MINUTES

CHANGE IN EMPLOYEE COMPENSATION COMMITTEE

DATE:	Wednesday, January 04, 2023
TIME:	9:00 A.M.
PLACE:	Room EW20
MEMBERS PRESENT:	Senators Co-chairman Cook, Guthrie, Burtenshaw, Carlson, Ward-Engelking
	Representatives Co-chairman Bundy, Holtzclaw, Kingsley, Wheeler, Gannon
ABSENT/ EXCUSED:	None

Co-Chairman Cook called the meeting to order at 9:00 a.m.

Christine Otto, Principal Budget & Policy Analyst, Legislative Services Office, gave an overview of the Change in Employee Compensation (CEC) process. First, the Division of Human Resources (DHR) gives a recommendation to both the Legislature and the Governor. The Governor will give his recommendation at his annual State of Address. CEC will meet and then give a recommendation to the Legislature through either a resolution or through a report to the Joint Finance - Appropriations Committee (JFAC). JFAC then sets the statewide CEC and it will be included in each agency's appropriation bill. The state of Idaho workforce currently employs 24,227 people which include classified and non-classified positions. Classified is subject to provisions, merit, promotion, etc., Title 67, Chapter 53, Idaho Code, while non-classified positions, Section 59-1603, Idaho Code, conform with classified positions if possible.

Ms. Otto reviewed the philosophy of CEC and the importance of competitive salary and benefits package, which is in statute in Section 67-5309A(1), Idaho Code. This section was added in 2006 and has not been amended since. Section 67-5309A(2) goes over the foundations of the benefits based on merit and performance. Section 67-5309A(3) goes over maintaining market competitiveness despite budgetary constraints.

Representative Wheeler asked if an employee does not perform well if this is a mechanism to decrease pay. **Ms. Otto** replied that if an employee is not performing well, the agency has the ability to decrease pay at its discretion.

Ms. Otto went over the four minimum considerations for a committee recommendation, which consisted of the market related changes or the salary structure; specific occupational inequities, which are also known as pay line exceptions; merit increases; and the benefits package. In Fiscal Year (FY) 2023, there was a 3% pay increase across the board due to salary structure shift, which was fully funded by the legislature. The salary structure has points in each pay grade level, with a minimum, a policy, and a maximum pay range. Pay line exceptions address specific employee retention or recruitment challenges and there are currently twenty-eight. **Ms. Otto** presented a 10-year history of the percent change in CEC.

Senator Guthrie stated that the report does not include the salary savings.

Ms. Otto said she could give actual amount at a later time and further explained that salary savings is money that the agencies have left over after attrition, and that the additional money at the end of the year may be used for merit increases and vacation payouts, etc.

Co-Chairman Bundy commented that on page 43-45 in the Division of Human Resources report there is more information on salary savings.

Ms. Otto added that the CEC average salary increase was 2.88% over ten years. In FY 2023, the Legislature also funded an additional $1.25 an hour, which equaled 7.8% on average, for each authorized FTP to be distributed on merit. **Ms. Otto** gave an overview of the Employee Benefit Package, which includes health insurance with various plan types, along with the Public Employee Retirement System of Idaho (PERSI) and has different contribution rates for the employer and employee. She went over sick, vacation, and compensation pay, which is included in annual salary, as are the eleven paid holidays. Employees also have the options of a 401k and a 457 plan at no cost to the employer.

Senator Carlson asked if Ms. Otto knows the overall costs per employee.

Ms. Otto said $12,500 on the employer's side for health insurance and variable benefit costs depend on agency. The average benefits cost per employee is around 21-22% of an employee's salary but it varies by agency.

Senator Carlson asked that with the additional $1.25 an hour, if that was why agencies have different percentage increase for CEC.

Ms. Otto confirmed that was the reason.

Senator Guthrie asked if the $12,500 is pulled from reserve funds.

Ms. Otto stated that amount does not include any money from reserves.

Representative Wheeler asked for clarification about the pay scale and if the maximum moves up with the 3% increase.

Ms. Otto replied in the affirmative.

Representative Wheeler asked what the concern about salary savings was and does the agency not hire more or disincentivizes the agency.

Ms. Otto said that salary savings varies by agency and that it can give agencies flexibility.

Co-Chairman Cook stated that more questions can be asked directly to the agencies later.

