

965 CMR: DEPARTMENT OF THE STATE AUDITOR

**PROPOSED REGULATIONS**

965 CMR 5.00: PRIVATIZATION CONTRACTS

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5.01: General Provisions

- (1) Authority. 965 CMR 5.00 is promulgated pursuant to M.G.L. c. 7, § 55(c).
- (2) Applicability. 965 CMR 5.00 is applicable to the Department of the State Auditor and to any Agency as defined by M.G.L. c. 7, § 53 and 965 CMR 5.02.
- (3) Scope. 965 CMR 5.00 shall govern the requirements for the privatization of state services pursuant to M.G.L. c. 7, §§ 52-55.

5.02: Definitions

As used in 965 CMR 5.00, unless the context otherwise requires, the terms set forth in 965 CMR 5.00 are defined as follows:

Avoidable Costs shall mean the net amount of expenses that the agency would be able to reduce if the agency were to privatize certain services.

Agency shall mean an executive office, department, division, board, commission, or other office or officer in the executive branch of the government of the Commonwealth of Massachusetts, the Massachusetts Bay Transportation Authority, the Massachusetts Turnpike Authority, the Massachusetts Department of Transportation, the Massachusetts Port Authority and the Woods Hole, Martha's Vineyard and Nantucket Steamship Authority.

Business Day shall mean any calendar day, excluding Saturdays, Sundays, and legal holidays.

Contract Projected Revenue shall mean the revenue associated with outsourcing the sale of goods or services to the private sector.

Cost Comparison shall mean a comparison of the total costs to the agency for performing the services in-house with the cost of the privatization contract. Where the contract is revenue based, Cost Comparison shall mean a comparison of the agency's Net Income from the In-House Cost Estimate to the Contract Projected Revenue.

Cost of Contract Performance shall mean all costs associated with purchasing a service from the private sector, including the contract administration costs, contract costs, and any unavoidable agency costs.

Department shall mean the Department of the State Auditor.

Dependent shall mean the spouse and children of an employee if they would qualify for dependent status under the Internal Revenue Code or for whom a support order has been or could be granted under M.G.L. c. 208, M.G.L. c. 209, or M.G.L. c. 209C.

Direct Costs shall mean costs that can be directly attributed to providing a service and that bear a direct relationship to the service.

Executive branch of the government of the Commonwealth of Massachusetts includes every entity that has been created by an act of the Legislature and is funded in whole or in part by the Legislature through general appropriations or supplemental appropriations acts, whether or not any such entity is within or subject to the control of an executive office, including without limitation all institutions of higher education.

Fully Allocated Cost shall mean the sum of all the direct costs that are attributable to performing a particular service in-house, as opposed to privatizing the service, and the indirect costs – i.e., agency overhead – that support the service.

Indirect Costs shall mean the costs that are not directly related to a product or service but are necessary for the agency to operate as a whole. Indirect costs include such costs as administrative and finance expenses, utilities and office space utilization.

In-House Cost Estimate shall mean the agency report that contains the agency's computations of the probable costs to the agency to produce a desired quality and quantity of services using agency resources in the most efficient method available to the agency.

In-House Revenue Projection shall mean the agency report that contains the agency's computations of the projected revenue earned by the agency for the services subject to the Privatization Contract.

Management Study shall mean an analytical evaluation of an organization or a service that an agency provides to determine whether the service can be provided more economically with no reduction in quality.

Net Income shall mean in-house revenue less avoidable costs.

Privatization Contract shall mean an agreement or combination or series of agreements by which a non-governmental person or entity agrees with an agency to provide services, valued at or above the Privatization Threshold Amount, which are substantially similar to and in lieu of, services theretofore provided, in whole or in part, by regular employees of the agency. Any subsequent agreement, including any agreement resulting from a rebidding of previously privatized service, or any agreement renewing or extending a privatization contract, shall not be considered a privatization contract. A contract for information technology services shall not be considered a privatization contract if an employee organization recognized under M.G.L. c. 150E as the exclusive representative of an affected employee, as determined by the Secretary of Administration and Finance, agrees to the terms of the contract in writing. An agreement solely to provide legal, management consulting, planning, engineering, or design services shall not be considered a privatization contract.

Privatization Law shall mean M.G.L. c. 7, §§ 52-55.

