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May 16, 1997

Patrick J. Moynihan
General Manager
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Dear Mr. Moynihan:

On April 18th, this office received the Massachusetts Bay Transportation Authority's (MBTA) proposals to privatize the operation and maintenance of bus routes from the Charlestown and Quincy garages, respectively.

Pursuant to the requirements of Chapter 7, Sections 52-55, MGLs, the privatization law, and specifically Sections 54(4), (6), and (7), and Section 55(a), the State Auditor's Office hereby notifies the MBTA of its objection to the awarding of these contracts.

One general finding of our review is that the two proposals submitted by the MBTA contained major defects in cost saving estimates, lacked statutorily required information, and were so deficient as to preclude this office from conducting a full review as contemplated by the statute. Implicit in this office's ability to conduct a review within 30 days is the requirement that the in-house cost estimates (s.54[4]), the analysis of the contract cost (s.54[6]), and the overall submission must be accurate, complete, reliable, and reasonable. Proposals that fail to meet this threshold standard preclude this office from relying on the overall presentation. The MBTA's submissions fell well below this standard. Although an agency's submission might not be free of error, be complete, or be reasonable, these deficiencies should not dominate each aspect of the submission. This decision is reached following a full review, to the extent possible under the circumstances and conditions of the proposals, of all materials provided by the MBTA, including materials submitted prior to April 18th and materials provided subsequent to the initial April 18th package. This letter will cite the specific proposal deficiencies that were encountered during our review and, as a result of these deficiencies, the sections of the law with which the MBTA has failed to comply.

Specifically, this office objects to these two proposals due to the MBTA's failure to comply with each of the substantive requirements contained in Section 54(7) – namely, cost, quality, compliance with regulatory statutes, and compliance with the privatization law.

I. COST SAVINGS

Section 54(7)(iii) – Pursuant to this section, the agency must certify and demonstrate that a proposed contract will be less than the estimated cost of keeping the service in-house, taking into account all comparable types of cost.

Based on the presentation of the cost information supplied to this office, it was not demonstrated and cannot be determined whether the costs of contracting out this service will result in a cost savings. This is due to deficiencies in the accuracy, completeness, and reasonableness of the MBTA's submission. These items are as follows:

A. Accounting Deficiencies

1. Inaccurate Cost Estimate

On January 2, 1997, pursuant to MGL c.7, 54(4), the MBTA submitted to this office its purported in-house cost estimate for the privatization of each of five "bundles" it had put out to bid. Subsequently, the MBTA selected private bidders to perform services at the Charlestown/Fellsway and Quincy garages.

However, the cost estimates accompanying the MBTA's April 18, 1997 submission revealed that the in-house cost estimates provided in January contained significant flaws, flaws that the MBTA failed to notify this office about during the intervening 3 1/2 months. This failure necessitates a significant diversion of our effort from evaluating the accuracy, completeness and reasonableness of the MBTA's April 18, 1997 cost estimates to a reconciliation of the cost differences between the January and April cost estimates.

This finding is also deemed to be a violation of MGL c.7, s.54 (1), which contains the statutory requirement that the MBTA submit a "comprehensive written estimate," which, by implication, must be accurate and complete.

2. Inaccurate, Incomplete Analysis of Contract Cost

Section 54(6) of Chapter 7, MGL requires an agency to submit comprehensive written analysis of the contract cost based upon the designated bid, specifically including the costs of transition from public to private operation; of additional unemployment and retirement benefits, if any; and of monitoring and otherwise administering contract performance. Implicit in this requirement is the principle that the analysis will be reliable, complete, and reasonable. However, numerous findings in this report clearly demonstrate that the analysis was unreliable, incomplete, and unreasonable. Therefore, the MBTA's submission is in violation of Section 54(6) of Chapter 7. Additionally, the deficiencies in the contract

cost analysis as noted herein, further detract from the reliability of the MBTA's two submissions.

