

BEFORE THE STATE PERSONNEL BOARD OF THE STATE OF CALIFORNIA

In the Matter of the Appeal by)	BOARD DECISION
)	
DEPARTMENT OF GENERAL SERVICES)	PSC No. 05-07
)	
from the Executive Officer's August 26, 2005)	
Disapproval of a Contract for Custodial)	
Services between the Department of General)	December 6, 2005
Services and American Building Maintenance)	
Janitorial Services.)	
)	

APPEARANCES: Anne M. Giese and Jay Dyer, Attorneys, on behalf of Service Employees International Union, Local 1000 (California State Employees' Association); Teresa Boren-Irwin, Senior Staff Counsel, on behalf of the Department of General Services.

BEFORE: William Elkins, President, Maeley Tom, Vice President; Ron Alvarado, Sean Harrigan and Anne Sheehan, Members.

DECISION

This matter is before the State Personnel Board (SPB or Board) after the Department of General Services (Department) appealed from the Executive Officer's April 22, 2005, decision, and August 26, 2005 supplemental decision, disapproving the contract (Contract) between the Department and American Building Maintenance Janitorial Services (ABM), to provide custodial services for the Franchise Tax Board (FTB). The matter was initially brought to the SPB after the Service Employees International Union, Local 1000 (California State Employees' Association) (CSEA), requested that the SPB review the Contract for compliance with the provisions of Government Code section 19130(a).

In this decision, the Board finds that the Contract is not justified as a cost-savings contract pursuant to the provisions of Government Code section 19130(a), because the Department failed to establish that sufficient cost savings would be realized under the terms of the Contract

BACKGROUND

By letter dated February 10, 2005, the Department notified the SPB that it intended to enter into a three-year cost-savings Contract under Government Code section 19130, subdivision (a), with ABM to provide custodial services for the FTB. The Department asserted that by contracting out the services over the three-year period with ABM, that the state would save \$2,272,465, well over the amount currently required to justify the Contract as a cost savings contract under Section 19130(a).

PROCEDURAL HISTORY

By letter dated March 25, 2005, SEIU Local 1000 (CSEA) asked SPB to review the proposed Contract for compliance with Section 19130(a). CSEA essentially maintained that the Contract was improper because civil service employees have traditionally performed the type of services contemplated under the Contract, and because the Department failed to establish that the Contract would result in cognizable cost savings to the State.

On April 22, 2005, after reviewing the respective submissions of the Department and CSEA, the Executive Officer notified the parties that he had concluded that the Department had not submitted sufficient information to show that the proposed Contract was justified under Section 19130(a). The Department

thereafter filed an appeal of that decision with the five-member State Personnel Board (Board), and a hearing on the matter was conducted on August 9, 2005.

After reviewing the written briefs and oral arguments presented by the parties, on August 9, 2005, the Board remanded the matter back to the Executive Officer with instructions to submit a Supplemental Decision that clarified the following issues: (1) What is the rationale and factual basis for the Executive Officer's determination that, based on past experience with similar contracts, state indirect costs would be five percent of civil service custodian's wages and benefits; and (2) What is the rationale and factual basis for the Executive Officer's determination that the cost to the state of continuing contract oversight would be two and one-half percent of the total cost of the Contract?

On September 6, 2005, the Executive Officer notified the parties that he had issued a Supplemental Decision that again found that the Contract was not justified pursuant to the provisions of Section 19130(a). The parties were thereafter afforded an opportunity to submit written briefs for the Board's review regarding the Executive Officer's Supplemental Decision. On September 22, 2005, the Board received the written briefs submitted by the parties regarding the Executive Officer's Supplemental Decision. On September 27, 2005, the Department filed an objection to CSEA's response, contending that the Board should not consider new evidence submitted in the response that had not previously been presented to the Board.

The Board has reviewed the entire record for this case, including the oral and written arguments submitted by the parties, and now issues the following decision.

ISSUE

The following issue is before the Board for review:

Is the Contract justified under Government Code section 19130, subdivision (a)?

DISCUSSION

In *Professional Engineers in California Government v. Department of Transportation*,¹ the California Supreme Court recognized that, emanating from Article VII of the California Constitution, is an implied “civil service mandate” that prohibits state agencies from contracting with private entities to perform work that the state has historically and customarily performed and can perform adequately and competently. Government Code section 19130 codifies the exceptions to the civil service mandate recognized in various court decisions. The purpose of SPB's review of contracts under Government Code section 19130 is to determine whether, consistent with Article VII and its implied civil service mandate, state work may legally be contracted to private entities or whether it must be performed by state employees.

