



Transmitted via e-mail

April 10, 2015

Mr. Michael Cohen, Director
California Department of Finance
State Capitol, Room 1145
Sacramento, CA 95814

Dear Mr. Cohen:

Final Report—Vacant Positions Audit

The Department of Finance, Office of State Audits and Evaluations, has completed its audit of state departments' compliance with vacant position requirements in accordance with Government Code section 12439 (code). The audit objectives were to assess the effectiveness of the code in determining the extent of compliance during the period July 1, 2012 through June 30, 2013.

The enclosed final report is for your information and use. The Administration indicated it plans to use the observations and recommendations to assist in developing statewide solutions and reforms.

We appreciate the assistance and cooperation of the various state departments. If you have any questions regarding this report, please contact me at (916) 322-2985.

Sincerely,

Original signed by:

Richard R. Sierra, CPA
Chief, Office of State Audits and Evaluations

Enclosure

cc: Ms. Marybel Batjer, Secretary, California Government Operations Agency
Mr. Richard Gillihan, Director, California Department of Human Resources
Honorable Betty T. Yee, State Controller

Audit Report

Vacant Positions Audit For the Period July 1, 2012 through June 30, 2013

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EXECUTIVE SUMMARY

In accordance with our oversight responsibilities, the Department of Finance (Finance), Office of State Audits and Evaluations, audited selected departments to determine compliance with Government Code section 12439 (code), which states in part, “any state position that is vacant for six consecutive monthly pay periods shall be abolished.” Our audit objectives were to assess the effectiveness of the code in determining the extent of compliance during the period July 1, 2012 through June 30, 2013. Specifically, we determined whether:

- Position transfers were made to circumvent code requirements.
- Vacant position reestablishments were properly authorized.
- Funds from abolished vacant positions were used for other purposes.

Our audit was limited to the above objectives and did not include an evaluation of the number of vacant positions abolished or savings achieved.

Results Summary

Widespread noncompliance with the code and circumvention of the vacant position requirements exists. Departments commonly misuse personnel transactions to circumvent the code and improperly maintain vacant positions that should otherwise be abolished. Although policies are in place for position reestablishment, departments are reluctant to use the existing processes because they are perceived as labor-intensive and lack assurance the requested positions will be approved. Additionally, there are no penalties or consequences for noncompliance. Further, departments are not required, nor do they track, the disposition of funds related to vacant positions. Moreover, departments’ accounting and administrative controls are ineffective in ensuring compliance with the code and preventing inappropriate or unjustified personnel transactions.

Due to widespread noncompliance, the code’s effectiveness is diminished and has resulted in a lack of overall budget transparency and accountability. Statewide improvements are necessary for departments to produce budgets that accurately reflect operational expenditures and positions. Our observations and recommendations are intended to promote more effective position control, accountability, and budget transparency.

BACKGROUND, SCOPE AND METHODOLOGY

BACKGROUND

The California budget process and numerous statutes require state departments to maintain control and accountability over their staffing resources. Recent media reports as well as prior audits have raised questions about whether state departments have misused their authority to maintain vacant positions, preserve funding, and take other actions inconsistent with state law.

California Government Code section 12439 (code) requires the State Controller's Office (Controller) to abolish positions that are vacant for six consecutive monthly pay periods, and specifies that departments are prohibited from executing personnel transactions for the purpose of circumventing the code.

The code identifies instances where vacant positions can be reestablished through the Department of Finance (Finance) and the Controller. The code authorizes Finance to reestablish a position for appropriate reasons, including instances where the position was abolished due to a hiring freeze, the classification is "hard-to-fill," or the department has "diligently attempted to fill" the position. Additionally, upon self-certification by departments, the Controller has the authority to reestablish certain vacant positions necessary for direct 24-hour care or for public health and safety.

Government Code Section 12439

(a) Any state position that is vacant for six consecutive monthly pay periods shall be abolished by the Controller on the following July 1.

(h) Departments shall not execute any personnel transactions for the purpose of circumventing the provisions of this section.