Privatization Threshold Amount shall mean the threshold amount requiring the application of the Privatization Law to any contract to privatize state services in any year, as determined by the Department in accordance with the CALCULATION OF PRIVATIZATION THRESHOLD, 965 CMR 4.00.

Regular Employee shall mean a permanent employee.

Revenue shall mean the total amount of money received by the agency for goods sold or services rendered.

Unavoidable Costs shall mean the costs that will remain at the agency regardless of the method of service delivery.

Written Statement of Services shall mean the clear, written statement of the required services, the performance standards, the acceptable levels of quality, the workloads associated with the services, bidding requirements, and scoring and evaluation of bids required for any Privatization Contract.

### 5.03: The Privatization Threshold Amount

- (1) The Privatization Law applies to all contracts valued at \$559,637 as of January 1, 2017, but, as of January 1 of each subsequent year, the amount shall change to reflect the change in the consumer price index that the United States Bureau of Labor Statistics calculates for all urban consumers nationally during the most recent 12

month period for which data are available, as determined by the Department in accordance with the CALCULATION OF PRIVATIZATION THRESHOLD, 965 CMR 4.00.

- (2) No agency subject to the Privatization Law shall set the term of a contract at a length of time that would enable the agency to manipulate the Privatization Threshold Amount and avoid the requirements of the Privatization Law. To determine whether a contract of a term of less than five years meets the Privatization Threshold Amount and is, therefore, subject to the Privatization Law, the Department will calculate the yearly contract price and allocate that price over a five-year period. For example, the Department will assume that a three-year contract valued at \$450,000 has an annual value of \$150,000 and a five-year value of \$750,000 which would exceed the Privatization Threshold Amount in calendar year 2016 and, therefore, subject such a contract to the requirements of the Privatization Law.

#### 5.04: The Written Statement of Services

- (1) No agency shall make any Privatization Contract and no such contract shall be valid unless the agency, in consultation with the Executive Office for Administration and Finance, prepares a Written Statement of Services.
- (2) The Written Statement of Services shall include the specific quantity and standard of quality of the subject services proposed to be the subject of the Privatization Contract.
- (3) The Written Statement of Services shall be a separate and distinct document that will become part of the request for bids.
- (4) In drafting the Written Statement of Services, the agency shall analyze the current delivery of the services, including consideration of the mission of the agency and what is needed to deliver the quantity of services at the desired level of quality.
- (5) Both the solicited private contract and the agency's In-House Cost Estimate or In-House Revenue Projection must be based on the same Written Statement of Services, i.e., the same scope of work and standards of performance.
- (6) In developing the Written Statement of Services, the agency must rely on one or more of the following performance measures: quantitative, qualitative, timeliness, effectiveness, cost, and/or revenue.
  - (a) Quantitative performance measures indicate how much is processed, produced, expended or sold.
  - (b) Qualitative performance measures demonstrate how well a product is provided or a service is performed.
  - (c) Timeliness performance measures specify when a product or service is completed and delivered.

- (d) Effectiveness performance measures validate the accomplishment of a mission.
  - (e) Cost performance measures calculate the total cost of a product or service provided.
  - (f) Revenue performance measures calculate revenue growth year over year.
- (7) For each position in which a bidder will employ any person pursuant to a Privatization Contract and for which the duties are substantially similar to the duties performed by a regular agency employee or employees, the Written Statement of Services shall include a statement of the minimum wage rate to be paid for each such position, which rate shall be the lesser of step one of the grade or classification under which the comparable regular agency employee is paid, or the average private sector wage rate for each such position as the Executive Office for Administration and Finance determines from data that the Department of Labor Standards and the Division of Purchased Services collect.
- (8) The Written Statement of Services shall be a public record, shall be filed in the agency and in the Executive Office for Administration and Finance, and shall be transmitted to the Department for its review pursuant to M.G.L. c. 7, § 55.

