CHAPTER ONE
SPENDING POLICY

1. Structural Budget Reform

Recommendations

1. Adopt performance-based, Priorities of Government budgeting to control the rate of spending growth and create more sustainable budgeting.

2. Place requirements for performance outcomes directly into the budget.

3. Require that updated four-year budget forecasts be tied to quarterly revenue forecasts or to the adoption of a new budget.

4. Adopt a 72-hour budget timeout.

5. Require that completed fiscal notes be made available before bills can be acted on.

6. Permanently repeal unaffordable programs instead of temporarily suspending them.

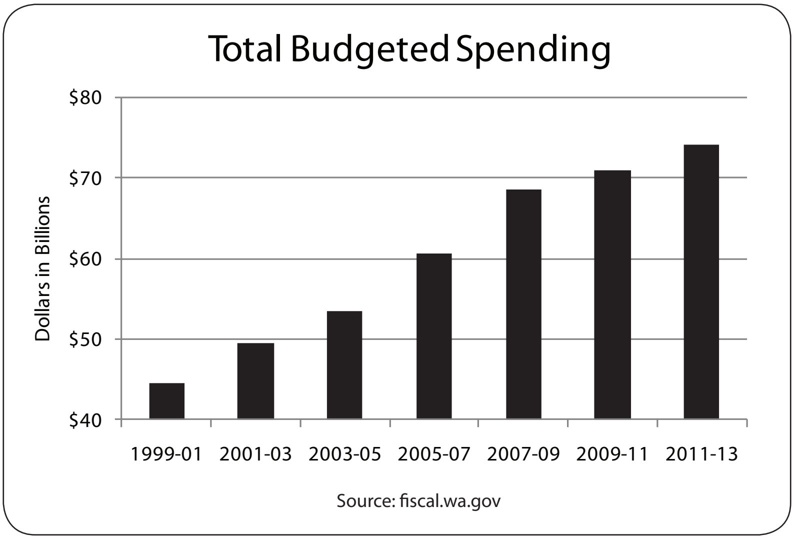
7. Provide the governor with discretionary authority to cut spending when revenues fall short of projected amounts.

8. Set aside a five percent reserve when adopting the biennial budget.

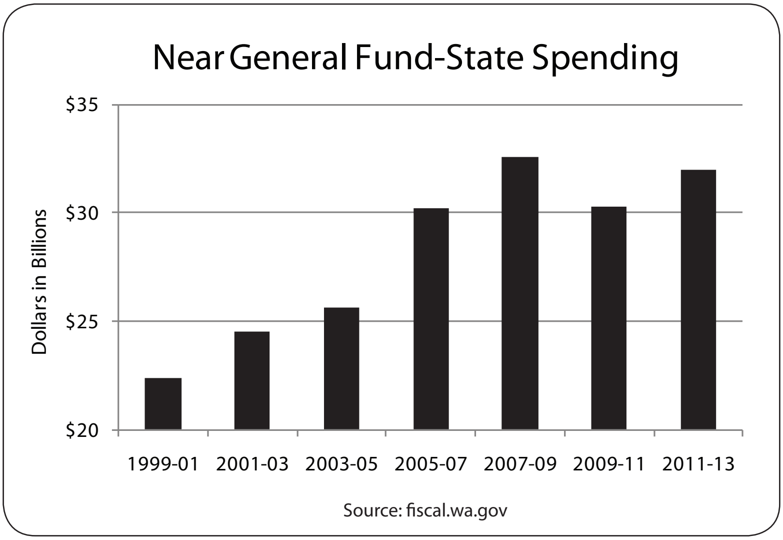
Background

A combination of past spending increases and a historic economic downturn has left lawmakers in Olympia facing difficult and important choices to reset state government. Though tax revenues dipped for the 2009–11 budget, they are projected to begin increasing again for the 2011–13 budget. While this should be cause for relief, lawmakers for years have been spending more than taxpayers provide, creating a structural budget gap that now threatens important public programs. This past overspending was unsustainable on its own, but the trend was exacerbated by the "Great Recession."

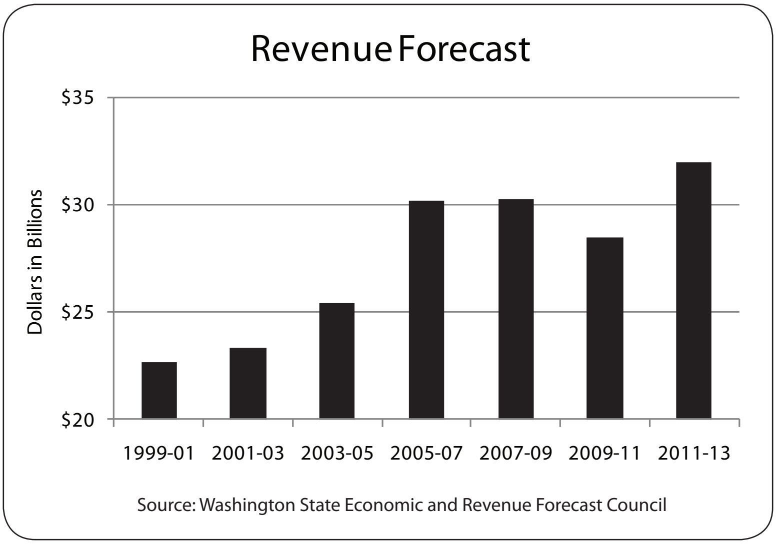
While the discussion focused on spending cuts during the 2011 legislative session, state spending is projected to increase both for "Total Budgeted" spending and for Near General Fund-State (NGF-S) spending. Although this increase in spending for the NGF-S follows a 2009–11 budget cycle that saw a significant decrease in spending, Total Budgeted spending has not decreased since the onset of the Great Recession. Total Budgeted spending includes the transportation, capital and operating budgets including federal funds and grants. Near General Fund-State is the account that principally pays for the operation of state government and is funded primarily by state sales, property, and business and occupation taxes.