3. State Fuel Taxes

- a) The MBTA's determination of the cost savings resulting from the planned privatization of the two "bundles" "double-counted" the amount of Massachusetts fuel taxes accruing to the Commonwealth. In response to our inquiry, the MBTA conceded in writing that the cost savings attributable to the Charlestown/Fellsway "bundle" was overstated by \$2,520,973 and by \$771,818 for the Quincy "bundle."
- b) The MBTA's cost savings determination for both "bundles" includes a 3% inflation factor for state fuel taxes to be paid per gallon. Because the state diesel fuel tax is currently set at 21 cents per gallon and can only be changed by legislation, we inquired why the MBTA's computed cost savings included a fuel tax inflation factor. The MBTA had not responded to our inquiry as of the date of our determination.

4. Building and Maintenance

In response to our inquiry relative to how the "avoidable cost" percentages were determined for this function, the MBTA conceded in writing that the MBTA's computed cost savings were overstated by \$263,595 for the Charlestown/Fellsway "bundle" and by \$88,165 for the Quincy "bundle."

5. Personnel Wage Inflation

The MBTA's claimed cost savings is based, in part, on a contemplated annual wage increase of 3% for each of the affected employees that will be avoided due to the planned privatization. However, according to documents provided by the MBTA, certain employees such as Executives (Class O) would receive only a 1% increase. Our review found that a 3% savings was projected for these employees.

6. Transition Costs

- a) **Adjustments:** We were advised by the MBTA during our review that the following additional adjustments need to be made to its cost savings determinations:

	Bundles	
Consultant Costs	Charlestown/Fellsway	Quincy
Decreased savings	\$2,410	\$1,432
Legal Costs		
Decreased savings	\$2,239	-
Increased savings	-	\$586

- b) The MBTA's cost considerations applied to outside consultant costs do not accurately portray the impact of those costs to the MBTA's bus privatization initiative. Of the \$212,335 expended by the MBTA for consultants and \$11,748 for outside legal fees relative to the proposed bus privatization, only a small portion of those costs were deemed by the MBTA to pertain to the Charlestown/Fellsway and Quincy "bundles" presumably because those are the only "bundles" to be privatized.

The total consultant and legal costs associated with the privatization initiative must be borne by the two "bundles" to be privatized. Therefore, the MBTA's proposed privatization savings are further overstated by the combined difference of \$139,653 for consultants and \$7,733 for legal services under both "bundles."

Although the cost of some of these noted inaccuracies on the MBTA's determined privatization savings are not overly significant, they together with the other significant inaccuracies and the flawed January 2, 1997 cost-estimate detract from the reliance that can be placed on the MBTA's contract cost analysis. In addition, we do not believe that the MBTA's April 18, 1997 cost representations are otherwise accurate and complete for the following reasons:

B. Unreasonable Cost Savings Assumptions

1. Vehicle Maintenance Plan

According to the proposed contracts with ATC/Vancom and ATE/Ryder, "The bus operations contractors shall continue to use the Everett facility for certain heavy maintenance functions for the first two years of the Agreement, at a cost at or below that detailed in Attachment (8): Heavy Maintenance Pricing Sheet. After that time, individual agreements with the Everett facility operator, or other vendors, shall be negotiated by the Contractor. The Maintenance Plan submitted by a contractor must include the details of its maintenance program."

- a) Since there is no assurance that the contractors will continue to utilize the Everett facilities during the third, fourth, and fifth years to the same extent (if at all) as they are required during the first two contract years, the MBTA's projected cost savings of \$23.8 million (Charlestown) and \$6.9 million (Quincy) is highly questionable and further detracts from the reliability of the MBTA's projected cost savings.
- b) There is a lack of reasonable assurance that the level of heavy maintenance and repairs to be paid for by the contractors during the required first two service years will approximate the MBTA's estimate

thereof. Because the MBTA does not maintain bus repairs by garage, it based its projected cost savings on an estimate of how much of the total \$14.9 million budgeted for the Everett facility during fiscal year 1997 pertains to the Charlestown/Fellsway “bundle” (\$4.6 million) and to the Quincy “bundle” (\$1.3 million) for each of the first two years of the private bus service.

