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THE VACANCY GAME REVISITED:
SPOTLIGHT ON STATE OPERATIONS

The CBP's 2002 Budget Brief, *The Civil Service Vacancy Game: Abusive Practices Or Underlying Structural Problems?*, examined state practices regarding vacant civil service positions.[1] This update highlights subsequent developments related to state agency vacancies, as well as other changes in state operations including position eliminations, budget cuts, and increased retirement payouts.

THE BIG PICTURE: WHICH AGENCIES WERE HIT HARDEST IN THE 2002-03 BUDGET?

Although spending for nearly every area of the budget was reduced in the 2002-03 budget agreement, some agencies experienced deeper cuts than others. The K-12 Education and General Government / Tax Relief portions of the General Fund budget were the only areas where spending increased, largely due to growth in the Proposition 98 guarantee and the increased cost of the Vehicle License Fee (VLF) backfill. By agency, the largest reductions occurred in the:

- Business, Transportation, and Housing Agency, with a 64.7 percent reduction ($417 million) from 2001-02 funding;
- Environmental Protection Agency, with a 60.4 percent reduction ($264 million);
- Technology, Trade, and Commerce Agency, with a 44.0 percent reduction ($33 million);
- State and Consumer Services Agency, with a 34.1 percent reduction ($244 million); and
- Resources Agency, with a 32.6 percent reduction ($504 million).[2]

The 2002-03 budget agreement also called for elimination of thousands of vacant positions across state agencies, as well as reductions in state operations. These developments are discussed in further detail below.

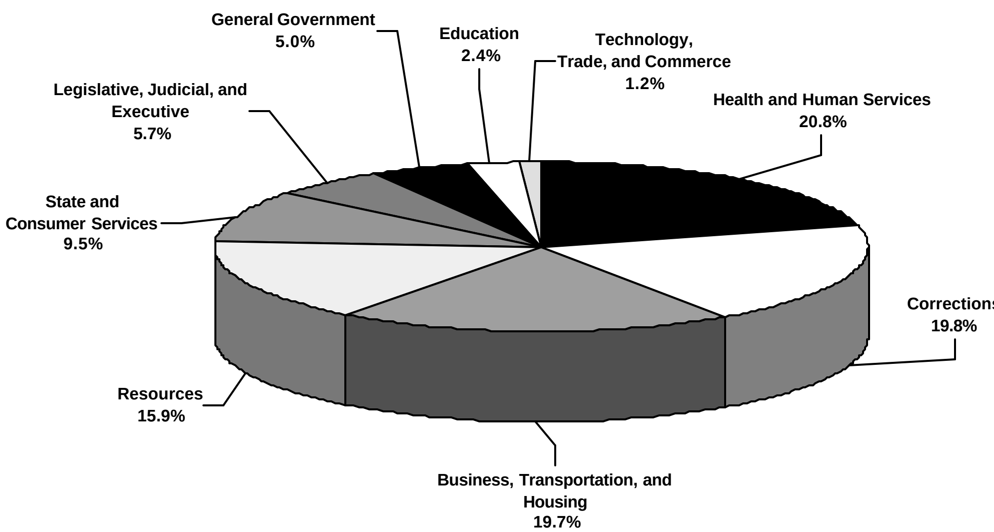
NEW DIRECTIVES: ELIMINATING POSITIONS AND CUTTING BUDGETS

In November 2002, the State Controller's Office estimated that approximately 23,395 positions were vacant out of a total of 203,260 established positions, for a vacancy rate of 11.5 percent.[3] In response to legislative pressure, the Department of Finance (DOF) eliminated 6,600 vacant positions in 2000-01 and 2001-02 that it considered "excess." The 2002-03 budget agreement included several provisions relating to the elimination of additional positions in 2002-03 and 2003-04, as well as a provision to reduce operating budgets.