#### 5.05: The In-House Cost Estimate

- (1) The agency shall prepare an In-House Cost Estimate – a comprehensive written estimate of the costs of regular agency employees' providing the subject services in the most efficient and cost effective manner. Where the contract is revenue based, the In-House Cost Estimate will include projected revenue from the sale of goods or services to be rendered.
- (2) The In-House Cost Estimate shall include all direct and indirect costs that the agency would incur as the result of providing the subject services by regular agency employees, including but not limited to, pension, insurance, and other employee benefit costs.
- (3) The calculation of the In-House Cost Estimate requires the completion of five separate steps.
- (a) Step One – the Management Study
1. The In-House Cost Estimate shall begin with a management study of the in-house organization that is presently providing the service to determine the most efficient and cost effective manner of providing the service.
  2. The management study shall analyze the current workforce, materials, equipment, facilities, and procedures needed to provide the service, and shall

determine whether changes in the service delivery can be made that would result in a more efficient and cost effective in-house operation.

3. The agency must document to the Department the analysis that the agency engaged in, the changes that could be made to provide the service in a more efficient and cost effective manner or to improve the service delivery, and the fiscal impact of such changes on the in-house costs.

(b) Step Two – Calculating the In-House Cost Estimate

1. The In-House Cost Estimate will be based on the Fully Allocated Cost – i.e., the direct and/or indirect costs – which will then be converted to the Avoidable Costs of the service – i.e., the costs that would be avoided if the service were privatized. Where the contract is revenue based, the In-House Cost Estimate will be based on the In-House Projected Revenue.
2. The In-House Cost Estimate must be prepared on forms provided by the Department, and must be supported by proper documentation. The preparer must sign and date the forms, which must then be approved by the agency head.
3. The In-House Cost Estimate shall be prepared for the same length of time as the proposed privatization contract, and shall consider all relevant matters, such as economic trends and anticipated changes in operation. Historical periods may be included with the In-House Cost Estimate, and all known or anticipated increases in costs should be considered.

(c) Step Three – Calculating the Fully Allocated Cost

1. The cost of performing the work in-house includes all direct costs that are attributable to the services under consideration, as well as the indirect costs, or overhead, that support the services, which constitute the Fully Allocated Cost.
2. All costs shall be included in the calculation of the Fully Allocated Cost, regardless of whether or not the costs would be saved – i.e., avoidable – if the services were performed by the private sector. The calculation must include both direct and indirect costs.
3. Direct Costs
  - (i) Direct Costs are those cost items that only benefit, and thus are totally chargeable to performing, the services. As budgets are sometimes organized in a different manner than accounting systems, the agency shall review the entire agency's operations for the direct costs of the services regardless of where the costs are budgeted.

(ii) Examples of Direct Costs include:

- (a) Personnel Costs – Personnel costs include direct personnel costs for accomplishing the services as set forth in the Written Statement of Services. The In-House Cost Estimate shall include the position title of the personnel used to perform the services and the percentage of each person’s time attributable to the services.
- (b) Fringe Benefits – Fringe benefits include retirement programs, health and life insurance payments, and other payroll costs. The agency shall include those amounts if the actual costs are readily available. If not, standard percentages may be used to calculate fringe-benefit costs, so long as care is exercised to ensure that the results are reasonable for the services being analyzed. If the standard percentages do not yield reasonable results, the agency must document the method used and the reasons for the change.
- (c) Materials and Supplies – This category includes all materials and supplies used to perform the services as required in the Written Statement of Services and outlined in the Management Study.
- (d) Other Direct Costs – Other direct costs that are entirely attributable to the services, such as equipment depreciation and utilities, must be considered.
  - 1. Depreciation –Where they are a factor, the In-House Cost Estimate must include an amount for annual depreciation costs. Depreciation is to be calculated by dividing the depreciable basis by the estimated useful life of the asset. Depreciable basis is the acquisition cost plus transportation and installation costs. Depreciation does not include those assets used for the in-house services that are provided to the contractor.
  - 2. Rent – The cost of renting or leasing equipment or facilities used in performing the services should be included in the In-House Cost Estimate.
  - 3. Maintenance and Repair – When appropriate, the direct costs incurred to keep facilities and equipment in working condition must be considered.
  - 4. Utilities – This category should include fuel, electricity, telephones, and water and sewer costs directly incurred in performing the services. If an allocation method is used to cost utilities, the method must be reasonable.

5. Insurance – While potential costs from casualty losses and liability claims are normally covered by insurance in the private sector, the Commonwealth of Massachusetts is primarily self-insured and pays for each loss incurred. The agency shall compute estimated insurance costs by using the guidelines issued by the Federal Office of Management and Budget in Circular A-76 Revised as a guide. If the Commonwealth remains liable for any of these particular losses, no cost for insurance would be included.
6. Other Direct Costs – Other specifically attributable direct costs may include training costs, travel expenses, uniforms, housing allowances, parking, and purchased services.