Total budgeted spending is set to increase by some $3 billion for 2011–13. This builds on increases of $2.4 billion for 2009–11, $8 billion for 2007–09 and $7 billion for 2005–07. Since 1999–01, Total budgeted spending has increased 66%.



Near General Fund-State spending is set to increase $1.7 billion for 2011–13. This follows a decrease of $2.3 billion for 2009–11 and increases of $2.4 billion for 2007–09 and $4.6 billion for 2005–07. Since 1999–01, NGF-S spending has increased 43%.



After years of flat or declining revenue, state revenues are projected to grow again by $2 billion for 2011–13 (based on the June 2011 Revenue Forecast). This follows a decrease of $1.8 billion for 2009–11 and increases of $88 million for 2007–09 and $4.8 billion for 2005–07. Since 1999–01, state revenues have increased 35%.

Due to ongoing economic uncertainty, lawmakers will face persistent budget problems in the future unless structural budget reforms are adopted that set the budget on a long-term sustainable course.

Policy Analysis

To begin the necessary changes, lawmakers should re-evaluate all existing programs and activities against a prioritized, performance-based matrix. To do this, agencies should be required to rank their activities as high, medium or low priority, with no more than one-third of the total costs allocated to each ranking. Lawmakers should direct agencies to identify at least one expected performance outcome for each program activity. Once lawmakers have this information, they can make informed decisions about which programs will deliver the highest results for taxpayers and everyone who relies on essential public services.

An example of how to do this was initiated by former Governor Gary Locke in 2002 when he established his Priorities of Government process.[1] The process requires each agency to rank program activities in order of their importance to the public.

The Priorities of Government process is centered on three strategies:

1. View state government as a single enterprise.
2. Achieve results, at less cost, through creative budget solutions.
3. Reprioritize spending, eliminating programs or consolidating similar activities in different agencies.[2]

Governor Locke described Priorities of Government as "focusing on results that people want and need, prioritizing those results, and funding those results with the money we have."[3]

Measuring Government Performance

The natural next step in the Priorities of Government budgeting process is to identify measurable performance outcomes for those programs funded in the budget. By having detailed performance information, better prioritization can occur by funding strategies that deliver the best results.

Providing Adequate Time to Review Spending Proposals

The state's combined budget (operating, capital and transportation) is hundreds of pages long. Despite the length and complexity of these documents, however, hearings are usually held the same day the budget bill is introduced, and it is amended and enacted with inadequate time for meaningful public input.

The opportunity for a detailed review by the public before legislative hearings or votes on budget bills would increase public trust in government and enhance accountability for the spending decisions lawmakers make on the people's behalf.

Know Full Impact of Spending Proposals Before Making Decisions

One of the most recognizable measurements of the state's fiscal health is the multi-year budget outlooks. These updates, however, are not done on a regular basis. To provide updated information throughout the year on the state's fiscal condition, the legislature should issue an updated four-year budget outlook each time a new official revenue forecast is released, or when a new appropriation bill is adopted.

Along with the budget outlook, another important tool lawmakers use to make spending decisions is the legislative fiscal note. These analyses provide information on the added cost a spending proposal would impose on taxpayers. Unfortunately, bills are sometimes acted on before these estimates are completed, thus robbing the public and lawmakers of the information they need to make informed decisions.

Repeal Unaffordable Programs

As lawmakers look for ways to achieve budget savings, they should resist the temptation to keep unaffordable programs alive in statute, especially when they have provided no funding for them. By suspending programs instead of repealing them, lawmakers are providing a false sense of hope to program supporters while putting undue pressure on future budget writers.

For example, during the 2011 legislative session lawmakers suspended Initiative 728 (class-size reduction), Initiative 732 (pay raises for teachers), paid family leave, and they instituted a temporary three percent salary reduction for state employees. By failing to repeal these programs and make a permanent reduction in the state salary base, these unfunded programs are automatically included in future budgets, creating significant problems for future lawmakers.

Surgical Budget Reductions

Under state law, if a cash deficit is projected the governor is required to order across-the-board cuts to bring spending into balance with revenues:

> RCW 43.88.110 (7): If at any time during the fiscal period the governor projects a cash deficit in a particular fund or account as defined by RCW 43.88.050, the governor shall make across-the-board reductions in allotments for that particular fund or account so as to prevent a cash deficit, unless the legislature has directed the liquidation of the cash deficit over one or more fiscal periods.