Eliminating 6,000 Vacant Positions in 2002-03. The budget agreement called for the elimination of a minimum of 6,000 vacant civil service positions, effective July 1, 2002 (the beginning of the 2002-03 fiscal year), for an estimated $150 million General Fund and $300 million total savings.[4] The DOF was directed to choose from positions that were vacant on June 30, 2002, regardless of how long the position had been vacant. The legislation allowed the DOF to count positions eliminated under the six-month rule toward the 6,000-position requirement.[5]

In November 2002, the DOF released a list of 6,129 positions to be abolished, for a savings of $300.4 million ($102.9 million General Fund). Of the agencies, Health and Human Services (HHS) suffered the largest numeric reduction, losing over 1,200 positions, or one-fifth (20.8 percent) of the total abolished positions (Figure 1).

Figure 1: Distribution of Abolished Positions



Source: CBP analysis of Department of Finance data

It is important to note that since HHS is a large agency with a number of departments, the cuts were spread across a large base; proportionately, the 1,200 positions were equal to 2.9 percent of the agency's total authorized positions. The Business, Transportation, and Housing Agency and the Legislative, Judicial, and Executive branches lost about 2.5 percent of their authorized positions, while Corrections lost 2.2 percent of its total authorized positions. Resources, State and Consumer Services, General Government, and Education each lost about 4 percent of their total authorized positions. In contrast, the Technology, Trade, and Commerce Agency lost nearly one-fifth (18.8 percent) of its total authorized positions (Table 1).[6]

Imposing Further 2002-03 Reductions in State Operations. In addition to eliminating employee positions, the 2002-03 budget agreement allowed up to a 5 percent reduction (or $750 million) in appropriations for state operations in 2002-03.[7] This target was arguably unrealistic, however, given the share of state operations that are either mandatory (for example, pensions and debt service), already committed as of the date the legislation passed (for example, the University of California and California State University had already completed fall enrollment), or exempted from the bill (for example, public safety and 24-hour facilities including corrections and mental health).

The Governor's proposed mid-year cuts included reductions of $320.8 million and 257.7 personnel years (PYs) in state operations costs across all agencies (Table 2). The proposal argued that "only a portion of the $750 million target can be achieved without statutory changes to programs…"[8] Education received the largest dollar reduction ($139.6 million), with the largest cuts in the University of California ($74.3

Table 1: Which Departments Received the Largest Cuts in Proportion to Their Total Staff?

	Abolished Positions	Total Authorized Positions*	Abolished Positions as Share of Total Positions
Technology, Trade, and Commerce Agency	69	367	18.8%
Department of Community Services and Development	15	137	10.9%
California Energy Commission	60	564	10.6%
Department of Corporations	30	297	10.1%
Office of Criminal Justice Planning	16	166	9.7%
Department of Conservation	66	712	9.3%
State Water Resources Control Board	164	1,790	9.2%
Department of Pesticide Regulation	42	462	9.1%
Office of Statewide Health Planning and Development	37	437	8.5%
State Lands Commission	20	248	8.1%

*As proposed in the 2002-03 Governor's Budget.
Source: CBP analysis of Department of Finance data

million) and the California State University ($59.6 million). The Health and Human Services Agency lost the largest number of staff (107.0 PYs), primarily in the Department of Developmental Services (85.0 PYs).

Eliminating 1,000 Positions in 2003-04. The 2002-03 budget agreement also required the DOF to eliminate at least 1,000 civil service positions by June 30, 2004. Although not specified, these are presumably in addition to the 6,000 discussed above, particularly since the two directives apply to different fiscal years. The legislation gave priority to vacant positions and "administrative and managerial positions that do not provide direct services to the public."[9] The Governor's Proposed 2003-04 Budget includes the elimination of an additional 1,900 positions relating to program cuts and eliminations.[10]

Reducing through Attrition: A "Golden Handshake." The budget agreement provided for a "golden handshake" program to encourage early retirement of state employees, generating an estimated $285 million in General Fund savings in 2002-03.[11] An agency's participation in the program was contingent upon generating sufficient savings to offset the costs of awarding additional retirement credit. Participation by employees was voluntary, and participating employees would have had to retire between December 3, 2002 and February 1, 2003. An employee participating in this program would have had to be otherwise qualified for retirement, meaning that he or she was at least 50 years old and had been employed for at least five years in state service.[12] As noted below, however, no departments chose to participate due to the costs and the risk of permanently losing positions, so no savings have been achieved through this proposal.