#### 4. Indirect Costs

(i) There are three types of indirect costs: departmental, executive office, and central services.

(a) Departmental indirect costs are those administrative, personnel, and supporting costs, including fringe benefits, incurred by the department on behalf of its programs that cannot be identified with specific programs.

(b) Executive office indirect costs are those costs incurred by the executive office on behalf of all the departments under its responsibility.

(c) Central service costs are those costs incurred by supporting functions and activities, such as the Comptroller's Office, personnel administration, and employee relations, that benefit all departments. The Statewide Cost Allocation Plan developed by the State Comptroller's Office and the Departmental Allocation Plan, if available, should be consulted for the agency's indirect costs.

(ii) Once they have been determined, these three indirect cost amounts should be allocated to the Fully Allocated Cost.

#### (d) Step Four – Converting the Fully Allocated Cost to the Avoidable Costs

1. When determining the potential cost savings or increase in revenue associated with the privatization of a service, the appropriate in-house costs to use in the comparison are the Avoidable Costs. Computing the Fully Allocated Cost is the starting point for determining the Avoidable Costs.
2. Avoidable Costs are defined as the net amount of expenses that would be eliminated by the agency if the services identified were not performed by the



agency. The Avoidable Costs are the amount that the agency and the Department will use when assessing the likely cost savings achievable through privatization.

3. Determining what portion of indirect costs are avoidable is a matter of professional judgment and depends largely on three factors: how efficiently resources are reallocated; the time period in which resource allocation will occur; and the extent of the privatization effort.
  - (i) Resource Reallocation. The decision to discontinue a particular service should result in some reduction or reallocation of resources in the areas that indirectly supported that service – e.g., personnel, procurement, accounting. Therefore, some of these overhead costs will be avoided to the degree that the agency is able to reallocate or reduce resources in these areas.
  - (ii) Time Period. There are many costs that cannot be avoided in the short term but may be avoidable in the long term. For example, privatizing a service may leave an agency holding a lease for a longer term than is necessary; however, the cost is not avoidable until the agency can decline to renew the lease. Similarly, there may be instances in which contracting out leaves an agency overstaffed but legally obligated not to lay off workers. In the short term, this represents unavoidable costs, but, in the long term, staff levels could be reduced to efficient levels through attrition. Costs that would be avoidable in the long term should be included only for those time periods in which they would be realized.
  - (iii) Extent of Privatization. The reduction in overhead costs is directly related to the size of the service that is being privatized. The larger the service is in comparison to the overall size of the agency, the more the overhead costs can be reduced. Similarly, if other services that use the same overhead are also privatized, a higher portion of overhead costs will likely be avoided. Generally, the greater proportion of a service contracted out, the greater potential reduction in overhead costs.

(e) Step 5 – How to Determine Avoidable Indirect Costs

1. Computing the avoidable indirect costs should be done in two stages. First, determine if at least one position would be eliminated in the supervisory work center above the service that is being privatized. Then determine if at least one position would be eliminated in any of the other agency or department activities that provide definable support to the service. If no positions would be eliminated, then the avoidable indirect costs are zero. If positions would be eliminated, compute personnel costs and other costs solely in support of positions to be eliminated, such as material and supply costs and other costs that are attributable to the positions to be eliminated.

2. Computing the avoidable executive office and central service costs is done in a similar manner. First, list all those activities external to the agency that provide general and administrative support that are essential to the service, that is, the activities of the executive office that oversees the agency and the central services. For each of these activities determine whether at least one position would be eliminated. If no position would be eliminated, the indirect cost is zero. If positions could be eliminated, compute personnel costs and other costs solely in support of those positions that would be eliminated – e.g., material and supply costs and other specifically attributable costs, if any. The avoidable costs that would be realized must be documented by the agency.
- (4) The In-House Cost Estimate shall remain confidential until after the final day for the agency to receive sealed bids for the Privatization Contract, at which time the estimate shall become a public record, shall be filed in the agency and in the Executive Office for Administration and Finance, and shall be transmitted to the Department for review pursuant to M.G.L. c. 7, § 55.