Unfortunately, this one-size-fits-all approach means all spending is treated equally and does not allow prioritization to occur. As a result, spending for K-12 education is treated the same as spending for low-priority government activities. This is why the across-the-board cut authority for the governor has been referred to as a budget "chainsaw" versus a "scalpel."

Though the budget-cutting authority for governors across the country varies, at least fifteen states provide their governor discretionary budget-cutting authority that allows prioritization of reductions to occur.[4]

Washington's governor should be provided a scalpel to make discretionary spending reductions that do not exceed a set percentage (between five and ten percent) of an agency's appropriations. Cuts in excess of the set percentage should require approval by a standing legislative emergency budget committee (made up of one member from each caucus in the House and Senate). No reductions should be made in the budget of an independently elected state official, like the attorney general or the secretary of state, without that official's approval or the approval of the standing legislative committee.

Any reductions made should be immediately reported to legislative fiscal committees and publicly posted on the state's budget transparency website (www.fiscal.wa.gov). This type of enhanced budget-cutting authority for the governor would provide spending reduction tools other than blind across-the-board cuts, while addressing any accountability or transparency concerns.

One benefit of this type of discretionary budget-cutting authority for the governor is enhanced taxpayer protection. While the legislature could decide to raise taxes in a special session to reduce a deficit, the governor cannot raise taxes on her own. This means the default response for budget deficits that arise when the legislature is adjourned would be surgical spending reductions, instead of the uncertainty of possible tax increases enacted in a special session.

This type of discretionary spending cutting authority for the governor would encourage the legislature to leave adequate reserves to avoid allowing the governor to decide what spending reductions to impose.

Five Percent Budget Reserve

Though Washington has one of the best nonpartisan revenue forecast processes in the country, forecasting state revenues and predicting economic activity remains an imprecise science. Yet the state budget is built around these imperfect assumptions. Consider what happened for the 2011–13 budget that was balanced for only one day.

The day after Governor Gregoire signed the 2011–13 budget, most of the ending fund balance (including the constitutional emergency reserve) was wiped out by a June 2011 forecast that showed state revenues increasing by less than expected. This left the state with total reserves of only $163 million, or less than 0.5% of spending. Prior to the June 2011 forecast there was $723 million in total reserves, or 2.3% of spending. This scant remaining reserve left the state unprepared when revenue projections failed to meet the legislature's expected level of spending increase.

To help provide for a more sustainable budget and avoid the need for special sessions or the governor ordering budget cuts, lawmakers should adopt structural requirements that mandate at least a five percent reserve (not counting the constitutional rainy-day account) be set aside when adopting the initial biennial budget. For a $32 billion budget, this would be reserves of around $1.6 billion, versus the $723 million initially set aside.

Ending the Sense of Crisis in State Finances

Reducing the long-term structural costs of government will ease the burden on taxpayers and ensure that future economic slowdowns do not force the state into yet another financial emergency. Structural budget reforms would promote efficiency, improve the quality of services to the public and resolve the constant sense of crisis that pervades the state's public finances.

Though daunting, the state's budget problems can be diligently addressed by refocusing on purchasing high-priority performance outcomes instead of lawmakers being influenced by emotional pleas for continued funding based on past spending decisions. This will help reprioritize excessive spending policies that have contributed to a projected budget deficit despite forecasted revenue growth.

By making structural reforms and focusing on purchasing performance outcomes, lawmakers can make informed decisions and build a solid budget focused on delivering the best results for taxpayers and users of government services. If lawmakers ultimately ask state citizens to pay higher taxes for additional spending, the public will know one of two things:

1. Lawmakers believe the state's lowest priorities are still worth purchasing even in this tough economic climate, and taxpayers need to sacrifice more, or

2. The budget is not properly prioritized and lower priorities are being purchased first, resulting in the request for tax increases to fund higher priorities.

Recommendations

1. **Adopt performance-based, Priorities of Government budgeting to control the rate of spending growth and create more sustainable budgeting.** The Priorities of Government standard has proved successful in the past. The legislature and executive agencies should adopt it as a permanent part of the budget process by requiring all budgets be adopted based on this sensible review process, so essential public services are funded first. Priorities of Government brings discipline to public spending, slows the growth of the tax burden government places on its citizens and directs limited government funding to where it is most needed.

2. **Place requirements for performance outcomes directly into the budget.** To improve budget accountability, high-level performance outcome measures should be placed directly into the budget so lawmakers and citizens can quickly see whether past goals have been met before each new increase in spending is considered.

3. **Require that updated four-year budget forecasts be tied to quarterly revenue forecasts or to the adoption of a new budget.** To provide updated information throughout the year on the state's fiscal outlook, an updated four-year budget outlook should be issued each time the official revenue forecast is released, or when a new appropriation bill is adopted.

4. **Adopt a 72-hour budget timeout.** To facilitate public involvement, the legislature should adopt a 72-hour timeout period in the legislative process once a budget, tax or spending bill is introduced or amended. This would allow lawmakers and the public a three-day period to calmly consider the two-year budget, new taxes or new spending before legislative hearings or final voting occurs.

5. **Require that completed fiscal notes be made available before bills can be acted on.** Lawmakers and the public should know the full impact of a spending bill before final legislative action is taken. Bills proposing increased spending should not receive hearings or votes until a thorough fiscal analysis is completed and released to the public.