The Department asserts that the Contract is justified under Government Code section 19130, subdivision (a), which authorizes a state agency to enter into a

¹ (1997) 15 Cal.4th 543, 547.

personal services contract with a private contractor under certain specified conditions.²

² Government Code section 19130(a) provides that: (a) Personal services contracting is permissible to achieve cost savings when all the following conditions are met:

(1) The contracting agency clearly demonstrates that the proposed contract will result in actual overall cost savings to the state, provided that:

(A) In comparing costs, there shall be included the state's additional cost of providing the same service as proposed by a contractor. These additional costs shall include the salaries and benefits of additional staff that would be needed and the cost of additional space, equipment, and materials needed to perform the function.

(B) In comparing costs, there shall not be included the state's indirect overhead costs unless these costs can be attributed solely to the function in question and would not exist if that function was not performed in state service. Indirect overhead costs shall mean the pro rata share of existing administrative salaries and benefits, rent, equipment costs, utilities, and materials.

(C) In comparing costs, there shall be included in the cost of a contractor providing a service any continuing state costs that would be directly associated with the contracted function. These continuing state costs shall include, but not be limited to, those for inspection, supervision, and monitoring.

(2) Proposals to contract out work shall not be approved solely on the basis that savings will result from lower contractor pay rates or benefits. Proposals to contract out work shall be eligible for approval if the contractor's wages are at the industry's level and do not significantly undercut state pay rates.

(3) The contract does not cause the displacement of civil service employees. The term "displacement" includes layoff, demotion, involuntary transfer to a new class, involuntary transfer to a new location requiring a change of residence, and time base reductions. Displacement does not include changes in shifts or days off, nor does it include reassignment to other positions within the same class and general location.

(4) The contract does not adversely affect the state's affirmative action efforts.

(5) The savings shall be large enough to ensure that they will not be eliminated by private sector and state cost fluctuations that could normally be expected during the contracting period.

(6) The amount of savings clearly justifies the size and duration of the contracting agreement.

(7) The contract is awarded through a publicized, competitive bidding process.

(8) The contract includes specific provisions pertaining to the qualifications of the staff that will perform the work under the contract, as well as assurance that the contractor's hiring practices meet applicable nondiscrimination, affirmative action standards.

(9) The potential for future economic risk to the state from potential contractor rate increases is minimal.

(10) The contract is with a firm. A "firm" means a corporation, partnership, nonprofit organization, or sole proprietorship.

(11) The potential economic advantage of contracting is not outweighed by the public's interest in having a particular function performed directly by state government.

In addition to the requirements of Section 19130(a), however, the Contract must also meet those requirements set forth in the implementing regulations adopted by the SPB.³ In order to ensure that a proposed contract achieves sufficient cost-savings to justify contracting under Section 19130(a), Title 2, California Code of Regulations, section 547.71 provides that:

- (a) Savings generated through cost-savings based personal services contracting must justify the size and duration of the contracting agreement. To do so, such contracts must meet one of the following criteria:
 - (1) Achieve a savings of 10% or more compared to the cost of performing the same function within the civil service over the duration of the contract; or
 - (2) Achieve a savings of at least \$50,000, in terms of 1988 dollars, per year compared to the cost of performing the same function within the civil service over the duration of the contract, provided that the savings equal at least 5% of the comparable civil service cost. The \$50,000 standard shall be adjusted at the beginning of each fiscal year to reflect changes in the California Consumer Price Index as reported by the Department of Industrial Relations, and the adjusted figure shall be communicated by Board staff to all departments.
- (b) Such savings need not be attained during each year of a multiyear contract, providing the overall savings meet one of the aforestated requirements.

On December 10, 2004, the Board issued a memorandum entitled “Justification of Cost-Savings Based Contracts” to provide state agencies with the annual update of the California Consumer Price Index (CPI) information required by Section 547.71, subdivision (a)(2). According to that memorandum, based upon

³ Title 2, Cal. Code Regs., §§ 547.59 and 547.69 – 547.71.

changes in the California CPI as reported by the Department of Industrial Relations, currently, a proposed contract must achieve a savings of at least \$80,100 per year in order to qualify as a cost savings contract under Section 19130(a). For a three-year contract such as the one at issue here, the total savings must, therefore, equal a minimum of \$240,300.

In the instant case, the Contract requires that ABM provide all of the custodial services and supplies necessary to clean FTB's existing facility and a new facility that FTB will be occupying. The total amount of the Contract over the three-year term is \$7,091,444.

The Department asserts that if the state utilized civil service employees to perform the custodial services, it would cost the state a total of \$9,363,909 over the Contract's three-year term. The total cost includes the following: \$7,052,458 for state civil service employee salaries and benefits; \$1,589,624 for indirect costs; and \$721,827 for supplies. As a result, the Department projects that by contracting out the services over the three-year period with ABM, the state will save \$2,272,465.