Table 2: How Were the December 2002 Reductions Allocated Among Agencies? (Ranked by Dollar Reductions)	Dollar Reductions (in Millions)	Share of Total Dollar Reductions	Staff Reductions (in PYs)	Share of Total PY Reductions
Education	$139.6	43.5%	16.5	6.4%
Resources	$34.7	10.8%	43.1	16.7%
General Government	$30.5	9.5%	11.4	4.4%
Labor and Workforce Development	$29.8	9.3%	0.0	0.0%
Health and Human Services	$26.5	8.3%	107.0	41.5%
Legislative, Judicial, and Executive	$18.9	5.9%	47.4	18.4%
State and Consumer Services	$16.4	5.1%	12.9	5.0%
Corrections	$13.8	4.3%	8.6	3.3%
Environmental Protection	$9.8	3.0%	8.8	3.4%
Technology, Trade, and Commerce	$0.4	0.1%	0.0	0.0%
Business, Transportation, and Housing	$0.3	0.1%	2.0	0.8%
TOTAL	**$320.8**	**100%**	**257.7**	**100.0%**

Source: Department of Finance

Vacancy Update: Cracking Down on Long-Term Vacancies

Many critics charge that high vacancy levels indicate abusive budgeting practices by managers who wish to avoid accountability. Others, however, argue that an outdated and unrealistic budget structure forces managers to keep positions vacant so they can redirect the savings (resulting from not paying salaries while the positions are vacant) to meet program requirements and needs. The 2002-03 budget agreement included two provisions addressing adherence to vacancy rules:

Eliminating Six-Month Rule "Cheating." Under the so-called "six-month rule," any civil service position that was vacant for six consecutive months during a single fiscal year would be eliminated. Since the six-month clock restarted every July 1 at the beginning of a new fiscal year, a manager could conceivably keep a position "safely" vacant for almost a full calendar year. The 2002-03 budget agreement, however, changed the six-month rule to apply to any consecutive six-month period, not just six months in a single fiscal year, effective July 1, 2002.[13]

Curbing Personnel Shifts to Preserve Vacant Positions. The use of personnel transfers known as "120 transactions," intended to allow managers to legitimately move employees between positions, increased significantly following the establishment of the six-month rule. In an apparent response to this practice, the budget agreement stated that "departments shall not execute any personnel transactions for the purpose of circumventing" the vacancy elimination policy.[14] The budget agreement also required departments to report on their compliance with the six-month rule.

NEXT STEPS: DEALING WITH THE FALLOUT

The implementation of cuts to the state employee workforce and state operations, as well as the prospect of continuing cuts, raises important policy questions. Policymakers should consider how departments that have already experienced significant cuts will address further reductions, how to motivate departments to produce voluntary cuts in positions and spending, and what state services, if any, should be eliminated in response to repeated reductions.

Cuts Are Not Evenly Distributed. Although the state employs roughly 200,000 people, a significant number are not included in the pool of positions to be eliminated. Public safety and health positions considered critical to the state are exempt from the cuts, and the Administration has publicly committed to preserving "the more than 65,000 positions in the departments whose primary function is to ensure the safety of the public: Department of Corrections, the California Youth Authority, the California Highway Patrol, and the Department of Forestry and Fire Protection."[15] In addition, positions in the University of California, California State University, and Legislature are exempt.[16] Reductions are thus somewhat unevenly unallocated, with the pool of non-exempt departments taking the burden of the staff cuts.