6. **Permanently repeal unaffordable programs instead of temporarily suspending them.** By suspending versus repealing programs,

lawmakers are providing a false sense of hope to program supporters while putting undue pressure on future budget writers.

7. **Provide the governor with discretionary authority to cut spending when revenues fall short of projected amounts.** Enhanced budget-cutting authority for the governor would provide budget-reduction tools other than the current one-size-fits-all, across-the-board, cuts option, allowing for prioritization of reductions to occur while addressing any accountability or transparency concerns.

8. **Set aside a five percent reserve when adopting the biennial budget.** To help provide for a more sustainable budget and avoid the need for special sessions or the governor ordering budget cuts, lawmakers should adopt structural requirements that mandate at least a five percent reserve (not counting the constitutional rainy-day account) be set aside when adopting the initial biennial budget.

2. State Spending Limit

Recommendation
Adopt a constitutional amendment to limit the growth of state spending to inflation and population growth.

Background

In 1993, Washington voters passed Initiative 601 to limit the annual growth of state spending to a three-year rolling average of inflation plus population growth.[5] The limit worked for a time. In the decade before Initiative 601, state spending increased on average by 17% per biennium. Between 1993–95 and 2003–05, state spending increased an average of eight percent per biennium under the provisions of Initiative 601, half the previous rate of spending increase. In 2005, however, lawmakers changed the spending limit growth factor, resulting in a 17% increase in spending during the 2005–07 biennium. Had the economy not gone into recession in 2008, it is likely state spending would have continued to increase beyond the eight percent per biennium average under the original Initiative 601 caps.

Initiative 601 was not made part of the Washington constitution, and it was easily overturned by a simple majority vote in the legislature. This is why it is imperative to put meaningful spending restrictions similar to the original Initiative 601 limits in the constitution, so that once the economy recovers, state spending grows at a more sustainable rate, and the financial burden lawmakers place on citizens is controlled.

Policy Analysis

Thirty states have some form of spending limit to protect their citizens from overtaxation.[6] More than half of these spending limits are part of the state constitution.[7]

Research shows that the most effective spending limits are constitutional instead of statutory.[8] Constitutional spending limits are insulated from attempts by narrow legislative majorities to open loopholes that allow higher spending increases. Research also shows that tying the growth of government spending to inflation plus population growth increases a limit's effectiveness, compared to other methods of measuring economic activity.[9]

Originally, Initiative 601 pegged government growth to a combination of inflation and population growth, but in 2005 the legislature and governor changed the fiscal growth factor to a ten-year average of state personal income growth.[10] This allows spending to increase at a much faster rate.

Tying increases in public spending to the growth in the average of personal incomes artificially exaggerates the impact of wealthy people's incomes on state spending. This budget rule increases unfairness in the tax system because state spending and taxation go up for everyone, even though not everyone's income has increased to keep pace.

Washington's economy and its citizens would benefit from a state spending limit that is both constitutional and tied to fair measure of growth in inflation and population.

Recommendation

Adopt a constitutional amendment to limit the growth of state spending to inflation and population growth. Reasonable budget limits similar to those of Initiative 601, but as part of the state constitution, would protect taxpayers and bring greater discipline to public finances.

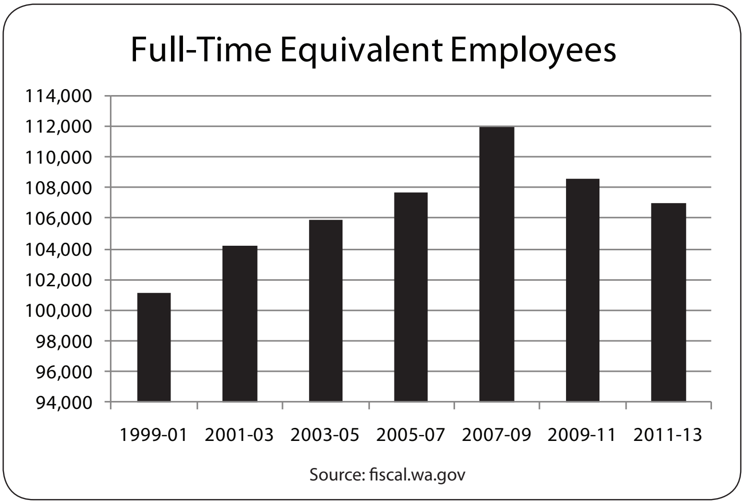
3. Public Workforce Policy

Recommendations

1. Restore the legislature's authority over state collective bargaining agreements.
2. Adopt collective bargaining transparency.
3. Bring state employee health care premium contributions more in line with the private sector.
4. End the compulsory taking of monthly union dues from public employee paychecks.
5. Phase in a defined-contribution retirement plan that gives state workers benefits that can never be taken away.

Background

State public employment grew sharply beginning in 1999, expanding by over 5,800 people and reaching a peak of 111,984 FTEs (full-time equivalent positions) in 2008.[11] State public employment grew six percent in just ten years, and has since dropped slightly from its previous high.



In 2010, the average annual compensation for a full-time equivalent state employee topped $74,700. This included a salary of more than $57,200, plus a generous $17,500 benefits package.[12] These state employee compensation costs accounted for 23.4% of total spending in 2007–09 or 30.4% of spending when accounting for K-12 pass-through funds (money provided to local school districts for compensation; K-12 school employees are not state employees).

