# FISCAL FACTS

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*Dedicated to Customer Service, Efficiency*

## Performance Review Builds "New Texas"

Given the opportunity to rebuild something important—our homes, for example—most of us would jump at the chance.

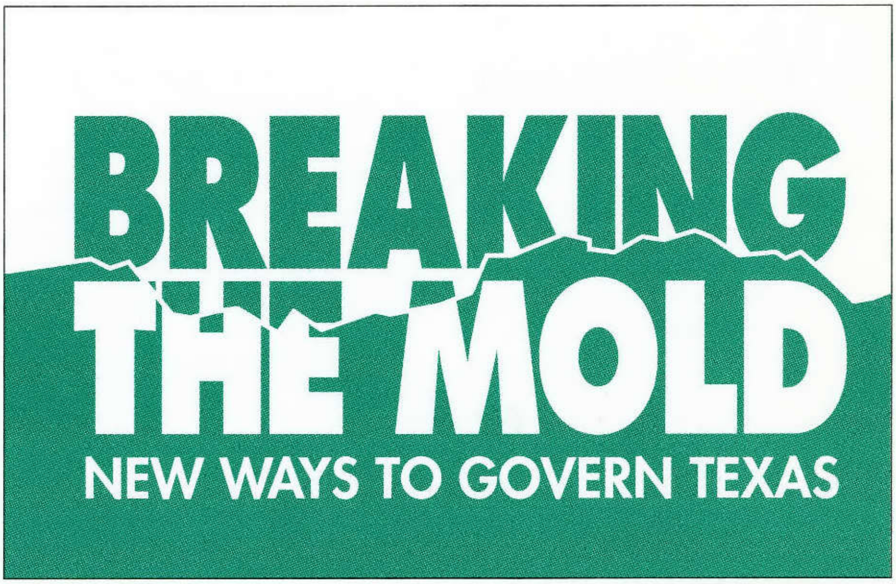
The same applies to our state government. Taxpayers, state employees and elected officials all have dreams of how they would transform this massive institution.

Enter, stage left, the ***Texas Performance Review***. Authorized by Senate Bill 111, the first bill passed by the 72nd Legislature, the ***Performance Review*** was directed to "challenge the basic assumptions about state government."

The Comptroller's Office, which headed the ***Review***, was told to design a new state government from scratch, as if it didn't exist. It was a once-in-a-lifetime opportunity to make Texas state government a shining star among the 50 states.

Two key pillars were the foundation of this project from the start. The team wanted to build a government that provides its customers—agency clients, school children and the business community—with fast, friendly and personalized service. The auditors also insisted that this new government give up the inefficiencies, duplications and frills that squander dollars that could pay for needed services.

The plan contains much more than a rehash of old ideas or tinkerings with the existing order. The report breaks the mold of traditional thinking and offers real improvements in government organization, services and efficiency.




Remember that the state faced a $4.6 billion budget shortfall for the 1992-1993 biennium when the Legislature ordered this review. By the time the review was done, the team had found ways to slice more than $4 billion from the budget while actually expanding services.

Some examples of the new state government, dedicated to the twin guideposts of customer service and government efficiency, include:

- Mothers of children with multiple handicaps would no longer have to wander from agency to agency to re-

### Special Issue

## Straight FACTS

We began the ***Texas Performance Review*** with a single goal in mind — to find ways to make state government leaner, more efficient and more responsive to the people of this state.

We produced a 1,200-page report which includes approximately 975 recommendations in nearly 200 different areas on ways to cut cost and improve state services.

It represents the best effort of hundreds of people at all levels of state government to find better ways of doing our jobs.

It was suggested back in January that we might find ways to cut at least $200 million from the state budget. We did that the first day.

On June 26, when we released the ***Performance Review*** report, we had identified ways to save the state over $4 billion in revenue over the next two years while avoiding a major new tax increase or an income tax.

If the Legislature enacted all the recommendations in the report, we calculate the savings to the state at $12.4 billion over the next five years.

A lot of people, including many of you, helped put this document together. We appreciate that help and believe the report represents our best effort to craft an effective state government for the 1990s and beyond. ■

John Sharp

## Performance Review Continued

ceive the services they need. Instead, they would have "one-stop shopping" at convenient Health and Human Services field offices.

- Drivers no longer would have to wait six weeks for their driver's licenses. Instead, they could leave local Department of Public Safety offices with their new licenses already tucked away in their wallets.

- School districts, with bloated administrative staffs, would have to streamline their front offices because state funding formulas would require them to concentrate their dollars in the classrooms.