The code was established in 1983 with the intent to create general fund and special fund savings through the abolishment of vacant positions.¹ The code has been amended in recent years. The Legislature amended the code in July 2000 to shorten the vacancy period from nine months to six consecutive monthly pay periods within a fiscal year. The code was amended again in July 2002 to include positions that remained vacant for six consecutive months within one fiscal year or between two consecutive fiscal years.

In March 2002, the California State Auditor issued an audit report² highlighting the misuse of personnel transactions to circumvent the abolishment of vacant positions and the overall ineffectiveness of the law. The Legislative Analyst's Office³ (LAO) also performed an analysis of vacant positions in 2008, concluding significant vacancies still existed throughout all state departments despite the strict guidelines of the code. LAO recommended the law be abolished due to the significant increase in paperwork without the intended effect of reducing vacant positions, noting that in fiscal year 2006-07, only 1 of every 63 vacant positions was abolished. In order to reinforce the requirements of the code, the California Department of Human

¹ Assembly Office of Research

² <https://www.auditor.ca.gov/pdfs/reports/2001-110.pdf>

³ http://www.lao.ca.gov/analysis_2008/general_govt/gen_anl08002.aspx

Resources issued Personnel Management Liaisons Memorandum 2014-011⁴ in May 2014, requiring state agencies to comply with the code. Further, Finance annually issues Budget Letters providing administrative guidance relating to vacant positions and the reestablishment process.

SCOPE

In accordance with our oversight responsibilities, Finance's Office of State Audits and Evaluations audited ten state departments to assess the effectiveness of the code in determining the extent of compliance during the period July 1, 2012 through June 30, 2013. Our objectives were to determine whether:

- Position transfers were made to circumvent code requirements.
- Vacant position reestablishments were properly authorized.
- Funds from abolished vacant positions were used for other purposes.

Additionally, our report recommends improvements over the state's position control, including, but not limited to, accuracy and transparency measures to be taken, policies and procedures requiring development or revision, effectiveness of the law in accomplishing its objectives, and needed statutory or administrative changes.

Our audit was limited to the effectiveness of the code with respect to compliance and did not include an evaluation of the number of vacant positions abolished or savings achieved.

Departments' management is responsible for ensuring accurate position reporting and compliance with applicable laws, regulations, and administrative requirements.

METHODOLOGY

To determine whether departments were in compliance with the code governing the abolishment and reestablishment of vacant positions, we performed the following procedures:

- Reviewed the applicable statute, relevant department policies and procedures, audit reports, and other information significant to the audit objectives.
- Interviewed Controller and Finance staff to gain an understanding of their procedures for the review and reestablishment of abolished positions.
- Selected a sample of personnel transfers to determine if they were valid and properly supported.
- Selected a sample of positions retained through the Controller's correction of technical errors, departments' self-certifications, and Finance's reestablishment process, to determine if reestablishments were properly authorized and supported.
- Interviewed departmental budget staff and reviewed Schedule 10s (Summary of Fund Condition Statements) and Governor's Budgets to assess whether funds from vacant positions were used for other purposes.

In conducting our audit, we obtained an understanding of the departments' internal controls, including any information systems controls that we considered significant within the context of our audit objectives. We assessed whether those controls were properly designed and implemented. Any deficiencies in internal control that were identified during our audit and determined to be significant within the context of our audit objectives are included in this report.

⁴ <http://www.calhr.ca.gov/PML%20Library/2014011.pdf>

Except as discussed in the following paragraph, we conducted this audit in accordance with generally accepted government performance auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our observations and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our observations and conclusions based on our audit objectives.

Finance and the audited departments are part of the State of California's Executive Branch. As required by various statutes within the California Government Code, Finance performs certain management and accounting functions. Under generally accepted government performance auditing standards, performance of these activities creates an organizational impairment with respect to independence. However, Finance has developed and implemented sufficient safeguards to mitigate the organizational impairment so reliance can be placed on the work performed.

