July 6, 2006

MOU Fiscal Analysis:

Bargaining Units 1, 3, 4, 11, 14, 15, 17, 20, and 21 (SEIU Local 1000)

LEGISLATIVE ANALYST'S OFFICE

Presented To:

The Legislature, Pursuant to Chapter 499, Statutes of 2005 (SB 621, Speier)

July 6, 2006

65 YEARS OF SERVICE

Summary

☑ ***Agreement Through June 2008.*** Service Employees International Union (SEIU) Local 1000 represents nine units, or about one-half of the unionized state workforce. The proposed memorandum of understanding (MOU) with these units extends through June 30, 2008. Assembly Bill 1369 (Nuñez) is the vehicle for legislative action on the MOU.

☑ ***Major Provisions.*** Significant provisions include:

- A 3.5 percent salary increase effective July 2006, and an inflation-based increase in July 2007.
- A one-time bonus of $1,000 upon ratification.
- Increases for classifications with recruitment and retention issues.
- Specified reductions in new employees' retirement and health benefits starting with hires in 2007.

☑ ***DPA Cost Projections.*** In the formal cost estimate submitted to the Legislature, the Department of Personnel Administration (DPA) projects that state costs will increase by $344 million ($137 million General Fund) in 2006-07 and by an additional $253 million ($106 million General Fund) in 2007-08 if the MOU is approved.

☑ ***LAO Bottom Line.*** We believe that DPA's estimate for 2006-07 is reasonable, but that the estimate for 2007-08 likely overstates costs by around $65 million due primarily to a high estimate of inflation. The scale of this MOU in terms of the number of employees affected means that small percentage changes can translate into tens of millions of dollars. Actual 2007-08 costs will depend on such factors as the rate of inflation, health premium growth, the pace of departmental hiring, court orders, and any unidentified factors underlying DPA's cost estimates for this 1,729-page agreement.

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Bargaining Units at a Glance

☑ ***SEIU Represents About One-Half of Unionized State Workers.*** The nine units include about 85,000 state workers, or about 50 percent of the unionized workforce. These workers perform a wide variety of tasks and work in nearly every state department.

☑ ***Most Work in Administrative and Financial Services.*** Figure 1 shows the distribution of employees represented by SEIU. About 70,000 of the workers are in Units 1 and 4 and work in administrative, financial, and office assignments.

Figure 1

SEIU Local 1000 Bargaining Units

Bargaining Unit	Represented Employees
1—Administrative, Financial, and Staff Services	41,346
3—Educators and Librarians (Institutional)	2,050
4—Office and Allied Workers	28,295
11—Engineering and Scientific Technicians	2,694
14—Printing Trades	539
15—Allied Services (Custodial, Food, Laundry)	4,204
17—Registered Nurses	3,572
20—Medical and Social Services Specialists	2,081
21—Education and Libraries (Noninstitutional)	582
Total	**85,363**

Source: SEIU Local 1000.

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Previous MOU

- ☑ ***Term.*** July 3, 2003 to June 30, 2005, except for Units 3 and 17 (which had MOUs that expired in 2003 and 2004, respectively).

- ☑ ***Pay Increases.*** Most of the employees last received a general salary increase of 5 percent on July 1, 2003, but payment was deferred for one year in exchange for other compensation.

- ☑ ***Health Benefits.*** In general, employees of these units receive health benefits under the "80/80" formula, which provides that the state's contribution to health premiums equals 80 percent of the average premiums of the four largest basic state health plans offered through the California Public Employees' Retirement System (CalPERS), plus 80 percent of the average additional premiums to enroll dependent family members.

- ☑ ***Retirement.*** Most of the employees are eligible for "2 percent at 55" retirement benefits and contribute approximately 5 percent of monthly pay to cover part of the costs of these benefits. Benefits paid to retired employees have been based on the highest pay received during a year of employment.

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Proposed MOU—
Pay Increases and Bonuses

☑ ***General Salary Increases.*** The agreement provides for two general salary increases for nearly all employees in the nine units:

- 3.5 percent increase effective July 1, 2006.
- Inflation-based increase of no less than 2 percent and no more than 4 percent effective July 1, 2007.

Excluded from these increases are teachers in the California Department of Corrections and Rehabilitation's Division of Juvenile Justice (formerly the California Youth Authority) affected by the *Farrell v. Allen* court case. A March 2006 agreement provides compensation increases for these employees.

☑ ***One-Time Bonus.*** Employees would receive a one-time $1,000 bonus upon ratification of the MOU. The SEIU estimates that this equals 2.3 percent of the average salary for employees in the nine units. Details of how the bonus would be distributed to part-time employees have not been finalized.

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Proposed MOU—Retirement and Health Benefits

- ***New Employees Would Be Affected by Changes.*** Employees in the nine units hired on or after January 1, 2007, would be affected by several changes in retirement and health benefits. The benefits of current and past employees generally are unaffected by this MOU.