This further calls into question the MBTA’s projected cost savings of \$23.8 million for Charlestown and \$6.9 million for Quincy and detracts from the reliability of the MBTA’s projected cost savings.

2. Heavy Maintenance and Bodywork

The proposed contract for the Quincy “bundle” (only) stipulates that:

In the unlikely event that any structural integrity issues should arise (e.g., floors needing replacing, bulk heads needing replacing, frame cracks, etc.). Ryder/ATE will work with the MBTA to identify the most cost effective correction; however, the cost for such corrections would be in addition to the current contract amounts. (underscoring added)

Although these proposed contractual provisions specifically provide for the MBTA to absorb the cost of the structural repairs, we did not note any consideration given by the MBTA in its cost savings determination for the Quincy “bundle” for this contractual obligation.

3. Changes and Extra Work

The proposed contract with each of the two contractors provides for additional pay at contractually stipulated rates for non-scheduled service, as follows:

Our review of the documents provided by the MBTA clearly establishes that these contractors will be required to perform unscheduled services such as, Extra school service, First Night activities, Flower Show, Puerto Rico Festival, Head of the Charles Regatta, and the Boston Marathon.

Furthermore, emergency unscheduled service also must be performed by these contractors, as the need arises. According to the contractual provisions, payments to these contractors for such unscheduled and emergency services could exceed \$24.3 million and \$4.9 million for the respective Charlestown/Fellsway and Quincy “bundles.”

These nonscheduled bus services are a contractual requirement for events that are certain to arise over the five-year contract period, the payments for which are directly related to the privatization of the two “bundles.”

It is our opinion, therefore, that the totality of the bus services being contracted out must be evaluated in any decision either to retain such service in-house or to contract out. The scheduled and non-scheduled bus services are an integral part of the services to be provided by the contractors and, in our opinion, are not deemed to be severable for decision formulation.

Accordingly, although we expected to review the considerations accorded by the MBTA for the required non-scheduled bus services we did not note any data pertaining thereto in the documents provided to us. Instead, those documents were confined solely to the scheduled portion of the total bus services to be provided by the two contractors.

In view of the potential dollar magnitude of the payments for unscheduled service which could exceed \$24.3 million and \$4.9 million for the respective "bundles," we do not consider the MBTA's decision to confine its contracting out deliberations solely to scheduled bus service to be sound or otherwise indicative of the savings to be achieved by such privatization.

4. Projected Cost Savings

In our opinion, the charges estimated by the MBTA for each of the five years forecasted should have been based on an analysis of the actual experience for a representative period. Selecting a representative period requires the exercise of sound judgment to ensure the appropriateness and reasonableness of the forecasted charges.

Several of these charges, such as materials, supplies, and services, forecasted by the MBTA, were based "solely" on its budget established for the 12-month period July 1, 1996 through June 30, 1997. No data were shown to us to establish that actual cost experienced for the nine-month period ended March 31, 1997 (immediately preceding the MBTA's April 18, 1997 in-house cost savings estimate) or for prior years were indicative of the level of such costs to be incurred over the next five years. For example, "materials" cost savings were estimated at \$3.9 million over the five-year term for the Charlestown/Fellsway "bundle" and at \$1.1 million for the Quincy "bundle" based on 1997 budgeted amounts. In response to our inquiry as to the reason the 1997 budgeted amount for materials is three times greater than that experienced for the preceding year (FY 1996) for the Charlestown/Fellsway "bundle" and more than 2.5 times greater for the Quincy "bundle", we were told that:

Actual costs for materials, supplies and services are "mapped" to the appropriate account in the general ledger from the purchasing system. This mapping was imperfect for FY 96, particularly in charging specific areas within a directorate... For this reason, the

budget represents a more accurate depiction of anticipated spending for scheduled service by location.

Since we were not shown a similar correction for the preceding fiscal year 1996, there is no assurance that fiscal year 1997 “revised” amounts are reasonable, appropriate, and representative of the savings that are expected to be achieved by the privatization of the respective “bundles” over the next five years.

