This statute creates an express APA exemption. It supersedes prior statutory and decisional law. Looking at an example of how the new statute

might apply. let us consider a policy manual containing the following sort of rule: decision 89-1 (a spouse who resigns a job in order to move to another city with the other spouse is not entitled to unemployment benefits). An issuance [in a policy manual] of a rule first developed in a quasi-judicial proceeding would violate Government Code section 11340.5. It would not matter if the decision were restated without commentary: the statement of the decision by itself contains a prospectively applicable standard of general application. However, the issuing agency could under section 11425.60 elect to designate it as a precedent decision. If this were done, the decision could be freely written up in departmental publications and could be used in lieu of a duly adopted regulation.”

54. Citing Government Code section 11343, *Tidewater* contains sweeping language in the nature of dicta indicating that regulatory material contained in letters directed to a specifically person or persons is not subject to the APA. Indeed, *Tidewater* then goes on to state that even compilations of such regulatory material in policy manuals are not subject to the APA if restated “without commentary.” The court stated:

“ . . . if an agency prepares a policy manual that is no more than a restatement or summary, without commentary, of the agency’s prior decisions in specific cases and its prior advice letters, the agency is not adopting regulations.” (59 Cal.Rptr.2d at 194.)

As noted in endnote 53, it is probably not possible to reconcile the proposition that agencies should gather quasi-judicial interpretations of precedential value into manuals with a statutory change concerning precedent decisions that subsequently took effect. Similarly, OAL has serious concerns about the portion of the quotation addressing what it characterizes as “advice letters.” The phrase “advice letter” does not appear in the APA.

The applicability of Government Code section 11343 was an issue in 1998 OAL Determination No. 29, which in part concerned a “regulation” issued in the form of a letter by the State Personnel Board. This determination was published in the California Regulatory Notice Register, 98, No. 46-Z, November 13, 1998, p. 2286. The following excerpt is taken from this 1998 determination (pp. 17-21 of the typewritten version). Nearly all endnotes are omitted.

**The quoted material begins here:**

**B. Rules directed to a *specifically named* person or group of persons *and* which do not apply generally throughout the state. (Government Code 11343, subdivision (a) (3).)**

The Board’s response states that the 1990 SPB letter “merely responds to a letter from an employee representative who was seeking an *advisory opinion* on behalf of a specific

client . . .” (Emphasis added.) When read in light of dicta concerning “advice letters” in a 1996 California Supreme Court case, this statement may be read to raise the issue of whether the regulatory material in the 1990 letter is exempt from the requirements of the APA pursuant to Government Code 11343 (a) (3), which states in part:

“Every state agency shall:

(a) Transmit to the office [of Administrative Law] for filing with the Secretary of State a certified copy of every regulation adopted or amended by it except one which:

. . . (3) Is directed to a specifically named person or to a group of persons *and does not apply generally throughout the state.*” (Emphasis added.)

In 1996, the California Supreme Court, in *Tidewater Marine Western v Bradshaw* in dicta, spoke to the practice of some agencies with respect to advisory opinions. Speaking to the practice, the court stated:

“Of course, interpretations that arise in the course of case-specific adjudication are not regulations, though they may be persuasive as precedents in similar subsequent cases. [citations] Similarly, agencies may provide private parties with *advice letters*, which are not subject to the rulemaking provisions of the APA. (Gov. Code §§ 11343, subd. (a) (3), 11346.1, subd. (a).) (Emphasis added.)

The issues before the court did not include the validity of an “advice letter.” The applicability of section 11343 to “advice letters” was not briefed. The court opinion does not fully develop the assertion that advice letters are not subject to the rulemaking part of the APA. It refers to Government Code section 11343, but does not quote the statutory language containing the two-part test that a regulation must meet in order to qualify for the exemption set forth therein. The opinion does not discuss the significance of Government Code section 11342, subdivision (g), which expressly exempts from the APA “legal rulings of counsel issued by the Franchise Tax Board or the State Board of Equalization,” which are advice letters on tax issues. If the Legislature had intended that advice letters in general be exempt from the APA pursuant to Government Code section 11343, there would seem little need for the exemption language in section 11342, subdivision (g).

Nor does the *Tidewater* opinion discuss *Winzler* (cited above in the analysis of the 1990 letter as a standard of general application). *Winzler* refers to Government Code section 11380, from which Government Code 11343 is derived, as making clear that the test for exemption from APA requirements includes the two prong test now set forth in Government Code 11343, that is, the regulation must (1) be directed to a specifically named person or to a group of persons *and* (2) not apply generally throughout the state.

Since 1986, OAL has consistently taken the position that there is no “automatic” APA

exemption for "regulations" directed to specifically named persons or group of persons. [Omitted endnote 44 lists 14 determinations issued between 1986 and 1998.] Some have argued that any "regulation" directed toward a specifically named person in response to a request for advice should be deemed exempt from the APA pursuant to section 11343(a)(3).

In order to qualify for an APA exemption pursuant to Government Code section 11343, subdivision (a) (3), however, state agency communications (including "advisory opinions") must meet both parts of the two prong test, that is, the regulation must be directed to a specific person or group of persons *and* not apply generally throughout the state.

Review of the legislative history of the APA indicates that the Legislature has strictly limited APA exemptions, with an eye toward making a much greater proportion of *state* agency rules subject to public notice and comment requirements than Congress sought to achieve in the federal APA regarding *federal* agency rules.

Though "interpretive guidelines" are expressly exempt from notice and comment requirements under the federal APA, the California Legislature has not enacted a parallel provision in the California APA.