Drilling down even further, however, there is a clear distinction between state employee compensation costs as a percentage of spending when comparing general government employees versus higher education employees.

Looking at just general government employees and spending (excluding higher education) the percentage of compensation costs to spending drops to 15.5% in 2007–09. Comparing just higher education employees and spending the percentage of compensation costs to spending was 64% in 2007–09.

This illustrates that when looking at compensation as a percentage of spending, higher education employee compensation is a much larger cost driver for higher education spending than general government compensation is for general government spending.

Whether these compensation figures are too high or too low is subject to debate, but the fact remains the cost of state employee compensation is one of the greatest budget cost drivers and is one under the total control of policymakers.

Policy Analysis

State collective bargaining law prevents the legislature, and the public, from knowing the process that determines employment contract costs. The current system undermines transparency and public accountability for the tax dollars being spent through the state payroll. Under the 2002 Civil Service Reform Act, the legislature can only vote "yes" or "no," with no amendments or other changes, to a contract negotiated secretly by the governor and union officials.

As a result, state unions no longer have their priorities weighed equally with other special interest groups during the normal legislative budget process. Instead, union executives now negotiate directly with the governor, while lawmakers only have the opportunity to say yes or no to the entire contract. Lawmakers cannot make any changes.

To put the legislature back in charge of the budget so spending can be prioritized to serve the public interest, the 2002 collective bargaining law should be repealed and replaced with something similar to the policy Indiana adopted in 2005.

When Indiana Governor Mitch Daniels took office in 2005 he issued an executive order that, in effect, ended secret state negotiations with unions.

According to Anita Samuel, Assistant General Counsel and Policy Director for Gov. Daniels:

> Employees are still able to pay union dues through payroll deductions. It is completely their choice. Union reps are allowed to represent employees in the grievance procedure. We expanded who was eligible to take a grievance through our State Employees Appeals Commission under this EO [Executive Order]. Every employee, merit and non-merit below an executive level could file a complaint. The prior process only applied to merit employees.
>
> The state does not negotiate with the unions on any issues. At times, the State Personnel Department will meet with the unions when requested. The state sets the compensation, pay for performance increases and benefits without negotiating with the unions. Governor Daniels put in place a robust pay for performance system starting in 2006. The first year the structure was 0% [pay increase] for [an employee who] does not meet expectation, 4% for meets [expectations] and 10% exceeds [expectations]. The second year it was 0, 3, 8.5%. Employees were also given a 1.5% general salary increase that the legislature called for. I think that most employees were pleased with this system.[13]

Unions exist to fight for their members, not to advocate for policy that is in the best interest of taxpayers. This why it is incumbent on the legislature to have the authority to weigh all spending requests equally in the context of the priorities of all taxpayers and citizens and not be cut out of budget decisions totaling hundreds of millions of dollars.

The legislature should reassert its authority over state employment policy to ensure greater public accountability and transparency. This would help advance improvements that reduce costs while rewarding the excellent work of state employees.

State Employee Medical Coverage

In 2012, state employees are projected to pay, on average, $75 per month, or $208 for a family plan, well below the typical employee cost of private sector plans.[14] Taxpayers will pick up the rest. Nearly 338,800 public employees and families members are enrolled.[15]

In addition to current costs, the legislature is adding to the financial burden of the program by expanding its generous coverage to more groups. In 2007, lawmakers passed five bills allowing groups such as same-sex domestic partners, part-time university employees and employees of tribal government to buy coverage under the state program.[16]

As health care costs continue to climb, the current arrangement will place a growing strain on the state budget. In order to make their employees better stewards of health care dollars, private sector employers have increased the share of premiums contributed by employees. This has the effect of making the cost of health care as a portion of overall compensation more visible. Washington policymakers should adopt a similar policy in order to help control costs.

In 2011, Governor Gregoire signed a bipartisan bill, SB 5773, giving state employees access to family Health Savings Accounts, a workplace benefit that is common in the private sector.[17] HSAs help control costs by giving employees control over their own health care dollars, making them better stewards of how that money is spent. To save money and enhance worker morale, state officials should encourage public employees to choose family Health Savings Accounts as the way to receive their health benefits.

Compulsory Union Deductions from Employee Paychecks

Currently, the Washington state workforce operates mostly as a closed shop. Most state employees must belong to an approved union as a condition of employment. Failure to join a union is cause for dismissal.

Union dues are automatically deducted from workers' paychecks. State law provides for mandatory union dues to be set through talks between union executives and the governor.[18] Part of this money is used to pay administrative costs and handle workplace issues, while some is devoted to lobbying, candidate campaigns and other political activities.

Washington's "Union Security" Clause

In 2007, the Washington legislature approved a new contract negotiated by unions and the governor behind closed doors, in which union executives insisted on a "union security" clause requiring mandatory paycheck deductions. Any employee who does not want to join the union or pay mandatory dues can be fired.

The text of a typical union security clause is shown below (emphasis added)[19]:

> **Article 36.3 Union Security**
>
> All employees covered by this Agreement will, as a condition of employment either become members of the Union and pay membership dues or, as nonmembers, pay a fee as described in A, B, and C below, no later than the 30th day following the effective date of this Agreement or the beginning of their employment. If an employee fails to meet the conditions outlined below, the Union will notify the Employer and inform the employee that his or her employment **may be terminated**.