5. Rental Costs – State Transportation Building

The \$235,886 and \$62,287 costs savings applied by the MBTA to the respective Charlestown/Fellsway and Quincy “bundles” were based on a reduction of 27 indirect employees currently employed at the State Transportation Building. According to the MBTA, of the 103,314 square feet of space being rented of the State Transportation Building, 252 square feet pertains to each of the 410 MBTA employees at the facility. At an annual rental rate of \$24 per square foot this results in an average annual rate of \$6,048 per employee or \$163,287 applicable to the 27-employee reduction attributable to the privatization of the two “bundles”, of which \$44,430 and \$11,544 were prorated to the respective two “bundles” as the first-year cost savings.

The MBTA presented no data or other supporting documents showing that its rental payments to the lessor will be decreased as a result of the 27-employee reduction. In this respect, the MBTA’s revised in-house cost estimate of April 18, 1997 shows that only a 13-employee reduction will be made (11 due to Charlestown/Fellsway and 2 due to the Quincy privatization “bundles”) rather than the 27-employee figure the MBTA calculated as a savings.

Rental costs are customarily based on the number of square feet to be occupied and not on the numbers of employees; otherwise rental adjustments would need to be made as the level of employees fluctuate. Since there is no evidence presented to us that the MBTA’s rental payments will be decreased due to the 13-employee staff reduction, we consider the MBTA’s rental cost savings estimate to be inappropriate.

6. Overstated Vacancy Claims

In its computation of transition costs, the MBTA claims that 85% of the affected employees will become employed by the private contractors and that the remaining 15%, or approximately 97 positions from the two “bundles”, will be retained by the MBTA in positions that will be available at the time of transition from public to private.

To support this position the MBTA stated in a May 13th letter that there were currently 36 vacancies in the current staffing requirements for full-

time and part-time operators; that 9 drivers will be lost to attrition for each of the next three months, and that the 32 additional vacancies will be available as a result of additional retirees in August. The MBTA claims that the 32 employees will retire due to the prospect that a collective bargaining agreement that will be reached at some point after August, 1997 may require employees not already retired to assume a copayment on their health premiums which are presently covered at 100% for retirees. We find two flaws with this analysis:

- a) Earlier documentation provided to this office by the MBTA claimed that its attrition rate for operators is eight, without explanation, the MBTA now cites a rate of nine. Again, this inconsistency detracts from the reliance that can be placed on the MBTA's overall cost presentation and calls into question the number of positions that will become available.
- b) We find the MBTA's assumption that 32 employees will retire on the premise that future collective bargaining negotiations could potentially result in the employees' incurring a health insurance copayment to be both arbitrary and unsupported. The MBTA provides no data or basis for the employee count of 32, and secondly, the MBTA has sought such a copayment without success in prior negotiations according to documents reviewed by this office.

Therefore, the MBTA will potentially incur 32-35 additional layoffs as a result of its unreasonable vacancy claims. Based on the MBTA's calculations of unemployment costs per "laid-off" employee, layoffs of 32-35 employees will result in additional transition costs to the MBTA of approximately \$170,000.

7. Unreported Buy-Out Costs

According to a May 14, 1997 memorandum to this office, the MBTA is liable for the payment of accrued vacation time to any employee who "quits or is terminated."

However, the MBTA states that it did not account for these payments in its cost savings determination. Our position is that these payments are obligations known to the MBTA and should have been factored into the respective cost savings determinations. To not do so further detracts from the reliability of the MBTA's cost savings determinations.

8. Retirement Benefits

The MBTA's five-year cost savings estimated for each of the two "bundles" to be privatized did not provide for any pension payments for any of the 800 employees whose positions are to be eliminated. According to the MBTA, those employees who are "vested" in its pension plan may

displace another employee, less senior to themselves, whose position is not being terminated or if the terminated employee does not so do, then that employee is deemed to have left on his/her own volition and not from the privatization of their respective positions. In this respect, we saw no offer being made to the affected employees either offering them another comparable position within the MBTA or otherwise reassigning them to such positions.