Widespread noncompliance with Government Code section 12439 (code) exists in the departments audited, diminishing the effectiveness of the code. Departments used personnel transactions to circumvent the code and maintain vacant positions that should otherwise be abolished. Although policies are in place for position reestablishment, departments are reluctant to use the existing processes because they are perceived as labor-intensive and lack assurance the requested positions will be approved. Further, departments are not required by the code, nor do they track, the disposition of funds associated with the vacant positions. Moreover, departments' accounting and administrative controls are ineffective in ensuring compliance with the code and preventing inappropriate or unjustified personnel transactions.

Our observations and recommendations are intended to promote more effective position control, accountability, and budget transparency. The results of our audit are based on our review of documentation, other information made available to us, and interviews with key staff.

Observation 1: Widespread Noncompliance with the Government Code Exists

Widespread noncompliance with the code exists in the departments audited, which diminishes the effectiveness of the code in eliminating vacant positions. Specifically, we tested 798 personnel transactions during the period July 1, 2012 through June 30, 2013. These transactions consisted of instances where individual employees were transferred among multiple positions at the departments audited. Of the 798 transactions, 463 (58 percent) lacked adequate justification or documentation to determine compliance or were found to be noncompliant.¹

The high rate of noncompliance prevents the state from effectively managing and controlling vacant positions. Several departments acknowledged using personnel transactions to routinely circumvent the code and maintain the vacant positions. Multiple factors led departments to use position transfers to avoid abolishing vacant positions. Based on our testing and interviews with department staff, we found the following primary causes for noncompliance with the code:

- Departments maintain vacant positions as a means to provide budget flexibility.
- The vacancy period is too short for completing hiring activities.
- The reestablishment process lacks clarity, assurance, and is labor-intensive.
- Specific criteria for the proper use of personnel transactions ("120" transactions) is lacking.
- Penalties for noncompliance do not exist.

¹ Testing of specific position transfers was based on a risk assessment to identify high risk transactions such as frequent transfers. Therefore, the test results may not be representative of the total population and should not be projected to the total population of position transfers.

Lack of Budget Transparency and Accountability

The original intent of the code was to provide savings from the abolishment of vacant positions. However, since the code was enacted 30 years ago, there have been substantial changes in the state economy and budget process. Recent downturns in the economic climate and corresponding budget deficits have altered departmental funding, requiring departments to enact substantial budget reductions. These reductions caused some departments' budgets to no longer align with actual expenditures or position authority.

To realign departments' budgets and increase budget transparency and accountability, the Department of Finance (Finance) issued Budget Letter 12-03 in March 2012. The Budget Letter eliminated budgeted salary savings and positions historically held vacant to support the departments' operational needs. Each department was directed to reallocate those funds to expenditure categories in which they were actually expended, simplifying position control and allowing departments to better align their budget plans with actual program operations.

Despite the Budget Letter requirements and intent, departments still maintain vacant positions to preserve funds and provide budget flexibility. Funds from vacant positions are available for departments to use at their discretion (within their overall budget authority).

Departments contend maintaining vacant positions is a viable tool to accomplish mission-critical projects quickly with limited funding. Another reason is fear of losing funding through unanticipated budget cuts. This practice diminishes position control and budget transparency and accountability.

Departments informed us that vacant position funds were generally used in the program in which the vacancy occurs, or for personnel or contract purposes to meet the overall program goals. They also asserted that funds from vacant positions often go unexpended. However, because departments are not required by the code, nor do they track the disposition of these funds, the assertions could not be confirmed.

Six-Month Vacancy Period is Not Sufficient

According to all departments audited, the code is frequently circumvented because the six-month vacancy period and hiring window are too short. State departments must adhere to strict guidelines relating to recruiting and hiring prospective employees. Many departments cited problems hiring within the required six-month period. Departments noted instances where they were unable to find qualified candidates, applicants failed lengthy background and security checks, and prospective candidates voluntarily removed themselves from consideration. These situations required departments to extend the hiring process beyond six months, and in many cases, the departments used improper position transactions as a means to preserve the positions. Although the code allows departments to request reestablishment of the positions, this process is not always preferred by their management as discussed below.