Erin Phipps, Revenue Analyst, Legislative Services Office, stated that to determine if Idaho is heading towards an economic slowdown there are five measures that are relevant to Idaho and Idahoans. First is Gross Domestic Product (GDP). When there are two consecutive quarters of falling real GDP growth that can indicate a slowdown. The next indicator **Ms. Phipps** gave was inflation, and explained the CPI (consumer price index) tracks those changes over time. She said that starting in 2021, CPI began growing and the average rate for 2022 through November was 7.9%. Factors include increased transportation costs, increased costs of production, and wage-price inflation which is when pay is raised to compensate the rising costs of living.

Ms. Phipps explained that the CPI numbers on the graph are a unit of cost measurement of a group of common goods that began in the year 1982. **Ms. Phipps** continued with information on the Federal Bank and interest rates. She presented the mortgage interest rates and the Idaho median house valuation, explaining that as interest rates rise, it will cost more to buy a home. The housing market accounts for more than 13% of the Idaho economy. **Ms. Phipps** stated that loans to start small businesses have increased rates so it may be harder for small businesses to grow which can then cause a contraction in GDP. Compared to the rest of the country, Idaho income kept up with per capita growth.

Ms. Phipps clarified that Idaho is growing at a faster rate than the national rate. She explained that Idaho unemployment rates have recovered from the pandemic and have sat below the national average since 2018. This means real personal income is keeping up, there is low unemployment along with record revenues and fund balances. Idaho has come in first in the Federal Funds Information for States reports and has been in the top ten for the last few years and Idaho looks good for the long term. If a recession were to occur, it would not be as severe as the Great Recession for Idaho.

Representative Gannon asked for the regional inflation rate for the western region.

Ms. Phipps stated that the western region has higher than the national average in inflation and had a sharp dip in CPI.

Senator Carlson asked if Ms. Phipps had included people who are moving here and retiring without an income.

Ms. Phipps stated that she does not have that information, but the Division of Financial Management is working on that.

Senator Carlson restated that Idaho doesn't know how much money or not people moving here are bringing into the state.

Ms. Phipps said that there is a possibility to calculate that revenue, but we are not looking at people individually.

Senator Guthrie gave his opinion about federal rates and how the federal money has inflated the economy so much. He asked when the Idaho economy could see a state of equilibrium.

Ms. Phipps replied that there were record revenues in the past couple years partially due to federal funds in the economy, but she has seen things slowdown in FY 2023 and seen cuts in income taxes. However, though there is slowdown in impact on state revenues but there are spending deadlines that are coming up, and so the impact of onetime federal funds may not have run its course.

Representative Wheeler asked if it possible to measure how much has not been disbursed by using saving rates.

Ms. Phipps replied that personal saving rate information specific to each COVID relief package is available and that she would it send out to the committee.

Keith Bybee, Division Manager BPA, LSO started his presentation on the update for the State Budget to go over the FY 2022 budget, the FY 2023 budget, and how well Idaho is prepared to handle downturn. He started with FY 2022, explaining that the state started the fiscal year with nearly a billion dollars in cash, and saw record revenues. Revenues came in at $6.2 billion, which means two consecutive years of 20% plus growth. Idaho ended up with $5.7 billion revenue to spend down in FY 2022. After JFAC and the Legislature took action, a budget was set for FY 2022 of $4.4 billion with an unspent appropriation amount of $15.4 million.

Mr. Bybee explained that the $15.4 million in authorized carryover at the end of that year was unusual because the Legislature approved several supplementals to spend down the revenue. Agencies were given carryover permission to use in FY 2023. Executive carryforward, moneys encumbered for specific projects, was historically treated as already expended, but now with the new statute, funds will show expended in the year expended. On Line 14, **Mr. Bybee** continued to explain $4.33 billion in expenditures, which is 13.3% more spent than in FY 2021 when there was a budget cut of 5% which forced budget cuts and agencies to put moneys in reserve. He concluded that the state ended with a budget surplus with $500 million more than the state started with.

Co-Chairman Bundy asked if the 5% holdback was based on projected revenue drops.

Mr. Bybee confirmed that was correct as it was thought revenues would not be able to keep up.

Mr. Bybee confirmed it was a strategic decision to balance the budget and manage resources. **Mr. Bybee** explained that starting FY 2023 with a $1.1 billion surplus, the Governor called an extraordinary session where a tax rebate was implemented, which spent down $500 million of the $1.1 billion surplus.