In our opinion, the elimination of the approximate 800 positions clearly stems from the privatization of those positions and the termination of the employees' employment with the MBTA cannot reasonably be deemed to be a voluntary action initiated by those employees.

Accordingly, we believe that the MBTA's failure to consider the financial impact of the pension payments that will in all likelihood have to be made to those "vested" employees to be "laid-off," which we estimate could range to a high of \$32,000 for some employees, per year, for each of the years beginning with the year that the employee becomes eligible to receive pension payments, has a material adverse effect on the MBTA's estimated cost savings expected to be achieved by the privatization.

9. Other Post-Employment Benefits

A note accompanying the financial statements of the MBTA and its component units for the fiscal years ended June 30, 1996 and June 30, 1995, which were audited by an independent auditor, contains the following statement:

Other Post-Employment Benefits

The Authority pays 100% of pension, medical and other benefits to retired employees not eligible for membership in the retirement plans and pays 100% of life and medical insurance costs to retired employees. The Authority also pays health benefits and life and medical costs for employees who participate in an early retirement program. These benefits are expensed on a current (pay-as-you-go) basis. There are approximately 3,800 retired employees eligible to receive post-employment benefits at June 30, 1996. The cost of these benefits was approximately \$22,200,000 in fiscal 1996 and approximately \$21,400,000 in fiscal 1995.

Although, based on the independent audit, the cost to the MBTA is \$5,842 per eligible employee for the described benefits, no offset to estimated savings resulting from the proposed privatization was made by the MBTA. According to our calculations, there are 295 eligible affected employees at the Charlestown/Fellsway "bundle" and another 74 at the Quincy "bundle," for a respective potential liability of \$1.7 million and \$0.4

million, per “bundle” per year for each of the years beginning with the year that the employee becomes eligible for such benefits.

Similar to the MBTA’s failure to provide for pension payments, the MBTA’s failure to provide for Other Post-Employment Benefits has a further adverse effect on the MBTA’s estimated cost savings expected to be achieved by the privatization.

II. QUALITY OF SERVICE

Section 54 (7)(ii)-Pursuant to this section, the head of the agency must certify that the quality of the services to be provided by the designated bidder is likely to satisfy the quality requirements of the statement prepared pursuant to paragraph (1), and to equal or exceed the quality of services which could be provided by regular agency employees pursuant to paragraph (4):

A. Failure to Demonstrate Equal or Better Quality

Upon our request for performance data on the two selected contractors, the MBTA provided us with certain material, including reports generated by MBTA staff from site visits, reference checks conducted over the phone with entities that employ the selected contractors, and performance data contained in reports from certain communities that contract with the selected contractors.

In a memorandum submitted by the MBTA on May 12th, the MBTA stated that:

“The MBTA has done a number of things to verify that the quality of service provided by the contracts would meet or exceed current MBTA standards.”

As evidence, they cited below this statement the site visits, reference checks, and collection of performance data.

However, through information provided by the MBTA and information gathered by this office from conversations with officials in communities that currently contract with the selected contractors, it is clear to this office that the great majority, if not all, of the above-described evaluative material was gathered by the MBTA after it had selected the contractor, negotiated the contract, and submitted the two proposals to this office.

Whereas the submission contains the MBTA’s certification (and that of the Commissioner of Administration) that the quality of services will equal or exceed that currently provided, the post-gathering of this material is highly irregular and calls into question the veracity of the certification and representation made by the MBTA to this office.

In a May 14, memorandum, the MBTA stated that all four site visits were made between the period of April 29 and May 2, nearly two weeks after its submission

of April 18. While site visits may be an appropriate tool for transition planning, the MBTA's written statements cited them as tools used to evaluate the quality of the contractors. According to officials in two of the locations visited, performance data were turned over, for the first time, to MBTA officials during these visits. In fact, the performance data submitted to this office on May 12 were limited solely to the communities that were visited. In addition, the data were in some cases not even publicly available until mid-April, according to the entities who published the data.

Finally, each reference check (8 out of 8) which this office verified during the period of May 13-15 indicated that the MBTA's reference checks had been conducted within the past 2-4 weeks, again after the April 18 certified submission.