Despite the mandatory requirement for most state workers to join and pay a union, the unions are not public entities; they are private organizations. This scheme shields the unions from the accountability and transparency requirements mandated under state law for public entities.

As an employer, the state should not force individuals to join selected private organizations. However, if such a requirement does exist, the unions should be treated as public entities and be subject to all applicable laws and disclosure requirements. State workers and the public should be fully informed about union activity.

Pension Reform

State and local government employees in Washington are required to participate in pension plans administered by the Washington State Department of Retirement Systems. The system pays benefits to more than 643,500 current and retired employees and pays out about $2.9 billion in benefits each year.[20]

The state pension plans have assets of $57 billion but are responsible for liabilities of more than $62 billion.[21] That means the state pension plans are underfunded by at least $5 billion, creating a potentially crushing financial burden for future taxpayers.

Defined Contribution Plans

Because they operate under the discipline of the marketplace, private companies have developed a smarter approach. They have moved away from old-style defined-benefit plans to modern defined-contribution plans and 401(k) accounts. Defined-contribution plans give employees their retirement money upfront, in the form of tax-free payments into their personal retirement accounts. Employees can contribute to their accounts as well, also tax-free.

The great advantage of defined-contribution plans is they give workers direct ownership of their own retirement money. As investment strategies and risk levels change with age, defined-contribution plans give workers the freedom and flexibility that one-size-fits-all government pensions do not. Employees in such plans are not forced to rely on promises that might be broken in the future.

As an additional benefit, defined-contribution plans protect future taxpayers from massive unfunded liability, such as the one state plans carry today.

Recommendations

1. **Restore the legislature's authority over state collective bargaining agreements.** The legislature should reassert its authority over state employment policy to ensure greater accountability and transparency, and it should advance improvements that reduce costs while rewarding the excellent work of state employees.

2. **Adopt collective bargaining transparency.** State employment contracts should not be negotiated in secret. Taxpayers are ultimately responsible for funding these agreements. They should be allowed to monitor the negotiation process and to hold state officials accountable for their actions.

3. **Bring state employee health care premium contributions more in line with the private sector.** In order to make their employees better stewards of health care dollars, the state should increase the share of health insurance premiums contributed by employees. Policymakers should also promote the option of Health Savings Accounts, so workers can have direct control over their health care benefits.

4. **End the compulsory taking of monthly union dues from public employee paychecks.** If government union leaders collected voluntary dues from their members instead of resorting to mandatory automatic payroll deductions, they would be more responsive to their members' needs and views. It would also encourage union officials to be more transparent and accountable for how they spend their members' money.

5. **Phase in a defined-contribution retirement plan that gives workers benefits that can never be taken away.** Personal retirement accounts with tax-free defined-contributions would mitigate the financial crisis in the state retirement system. Lawmakers can best keep their promises to retirees by creating a modern pension system that is personal, flexible and financially sustainable.

4. Performance-Based Competitive Bidding

Recommendations

1. Encourage state agencies to save money and improve service to the public by using performance-based competitive bidding authority.

2. Protect competitive bidding authority from being restricted or bargained away during secret collective bargaining negotiations.

3. Adopt a competition council to help agency managers identify cost savings and public services that could be improved through competitive contracting.

Background

The state's tight financial situation lends fresh urgency to the use of performance-based competitive bidding. Competitive bidding allows state agencies to open work normally performed by in-house employees to bids from a variety of sources. Public employees are allowed to bid for contracts along with contractors from the private sector. Competition allows government managers to provide improved services to the public at lower cost to taxpayers.

Until recently, state law, following a court ruling in the 1978 Spokane Community College case, held that any work historically performed by state workers had to always be performed by state workers.[22] Private companies were not allowed to submit bids to see if the same amount and quality of work could be done at lower cost.

In 2002, the legislature, as part of a larger collective bargaining and civil service reform measure, enacted a law which gave state agencies the authority to open work contracts to competitive bidding.[23] The new rule went into effect in July 2005.

Unfortunately, the state has done little to gain savings from competitive bidding with the private sector under the provisions of this law. This is partly because of the current political climate in Olympia and the fact that the 2002 reforms created an overly complicated process for pursuing bidding. Currently, opposition from government unions and a burdensome process prevent the state from realizing the full benefits of competitive bidding.

A performance audit conducted by the Joint Legislative Audit and Review Committee (JLARC) in January 2007 found:

> few agencies have competitively contracted for services in the 16 months since receiving authorization to do so.
>
> Agency managers reported two main reasons for not competitively contracting. First, managers perceive the process itself to be complicated and confusing, providing a disincentive to pursue competitive contracting. Second, competitive contracting is a subject of collective bargaining, which creates additional challenges by requiring labor negotiations. Managers must bargain, at a minimum, the impacts of competitive contracting.
>
> Additionally, some agency collective bargaining agreements include provisions which [sic] prohibit agencies from competitively contracting.

In a 2009 update of the JLARC audit, Washington Policy Center asked the state Office of Financial Management's contract division how many personal service contracts have been requested or approved by agencies under the Civil Service Competition provision of the 2002 law. The answer was zero.[24] Washington Policy Center also surveyed various agencies to see how they were taking advantage of this reform.