Co-Chairman Bundy asked if the tax rebates could show an increase in the personal savings rate.

Mr. Bybee responded that the impact of the tax rebates could be looked into, but credit card spending has gone up and savings have gone down nationally.

Senator Guthrie stated he doesn't see the $410 million for education from House Bill 1.

Mr. Bybee replied that the $410 million for education from House Bill 1 won't show in the budget until FY 2024 when the Governor's Recommendation is released on January 9. **Mr. Bybee** continued to explain the Legislature took the step to spend down the surplus by giving a tax rebate as seen on Line 5. The August forecast of $5.18 billion was revised up another $904 million to almost $6.1 billion which is on Line 6 and is the Division of Financial Management revised forecast. The new holding rates went into effect January 3, 2023, so we have $5.9 billion available to spend this session due to onetime spending programs, and unanticipated tax revenues. That leaves a projected balance of $1.5 billion, leaving more than a $1.3 billion surplus.

Senator Ward-Engelking asked how much of the balance is onetime and not ongoing.

Mr. Bybee said that the revenue forecast of $6.08 billion seen on Line 6 is historically treated as ongoing, but the report may suggest that part of the balance is one time because in 2018, US Congress' Tax Cuts and Jobs Act changed what is treated as taxable income, capped the amount of taxable income, and changed how pass-through entities can take on tax liabilities. He explained that last year, corporate revenue went to over $1.03 billion from $220 million to $350 million on average. These last two months, refunds started to pick up so there is some onetime money built into that revenue stream.

Mr. Bybee explained what the major reserve cash balances were in 2009 as it was when Idaho started feeling the effects of the Great Recession. There was a 23% revenue drop in 2009 and it took about two years to recover. At that time the state had 21.7% of cash to use to weather the recession and the Legislature took three years to spend down the cash balance and reserves. The beginning cash balance of $912 million, $850 million in Budget Stabilization Fund, $204 million in the Public Education Stabilization Fund, with other emergency funds totaling $144 million dollars so Idaho has a total of $2.4 billion in reserve funds which is 46% of FY 2023. Idaho is well prepared to weather a recession.

Mr. Bybee explained the General Fund revenue collections from FY 2016 to FY 2020. FY 2021 and FY 2022 were left out of the average annual growth rate due to being anomalies. The average growth rate was 5.7%. This average growth rate is much lower than the forecast rate for FY 2023 which can be considered the worst case scenario, where the state would see greater revenue drop than the Great Recession. The top two lines are the DFM forecast with revenue reduction in FY 2023 and 2024 with a rebound in FY 2025. The state is doing a good job of maintaining budgets and having structural balance.

Senator Guthrie asked in 2021 and 2022, how much of the budget revenue does Mr. Bybee think was federal money.

Mr. Bybee replied that with stimulus payments and payments to local governments impacting tax revenue, Idaho saw tremendous growth on the personal and corporate income tax, which means there is big growth in personal income. Sales tax has increased but not as much as income tax. He concluded that the federal amount was less than $300 million in 2021.

Lori Wolff, Administrator, Division of Human Resources (DHR), started her presentation about attracting talent and retaining good employees. She went over the report that DHR publishes every year and how it has very detailed information then gave an overview of the State Employee Compensation Statute Section 67-5309A, Idaho Code. **Ms. Wolff** stated that the results of the compensation study that was completed last year should give a path forward. However, using all the recommendations at once from the study is not affordable, so **Ms. Wolff** said she has a 2-year recommendation to show how to fund the increase to employee compensation. Her 2-year recommendation includes an 8.5% [core structure] increase for all state employees, a 10% increase for law enforcement positions, and a 14% increase for IT/engineering and nursing/healthcare to retain and attract employees. She recommended for FY 2024, a 4% merit increase for all state employees, an additional 6% salary adjustment for law enforcement positions, which would be a total of 10% for those classifications. She also recommends a shift in the salary structure. The total cost to implement the recommendation for FY 2024 would be just over $53 million in from the General Fund, and this estimate does not include public schools. She said that the Division of Human Resources recommends pay-line exceptions continue this year and then be eliminated the following year and the state would maintain the current benefits package.

Ms. Wolff continued with the second year recommendation for FY 2025, which would be a request for a 4.5% merit increase and an additional 5.5% for healthcare, IT, and engineering positions, which would improve competitiveness of the pay structure with the current labor market.