For its part, CSEA disputes the Department's calculations and asserts that it will actually cost the state \$788,203 more to contract with ABM rather than retain civil service employees to perform the contracted services. According to CSEA, additional costs of \$300,000 for oversight and \$300,000 for security monitoring must be added to the contracting costs for a total of \$7,691,444.⁴ CSEA asserts that if civil service employees performed the custodial services, it would cost the state only \$6,903,241 over the three-year period by decreasing the number of employees,

salaries and benefits required to perform the contemplated duties, and by eliminating indirect costs.

(State Indirect Overhead Costs)

The Department estimates that, if the state were to perform the contracted work utilizing state employees, it would incur indirect costs amounting to 22.54 percent of civil service custodians' wages and benefits, for a total of \$1,589,624. CSEA asserts that these indirect costs should be completely eliminated because the Department did not provide sufficient justification to support them.

Government Code Section 19130(a), subdivision (1)(B) states that:

In comparing costs, there shall not be included the state's indirect overhead costs unless these costs can be attributed solely to the function in question and would not exist if that function was not performed in state service. Indirect overhead costs shall mean the pro rata share of existing administrative salaries and benefits, rent, equipment costs, utilities, and materials. (Emphasis added.)

In its brief to the Board, the Department asserted that:

Pursuant to Government Code section 19130, subdivision (a), paragraph (1), subparagraph (B), the indirect costs calculated by the DGS were based upon wage and benefit total [sic] associated with custodian positions. [Citation.] *DGS has these costs whether or not we contract out janitorial [sic] and are attributed solely to the DGS custodial program.* (Underline emphasis in original. Italics emphasis added.)

During oral argument before the Board, the Department conceded that the indirect costs of the Contract would be the same whether the work was performed by

⁴ CSEA asserts, without providing supporting documentation, that it would cost the state \$300,000 to oversee and monitor the Contract over the three-year term, and that it would cost an additional \$300,000 to monitor ABM's staff to ensure the security of FTB's files and facilities.

civil service employees or private sector employees. Given that concession by the Department, the Board must necessarily conclude that the Department failed to submit sufficient information to substantiate that all the indirect costs that it asserts should be included if civil service employees performed the contracted for services, would not also exist if the custodial services were performed by non-civil service employees. Consequently, the Department failed to establish that the state would incur any additional indirect costs were the job duties in question performed by state civil service employees.

As a result of the foregoing, the \$1,589,624 in indirect costs that the Department associates as part of the \$9,363,909 in total costs that would be incurred if civil service employees performed the janitorial services in question must be disallowed. That brings the total cost of state civil service employees performing the janitorial services down to \$7,774,285. Based on this reduced figure, the state would still save \$682,841 by contracting out the janitorial services. Those savings are still significantly higher than the \$240,300 needed in savings to justify the Contract.

(State Employee Salary and Benefits Costs)

In determining the costs to the state of utilizing civil service employees to perform the contracted services, the Department estimates that the state would have to pay benefits totaling 48.56 percent of employees' salaries. In arriving at that figure, the Department included the cost of workers' compensation, industrial disability, and unemployment compensation benefits paid to state civil service employees. We agree with the Executive Officer that the Department erred when it

included the costs of workers' compensation, industrial disability and unemployment compensation benefits in calculating benefits costs, particularly as Title 2, California Code of Regulations, section 547.69 specifically provides that: "In no case shall a contractor's wages be more than 25% below the State's pay rate. Comparison of wages for this purpose shall not include the cost of benefits." (Emphasis added.) In addition, State Administrative Manual (SAM) section 8740 indicates that expenses such as workers' compensation and other insurance costs are not commonly considered "benefits" to the employee, but rather overhead to the employer.

Given the express requirements of Section 547.69, we concur with the Executive Officer that state employee benefit costs are more correctly calculated at 35.03 percent of the employees' salaries, as opposed to the 48.56 percent figure cited by the Department. That reduces the salaries and benefits costs for state civil service employees from \$7,052,458 to \$6,410,160. That, in turn, brings the total cost of state civil service employees performing janitorial services at FTB down from \$7,774,285 to \$7,131,987. Because the \$7,091,444 cost of the Contract is not \$240,300 lower than the cost of state civil service employees performing the Contract duties, it necessarily follows that the Contract is not justified as a cost savings contract under Section 19130(a).