Finance Budget Letter 12-03

Finance Budget Letter 12-03 provided direction to departments to make necessary adjustments to accurately reflect budget expenditures and positions for a more transparent budget, specifically stating:

“Although dollars may be redistributed within state operations expenditure categories and positions may be reduced, this process will not result in a change to each department’s total state operations funding.”

Reestablishment Process Lacks Clarity, Assurance, and is Labor-Intensive

As discussed in the Background section, vacant positions can be reestablished through Finance and the State Controller's Office (Controller).

Finance's Reestablishment Process

We found most departments are hesitant to use the Finance reestablishment process. Specifically, for the fiscal year ending June 30, 2013, half the departments audited did not utilize this process, although positions were eligible for reestablishment. Eight departments stated that ambiguous language and uncertainty relating to the process are primary reasons for circumvention of the code.

The code provides multiple criteria that can serve as justification for the retention of vacant positions. Code section (b) states positions can be maintained if a classification is determined "hard to fill" or if the department "diligently attempted to fill" the position. However, departments stated these terms were subject to interpretation, leading to confusion and uncertainty as to what qualifies as "hard to fill" or "diligently attempted to fill." No additional guidance or explanation exists to further define the terminology or the documentation necessary to support the justification.

Department Requests for Finance Reestablishment

Government Code section 12439(b) authorizes Finance to reestablish vacant positions in instances where the position is "hard to fill" or if the department "diligently attempted to fill" the position.

Further, Budget Letter 14-17 states "departments should not assume that a position will be reestablished simply because it meets one of the [reestablishment] criteria."² This uncertainty, combined with the ambiguities in the code language, resulted in departments' reluctance to pursue compliance with this requirement. Instead, departments have chosen noncompliance out of convenience and to reduce the risk of permanently losing the positions.

Controller's Reestablishment Process

We found departments are more likely to seek vacant position reestablishment through the Controller's self-certification and technical correction processes. All ten departments audited sought reestablishment of vacant positions through these processes. The self-certification process allows departments to maintain vacant positions necessary for direct 24-hour care, services for public health and safety, or specific agricultural purposes. However, departments must request self-certification annually to maintain vacant positions that meet this criteria. Departments dedicate substantial resources on an annual basis to maintain positions that clearly relate to public health and safety.

Controller's Self-Certification Process

Government Code section 12439(c) authorizes the Controller to reestablish vacant positions in instances where positions are necessary for direct 24-hour care, involved in services for public health and safety, or specific agricultural purposes.

For example, one department submitted 450 self-certification requests to the Controller for the fiscal year ending June 30, 2013. While we did not review all of these requests, we were informed by the department that a majority related to health and safety positions.³ Since the

² http://www.dof.ca.gov/budgeting/budget_letters/documents/BL14-17.pdf

³ We reviewed a limited sample of the 450 requests, and verified the requests were related to public health/safety positions.

self-certification process is an annual process, all departments must seek self-certification every year for the same positions, which can be labor-intensive. The department noted it takes approximately 120 hours per year to process self-certification requests.

Departments are also unfamiliar with the self-certification process. As a result, some departments are inappropriately using personnel transactions (discussed below) to maintain vacant positions when the positions would most likely be reestablished through the self-certification process. For example, we identified numerous agricultural positions at one department and direct 24-hour care positions at another department that were inappropriately transferred between various vacant positions to preserve the vacancies. In both cases, the departments' staff were not aware the positions were eligible for reestablishment under the Controller's self-certification process.