Ms. Wolff explained the state workforce is the largest in the state with 24,227 employees that serve in a variety of positions and fill some of the most critical jobs and with the current labor market, and it has been challenging to keep positions filled. The demographic of the national workforce has a median age of 42 years for the 2020-2021 year. Of the State's workforce, it is 45 years with 20% set to retire in the next 9 years without enough people to fill those positions. Idaho saw the highest turnover in the last year than in any of the last 15 years, which was almost 25% in one year with the highest turnover in nurses, labor and trades, and crafts. Many of those had more than ten years of service and still chose to leave. **Ms. Wolff** emphasized that it costs less to onboard and train entry level position than higher level positions. She touched on the low Idaho employment rates, with Idaho being one of top three states creating jobs, however, high inflation still a challenge. She explained that current market lag results in difficulty in filling positions and retention with there being two jobs per one job seeker. Idaho has 2,500 unfilled state jobs, which is a 12% vacancy rate which has been trending for two years.

Co-Chairman Cook asked what the vacancy rate was before COVID hit.

Ms. Wolff replied that at the Department of Health and Welfare, it was typically at 7% while smaller agencies had about a 5% rate. Presently, social workers have experienced as high as 17% unemployment.

Ms. Wolff explained that it currently takes about 57 days to fill a job and that hiring process needs to be streamlined. She stated hired a recruiting manager was hired to evaluate job requirements, substituting experience for education, and are improving flexibility with work schedules. Also, there is focus on better training and apprenticeships to fill critical jobs, so improvements have been since summer, and agencies were able to hire more staff and there was less staff leaving.

Ms. Wolff explained that externally, agencies have received more applications as the economy has softened, internally improved the application process, relooked at minimum qualifications to see what is actually needed, and had a big lift in social media campaigns so agencies are able to fill jobs better.

Ms. Wolff continued with the top things that mattered to employees outside of compensation along with reasons why people leave jobs such as burnout, lack of appreciation, work-life balance, and poor management. Thanks to the Legislature, the Division of Human Resources was able to do an employee engagement survey last year to see what motivates state employees. She said that employers want high engagement scores as employees are more likely to stay and work harder. **Ms. Wolff** gave the top results which were employee engagement, employees have what they need to do their job, manager effectiveness with the highest score of 71% and there was 74% response rate to the survey. Engagement rates vary on length of tenure with 65% being the average, with those having the highest scores having the shortest length of employment. She concluded that the survey shows that agencies should focus on compensation and recognition, implementing better systems and tools, and helping employees feel connected.

Ms. Wolff stated that the main objective of the presentation is compensation. Low pay was a major reason for employees leaving in 2022. She referred to state statute [Section 67-5309(A), Idaho Code] about the state needing to be competitive with relevant labor markets and that if it is not, then employees have reason to look for other positions. The results of CEC and the Legislature decision to increase compensation of 3% along with a $1.25 merit increase last year showed that lower pay rates received a higher percentage rate of pay increase and it had a positive impact such as being able to afford housing. However, compensation has not kept up with the market or inflation. Total compensation for state employees is all forms of compensation and benefits and on average, the state contributes more than 40% of an employee's salary to benefits.

Ms. Wolff explained the annual salary surveys, which compares Idaho salary midpoints, showed that despite the aggressive CEC last year, Idaho still lost ground in market competitiveness. On average, total compensation is 15% below market of the private sector and 9% below market of the public sector. When only comparing salary, compensation would be 26% below the private sector and 8% below the public sector. When comparing only benefits, compensation is about 6% below public sector counterparts. She referred to page 14 of the DHR report to show that certain expenses and out-of-pocket costs employees pay compared to what other counties and cities pay. Furthermore, the survey shows the higher the paygrade, the bigger the discrepancy with the lower pay grades lagging behind at 6% and the higher pay grades at 15%. **Ms. Wolff** clarified that when conducting surveys regarding Idaho's market position, 10% discount is automatically given to the cost of living for Idaho when comparing to other states.

Senator Ward-Engelking asked with the cost of living currently being very similar, at least in the Treasure Valley, to other areas in the Pacific Northwest if the 10% adjustment to cost of living was still needed.

Ms. Wolff explained that the state of Idaho has employees living throughout the state and that this has been calculated this way for several years, so it is needed to maintain consistency.

Co-Chairman Cook asked where the 25th percentile goal for salary compensation come from.