- State employees could no longer spend tax dollars casually on a whim. Instead, new personal incentives to save, combined with rewards for innovation, would create an "I've got a stake in this" spirit among state workers.

There is some tough medicine in the report. Many of the recommendations demand that we do things very differently.

The ***Performance Review*** recommendations include many substantial changes in state finance and accounting. If implemented, those changes will require state agencies and their finance officers to begin new procedures.

The remainder of this special issue of ***Fiscal Facts*** is dedicated to explaining some of those key recommendations. As the issue goes to press, the Legislature is in special session to consider the ***Performance Review*** report and write the 1992-1993 state budget.

Future issues of ***Fiscal Facts*** will keep you up to date on important changes in state financial policy. ■

FISCAL FACTS

JOHN SHARP • TEXAS COMPTROLLER OF PUBLIC ACCOUNTS

**Fiscal FACTS** is a publication of the Texas Comptroller of Public Accounts, written to help inform Texas agencies about the latest developments in Texas government and changes in state tax law.
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*Innovative State Workers Can Earn Extra Bucks*

# Incentive Plan Rewards Employees While Saving Money

One of the most creative recommendations in the ***Texas Performance Review*** relies on the ingenuity of state employees to save at least $150 million in general revenue for the 1992-1993 biennium. As an incentive, those innovative state workers who help save big bucks for the taxpayers can pick up a few bucks for themselves as well.

The Incentive Cost-Sharing Plan in the ***Performance Review*** is based in part on the existing Productivity Bonus Program, designed to reward employees for reducing operating costs. Since the 69th Legislature enacted it, the Productivity Bonus Program has suffered from a lack of direction and appropriations, and there was little incentive to boost the program into a viable cost saving measure for the State of Texas.

National observers of state and local governments, however, say the concept is sound. Efficient and effective government results when managers and front-line employees are given the opportunity to manage their programs, achieve results and then share in the benefits.

To save taxpayer money, boost employee morale and encourage better management, the ***Performance Review*** recommended:

**The Legislature should enact an incentive cost sharing program to reward state agency managers and front-line employees for achieving cost savings. Half of the savings should be reappropriated to the agency for salary bonuses for those employees directly involved in producing the savings and, at the option of agency management, funding for new or innovative programs.**

The Comptroller's Office, the Legislative Budget Office and the Governor's Office of Budget and Planning would measure actual savings at the end of fiscal 1992 as well as projected savings for fiscal 1993. Half of these savings would be reappropriated to the agencies for one-time bonuses, up to $1,000 each, for employees directly involved in producing the savings. Agency managers also could direct savings into new or innovative programs.

Although many businesses and governments have shown that an incentive cost-saving plan works, the Texas Constitution does not allow the Legislature to balance the budget based on conjecture. For the Comptroller to certify the projected savings as available for expenditure, across-the-board budget reductions must be authorized to fill any gap between the voluntary savings and the $150 million goal. That "fail-safe" mechanism would enable the Comptroller to certify that the entire $150 million was available.

Here's how it would work. At the end of the first year of the biennium, the actual and projected savings from the voluntary program would be measured. The Comptroller's Office would calculate any shortfall between the estimated actual savings and the $150 million goal. An across-the-board budget reduction would be implemented for fiscal year 1993 to make up the difference.

This approach was used to obtain some of the savings in Senate Bill 111, which reduced agency operating budgets by 1.5 percent. The reductions excluded much of the state's budget priority programs, such as:

- Employee benefits (including the retirement systems and insurance);
- Workers' compensation benefits for injured state workers;
- Department of Human Services—all budgeted items;
- Department of Mental Health and Mental Retardation—all budgeted items;
- Foundation School Program;
- Higher education, $100 million constitutional HEAF appropriation;
- Debt service on bonds;
- State Purchasing and General Services Commission lease payments on buildings;
- Any specific employee salary increase appropriation;
- Constitutional funds such as highway and Available University funds;
- Funds held outside the treasury; and
- Federal, trust or escrow funds.

Those exclusions accounted for about 78 percent of the total state budget.

Under the new plan, all agencies, both general revenue and special funded, would be directed to participate in the program. That means all state employees would have the opportunity to save money and reap the rewards.

Even if the incentive cost-sharing plan saves no more than half of the targeted $150 million in 1992-93, the across-the-board budget reduction for the non-exempted programs would not exceed 1 percent of their "operating budgets" for the second year of the biennium. ■

*Simplifying State Accoounting*

# Funds Consolidation

In an effort to monitor and control state spending, the Legislature has created numerous state funds. By the end of 1990, there were 365 funds created either constitutionally or by statute in the State Treasury.