Of all the agencies surveyed, only the Health Care Authority reported it had used competitive contracting under the 2002 law. Typical of agency responses was this answer from Washington State University (WSU):

> I have been advised that WSU has not executed any contracts under this 2002 Civil Service Reform/RCW 41.06.142 process. It's apparently a complicated process and the administrative decision was made early on that WSU would not participate or take any action that would implicate this process (i.e., contract for purchased services that would displace classified staff).[25]

The primary flaw lawmakers included in the 2002 civil service law was making an agency's contracting out authority subject to collective bargaining. Public sector unions have a strong financial incentive to induce agency managers to surrender their ability to seek lower prices because the agency's work is then reserved for union members, regardless of cost to taxpayers.

Policy Analysis

The benefits of competitive pricing that the legislature and Governor Locke expected to achieve from the Personnel System Reform Act of 2002 have not been realized. A performance audit investigation by JLARC staff, supported by Washington Policy Center's independent survey of major agencies, finds that state managers have done almost nothing to carry out the legislature's intended competitive pricing policy.[26]

This is not because agency managers are not interested in lowering the cost of delivering public services. State employees routinely look for ways to do their jobs better and to make their agency's budget go further. The reason is that managers face two insurmountable obstacles in seeking savings from ending in-house monopolies and moving to competition.

First, the 2002 law made competitive bidding subject to mandatory collective bargaining negotiations. Leaders of public sector unions have made no secret of their stout opposition to any form of competition, seeing the possibility of contracting out as threatening their access to government workers. Among the key provisions of most mandatory collective bargaining agreements adopted since 2002 is the restriction or elimination of an agency's ability to seek lower prices through competition.

Second, a successful 2008 lawsuit filed against the state by leaders of public sector unions has made it difficult or impossible for an agency to implement a competition program if a state worker might become a "displaced employee" as a result. Given these severe limitations, competitive bidding in Washington remains an impressive management tool in theory but is completely useless in practice.

Four Benefits of Competitive Bidding

There are four key benefits of performance-based competitive bidding that show how competition successfully improves quality and eases the budget strain of core government programs. These are presented below.

1. **Lower cost**. Private companies are disciplined to seek efficiencies through the need to operate at a profit while providing superior service at a competitive price. By employing the techniques of competition, public managers find efficiencies within their operations and lower the cost of performing a service.

2. **Higher service levels**. Monopolies, whether public or private, frequently lack the stimulus to innovate and improve service delivery. By opening services to competition, governments can upgrade services and achieve cost savings.

3. **Better management**. Government can streamline its operations by using the same accounting procedures and productivity measures that the private sector uses, which are more accurate and comprehensive than traditional government methods.

4. **Changed government culture**. When a government seeks dynamic competition over a monopoly status quo its culture changes. Instead of performing many functions with limited expertise, governments that are open to competition liberate themselves to perform a smaller set of core functions better than ever before, while leaving much of the routine work to contractors.

Across the country, state, county and city governments are opening services to competitive bidding that were once performed exclusively by government agencies. These competitions are often won by government workers themselves, showing that efficiencies can be found even when public employees continue to do the work. For public leaders, tapping the benefits of competition is a better alternative than pushing for ever-rising levels of taxation.[27]

Competition Council

To help facilitate the move to robust performance-based competitive contracting, state agencies would benefit from the creation of a formal competition council. The state auditor's office notes that this is a "leading practice" across the country. Following is one of the recommendations from a recent performance audit of the state's contracting process conducted by the state auditor:

> Create a centralized office or staff with a high degree of expertise in performance measurement and performance-based contracting to provide technical assistance to agencies in developing and improving their use of performance measures and outcomes.[28]

Though not identical to this recommendation, companion bills were introduced in 2011 to create a version of this reform (HB 1873 and SB 5316), but they were not acted on by the legislature. From the bill reports:

> Creates the Washington competition council as an advisory council within the office of financial management to, among other duties:
>
> > (1) Examine and promote methods of providing select government-provided or government-produced programs and services through the private sector by a competitive contracting program; and
> >
> > (2) Develop an institutional framework for a statewide competitive program to encourage innovation and competition within state government.[29]

As noted by the state auditor, several states take advantage of this type of reform. Here are two examples:

> **Florida** – In 2006, lawmakers in Florida created the Council on Efficient Government to help managers at state agencies focus their public workforce on carrying out each agency's core mission, while hiring outside contractors to perform lower-priority work. The council's goal is to "deliver services by outsourcing or contracting with private sector vendors whenever

vendors can more effectively and efficiently provide services and reduce the overall cost of government."

The council evaluates state services for feasibility and cost-effectiveness before any public work is considered for competitive bidding. If a bidding process would not reduce costs to the public, the work is not contracted out.[30]

Texas – In 1993, Texas lawmakers created the Council on Competitive Government to identify opportunities within state agencies to lower costs through competition. The legislature gave the Council instruction to "identify, study and finally determine if a service performed by one or more state agencies may be better provided through alternate service methods, including competition with state agencies that provide the service or commercially available sources."[31]

Public employees should be encouraged to participate in competitive bidding processes, but union leaders should not be able to exercise a veto over a management decision that a public service can be improved and streamlined through price competition. Adopting a formal competition council would help agency managers identify cost savings and public services that could be improved through competitive contracting.