- ***Retirement Changes.*** For the typical state employee receiving 2 percent at 55 benefits, for example, retiring at age 55 after 25 years of service can result in a retirement benefit equal to 50 percent (or 2 percent multiplied by 25 years of service) of the employee's highest *single year* of pay. Under this MOU, employees hired after January 1, 2007, would be eligible for retirement benefits based on the highest average annual pay received over any consecutive *three years* of state service.

- ***Health Benefit Changes.*** Employees would continue to be eligible for 80/80 health benefits except that employees hired after January 1, 2007, would receive the full state premium contribution for dependents only after two years of state employment. The state would contribute 50 percent of the 80/80 formula amount for dependents during a new worker's first year and 75 percent of this amount during the worker's second year.

Proposed MOU—
Recruitment and Retention

- ☑ ***Increases to Address Recruitment Issues.*** The MOU provides additional targeted pay increases to selected employees. These employees total 21 percent of the workforce represented by SEIU. They are in classifications where there have been problems with vacancies and turnover.

- ☑ ***Step Increases of 5 Percent.*** Several groups of employees would have a step added to current pay ranges, thereby increasing the maximum salary for targeted classifications by 5 percent, effective (except as noted below) January 1, 2007:

  - Information technology personnel throughout state government.
  - Auditors, such as those working at the Board of Equalization, the Employment Development Department (EDD), and the Franchise Tax Board.
  - Licensed vocational nursing, clinical laboratory, dental hygiene, and dental assistant employees, such as those working at correctional, mental health, developmental services, and veterans facilities. (Changes for dental classifications take effect January 1, 2008.)
  - Educators and librarians in adult correctional, mental health, and other facilities effective January 1, 2008.

- ☑ ***Step Increase of 7.5 Percent.*** Effective January 1, 2007, registered nurse classifications would have their top salaries increased by 7.5 percent. These and other increases would be administered so that correctional and mental health nurses that received 18 percent pay increases this spring (as a result of court orders in the *Plata v. Schwarzenegger* case) would have pay levels 10 percent over those of nurses in other departments.

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Proposed MOU—Recruitment and Retention *(Continued)*

- ☑ ***Step Increases of 10 Percent.*** Effective January 1, 2007, respiratory care practitioners (such as those working in the Department of Developmental Services) would have two additional steps added to existing pay ranges, thereby increasing the maximum pay by 10 percent. The DPA's *Total Compensation Survey* released in April 2006 found that compensation for these practitioners lagged those of other public sector employers by the greatest percentage of any group of state employees studied (56 percent below the median for other public employers).

- ☑ ***State Special Schools.*** Effective July 1, 2006, employees in classifications at state schools for the blind and deaf would receive a $200 per month recruitment and retention differential.

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Proposed MOU—
Other Significant Provisions

- ☑ ***Mileage Reimbursement.*** Prior MOUs provided for employees to be reimbursed for use of their privately owned vehicles while on state business, generally at a rate of 34 cents per mile. This rate has not been increased for several years, despite significant increases in gasoline prices. The proposed MOU would instead provide reimbursement at the Federal Standard Mileage Rate (FSMR), which is set by the Internal Revenue Service and typically rises or falls annually based on changes in fuel prices. Currently, the FSMR is 44.5 cents per mile.

- ☑ ***State Disability Insurance.*** State Disability Insurance (SDI)—administered by EDD—pays part of an employee's wages if he or she stops working because of illness or injury not related to work or a family-related leave. Effective April 1, 2006, pursuant to prior agreements, employees are covered by SDI in lieu of nonindustrial disability insurance programs. Under the MOU, the state would pay health premiums for employees and dependents for the length of an employee's disability up to a maximum of 26 weeks. Leave time could be used to supplement SDI payments during disability periods. The MOU also makes other adjustments to SDI.

- ☑ ***Uniform and Footwear Reimbursements.*** The MOU provides for uniform and safety footwear reimbursement allowances for several groups of employees.