The ***Texas Performance Review*** recommends consolidation of these funds to simplify reporting and increase the funds available for discretionary state spending. Consolidation would result in a one-time gain to the state's General Revenue Fund of $540 million.

The numerous funds with revenues dedicated for a specific purpose limit the options available to meet the changing needs of the state. The original function of a dedicated fund may not be relevant in the current environment.

A review of the original purpose, current use and classification of each fund is necessary to develop a consolidation plan to achieve greater flexibility and efficiency in state financing. Priorities change, and the current system makes it difficult to address the state's immediate and future needs. Tying specific revenues to programs that may no longer be needed or may be overfunded severely limits adaptability.

The proposal recommends that in conjunction with conversion to the Uniform Statewide Accounting System, the more than 300 non-constitutional funds be consolidated into five super funds. The five funds proposed are the General Operating Fund, Federal Fund, Pledged Fund, Trust Fund and Suspense Fund. These classifications correspond to the current classifications in the Annual Cash Report and differ from the fund classifications in the Texas Comprehensive Annual Financial Report prepared in accordance with generally accepted accounting principles (GAAP).

Although five super funds are recommended, the comptroller could create additional funds to comply with governmental accounting requirements. The consolidation would merge existing funds and accounts into a comprehensive system that is more in accordance with generally accepted accounting principles. With a reduction in the number of funds, accountability for specific programs would be transferred to the account or agency level.

The consolidation of all general and operating funds into one General Operating Fund would include agencies currently using special funds. Transfers from the General Revenue Fund to special operating funds would no longer be necessary, with a significant reduction in accounting transactions. ■

## Fiscal 1990 Ending Cash Balances By Fund Group

| Fund Group | Number of Funds | Cash Balance on August 31, 1990 (in millions) |
|---|---|---|
| General State Operating and Disbursing Funds (excludes the General Revenue Fund, $767 million) | 208 | $ 675.8 |
| Constitutional Funds Expendable for Specific Purposes | 59 | 806.8 |
| Federal Funds | 21 | 99.7 |
| Pledged Funds | 8 | 569.9 |
| Constitutional Nonexpendable Funds | 6 | 205.1 |
| Tax Clearance Funds | 2 | 90.8 |
| Trust Funds | 55 | 1,967.7 |

# Changing Budget Execution

History has proven that the biennial budget system used in Texas, requiring the projection of revenues and expenditures almost three years in advance, is often subject to revision before the two-year appropriation cycle ends.

The Legislature has frequently had to meet in special session to solve problems involving revenue shortfalls or emergency funding needs.

In November 1985, Texas voters approved a constitutional amendment allowing emergency transfers of appropriated funds when the Legislature is not in session. The 1987 Legislature enacted Chapter 317 of the Government Code to serve as the statutory authority and establish a specific procedure for appropriation transfers.

The statute permits the Governor, when the Legislature is not in session, to recommend:

- appropriations be transferred from one agency to another;
- appropriations be retained by an agency and available for expenditure for a different purpose; or
- appropriation distribution or utilization time frames be changed.

Following the Governor's recommendation and a 10-day publication period in the ***Texas Register***, the Legislative Budget Board (LBB) may meet to act on the proposal.

After holding a public hearing, the LBB may approve, modify or reject the proposal. A modified proposal is called a "contingent order" and must be approved by the Governor before it takes effect.

The ***Texas Performance Review*** recommended three policy changes:

- **The 5-percent increase limit and 10-percent decrease limit on the total appropriations of an agency should be eliminated.** An effective double check system of approval by both the Governor and LBB already prevents any possibility of increasing or decreasing an agency budget beyond reasonable limits. Several past situations could have been resolved easily if the statutory limitations had not prevented access to unused agency balances. As spending priorities change, some agencies could have budgeted funds unspent and unavailable, while other agencies might be left with critical spending needs that could only be solved by a special session of the Legislature.
- **Budget execution proposals should be authorized by both the Legislative Budget Board and the Governor.** Currently, the only way a fiscal problem can be solved is if the Governor takes the initiative. Recent statutory changes, however, clarify the authority of the Comptroller to review the efficiency and effectiveness of policies, management, fiscal affairs and operations of state agencies. The Comptroller reports to the Governor, Lieutenant Governor and Speaker of the House of Representatives on the result of the agency's operation reviews.

  Consistent with this statutory responsibility, the Comptroller should recommend to the Governor and LBB that they propose a budget execution action.
- ***Budget execution proposals by the Governor or LBB must be approved by the non-proposing party.*** Budget execution proposals by the Governor must be approved by LBB, and conversely, LBB proposals must be approved by the Governor. Any changes to the proposals by the approving party must receive concurrence by the originating party before the proposal becomes final.