#### 5.06: Bidding Requirements

- (1) In procuring a Privatization Contract, the agency shall solicit competitive sealed bids based upon the Written Statement of Services. The procurement processes must be consistent with applicable state procurement law and any rules, regulations, and procedures established by the Operational Services Division. If the Department determines that proper procurement protocols were not followed, it shall object to the Privatization Contract.
- (2) The day designated by the agency upon which it will accept sealed bids shall be the same for all bidders.
- (3) Every bid for a Privatization Contract shall include provisions specifically establishing the wage rate 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 agency employee or employees. Such a wage rate shall not be less than said minimum wage rate as set forth in 5.04(7) above.
- (4) Every bid shall also include provisions for the contractor to pay not less than a percentage, comparable to the percentage paid by the Commonwealth of Massachusetts for state employees, of the costs of health insurance plans for every employee employed for not less than 20 hours per week pursuant to the contract. Such health insurance plans shall, at a minimum, be sufficient to ensure that the bidder is a contributing employer under M.G.L. c. 149, § 189, and shall provide coverage to the employee and the employee's Dependents.

#### 5.07: Bids by an Employee Organization

- (1) After consulting with all employee organizations representing employees who might be displaced by the Privatization Contract, the agency must provide adequate resources to encourage and assist present agency employees, or the exclusive representatives of such employees, in organizing and submitting a bid to provide the subject services. In determining what resources are adequate for this purpose, the agency shall refer to the existing collective bargaining agreement or agreements of the potentially-affected employees, or, if no such agreement is available, to a collective bargaining agreement of a similar employee organization whose members perform the same or similar services, if available, if the agreement includes a provision regarding the level of resources to be provided in the event of a proposed privatization, or, if no such collective bargaining agreement exists, the agency shall refer to any existing collective bargaining agreements providing such resources, and shall provide such resources at the minimum level of assistance provided for in such agreements.
- (2) An employee organization may submit a bid as agency employees who wish to retain the work in-house, a separate entity with whom the agency can contract, or a joint venture with other persons with whom the agency can contract.
- (3) The agency shall consider any such employee bid on the same basis as all other bids.
- (4) The agency must document to the Department the agency's efforts to meet the intent stated in paragraph 5.07(1) above.
- (5) Employee organizations that do not receive adequate resources, as stated in paragraph 5.07(1) above, must notify the Department of that claim prior to the closing of the acceptance of the bids. In the event that an employee organization makes such a claim, the Department will determine whether adequate resources were made available to the organization in conformity with the requirements of the Privatization Law. If the Department determines that adequate resources were not made available, it shall object to the Privatization Contract.

#### 5.08: Proposed Amendments to Collective Bargaining Agreements by Employee Organizations

- (1) Any employee organization that represents any of the affected members may, at any time before the final day for the agency to receive sealed bids, propose amendments to any relevant collective bargaining agreement to which the employee organization and the agency are parties.
- (2) Any such amendment to a collective bargaining amendment shall take effect only if the amendment is necessary to reduce the In-House Cost Estimate below the Cost of Contract Performance during the cost comparison stage.
- (3) Such an estimate – as to whether the amendment reduces the In-House Cost Estimate below the Cost of Contract Performance – shall remain confidential until after the

final day for the agency to receive sealed bids for the proposed Privatization Contract, at which time the estimate shall become a public record, shall be filed in the agency and in the Executive Office for Administration and Finance, and shall be transmitted to the Department for review pursuant to M.G.L. c. 7, § 55.

- (4) Any amendment to a collective bargaining agreement made under 965 CMR 5.08 shall be in the form of a side agreement between the employee organization that represents the affected employees and the agency. Any such side agreement, so long as it otherwise comports with the requirements of M.G.L. c. 150E, § 7, shall be binding on the affected employees and the agency.

