Department of Legislative Services

Maryland General Assembly
2007 Session

FISCAL AND POLICY NOTE

House Bill 450 (Delegate Rosenberg, *et al.*)
Economic Matters

Procurement - Service Contracts - Employee Compensation Standards

This bill requires certain State service contracts to provide employee compensation (wages and benefits) that is at least equivalent to compensation that would be provided to State employees for performing the same or similar work. Failure to provide equivalent compensation would be deemed a material breach of the service contract.

Fiscal Summary

State Effect: By requiring nonexempt contracts to pay equivalent compensation and maintaining a $200,000 or 20% threshold for savings, the bill would likely preclude the State from reducing expenditures on nonexempt services that are currently contracted out to firms that provide lower compensation packages to their employees. The impact on expenditures could be significant. Revenues would not be affected.

Local Effect: None.

Small Business Effect: Potentially meaningful to the extent that the State decreases the number of service contracts with small businesses that do not provide comparable compensation to their employees.

Analysis

Bill Summary: The bill applies to service contracts that are not exempt from an existing preference in State law that State employees perform all State functions in State-operated facilities. The bill does not apply to contracts that are exempt from this preference, including emergency contracts and those for which State employees are not available.

Except for contracts with nonprofit organizations, nonexempt contracts have to provide employee compensation for each position that is at least equivalent to the employee compensation provided to a State employee who performs similar duties. In addition, the bill requires a contractor to offer available positions to qualified displaced State employees.

State agencies planning to solicit a nonexempt service contract must notify employees who may be affected by the contract of the nature of the work to be performed and of their rights as State employees at least 60 days before they issue a solicitation for a service contract. The agency must also include a comparison providing State employee equivalent compensation to contracted employees in their cost comparison analysis submitted to the Department of Budget and Management (DBM).

At least 15 days before certifying a service contract as nonexempt to the Board of Public Works (BPW), DBM must notify affected employees of its intention to certify the contract. Employees may then review and comment on the contract. After certifying the contract as nonexempt, DBM must notify affected employees of their rights to receive a free copy of the certification and the contract and comment on them before BPW.

DBM and the Department of General Services (DGS) are authorized to issue regulations to carry out the bill's provisions.

Current Law: Using State employees to perform all State functions in State-operated facilities is deemed preferable to contracting with the private sector to perform the same functions.

Exempt Service Contracts

Generally, service contracts that are exempt from this preference are those in which:

- the General Assembly has required or authorized the services to be performed by an independent contractor;
- State employees are not available to perform the necessary services;
- a conflict of interest would result if a State employee performed the services;
- the services require emergency appointments;
- the services are incidental to the purchase or lease of personal or real property; or
- a clear need exists to obtain an unbiased finding or opinion.

Nonexempt Service Contracts

DBM may certify to BPW a service contract that is not exempt only if:

- the agency seeking to enter into the contract has submitted necessary information related to consideration of alternatives, cost comparison, and a plan of assistance to State employees adversely affected by the service contract;
- DBM finds that economic advantage of entering into the contract outweigh the State employee preference stated above;
- the service contract does not adversely affect State affirmative action efforts;
- there are control mechanisms ensuring the services will be performed in accordance with the contract; and
- the service contract complies will the requirements of the State's general procurement law.

An agency that seeks to enter into a nonexempt service contract must show in a cost comparison analysis that the contract will save the State at least $200,000 or 20% of the value of the contract, whichever is less, over the contract's life. In addition, the agency has to show that it has taken formal and positive steps to consider alternatives to the service contract, including reorganization and reevaluation of service and performance. Finally, the agency is required to submit to DBM a formal plan of assistance for all State employees who will be adversely affected by the service contract.

There is no requirement that nonexempt contracts provide employee compensation that is equivalent to compensation provided to State employees for the same or similar services. In addition, there is also no requirement that affected State employees be notified in advance and be given an opportunity to review and comment on the contract.

Background:

Average State Personnel Management System Employee Compensation

The average annual wage of an employee in the State Personnel Management System is $44,464. For fiscal 2008, the Department of Legislative Services (DLS) estimates that the employer contribution rate for State employee fringe benefits is 17.91% of an employee's salary. In addition, DLS assumes a $10,650 annual contribution for health insurance, and $250 for a matching contribution to a deferred compensation plan. Based on the above assumptions, a State employee is directly compensated (on average) $63,328 for wages and benefits.

This estimate does not include indirect expenditures associated with holidays and leave benefits. DBM estimates that leave indirectly costs $6,498 per employee for personal leave (6 days), holiday leave (12 days), annual leave (15 days), and sick leave (5 days).

In total, the average State employee receives $69,826 in direct and indirect compensation annually.

Contract Requirements in Other States

DLS is aware of other states with employee compensation requirements for service contracts. In California, proposals to contract out work must not be approved solely on the basis that savings will result from lower contractor pay rates or benefits. Proposals to contract out work are eligible for approval if the contractor's wages are at the industry's level, and do not significantly undercut state pay rates.

In Massachusetts, every bid for a service contract where the services provided are substantially similar to a regular state employee in the contracting agency must establish the wage rate for each position. The wage rate cannot be less than the minimum wage rate as set by the contracting state agency. The minimum wage rate is the lesser of either step one of the grade under which the comparable regular agency employee is paid, or the average private-sector wage rate for the position as defined by the Executive Office of Administration and Finance. In addition the bid and contract must require the contractor to pay comparable health insurance costs (within one percentage point) for every employee employed for at least 20 hours under the contract. The contractor must submit quarterly payroll records to the agency.

Rhode Island requires that a contract to provide personnel to the state or the Rhode Island Public Transportation Authority must stipulate prescribed rates of wages as determined by the director of the state Department of Labor and Training. The rates of wages to be paid the employees under the contract or any subcontract must be based upon the prevailing rates for state employment.

State Fiscal Effect: The bill would make it more difficult for agencies to contract out certain services currently performed by State employees by requiring equivalent compensation and maintaining the $200,000 or 20% threshold for savings, resulting in a significant expenditure increase (all funds). To the extent that State agencies currently are able to reduce expenditures by contracting out services, such agencies would no longer realize these savings under the bill. For example, DGS has 88 nonexempt contracts. In one such contract involving 56 personnel, the hourly pay differential between what the contractor pays each employee and the State employee equivalent wage is $4.16 per hour. If the contractor were to pay his/her employees the State employee equivalent rate, the annual wage differential alone would be $484,557.

It is assumed that State agencies could implement the bill's employee notification provision within existing resources.

Additional Information

Prior Introductions: HB 1320 of 2006, a similar bill, was heard in the House Economic Matters Committee, but no further action was taken.

Cross File: None.

Information Source(s): Department of Budget and Management, Judiciary (Administrative Office of the Courts), Office of Administrative Hearings, Board of Public Works, Maryland Department of Transportation, Department of General Services, University System of Maryland, Department of Legislative Services

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