It appears the Legislature intended that there be no exemption for "interpretive rules." Exempting interpretive guidelines was--and is--a clear policy alternative. The federal APA, first enacted in 1946, exempts "interpretive rules" "policy statements" from notice and comment requirements. In enacting the California APA in 1947, the Legislature rejected a proposal to exempt "*any interpretative rule* or any rule relating to public property, public loans, public grants or public contracts" (emphasis added) from APA notice and hearing requirements. It, therefore, seems that the 1947 Legislature considered and rejected the idea of following the federal example of exempting "interpretive rules" (including "advisory letters" or "advice letters") from notice and comment requirements.

In recent years, however, the Legislature has enacted several significant APA provisions that address the issue of agency communications regarding application of law within the agency's jurisdiction. These amendments were enacted on the recommendation of the California Law Revision Commission, which will shortly be forwarding to the Legislature an additional Commission recommendation on a similar topic.

In 1995, the Legislature enacted a major revision of the adjudication portion of the Administrative Procedure Act, developed over a period of years by the Law Revision Commission. Among other things, the legislation authorizes a state agency to issue a "declaratory decision" in response to an application to the agency for a decision as to the applicability to *specified* circumstances of a statute, regulation or decision within the jurisdiction of the agency, in other words, to issue an "advisory opinion." Article 14 of Chapter 4.5 Division 3 of Title 2 of the Government Code (commencing with section 11465.10). The Commission's commentary to section 11465.10, the introductory section

Article 14, states the following.

“Article 14 . . . creates, and establishes all of the requirements for, a special proceeding to be known as a ‘declaratory decision’ proceeding. The purpose of the proceeding is to provide an inexpensive and generally available means by which a person may obtain fully reliable information as to the applicability of agency administered law to the person’s particular circumstances.

“The declaratory decision procedure is thus quasi-adjudicative in nature, enabling an agency to issue in effect an *advisory opinion* concerning assumed facts submitted by a person. The procedure does not authorize an agency ‘declaration’ of a guideline, criterion, bulletin, manual, instruction, order, standard of general application, or other rule that is an ‘underground regulation . . . .

“The declaratory decision procedure provided in this article applies only to decisions subject to this chapter . . . .” (Emphasis added.)

The Law Revision Commission and the Legislature both recognized that there would be cases in which an agency, having issued an advisory opinion to one person based on specific facts, would want to utilize the opinion in situations where **similar facts** exist, in other words, utilize the opinion as a standard of general application. Consequently, the 1995 legislation provides that a “declaratory decision” can be given “precedential effect,” according to procedures specified in the legislation. Under these procedures, an agency “may designate as a *precedent decision* a decision . . . that contains a significant legal or policy determination of general application that is likely to recur.” (Emphasis added.) [Endnote 49: Government Code section 11425.60.] The official Law Revision Commission comment states that the legislation “recognizes the need of agencies to be able to make law and policy through adjudication as well as through rulemaking. It codifies the practice of a number of agencies to designate **important** decisions as precedential . . .” and applies notwithstanding APA provisions prohibiting “underground regulations.” In other words, the Legislature expressly exempted “precedent decisions” from the requirements of the APA, proving once again that the Legislature knows how to grant an express exemption when it makes a policy decision to do so.

The exemption for “precedent decisions” draws attention to the fact that *no* express exemption was enacted with respect to “declaratory decisions.” Thus, the Legislature specifically authorized agencies to issue advisory opinions that apply the law to **specific**, not general, circumstances. The opinions may not apply *statewide*. They are not to be used as standards of general application in lieu of duly adopted regulations or without the formality of designation as “precedent” decisions.

As part of its ongoing study of the APA, the Law Revision Commission is currently drafting a final recommendation setting forth an APA procedure for issuance of “advisory

interpretations” by state agencies. The recommendation would create a simplified notice and comment procedure an agency may use to issue generally applicable, nonbinding, interpretive advice, another form of an advisory opinion. The purpose is to “expedite beneficial communication between agencies and the public while preserving the benefits of public participation in agency deliberations.” Under the Law Revision Commission’s proposal, an advisory interpretation: 1) is an expression of an agency’s opinion regarding the meaning of a provision of law that the agency administers; 2) cannot purport to bind or compel; 3) is not to be given any judicial deference or binding effect; and 4) provides a “safe harbor” for those who conform their conduct to the interpretation.

In summary, OAL concludes that though the SPB policy that persons answering question 2E are expected to disclose all dismissals, including those set aside by court action, was directed to a specifically named person, it is nonetheless a standard of general application: it applies generally throughout the state to all persons who have experienced a dismissal set aside by court action. (See part II.A of this determination.) Because this policy applies generally throughout the state, it thus fails to satisfy the second part of the two-part test contained in Government Code section 11343, subdivision (a)(3).

**The material quoted from 1998 OAL Determination No. 29 ends here.**

55. *Tidewater Marine Western, Inc. v. Bradshaw* (1996) 14 Cal.4th 557, 573, 59 Cal.Rptr.2d 186, 196.
56. *Tidewater Marine Western, Inc. v. Bradshaw* (1996) 14 Cal.4th 557, 574; 59 Cal.Rptr.2d 186, 197.
57. 59 Cal.Rptr. at 196. The *Tidewater* court disapproved the approach of the lower court in *Bono Enterprises*, which had reasoned that “DLSE had to have *discretion* to interpret the IWC regulation in particular factual contexts” (Id.: emphasis added), and then concluded that because of this need to have discretion, that DLSE interpretations of duly adopted regulations were not subject to the APA. The *Tidewater* court made clear that an agency need for interpretive discretion did not mean the agency could memorialize a blanket interpretation in a document such as a policy manual, intending to apply it in all cases of a particular class or kind. Such “blanket interpretations” are subject to the APA. Government Code sections 11342, subdivision (g), 11340.5.