Lack of Criteria for Personnel Position Transfers

Due to the lack of specific criteria relating to certain personnel transactions, departments are able to circumvent the code through the use of position transfers. To ensure positions are not vacant more than six months, departments transfer existing employees into vacant positions utilizing transaction codes "A02" or "120," giving the appearance of compliance. These transactions were performed to move an employee from an existing position into a vacant position, with no change in the employee's job duties or responsibilities, or other legitimate reason for the transfer. Departments regularly review their vacant positions and initiate "A02" or "120"

transactions as needed to retain the positions. Code section (h) states "Departments shall not execute any personnel transactions for the purpose of circumventing the provisions of this section."

Departments generally use transaction code "120" to maintain vacant positions (as opposed to the "A02" transaction code which was used infrequently). Currently, no established criteria or uniform procedures relating to the proper use of "120" transaction codes exists. For instance, departments are capable of entering "120" transactions into the Controller's system without any support or justification. Nine departments audited used the "120" and "A02" transaction codes to preserve their vacant positions. Departments often use nondescript justifications, such as "operational needs" or "transfer to meet workflow needs" to support these transfers. For example, we found several instances at a department where the same employee was transferred into multiple positions during our audit period based on "operational needs." The department was unable to provide adequate justification for these transfers, and noted these types of transfers were typically initiated to preserve the positions.

Most transactions reviewed also lacked sufficient documentation to support the transfer of an employee into a vacant position. For example, of the 118 position transfers tested at one department, 104 lacked supporting documentation (such as duty statements and organization charts). Several departments informed us that a lack of supporting documentation was often an indication the transfer was performed to circumvent or avoid compliance with the code.

Types of Position Transfers

"A02" Transaction – A change in position number related to agency or classification code change.

"120" Transaction – A change in position number not classified as an "A02" transaction, most commonly a change in reporting unit code or serial number.

Each department also had different interpretations for what constituted a position transfer. Several departments changed employees' position numbers, even if there were no changes to duty statements or funding sources. Examples include:

- An employee was transferred twice in one month, with no change in the employee's unit and no duty statements to support the transfer.
- One department has a practice of transferring the oldest vacant position numbers among units prior to filling vacant positions. For example, the department will move a vacant position nearing the six month period to a unit that can fill the position in exchange for a position that has been vacant a shorter period of time. No state policies or procedures exist regarding the practice of moving vacant positions within a department.

No Penalties for Noncompliance

The code relies on the departments to ensure compliance with its requirements. Specifically, accountability measures do not exist, except within the Financial Integrity and State Manager's Accountability Act (FISMA), which requires departments to self-report their compliance. All ten departments reported compliance in their most recent FISMA report; however, nine were found not to be in full compliance. There are no consequences or penalties if departments do not comply with code requirements. As further described in Observation 2, we found a general lack of commitment to comply with the code at the departments audited. In the absence of specific accountability measures, consequences or penalties, departments appear willing to circumvent the code to preserve positions.

Recommendations:

Effective policies and procedures are necessary for the Administration to properly manage positions and their respective costs. Because widespread noncompliance has diminished the code's effectiveness and resulted in a lack of overall budget transparency and accountability, statewide improvements are necessary for departments to produce budgets that accurately reflect operational expenditures and positions.

We provide the following options to achieve effective position control, budget transparency, and accountability.

Option 1: Abolish the Code and Consider Alternative Solutions

Consider abolishing the code. Because position control and monitoring are necessary to promote a transparent budget, the Administration should evaluate alternative statutory and/or administrative mechanisms to achieve these goals.

Additional reform, consistent with Budget Letter 12-03, is needed to address structural differences with departments' budgets and further promote budgets that properly align with operational needs. Reform should also include monitoring provisions and education so that unnecessary positions can be identified and abolished, and departments eliminate the practice of creating "salary savings" from vacant positions to redirect funds for other operational needs.

Option 2: Amend the Code and Strengthen Coordination and Oversight

Consider amending the code and implementing reforms to improve compliance and ensure effective resource management and budget transparency.