Although the recommendation is not expected to produce immediate and direct fiscal savings, the basic structure will enhance the ability of state leaders to address fiscal concerns without the need for special sessions. Additionally, agency administrators could use the new process to help them resolve pressing budget concerns in a more timely and less complicated way. ■

**CHANGING BUDGET EXECUTION WILL ENHANCE THE ABILITY OF THE STATE'S LEADERS TO ADDRESS FISCAL CONCERNS WITHOUT NEED FOR SPECIAL SESSIONS.**

*Privatizing State Services:*

# The Privatization Council

**Private companies would be allowed to bid on any non-constitutionally mandated services.**

Privatizing certain state services and creating a privatization council could save the state more than $30 million annually, according to the report issued by the ***Texas Performance Review***.

The report outlines several recommendations to make this saving possible, including the creation of the Privatization Approval Council of Texas (PACT). The ***Review*** also recommends the Competitive Cost Review Program (CCRP) statutes be repealed and CCRP be replaced with the PACT.

The CCRP, created by the 70th Legislature in 1987, was designed to identify services for privatization and provide systematic cost analysis for management information on the quality, quantity and cost of products or services delivered by the state. Since the CCRP was enacted, little has been accomplished by state agencies beyond attempts to identify services and analyze costs, the ***Review*** reported.

By comparison, the PACT would be required to review vendor or agency proposals to privatize state services or sell assets. The PACT would include the following members or their appointees: the Governor, Lieutenant Governor, Comptroller, executive director of the Department of Information Services, executive director of the State Purchasing and General Services Commission (SPGSC). The Speaker of the House would serve as an ex officio member.

Private companies or state agencies would be allowed to bid on any non-constitutionally mandated service. Privatization of services would be considered when the private sector can provide service equal to that performed by the state at a savings greater than 10 percent of the state's cost to provide the service.

Sometimes the state will develop assets because no private sector company exists to provide the service. Once a private market develops that can provide the service at a competitive cost, the state will consider selling that asset, under the proposal. When that happens, PACT would be required to sell the state assets, gaining the state one-time revenues and reducing administrative overhead.

Due to market competition, the private sector can sometimes provide cheaper services. In response, state agencies bidding against the private sector would need to identify areas of improvement in service delivery and improve operating expenditures to bid competitively.

To save any money, however, the state would be required to first identify current service delivery costs and then compare these costs with private services. Currently, there is no available system to assess potential savings because of unclear guidelines on how to compare state services against private services, including indirect costs.

The Privatization Council would provide the state with a greater opportunity to privatize and improve the delivery of selected services, when it is appropriate. The PACT also would allow the state to evaluate gains from effective competition and exchange ideas on public-private partnerships nationwide. ■

# Centralized Purchasing

The ***Texas Performance Review*** found the state is not reaping the full benefits of a centralized purchasing system. Since the state's purchasing system is decentralized, only some purchasing requests are reviewed and approved by the State Purchasing and General Services Commission (SPGSC) or the Department of Information Resources (DIR).

***Performance Review*** research reveals that the number and scope of exemptions from SPGSC and DIR are key factors affecting state savings that should result from a centralized purchasing system. While the state spent more than $6.7 billion in fiscal 1990, only $760 million was reviewed by SPGSC.

The report noted that a truly centralized purchasing system should allow the state to receive reduced prices through negotiations on volume purchases, while also providing state agencies with a standard quality on products. Agencies could avoid maintaining large purchasing staffs. Centralized purchasing should also result in increased consistency in operations and procedures statewide.

According to a 1989 report by the State Auditor's Office, SPGSC reviewed less than 20 percent of purchases of goods and services. Research by the ***Texas Performance Review*** revealed that less than 15 percent of purchases were reviewed in fiscal 1990. The low percentages were due to the exemptions from SPGSC review, creating a situation where numerous high-dollar purchases were made without review. In addition, although the number of purchases increased from fiscal 1989 to 1990, the average dollar cost reviewed by SPGSC decreased by almost 8 percent.

Another analysis by the ***Review*** indicated that 49 percent of all open market purchase requests reviewed and made by SPGSC in 1989 were for less than $5,000, yet these requests accounted for only 3.8 percent of the total dollars reviewed. This trend continued in 1990, with 51 percent of all open market purchases reviewed cost less than $5,000 while accounting for 4.2 percent of the total dollars reviewed.

In addition to the many agency exemptions, local funds used by universities for purchases without SPGSC review represent significant expenditures. While universities sometimes use SPGSC even though they are not required to do so, most of their local funds purchases are made without SPGSC review.