Proposed MOU—DPA Cost Estimates

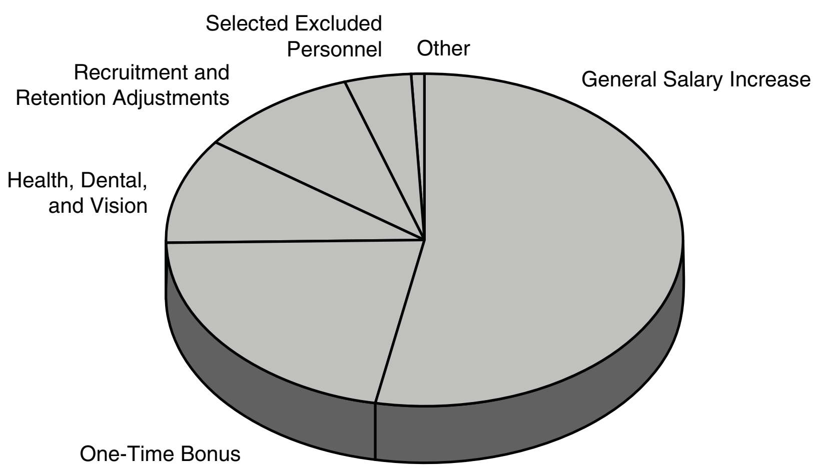
- ***2006-07.*** Figure 2 shows details of DPA's estimate of new state costs that would result from the MOU in 2006-07. The DPA estimates that new state costs associated with this MOU for rank-and-file employees would be $329 million ($130 million General Fund). In addition, DPA's estimate includes raises for some, but not all, excluded personnel totaling $15 million ($7 million General Fund) in 2006-07.

- ***2007-08.*** The DPA estimates that ongoing costs would increase by $329 million ($135 million General Fund) in 2007-08 for rank-and-file employees and an additional $6 million ($4 million General Fund) for the selected excluded personnel described above. Accounting for the one-time costs for the $1,000 bonuses in 2006-07, the budgetary increase in 2007-08 would be less—$253 million ($106 million General Fund).

Figure 2

DPA's Fiscal Impact Estimate of SEIU Local 1000 MOU

2006-07



DPA Estimated Costs: $344 Million

LAO Comments

☑ ***2007-08 Estimate Too High.*** We believe that DPA's estimate for 2006-07 is reasonable, but that the estimate for 2007-08 is likely too high by around $65 million due to a high estimate of inflation and not accounting for health care savings.

- ***Inflation.*** While DPA's estimates assume that employees receive a 4 percent salary increase in 2007-08 (the highest level possible under the MOU), our estimates assume that there is a 3 percent increase, consistent with our forecast of inflation. Our estimate for inflation costs is about $57 million lower than DPA's.

- ***Health Costs.*** About 20 percent of increased costs would result from the continuation of current health benefits for most employees. The state will experience these costs even if the Legislature does not approve the MOU. The DPA's estimates for 2006-07 include only the 12 percent premium increases approved by CalPERS for calendar year 2007 because departments already have absorbed CalPERS' monthly cost increases for calendar year 2006. The DPA's formal submission to the Legislature does not assume any savings from the reduction in dependent health benefits for new employees hired in 2007 and thereafter. Subsequent calculations by DPA indicate the possibility of $2 million in savings in 2006-07 and over $7 million in savings in 2007-08. These savings could vary based on departmental hiring practices and the demographics of employees. These new savings estimates appear to be reasonable.

LAO Comments *(Continued)*

☑ ***Costs of Filling Vacant Positions and Step Increases.*** As of March 2006, about 14 percent of positions in the nine units were vacant. For purposes of calculating the additional annual costs resulting from the MOU, DPA reports that it assumed these vacant positions were filled. (For example, DPA's estimated cost for the 3.5 percent increase in 2006-07 equals roughly the cost of providing this percentage increase to *all* positions, including the vacant ones.) The DPA also assumes that all employees in targeted classifications are at the top of their pay ranges and, therefore, will receive step increases. In fact, some employees are at lower steps and will not immediately benefit from this change. These techniques tend to overestimate costs—particularly for departments that are unable to fill currently vacant positions. (We have used DPA's estimates, however, because there is limited data to make more precise calculations.)

☑ ***Retirement.*** The changed retirement provisions for employees hired after January 1, 2007, will result in some savings to the state over the long term, but these will not begin to materialize until at least 2008-09. Compared to other factors such as returns from CalPERS' investment portfolio, the changes under the proposed MOU will have only a modest fiscal effect, particularly in the shorter term.

☑ ***Supervisor and Manager Pay.*** The DPA's estimates for the costs of this MOU relate primarily to rank-and-file employees, but also include costs for a small portion of excluded employees. The administration determines whether to approve increased pay and benefits for supervisors and managers separately from the MOU process. We estimate that the costs to provide a 3.5 percent pay increase to all excluded personnel connected to workers in these nine units could be roughly $50 million ($18 million General Fund) above the costs identified by DPA.

LAO Comments *(Continued)*

☑ ***Total Costs Under the Proposed MOU.*** We estimate that the total compensation costs (including benefits) for rank-and-file employees represented by SEIU was about $5.2 billion in 2005-06, of which about 40 percent was paid from the General Fund. As shown in Figure 3, we estimate that 2006-07 costs would rise to over $5.5 billion under the proposed MOU for a cost increase of almost 7 percent. In 2007-08, we estimate that costs would increase to $5.7 billion, or more than 3 percent above 2006-07.

Figure 3

LAO Estimated Compensation Costs for SEIU Rank and File

(In Billions)