The effect of this information is to call into serious question the integrity and completeness of the MBTA's quality comparison between current and projected service. While the MBTA possesses information concerning the experience of the selected contractor's top officials, the communities where the vendors held contracts, the fiscal statements of the contractors, and each contractors' proposal relative to providing quality services, this information does not allow for a substantive quantitative comparison between the MBTA's current service and the contractors' projected service, and, in fact, the MBTA submitted no such comparison to this office.

B. INCENTIVE PAYMENTS

Proposals for the privatization of fixed bus route services for both the Charlestown/Fellsway "bundle" and the Quincy "bundle" would provide quarterly incentive payments to the contract service providers for service levels at or below current MBTA performance. Specifically, the contract service providers would receive annual incentive payments equal to 800 bus service hours if 99.75% of all scheduled trips are completed (no incentive payments will be made during the first six months of contract for the Charlestown/Fellsway "bundle" or during the 12-twelve months of contract for the Quincy "bundle"). According to the MBTA's Management reports for the period of January 1996 – March 1997, the MBTA presently completes more than 99.75% of all scheduled trips within these service "bundles."

Massachusetts General Laws, Chapter 7, Section 54(ii) states:

the quality of the services to be provided by the designated bidder is likely to satisfy the quality requirements of the statement prepared pursuant to paragraph (1), and to equal or exceed the quality of services which could be provided by regular agency employees pursuant to paragraph (4);

The MBTA has incorporated into these proposals incentive clauses that allow the contract service providers to earn incentive-based credits though not exceeding or equaling established MBTA service standards. The provisions of the

Massachusetts General Laws, Chapter 7, Section 54, require the quality of services provided by a private contractor to equal to or exceed the level of service presently provided. If this statutory requirement had been satisfied by the MBTA, the contractors would not automatically be eligible for the awarding of this incentive.

- The proposed contractor for the Charlestown/Fellsway “bundle”, ATC/Vancom, would earn \$271,515 over the life of the contract by simply meeting the scheduled trip completion standard currently met by the public provider of this service at the affected “bundles.”
- The proposed contractor for the Quincy “bundle”, Ryder/ATE, would earn \$235,576 during the life of the contract by meeting the scheduled trip completion standard, which is currently met by the MBTA.

As presently constructed, this incentive earning indicator would result in additional payments in excess of \$0.5 million dollars to the two proposed contractors if they provide services at a level which is mandated by the provisions of the Massachusetts General Laws, Chapter 7, Section 54.

Accordingly, these costs should not be deemed as potential incentive earnings but must be included as part of the contract price.

C. LACK OF QUALITY STANDARDS

Although both parties certified to the statutory quality standard, no data were provided to us demonstrating that the quality of the proposed purchased services “. . . equal or exceed the quality of services” that are currently being provided by regular MBTA employees.

Furthermore, although both the proposed contracts with the two contractors provide for two differing incentive payments to them not to exceed \$3 million and \$2.9 million under one version and \$2.3 million and \$2 million under the other version for the respective Charlestown/Fellsway and Quincy “bundles,” not all the base line criteria are set forth in the proposed contracts. For example, the version contained in the body of the contract states:

- a. Customer Complaints: Complaints about the service and Contractor personnel will be recorded monthly directly by the MBTA through the customer service logs. Today, complaints vary significantly by service bundle, based upon the type of service offered. If the Contractor can decrease the number of customer complaints per month by 5%, it shall receive an incentive payment equal to one hundred (100) bus service hours. If the Contractor can decrease the number of customer complaints per month by 10%, it shall receive an incentive payment equal to one hundred twenty (120) bus service hours. If the number of complaints increases by 5 or 10%, the MBTA shall receive a credit of*

one hundred (100) or one hundred twenty (120) bus service hours, respectively. Penalties shall not be imposed during the first six months of the Agreement to allow for transition.