Letting state agencies use competitive pricing to lower the cost of delivering public services, and at the same time improve service quality, is one of the reforms necessary to solving the state's long-term budget problem. Properly implemented, a well-managed competitive pricing policy would lead to a more cohesive state government that focuses on core services, while using competition to tap the efficiencies of the open marketplace.

Recommendations

1. **Encourage state agencies to save money and improve service to the public by using performance-based competitive bidding authority.** Many opportunities for competitive contracting exist throughout state government. Experience from other states shows typical cost savings of 10 to 25% are gained when agency managers introduce open competition for government work.

2. **Protect competitive bidding authority from being restricted or bargained away during secret collective bargaining negotiations.** Washington policymakers should simplify the bidding process to make it easier for agencies to use competition to improve services. Lawmakers should shield contracting out from union and political influence by removing it from the secretive collective bargaining process. Improving service to the public is too important to be a bargaining chip in closed-door government labor negotiations.

3. **Adopt a Competition Council to help agency managers identify cost savings and public services that could be improved through competitive contracting.** A competition council would help take the politics out of contracting and provide the business case and monitoring expertise necessary to ensure taxpayers are receiving contract value and results.

Additional Resources from Washington Policy Center, Available at washingtonpolicy.org

"A Review of Washington State's 2011–13 Budget and Recommendations for Structural Reform," by Jason Mercier, July 2011.

"Ending the Spending Crisis: Structural Reforms for a Sustainable State Budget," by Jason Mercier, January 2011.

"How Competitive Contracting Can Help Balance the Budget without Raising Taxes," by Jason Mercier, December 2009.

"Resources for Building the State Budget," by Jason Mercier, February 2009.

"Changing the Budget Status Quo," by Paul Guppy and Jason Mercier, December 2008.

"Citizens Guide to SJR 8206, Budget Stabilization Account," by Jason Mercier, August 2007.

"Washington Votes for Fiscal Discipline, Against Tax Increases," by Jason Mercier, November 2007.

"State Lawmakers Should Return the Extra Money They are Taking from Taxpayers," by Paul Guppy, December 2006.

"New Audit Law to See Whether Government Agencies are Keeping Their Promises," by John Barnes, May 2006.

"The State Budget Tug-of-War," by Paul Guppy, January 2006.

"Guide to Initiative 900: Reviewing Government through Performance Audits," by John Barnes, October 2005.

Endnotes

[1] "Gov. Gary Locke Announces 'Priorities of Government' Strategy for Lean, Results-Oriented State Budget," news release, Office of the Governor, Olympia, November 14, 2002, www.governor.wa.gov/press/press-view.asp?pressRelease=1222&newsType=1.

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[3] "Priorities of Government," Governor Gary Locke, news conference, November 14, 2002, at www.digitalarchives.wa.gov/governorlocke.
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[9] Ibid.
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[13] "Executive Order 05-14," email communication from Anita Samuel, Office of Indiana Governor Mitch Daniels, August 16, 2011, copy available on request.
[14] "Premium averages," email communication from Sharon Michael, Washington State Health Care Authority, July 22, 2010, copy available on request.
[15] "PEBB Enrollment Report for July 2011 Coverage," Public Employees Health Benefits Board, Washington State Health Care Authority, July 2011, at www.pebb.hca.wa.gov/documents/enrollment/jul2011.pdf.
[16] SHB 1417, HB 1644, SSB 5336, SB 5640 and E2SSB 5930, "Legislature expands access to PEEB coverage," PEBB Perspective, Public Employees Health Benefits Board, Washington State Health Care Authority, July 2007, at www.pebb.hca.wa.gov/documents/empjuly2007.pdf.
[17] SB 5773, "Offering a health savings account option and high deductible health plan to public employees," Washington State Legislature, 2011 Session. The bill was sponsored by Republican Senator Joe Zarelli and signed by Governor Gregoire on May 31, 2011, at www.washingtonvotes.org/Legislation.aspx?ID=131500.
[18] Revised Code of Washington 41.80.100.
[19] "Collective Bargaining Agreement By and Between The State of Washington and Washington Public Employees (WPEA)," July 1, 2005 through July 1, 2007, Article 36.3, at www.ofm.wa.gov/labor/agreements/05-07/wpea/wpea.pdf.
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[22] *Washington Federation of State Employees v. Spokane Community College*, 90 Wash. 2d 698, 585 P. 2d 474 (1978) and codified by the legislature in RCW 41.06.380.
[23] Substitute House Bill 1268, The "Personnel System Reform Act of 2002."
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[26] "Performance Audit of the Implementation of Competitive Contracting," Joint Legislative Audit and Review Committee (JLARC), January 2007.
[27] For examples from other states of the effectiveness of contracting out, see "Competing for Highway Maintenance: Lessons for Washington State," by Dennis Lisk, Washington Policy Center Policy Brief, September 1998, and "Research Shows Private Prisons Enable States to Improve Quality and Control Costs," Washington Policy Center Legislative Memo, February 28, 2005, both at www.washingtonpolicy.org.
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