

February 9, 2005

Hon. Bill Lockyer
Attorney General
1300 I Street, 17th Floor
Sacramento, California 95814

Attention: Ms. Tricia Knight
Initiative Coordinator

Dear Attorney General Lockyer:

Pursuant to Elections Code Section 9005, we have reviewed the proposed initiative entitled "The Fair Competition and Taxpayer Savings Act" (File No. SA2005RF0001).

Background

State Government. Based on court interpretation of the provisions in the State Constitution, services provided by state agencies generally must be performed by state civil service employees. Case law and state statute have established parameters for contracting out state services to private companies. State law requires that proposals for contracting must, at a minimum, meet the following criteria:

- Contracts must result in cost savings to the state.
- Contractor's wages may not significantly undercut state pay rates.
- Contracts cannot cause the displacement of civil service employees.

As a result of these provisions, the instances of contracting out for many types of services are limited. State law, however, does allow contracting out in specified circumstances, such as for new state functions or when highly specialized skills are required.

In November 2000, Proposition 35 added Article XXII to the Constitution to explicitly allow for the contracting out of services for architectural and engineering services. These are the only types of state services with such authorization.

Local Governments. The authority of local agencies (counties, cities, special districts, and school districts) to contract for services varies markedly by the type of local agency

and the existence, if any, of a locally approved charter. For example, chartered cities generally have the broadest authority to contract for services. Specifically, Article XI, Section 5 (a) of the Constitution authorizes charter cities to exercise plenary authority over all municipal affairs, free from any constraint imposed by the state Legislature and subject only to constitutional limitations. In contrast, general law counties have limited authority and may contract out only for a limited list of specialized services identified in state statute, including special services and advice in "financial, economic, accounting, engineering, legal or administrative matters." Prior to 2002, school districts and community colleges had considerable authority to contract out for services. Chapter 894, Statutes of 2002 (SB 1419, Alarcón), however, significantly reduced the ability of school districts and community colleges to contract out for services that could be provided by classified employees.

Major Provisions

This measure amends the State Constitution to allow the state and all other governmental entities (including counties, cities, special districts, and school districts) to contract with "qualified" (not defined in the measure) private entities for any service, except police and fire protection services, when the governing body determines the "public interest will be better served." Under the measure, police and fire protection services that are already performed by private entities may continue.

Fiscal Effect

Eliminating restrictions on contracting for services would make it easier for the state and some local governments to enter into contracts with private individuals or firms to obtain services. As a result, the state and some local governments likely would contract out for more services.

The fiscal effect would depend on the cost of salaries and benefits for state and local employees performing services compared to the cost of contracts with private firms. The measure provides the state and local governments the discretion to determine when contracting out is most beneficial. Presumably, public entities would use this discretion primarily in instances where contracting out would result in savings to them. There may be instances, however, where contracting out costs more. For example, a public entity might knowingly pay more under a contract in order to provide a particular service faster than could be accomplished with public employees (due to timing considerations related to hiring and training new employees). In addition, a public entity might unknowingly pay more for a contracted service because of an inadequate or erroneous fiscal analysis.

Given these factors, the fiscal impact of the measure is unknown and would depend on future actions by the state and local governments. However, because the measure

gives public entities increased options for providing services, it has the potential over the long run for net savings statewide.

Summary. This measure would have the following major fiscal effect on the state and local governments:

- Unknown fiscal effect, with potential net savings to state and local governments due to increased options for providing public services.

Sincerely,

Elizabeth G. Hill
Legislative Analyst

Tom Campbell
Director of Finance