- A. Consider amending the code to:
 - Automatically reestablish vacant positions required for direct 24-hour care, services for public health and safety, and specific agricultural purposes, and remove the Controller’s annual certification requirement for these positions. Departments will still be held accountable for justifying resource requirements as part of the annual budget process.
 - Require departments to track and report on the disposition of funds related to vacant positions. This will improve budget transparency by creating a direct link between budgeted and actual expenditures.
 - Include penalties for noncompliance.
- B. Implement oversight procedures:
 - Review Finance Budget Letter 12-03 and continue to ensure budget plans are consistent with program operations.
 - Periodically review and take steps to ensure unneeded positions and positions vacant for six consecutive pay periods are abolished.
 - Seek reestablishment through the Controller or Finance for positions that are at risk of abolishment, but are necessary to retain.
 - Develop and implement policies and procedures to ensure personnel transactions are appropriate, adequately justified, and supported by relevant documentation. Additionally, ensure departments’ staff are aware of, and appropriately trained on, the established policies and procedures.
- C. Consider the following additional actions:
 - Evaluate whether to provide further guidance on what constitutes “hard to fill” or “diligently attempted to fill” positions, including specific documentation and justification requirements for reestablishment.
 - Determine the underlying causes for vacancies and develop solutions to department hiring problems.
 - Consider providing position control and related budget process training to departments’ human resource and budget staff.
 - Continue to notify departments via Budget Letters or other media that targeted audits may be conducted to verify compliance with the code.
- D. Continue efforts to streamline statewide hiring processes as part of the state’s ongoing civil service improvement project.
- E. Establish more specific criteria on the use of “120” transactions, including guidance on what constitutes a legitimate and justified transfer, and documentation requirements.

Observation 2: Ineffective Control Environment Hinders Compliance

A general lack of commitment to comply with the code has resulted in management override of controls. We observed a culture at some departments where circumvention of the code was commonplace and even encouraged by management. Specifically, we observed:

- Instances at two departments where e-mails were circulated instructing staff to transfer employees into vacant positions to avoid abolishment.

- Failure to implement policies and procedures requiring supporting documents for personnel transactions. At one department, 88 percent of the transactions tested did not contain required supporting documents (i.e. organizational charts, duty statements, and/or justification memos).
- Processing of personnel transactions where the supporting justifications were vague or generic.
- Inconsistent policies and procedures related to processing personnel transactions. For example, two departments do not have uniform request for personnel action (RPA) processes throughout their many field offices/units. One of the departments, for instance, does not have a standardized RPA process among the various field locations, resulting in inconsistencies in the level of oversight or justification required when filling a vacant position.

The State Administrative Manual (SAM) section 20050 requires state entity heads, by reason of their appointments, to be accountable for activities carried out in their agencies. This responsibility includes establishment and maintenance of internal accounting and administrative controls.

Further, FISMA requires each state agency to biennially report on the adequacy of their internal controls. As mentioned in Observation 1, included in the FISMA report is a discussion on compliance with vacant position abolishment, as required by code section (i). Although the ten departments audited reported compliance with the code in their FISMA reports for the period ending June 30, 2013, nine were found to not be in full compliance.

Since issuance of the May 2014 California Department of Human Resources' Personnel Management Liaisons Memorandum, six departments informed us they have strengthened internal controls with respect to management oversight of position transfers. Of these six departments, three stated they now require specific justification and documentation for "120" position transfers. However, because the departments developed these new procedures at the time of our audit, we were unable to confirm if the controls were implemented and operating as intended.

Recommendations:

These recommendations are intended to improve the culture and control environments at state departments relating to position control, and should be implemented regardless of the outcome of Observation 1.

- A. Establish an appropriate environment and culture where circumvention of the code or failure to implement statewide policies and procedures are not acceptable practices.
- B. Strengthen internal accounting systems and administrative controls by:
 - a. Implementing the recommendations noted in this report.
 - b. Requiring detailed justifications for personnel transactions.
 - c. Ensuring policies and procedures are consistent among all departmental field offices/units.
 - d. Ensuring established policies, procedures, and controls are implemented and operating as intended.
- C. Periodically re-assess and evaluate code compliance, and ensure the level of compliance is accurately reported in biennial FISMA reports.