(Continuing State Costs)

The Department did not include any costs to the state to administer the Contract. CSEA asserts that it will cost the state \$300,000 to oversee the contractor's performance over the Contract's three-year term. CSEA, however, provided insufficient information to establish an annual cost of \$100,000 to oversee

the Contract. On the other hand, we do not find credible the Department's contention that there would be no costs to administer the Contract, because those duties would be assumed by an existing Building Manager. As the Executive Officer correctly noted, oversight of such a significant contract certainly would assume more than a de minimis amount of the Building Manager's time.

Given the foregoing, we find that the Department failed to prove that the state would incur no additional costs in the oversight of the Contract. In light of our previous finding, however, that the Contract does not result in sufficient cost savings to be approved as a cost savings contract under Section 19130(a), we need not reach the issue of what is the actual amount of continuing state costs to monitor the Contract.

(Number of State Employees)

CSEA disputes the Department's estimate that 63 state employees would be required to perform the contracted services,⁵ and instead asserts that the state could save approximately \$900,000 by using fewer state workers. CSEA failed, however, to provide sufficient evidence to support its contention. The Board, therefore, agrees with the Executive Officer's determination that, given the Department's past experience in providing custodial services, the Department's determination as to the required number of state employees appears to be sound.

(Security Monitoring Costs)

CSEA next asserts that the state would incur \$300,000 to monitor the ABM's staff to ensure the security of FTB's files and facilities. Although the Department did

⁵ 58 Custodians, four Custodian Supervisor IIs, and one Custodian Supervisor III.

not include any cost for security monitoring of the contractor's staff, the Contract itself specifically identifies the security measures that ABM is required to follow. As a result, we find that CSEA has not provided sufficient information to show that additional security costs should be factored into the Contract cost.

(Displacement of Existing Employees)

The Department further maintains that the Contract will not require the lay-off of any existing civil service employees. Instead, the Department contends that existing civil service employees will be reassigned to different buildings in the same general area. CSEA claims that these reassignments should be deemed to be impermissible "displacements" under the law.

We again agree with the Executive Officer's determination that CSEA's position regarding the alleged "displacement" of civil service employees is not correct. Section 19130(a)(3) specifically declares that displacement, "does not include changes in shifts or days off, nor does it include reassignment to other positions within the same class and general location." Here, CSEA has provided no evidence to refute the Department's assertion that existing civil service employees would be reassigned, not laid-off, if the Contract is implemented. Consequently, CSEA has failed to present sufficient evidence to establish that implementation of the Contract will result in an impermissible displacement of existing civil service employees.

CONCLUSION

The Board finds the Contract is not justified as a cost savings contract under Government Code section 19130, subdivision (a). In order to be justified as a cost

savings contract, the disputed Contract must result in a minimum savings of \$240,300 over the three-year contract term. Here, however, the Department concedes that the State's indirect overhead costs for hiring state civil service employees to perform those duties contemplated under the Contract would be the same regardless of whether civil service employees or private sector employees performed those job duties. As a result, the \$1,589,624 in purported indirect cost savings initially included by the Department must be disallowed. That disallowance alone drops the purported cost savings from the Department's initial estimate of \$2,272,465 to \$682,481.

With respect to the Department's estimate of the cost to the state in civil service employee salary and benefits to perform those duties contemplated under the Contract, we find that the Department's estimate is too high, in that the Department improperly included in its calculation of benefits the cost of workers' compensation, industrial disability and unemployment compensation benefits that would be paid to civil service employees. As a result, we find that the correct number for civil service employee salary and benefits during the three-year Contract term would be \$6,410,160, not \$7,052,458 as estimated by the Department. Based on the above adjustments, the total cost of civil service employees performing the Contract duties would have been \$7,131,987. Given the \$7,091,444 Contract cost, the Department failed to establish that the State would save at least \$240,300 during the three year Contract term. Consequently, the Contract cannot be justified as a cost savings contract.

Finally, although the Department presented insufficient evidence to support its contention that the State would incur no continuing costs to monitor the Contract, neither did CSEA provide sufficient information to establish that the State would incur \$300,000 in continuing monitoring costs. Given our prior finding, however, that the Contract is not justified as a cost savings contract, we need not reach the issue of what continuing costs the State would reasonably incur in monitoring the Contract.

ORDER

The Board hereby disapproves of Contract No. 3078805, entered into between the Department of General Services and American Building Maintenance Janitorial Services for the provision of provide custodial services for the Franchise Tax Board, on the grounds that the Contract is not justified as a cost savings contract under Government Code section 19130, subdivision (a).

STATE PERSONNEL BOARD

William Elkins, President
Maeley Tom, Vice President
Ron Alvarado, Member
Sean Harrigan, Member
Anne Sheehan, Member

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I hereby certify that the State Personnel Board made and adopted the foregoing Decision and Order at its meeting on December 6, 2005.

Floyd Shimomura
Executive Officer
State Personnel Board