DIR reviewed 81 purchases in fiscal 1989, of which, 95 percent were approved at an average cost of $1.7 million. In fiscal 1990, the agency reviewed 87 purchases, and of those, 91 percent were approved at an average cost of $1.5 million. While the approval rates remain high, DIR has been able to affect the size of the purchases. DIR estimates it saved the state $16 million dollars in direct cost savings and avoided $33 million in costs.

A key concern with the purchase of automated equipment and services is that agencies do not generally include internal development costs in the overall costs of a project. Therefore, an agency can spend extensive time and resources prior to involvement by DIR. By requiring agencies to include internal development costs in the total costs of projects, more projects would be subject to DIR review, increasing the state's opportunity to save on automated equipment purchases.

Separating purchase contracts from service contracts is another key concern. The design of a project and its implementation are separately bid. This gives the vendor who designs the system an unfair advantage when it comes time to bid on implementation. The ***Review*** suggests modifying the automated procurement process to enhance competition.

The recommendations issued by the ***Texas Performance Review*** include the repeal of exemptions from the procurement process to ensure that significant purchases are made with SPGSC or DIR review. More control of state purchasing by SPGSC and DIR can increase savings by volume discounts.

The ***Review*** also recommended that SPGSC statutes be amended so that SPGSC would only be required to review purchases greater than $5,000. This change would allow the SPGSC to review the acquisition and quality of larger purchases, which is more cost effective. Discounts for goods and services purchased regularly could be consolidated and negotiated through group purchases. ■

**A TRULY CENTRALIZED PURCHASING SYSTEM SHOULD ALLOW THE STATE TO SAVE THROUGH VOLUME DISCOUNTS, WHILE ALSO PROVIDING AGENCIES WITH A STANDARD QUALITY ON PRODUCTS.**

# Changes in Travel Policy Recommended

Recommended changes in travel policies, including mandatory participation in the State Travel Management Program and the elimination of partial per diem, would save the state $5.9 million dollars each year, according to the report issued by the ***Texas Performance Review***.

Current travel procedures vary from agency to agency. Although the Comptroller's Office requires all travel vouchers to be completed in the same manner, the methods used by agencies to authorize, approve and book travel arrangements differ. Mandatory participation by state agencies and institutions of higher education in the State Travel Management Program (STMP) would result in estimated savings of $1.6 million annually, the ***Review*** noted.

In 1987, the Legislature created the Travel and Transportation Division (TTD) in the State Purchasing and General Services Commission (SPGSC), which developed the State Travel Management Program (STMP). Through this program, state agencies have access to services such as air and car rental reservations, negotiated discounts for hotels and autos, credit cards and group meeting planning services.

State agency participation is voluntary, and services are offered by the division at no cost. Currently, 130 of 250 state agencies participate in the STMP.

According to SPGSC, higher education institutions that do not currently participate in the program account for approximately 56 percent of the state's total travel expenditures. SPGSC does not know if the universities have negotiated rates with the savings potential offered by STMP. However, according to the recommendations of the ***Texas Performance Review***, if the universities used the STMP's services, there would be a greater opportunity to benefit from the current contract. Although the state receives a discount, increased participation through SPGSC by all state agencies and institutions of higher education could possibly gain even better discounts.

Another recommendation for saving the state millions of dollars includes the elimination of partial per diem. The intent of partial per diem and the Travel Act is to reimburse employees who are away from their designated headquarters on official state business. The Internal Revenue Service's (IRS) position is that most of these payments are not deductible as a business traveling expense. Therefore, they must be included as gross income for the employee and are subject to income tax withholding, Social Security (FICA) contribution and FICA matching by the employer.

State agencies that pay the partial per diem must change their travel voucher systems so that the partial per diem portion of the reimbursement is handled like a payroll item. Beginning July 1, 1991, the IRS began assessing penalties for non-compliance with their tax withholding regulations. Agencies will be subject to a penalty of $100 per occurrence for failure to withhold and errors on the forms.

In addition, IRS rulings could result in other costs. The Comptroller's Office estimates the new IRS withholding requirements could require the agency to audit and process about 7,000 additional vouchers per month. The additional state expense of the matching FICA may be as much as $300,000 per year in addition to the per diem. Agencies also estimate an additional one-time programming cost of $10,000 to $20,000 to change their systems.

Eliminating partial per diem will save the state an estimated $4.3 million per year based on the expenditures in fiscal year 1990, the ***Performance Review*** found.

The ***Performance Review*** recommends that the Travel Act be amended to prohibit paying partial per diem unless employees travel overnight. ■

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