#### 5.09: Privatization Contracts

- (1) Every Privatization Contract shall include provisions specifically establishing the wage rate 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 agency employee or employees. Such a wage rate shall not be less than said minimum wage rate as set forth in 5.04(7) above.
- (2) Every such Privatization Contract shall also include provisions for the contractor to pay not less than a percentage, comparable to the percentage paid by the Commonwealth of Massachusetts for state employees, of the costs of health insurance plans for every employee employed for not less than 20 hours per week pursuant to the contract. Such health insurance plans shall, at a minimum, be sufficient to ensure that the bidder is a contributing employer under M.G.L. c. 149, § 189, and shall provide coverage to the employee and the employee's Dependents.
- (3) Every Privatization Contract shall contain provisions requiring the contractor to offer employee positions available under the contract to qualified regular employees of the agency whose state employment is terminated because of the Privatization Contract and who satisfy the hiring criteria of the contractor.
- (4) Every such Privatization Contract shall also contain provisions requiring the contractor to comply with a policy of nondiscrimination and equal opportunity for all persons protected by M.G.L. c. 151B, and to take affirmative steps to provide equal opportunity for all such persons.
- (5) The term of any Privatization Contract shall not exceed five years.
- (6) Any subsequent agreement to a Privatization Contract, as defined by M.G.L. c. 7, § 53 and as stated in paragraph 5.02 above, which had initially complied with the Privatization Law, including any agreement resulting from a rebidding of previously privatized services, or any agreement renewing or extending a Privatization Contract, shall not be considered a Privatization Contract.
- (7) No amendment to a Privatization Contract shall be valid if it has the purpose or effect of avoiding any requirement of the Privatization Law. No agency subject to the

Privatization Law shall set the term of a Privatization Contract at less than five years in order to rebid, renew, or extend the contract so as to avoid the employee safeguards established by the Privatization Law.

5.10: The Cost of Contract Performance

- (1) Upon selecting the successful bidder, the agency must prepare a comprehensive written analysis of the contract cost based upon the designated bid, specifically including the costs of: the transition from public to private operation; additional unemployment and retirement benefits, if any; and monitoring and otherwise administering contract performance. Where the contract is revenue based, the written analysis must also detail the projected revenue based upon the designated bid, specifically including the dedicated revenue to be allocated to the agency.
- (2) **Contract Price.** The first category of cost to be included in the Cost of Contract Performance is the contract price. The contract price must be supported by a firm bid, and the bid must be based on the same Written Statement of Services used in preparing the In-House Cost Estimate. While the agency and the successful bidder may, during subsequent negotiations, make minor changes to the contract terms, the parties may not make any changes that are inconsistent with the Privatization Law, 965 CMR 5.00, or the Written Statement of Services.
- (3) **Contract Administration.** Contract administration costs are the costs incurred by the agency in ensuring that the quantity and quality of a service purchased from a contractor is acceptable, and that the contract is executed in accordance with the contract specifications.
  - (a) Contract administration costs include the cost of monitoring and evaluating contractor performance and compliance with the terms of the contract – i.e., quality assurance – but may also include processing contract payments, negotiating change orders, and monitoring contract operations. Agencies must identify and document all direct and indirect costs expected to be incurred for contract administration. The amount will vary depending on the type of service being performed, the size of the contract, the extent of contract monitoring desired, and the extent to which any of the functions could be performed by the current workforce without an increase in cost.
  - (b) If additional costs will not be necessary to perform the services, contract administration costs should not be included with other contract costs. For example, if the increase in workload can be done by existing employees, there may be little or no additional cost.
  - (c) If cost data based on prior experience is not available to make a reasonable estimate of contract administration costs, the agency shall use the guidelines issued by the Federal Office of Management and Budget in Circular A-76 Revised as a guide.

- (4) Transition Costs. With regard to one-time costs incurred by an agency that discontinues an in-house activity and obtains the service by contract, those costs must be amortized over the life of the contract, and recurring costs should be included for each year of the contract. Transition costs include, but are not limited to:
- (a) Unemployment and Retirement Benefits. For those employees whose jobs will be terminated and who become unemployed or retire because of the discontinued in-house operation, the cost of unemployment and retirement benefits, if any, should be included in the Cost of Contract Performance. When the agency knows which employees will retire, the agency must compute the public employer's share of retirement costs for the performance period of the contract. When the agency knows which employees will become unemployed, the agency must compute the employer's share of the unemployment compensation costs for the average benefit period, as provided by the Division of Unemployment Assistance. When the employee attrition figure is not known, the agency must use estimates based on information available from prior experiences on the number of employees who retire or become unemployed as a result of a privatization.
  - (b) Other Transition Costs:
    - 1. If the transition is expected to result in one-time labor-related costs such as severance pay, outplacement services, or retraining expenses, the agency must compute and include those expenses in the Cost of Contract Performance. When those costs are not known, the agency must use estimates based on information available from prior experiences.
    - 2. If the transition requires an agency to take certain actions that would not be necessary if the activity continued in-house – for example, costs associated with terminating a lease or with disposing of materials that are no longer needed – the agency must include those costs in the Cost of Contract Performance.
    - 3. If any agency facilities or equipment are to be used by the contractor, which were not used under the in-house function, the Cost of Contract Performance must be increased by the estimated rental value of the facilities or equipment.
  - (c) Gain or Loss on Disposal of Assets. The disposal value of agency assets no longer needed must be included in the Cost of Contract Performance, minus the estimated costs of disposal, and treated as a gain that would reduce the Cost of Contract Performance.
  - (d) Other Revenue. Any other revenues that would be realized as a result of privatizing the services must be included and treated as a gain that would reduce the Cost of Contract Performance.
  - (e) Savings. Any savings that would be realized as a result of the privatization, such as redeploying trained employees, thus avoiding the need to train new employees,