- b. *Mean Distance Between Mechanical Failures (MDBF): MDBF for buses today also vary based on the type of service the buses provide (Local urban v. highway express). If the Contract can increase the MDBF for its bus fleet by 10%, it shall receive an incentive payment equal to eighty (80) bus service hours. If said value decreases by 10%, the MBTA shall receive a credit of eighty (80) bus service hours. A “mechanical failure” shall be defined as any occasion when a mechanical failure (including a malfunctioning wheelchair lift and/or securement device) on a bus requires technical or supervisory assistance and significantly delays or eliminate a schedule run.*

The second incentive payment provision established in Exhibit I to the proposed contract states that appropriate targets will be established at a later date, as follows:

Benchmarking and Initiation Period

Starting with the Commencement of Service Data, all elements of this service quality program will be collected, analyzed and reported. During this initial six month period, no incentives or penalties will be assessed. The results of the first six-months will be used to develop appropriate target for each of the applicable areas. At each anniversary of the contract, the two parties shall in good faith revise these target levels to ensure both continued service quality and establish an appropriate track towards improving service beyond existing levels. After the initial six-month period, all provisions, incentives and penalties will apply as described in this Exhibit.

In the event that target levels cannot be identified in mutually acceptable manner prior to the anniversary of the contract, the resolution process described in Section 31.0 of the Contract will prevail.

Neither these incentive provisions nor the documents furnished to us identify the baseline from which to measure whether the contractor's service meets the incentive requirements or fall below the underfined baseline. Further, since no data were shown to us establishing the level and quality of the service currently provided by MBTA employees, there is no reasonable assurance that the quality of service to be provided by the contractors will equal or exceed the quality of service that is currently being provided as required by Chapter 296.

III. NONCOMPLIANCE WITH PRIVATIZATION STATUTE

Section 54(7)(i) of Chapter 7, MGL requires the agency to certify that it has complied with all provisions of Section 54 of the privatization law.

A. Contractor's Wage Rate

Section 54(2) of Chapter 7, MGL requires that:

(2) For each position in which a bidder will employ any person pursuant to the privatization contract and for which the duties are substantially similar to the duties performed by a regular employee or employees, the statement required by paragraph (1) shall include a statement of the minimum wage rate to be paid for said position... Every bid for a privatization contract and every privatization contract shall include provisions specifically establishing the wage rate for each such position, which shall not be less than said minimum wage rate as defined above. (underscoring added)

Neither of the two contracts include provisions specifically establishing the wage rate for each ... position in which the respective contractor will employ a MBTA employee pursuant to the privatization contract and for which the duties are substantially similar to the duties being performed by such employee. Accordingly, the proposed contracts are not in full compliance with Chapter 296 of the Acts of 1993.

IV. NONCOMPLIANCE WITH PUBLIC INTEREST REQUIREMENT

A. Liquidated Damages

Section(7)(v) of Chapter 7, MGL states:

No agency shall make any privatization contract and no such contract shall be valid unless the agency ... first complies with each of the following requirements:

.. (v) the proposed privatization contract is in the public interest, in that it meets the applicable quality and fiscal standards set forth herein.

The proposed contract for the privatization of the Charlestown/Fellsway "bundle" includes the following terms in the Termination Without Cause provision:

In the event that the MBTA terminates this Agreement without cause at any time, the MBTA shall pay to the contractor liquidated damages in the following amounts for the respective periods set forth below:

According to the contractual terms such payment can range from a high of \$740,000 during the initial stages of contract performance to less than \$50,000 during the latter stages. The contract further states that:

Such liquidated damages shall be deemed to be full compensation to the Contractor for any losses, costs, or expenses which it may suffer or incur as a result of such termination.

Because the proposed contract does not define the specific losses, costs, or expenses, we asked the MBTA for such definitions but were told that:

These figures (potential payment) are not an element of the "contract cost" under C.7, S. 54 (6), since they are not a component of the cost of performance under the designated bid (not would they be incurred in addition thereto), and are accordingly immaterial to the review contemplated MGL, C.7 S. 55.

We do not agree that the Liquidated Damages provision of the proposed contract whereby the contractor assesses damages against the MBTA is immaterial to our review.