Few Easy Choices. As noted earlier, 6,600 positions have already been eliminated in the past two budgets, meaning that many of the "easy" cuts have already been made. In an effort to reduce positions by attrition, the Governor attempted to offer a golden handshake program, which was intended "to generate savings by encouraging early retirement of personnel and then holding vacant the positions held by the retiring personnel for as long as necessary to realize net savings."[17] The thinly veiled intention, however, was to create a pool of vacant positions that could be eliminated. While the DOF stated that it would consider re-establishing any position lost to the six-month rule because of the golden handshake program, this was not guaranteed. Even if the DOF did choose to reinstate a position under such circumstances, the current hiring freeze, which is effective until June 30, 2003 and could be extended further in light of the state's fiscal situation, would make it difficult to fill the position. In light of these risks, it is not surprising that all departments and agencies opted out of this program, arguing that retirement payout costs would exceed salary savings. This has forced the DOF to identify positions to be cut without any "easy" decisions created by voluntary departures.

Reducing State Services. *The Civil Service Vacancy Game* noted that policymakers may wish to address the issue of how services are provided in departments with high vacancy levels. The staff cuts imposed by the 2002-03 budget agreement raise a similar question, which was addressed by the DOF in a July 2002 directive to departments:

> "If an Agency believes that a critical function cannot be performed due to [elimination of positions], it may propose a redirection of staff in its fall budget submittal or propose legislation to eliminate the statutory requirement(s) for such function(s)."[18]

In addition, the DOF's August 2002 directive relating to spending reductions instructed agencies to consider repeal of statutorily required programs, elimination of discretionary programs, program consolidation, agency reorganization, restructuring of program responsibilities, and reductions in cost and / or service levels. The directive conceded that "because of the significant reductions taken during the 2002-03 budget process, it is likely that this level of reduction can only be achieved by elimination of programs in their entirety."[19]

A New Budget Hurdle: Rising Retirement Contributions

In addition to the estimated $28 billion budget gap, the economic downturn has created potentially significant increases in state retirement contributions for its employees. Under state law, state employees receive a set amount for retirement each year; the state contribution varies depending upon factors including earnings of the fund's investments and projections for future earnings. When investments perform above expectations, employer contribution rates are lowered; conversely, when investments come in below expectations, employer contribution rates are increased to make up the difference. During the 1990s, state agencies reaped the benefits of boom markets through lower contributions (or even zero contributions, in some cases). Due to the downturn in financial markets, however, the Public Employees Retirement Fund suffered a negative rate of return on investments in 2000-01, and the California Public Employees' Retirement System (CalPERS) estimates a negative rate of return for 2001-02.[20] CalPERS is projecting potentially significant employer contribution rate increases over the next two years for many state agencies.[21] This will add to the cost pressures on future budgets.

Conclusion

The 2002-03 budget agreement imposed significant staff cuts on state agencies, many of which were already reeling from spending reductions imposed midway through the 2001-02 budget year. At the time of this writing, the Legislature is considering additional cuts to the 2002-03 Budget, and the Governor's Proposed 2003-04 Budget includes even further reductions. Upcoming budget deliberations will need to address how to balance reductions in current levels of state services with the need to provide those services. Before making further reductions, policymakers should address whether it is realistic to expect agencies to continue to provide the same level of services even as funding and personnel are significantly reduced. If this expectation is not realistic, policymakers need to set priorities as to which services are essential and should remain intact. Ultimately, policymakers face difficult choices and compromises between eliminating services and providing funding for those services.

Erin Riches prepared this Budget Brief. The California Budget Project (CBP) was founded in 1994 to provide Californians with a source of timely, objective, and accessible expertise on state fiscal and economic policy issues. The CBP engages in independent fiscal and policy analysis and public education with the goal of improving public policies affecting the economic and social well-being of low- and middle-income Californians. General operating support for the California Budget Project is provided by foundation grants, individual donations, and subscriptions. Please visit the CBP's web site at www.cbp.org.