must be included and treated as a gain that would reduce the Cost of Contract Performance.

- (5) Lost Tax Revenue. If the designated bidder proposes to perform any or all of the contract outside of the boundaries of the Commonwealth of Massachusetts, the contract costs must be increased by the amount of income tax revenue, if any, which would be lost by the corresponding elimination of agency employees, as determined by the Department of Revenue to the extent that it is able to do so.
- (6) State Income Tax. Because contract performance may provide the contractor with income subject to state taxation, an estimated amount of such taxes must be a deduction from the net cost to the Commonwealth of Massachusetts, unless the contractor is a tax-exempt organization.

#### 5.11: The Cost or Revenue Comparison

- (1) After the Cost of Contract Performance or Contract Projected Revenue and the In-House Cost Estimate have been determined, they must be compared to determine whether privatization would provide any potential cost savings or increase in revenue. If there are potential cost savings or revenue gain, the head of the agency and the Secretary of the Executive Office of Administration and Finance may certify that:
  - a. the Cost of Contract Performance will be less than the Avoidable Costs of the In-House Cost Estimate; or
  - b. the Contract Projected Revenue will be more than the In-House Projected Revenue.If there are no potential cost savings or increase in revenue, the work must continue to be performed in-house with agency employees.
- (2) For an agency to justify awarding a Privatization Contract, there must be a cost savings or increase in revenue with no reduction in the quality or level of service. The Privatization Law does not provide a threshold for an amount of cost savings or revenue gain – the Privatization Law simply requires that the Cost of Contract Performance be less than the In-House Cost Estimate, and that the proposed contract otherwise be in the public interest. The agency should consider all factors specified in the Privatization Law, as well as costs and quality of services, in deciding whether to award a Privatization Contract.
- (3) Under the Privatization Law, the work must be done in-house if the agency In-House Cost Estimate is less costly than the Cost of Contract Performance, or a bid by agency employees, prepared in accordance with 965 CMR 5.07, is the successful bid. Where the contract is revenue based, the work must be done in-house if the Net Income from the agency In-House Cost Estimate is greater than the Contract Projected Revenue.
  - (a) If the work is retained in-house because it would be less costly than the Cost of Contract Performance, the agency is expected to perform the work at the quantity and quality levels outlined in the Written Statement of Services and within the In-House Cost Estimate. If the agency fails to do so, the agency may issue another

request for bids or, to the extent allowable under the procurement laws, reopen negotiations with the vendor who would have been the successful bidder under the earlier request for bids. Whether the agency issues a new request for bids or reopens negotiations with a former vendor or employee organization, the agency must notify the Department.

- (b) If the work is to be retained in-house because an employee bid is successful, the agency and the employee group must execute a memorandum of understanding that sets forth the requirements and obligations of both parties. The memorandum of understanding may include provisions for termination should the employee group fail to perform at the quality and quantity levels outlined in the Written Statement of Services and within the bid amount. If the contract is terminated, the agency may issue another request for bids or, to the extent allowable under the procurement laws, reopen negotiations with the vendor who was the next successful bidder under the earlier request for bids. Whether the agency issues a new request for bids or reopens negotiations with a former vendor or employee organization, the agency must notify the Department.