In our opinion, any contractual provision that is not in the public interest is a matter within the purview of our mandated review of proposed privatization contracts.

Since the MBTA has not defined the "losses" to be paid for as liquidated damages, we relied on the contractor's position relative thereto, namely:

In the event the Contract is terminated without cause by MBTA, MBTA shall pay to the contractor all costs and expenses in connection with the cancellation ...as well as Contractor's projected profit as reflected in its Response to the RFP.

Considering that neither the proposed contract nor the MBTA has identified the nature of the "losses," there is no reason to believe that such "losses" are not for the "Contractor's projected profit" as it requested for contract inclusion.

In the absence of any data to the contrary, the payment for "projected profit" for services not performed is clearly not in the public interest and, accordingly, not in compliance with the referenced statutory provision.

V. NONCOMPLIANCE WITH REGULATORY STATUTES

Section 54(7)(iv) of Chapter 7 requires the agency to certify that:

The designated bidder and its supervisory employees, while in the employ of said designated bidder, have no adjudicated record of substantial or repeated willful noncompliance with any relevant federal or state regulatory statute including, but not limited to, statutes concerning labor relations, occupational safety and health, nondiscrimination and affirmative action, environmental protection and conflicts of interest.

Our position is that the MBTA failed to fully comply with the requirements of this provision. Specifically, we find the MBTA's documentation relative to each contractor's compliance with environmental protection statutes to be insufficient and nonresponsive to the requirements of the statute.

VI. UNION CONCESSIONS

Section 54(4) of Chapter 7, MGL states in part:

Any employee organization may, at any time before the final day for the agency to receive sealed bids pursuant to paragraph (1), propose amendments to any relevant collective bargaining agreement to which it is a party. Any such amendments shall take effect only if necessary to reduce the cost estimate pursuant to this paragraph below the contract cost pursuant to paragraph (6).

Pursuant to this provision, the employee organizations affected by the two submissions, collectively known as the Union Consortium (UC), submitted collective bargaining changes in a timely manner. The MBTA valued the UC concessions at approximately \$4 million, \$3 million for Charlestown/Fellsway and \$1 million for Quincy. The UC believes that the value of its concessions is approximately \$29.5 million.

As is explained in Section I of this report, we do not reach a determination of whether each "bundle" produces a cost savings. Therefore, we do not "factor in" the value of the UC concessions into the cost savings.

RECOMMENDATIONS:

"13c Liability"- Under federal transportation law, an agency can be liable for substantial severance costs to displaced workers. The affected unions and the MBTA disagree on the application of the so-called "13C" provisions and the matter is currently in binding arbitration.

Whereas the MBTA indemnifies both contractors from any potential "13C" liability as a result of this initiative, the MBTA is faced with a contingent liability that they estimate is between \$3 million and \$8 million over a five-year period. The union's position is that this liability could be many times more than the MBTA's estimates.

The Federal government, in a letter to the MBTA in October, 1996, stated that there was a "reasonable likelihood" of "13C" being applicable to this privatization initiative.

This office does not take an affirmative position on the application of this law, whereas it is a complex matter currently in arbitration and apparently a legal issue without clear precedent as to the particular facts of this initiative. In addition, we do not "factor in" "13C" costs into our determination that the MBTA has not demonstrated that these two submissions will result in a cost savings.

We do, however, strongly recommend that the MBTA resolve the full extent, if any, of its liability to affected MBTA employees, prior to privatization.

CONCLUSION:

Therefore, pursuant to Section 55(a) of Chapter 7, MGL, this office hereby notifies the MBTA of its objection to the awarding of this contract. In accordance with Section 55(d), this objection is final and binding on the MBTA, until such time as a revised certificate is submitted and approved by this office.

As always this office is available to discuss our findings and provide further assistance to the agency.

Sincerely,

A handwritten signature in black ink, reading "A. Joseph DeNucci". The signature is written in a cursive, flowing style with a large initial "A" and "D".

A. JOSEPH DeNUCCI
Auditor of the Commonwealth