ENDNOTES

[1] California Budget Project, *The Civil Service Vacancy Game: Abusive Practices or Underlying Structural Problems?* (May 2002).
[2] CBP analysis of data from Department of Finance, *2002-03 California State Budget Highlights* (September 2002). These numbers refer to the 2002-03 Budget as passed and do not account for the Governor's proposed mid-year cuts.
[3] State Controller's Office, *Summary Totals of Civil Service and Exempt Established Positions Filled and Vacant by Month* (November 1, 2002). The number cited is as of October 31, 2002, and includes both General Fund and non-General Fund positions. See *The Civil Service Vacancy Game* for a discussion of the differences between established and authorized positions.
[4] Legislative Analyst's Office, *California Spending Plan 2002-03: The Budget Act and Related Legislation* (September 2002), p. 71 and AB 425 (Oropeza), Chapter 379, Statutes of 2002.
[5] AB 425 (Oropeza), Chapter 379, Statutes of 2002. See California Budget Project, *The Civil Service Vacancy Game: Abusive Practices or Underlying Structural Problems?* (May 2002) for further discussion of the six-month rule.
[6] CBP calculations of data from Department of Finance, *Vacant Position Recap,* downloaded from http://www.dof.ca.gov/HTML/BUD_DOCS/Bud_link.htm on November 14, 2002 and Department of Finance, *Salaries and Wages Supplement 2002-03* (March 2002), downloaded from http://www.osp.dgs.ca.gov/On-Line+Publications/Salaries+and+Wages+Supplement+2002-2003.htm on November 14, 2002. Abolished positions are based on departments that lost at least 10 positions, representing 97 percent of the total 6,129 positions abolished. Total authorized positions are as proposed for 2002-03, and only include departments that lost at least 10 positions.
[7] AB 593 (Oropeza), Chapter 1023, Statutes of 2002.
[8] Department of Finance, *Governor's Budget Summary 2003-04,* p. A-104.
[9] AB 593 (Oropeza), Chapter 1023, Statutes of 2002.
[10] Department of Finance, *Governor's Budget Summary 2003-04,* p. 215.
[11] Legislative Analyst's Office, *California Spending Plan 2002-03: The Budget Act and Related Legislation* (September 2002), p. 71.
[12] AB 593 (Oropeza), Chapter 1023, Statutes of 2002, Executive Order D-63-02 (October 4, 2002), Government Code Section 20901, and Education Code Section 22715.
[13] AB 3000 (Committee on Budget), Chapter 1124, Statutes of 2002.
[14] AB 3000 (Committee on Budget), Chapter 1124, Statutes of 2002.
[15] Department of Finance, *Governor's Budget Summary 2003-04,* p. 215.
[16] Most or all of these positions are also exempt from the six-month rule, although agencies are encouraged to participate on a voluntary basis. Universities are not exempt from the 1,000-position requirement, but are exempt from the 6,000-position requirement. Both the University of California and California State University took significant state operations reductions in the Governor's proposed mid-year cuts.
[17] Department of Finance, *Budget Letter 02-33: Early Retirement Program* (October 10, 2002).
[18] Department of Finance, *Budget Letter 02-13: 2002-03 Statewide Position and Dollar Reduction Plan* (July 1, 2002).
[19] Department of Finance, *Budget Letter 02-21: 2003-04 Budget Reductions* (August 7, 2002).
[20] California Public Employees' Retirement System, *Circular Letter No. 200-023-02: Sluggish Economy and Lower Stock Prices Will Cause Public Agency Contribution Rates to Increase Beginning in 2003-04* (June 26, 2002).
[21] California Public Employees' Retirement System, "AESD Flooded With Calls Following 'Sluggish Economy' Letter," *Employer News* (Winter 2002), downloaded from http://www.calpers.ca.gov/employer/pubs/ernews/02fall/page2.htm on November 11, 2002.