5.12: Certification to the Department of the State Auditor

- (1) The head of the agency and the Secretary of the Executive Office of Administration and Finance shall each certify the following in writing to the Department:
  - (a) The agency has complied with all the provisions of M.G.L. c. 7, § 54, and of all other applicable laws.
  - (b) The quality of the services to be provided by the designated bidder is likely to satisfy the quality requirements of the Written Statement of Services, and to equal or exceed the quality of services which could be provided by regular agency employees. The agency must document its efforts to meet the intent of M.G.L. c. 7, § 54(7)(ii), and describe the process to be used to monitor the quality of the services provided by the contractor.
  - (c) Taking into account all comparable types of costs, the Cost of Contract Performance is less than the In-House Cost Estimate. Where the contract is revenue based, the Contract Projected Revenue is greater than the Net Income from the In-House Cost Estimate.
  - (d) The designated bidder and its supervisory employees, while in the employ of the designated bidder, have no adjudicated record of substantial or repeated willful noncompliance with any relevant federal or state regulations or statutes including, but not limited to, regulations or statutes concerning labor relations, occupational safety and health, nondiscrimination and affirmative action, environmental protection, and conflicts of interest.
  - (e) The proposed Privatization Contract is in the public interest, in that it meets the applicable quality and fiscal standards set forth in the Privatization Law.



- (2) A copy of the proposed Privatization Contract shall accompany the certificate transmitted to the Department.

#### 5.13: Objection by the Department of the State Auditor

- (1) An agency shall not make any Privatization Contract and no such contract shall be valid if, within 30 business days after receiving the certificate required by M.G.L. c. 54, § 7, the Department notifies the agency of its objection.
- (2) The Department's objection must be in writing and must specifically state its finding that the agency has failed to comply with one or more requirements of G.L. c. 7, § 54, including that the Department finds incorrect, based on independent review of all the relevant facts, any of the findings required by M.G.L. c. 54, § 7.
- (3) The Department may extend the time for its objection for an additional period of 30 business days beyond the original 30 business days by written notice to the agency stating the reason for such an extension.
- (4) For the purpose of reviewing the agency's compliance with the Privatization Law, and the certificate required by M.G.L. c. 54, § 7, the Department or its designee may require by summons the attendance and testimony under oath of witnesses and the production of books, papers, and other records relating to that review. All provisions of law relative to summonses in civil cases, including the manner of service, the scope and relevance to the review, and the compensation of witnesses who are not state employees, shall apply to such summonses, which may be enforced pursuant to M.G.L. c. 233, § 10.
- (5) The objection of the Department shall be final and binding on the agency, unless the Department thereafter in writing withdraws the objection, stating the specific reasons, based upon a revised certificate by the agency and by the Secretary of the Executive Office of Administration and Finance, and the Department's review of the revised certificate.

#### 5.14: Advisory Opinions

- (1) In case of doubt as to the meaning or applicability of any provision or requirement in the Privatization Law or 965 CMR 5.00, including whether an entity is an Agency, or whether a proposed contract meets or exceeds the Privatization Threshold, an agency or person may request an advisory opinion from the Department in accordance with M.G.L. c. 30A, § 8. The request may be accompanied by such data, views, and arguments as the requesting person or agency deems pertinent
- (2) The Department shall review all requests for advisory opinions and may request that additional or more specific information or questions be submitted by the requesting person or agency.

- (3) The Department may determine that a particular request for an advisory opinion poses issues that are not within its jurisdiction, the questions posed are not appropriate to an advisory opinion, or sufficient information has not been provided by the requesting person or agency.
- (4) For the reasons stated in 5.14(3) above, the Department may determine that an advisory opinion will not be rendered. If such a determination is made, it shall, within a reasonable time, notify the requesting person or agency that the advisory opinion will not be rendered. If such a determination is not made, the Department shall, within a reasonable time, issue to the requesting person or agency a written advisory opinion or guidance letter.
- (5) All advisory opinion requests and all advisory opinions shall be public records, under M.G.L. c. 4, § 7(26), and shall be subject to public inspection as required by M.G.L. c. 66, § 10.
- (6) The Department may, in its discretion, issue guides, interpretive bulletins, and legal memoranda which concern matters of general application of the Privatization Law and 965 CMR 5.00.

#### REGULATORY AUTHORITY

965 CMR 5.00: M.G.L. c. 7, § 55(c).