Ms. Wolff answered that it is not in statute or rule, but it was a reasonable goal to have to when looking at the labor markets and when considering the cost of living, the benefits package, and the work. The 25th percentile would be competitive pay and a good way to compare other employers.

Senator Burtenshaw asked how the wages are figured with the compensation and if 40% of it was benefits.

Ms. Wolff replied in the affirmative and further explained that when talking total compensation, it is compared separately and then as a total package. She gave details on where our current compensation challenges lie, outlining the pay grades and that CEC changes within pay grades. Last year's CEC increase did have the negative effect of salary compression which occurs when new employees make more than existing employees, reports make similar to their supervisors, or individuals that make more than those with more responsibilities. The lower pay grades, G-H are actually above labor market rates, pay grades K-O are below the 20th percentile, and pay grades P-U are making less than the 10th percentile.

Senator Guthrie asked what Ms. Wolff is referring to when saying market rate.

Ms. Wolff replied that she is using the 25th percentile as market rate.

She explained the ongoing compensation and classification study which should be done this fiscal year with the goal to make meaningful changes to the salary and compensation structure to be competitive enough to fill positions.

Ms. Wolff summarized the recommendations to move the core salary structure to the 25th percentile and to implement three new salary structures specific to their job families of law enforcement, IT and engineering, and healthcare, or job markets to have better recommendations for compensation planning.

Senator Ward-Engelking asked if compensation will still be behind if following these recommendations in two years as the private market is also moving forward.

Ms. Wolff replied that all of this analysis is based off of current market conditions, and 8.5% would be best in one year but would be cost prohibitive.

Representative Gannon asked if the $35 million is for the 4% increase so would it then be $70 million for both years.

Ms. Wolff clarified that it would be $53 million including the additional 6% increase for law enforcement this year and that estimates still need to be done for the following year but the high level estimates to complete the second year implementation would be $65-70 million from the General Fund.

Representative Gannon asked if the 8.5%, would it be closer to $108 million.

Ms. Wolff answered that it would around $108 million. She concluded that the recommendation for the two year compensation was what was needed to need to stay competitive and that a single salary structure is not enough to stay competitive.

Senator Ward-Engelking commented about how frightening it is to see so many unfilled positions. One of her big concerns is seeing the 8% inflation and countering only with 4% CEC increase.

Ms. Wolff said it was a very challenging decision to focus on law enforcement positions due to the need and that there have been efforts within agencies to look at positions and promote equity, recruit, and to address pay.

Representative Gannon said he has the same concern about inflation and not keeping up with it and that costs such as utilities and rent are going up 40%. He stated that the recommendation feels like a pay cut.

Ms. Wolff stated that the police enforcement will be receiving the 6% in salary and up to 4% in merit increase.

Senator Guthrie said that salary savings should be in the report as it is not a small amount; it was $100 million the last time reported. He asked if last year's CEC had a significant effect on recruitment and retention.

Ms. Wolff said last year's CEC did have an impact on the employees and ability to recruit and the Division of Human Resources is hoping to see the turnover being reduced but it may not be enough.

Representative Wheeler asked how what matters to employees is measured.

Ms. Wolff said she only showed a high level of the results of the study and that the Governor is focused on agency leadership resulting in training courses and employee development so agencies can be in tune with cultures that will attract and retain employees.

Representative Wheeler asked that if 11% of state employees are fully remote how do employees stay engaged with their team.

Ms. Wolff replied that work schedule flexibility tended to bring up engagement scores and that call center type jobs can be done at home with the same type of results.

Co-Chairman Cook remarked that working remotely for the last three years, he noticed certain jobs work really well at home and that some individuals work really well in the office while others can at home but working from home puts a lot of weight on leadership.

Representative Guthrie stated the legislators represent the citizens of Idaho and that every citizen and business of Idaho is struggling with inflation and hiring issues, and it is not exclusive to the state. We obligate tax dollars and we have to remember that there are 1.8 million people out there as well.

Representative Gannon asked for the Employee Engagement report from page 40 of the Division of Human Resources report in its entirety as it does not include of state employees working two or more jobs.

Ms. Wolff said she would get that report to the committee.

Representative Gannon commented that the CEC committee should remember the over a billion dollar surplus and that the committee needs to do what it can to keep our employees whole.

ADJOURN: There being no further business to come before the committee, the meeting adjourned at 12:16 p.m.

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Senator Cook
Co-Chair

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Angela Haugh
Secretary

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Representative Bundy
Co-Chair