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MEMORANDUM OF LAW

DATE: June 27, 1997

TO: Cathy Lexin, Labor Relations Manager

FROM: City Attorney

SUBJECT: Competition Program

QUESTION PRESENTED

May the City go forward with its Competition Program, and distribute Requests For Proposals ("RFP") for various City services, in light of the recent California Supreme Court decision Professional Engineers in California Government v. Department of Transportation, 97 Daily Journal D.A.R. 6201 (May 15, 1997).

SHORT ANSWER

The City may go forward with the Competition Program in the circumstances outlined by the court in Professional Engineers. Generally, the case prohibits contracting out services traditionally performed by civil service employees unless the services cannot be adequately or competently performed by those employees. However, the courts have, over the years, carved out a number of specific exceptions to this general rule. The Competition Program itself is not in jeopardy as it provides a mechanism to evaluate a specific proposal, and each proposal must be judged on it own merits. If an RFP for City services meets the criteria for one of the specific exceptions, a contract may be awarded for the provision of those services.

BACKGROUND

As part of the overall vision to take San Diego into the twenty-first century, the Mayor and Council issued a directive to the City Manager to explore avenues which might allow the City to operate in a more efficient and cost-effective manner. To that end, and in conjunction

with a number of other programs, the Competition Program was developed. Over the past two years, City departments have actively sought to streamline operations and perform more efficiently with the ultimate goal of allowing City departments to bid on the performance of services in a competitive process. City departments will compete in the bidding process on the same basis as private contractors seeking City service contracts.

Recently, as part of the Competition Program, an RFP for the Lower Otay Water Treatment Plant was distributed for review and comment. After distribution of the RFP, attorneys for the American Federation of State, County and Municipal Employees ("AFSCME"), Local 127, sent a letter to the City Manager requesting the withdrawal of the RFP based upon a recent California Supreme Court decision regarding the "contracting out" of engineer services by the California Department of Transportation ("Caltrans"). That case is Professional Engineers in California Government v. Department of Transportation, 97 Daily Journal D.A.R. 6201 (May 15, 1997). AFSCME attorneys maintain the case precludes the City from seeking competitive bids for contracts to perform duties and provide services traditionally performed by City employees. You have asked for an analysis of the case and its impact on the City's Competition Program.

ANALYSIS

The Professional Engineers case addressed whether "contracting out" of personal services is permitted under the state civil service provisions found in Article VII of the California Constitution. These constitutional provisions apply only to the state civil service system. The threshold question for purposes of this discussion then, is whether interpretations of state constitutional provisions are applicable to the City, especially in light of a court decision which says: "San Diego is a charter city. It can make and enforce all ordinances and regulations regarding municipal affairs subject only to the restrictions and limitations imposed by the city charter, as well as conflicting provisions in the United States and California Constitutions and preemptive state law." Grimm v. City of San Diego, 94 Cal. App. 3d 33, 37 (1979).

The Grimm case specifically addressed a compensation issue. However, Grimm, and many other cases, hold the regulation of personnel issues to be solely a matter of municipal concern. See Sonoma County Org. of Public Emp. v. County of Sonoma, 23 Cal. 3d 296, 316-17 (1979); Swift v. County of Placer, 153 Cal. App. 3d 209, 217 (1984). Given the strong language adopted by the courts in ascribing plenary authority over personnel and labor relations issues to municipalities, it would appear that the Professional Engineers case is inapplicable to the City. Case law lends credence to the proposition that the decision to develop a Competition Program for purposes of "contracting out" certain services previously performed by City employees is a matter of managerial authority and thus, not subject to the strictures of the Professional Engineers case.

Further support for the proposition the Professional Engineers case is not binding on the City is found in Baggett v. Gates, 32 Cal. 3d 128 (1982). That case states "cities are granted 'plenary authority' to provide in their charters for the 'compensation, method of appointment, qualifications, tenure of office and removal' for their employees." Id. at 137. Pursuant to this authority granted to charter cities, the City has established a system for compensation, appointment, tenure and removal of employees under its own civil service system established by charter provision and codified in San Diego Municipal Code sections 23.0201 through 23.1211.

That conclusion, however, does not end the inquiry. While constitutional provisions regarding state civil service employees are not applicable to City employees, if City civil service provisions, embodied in the City Charter as provided for in the Baggett case, are similar to the state civil service provisions, the determinations made by the Supreme Court in the Professional Engineers case could, by analogy, be applicable. See, e.g., Kennedy v. Ross, 28 Cal. 2d 569, 571-74 (1946) (interpreting city charter provisions analogous to state civil service provisions); San Francisco v. Boyd, 17 Cal. 2d 606, 618-20 (1941). In other words, the rationale of Professional Engineers could apply to an interpretation of City Charter provisions.

A comparison of the two civil service systems shows state provisions apply to "every officer and employee of the state but exempts from the civil service certain positions . . . ." Professional Engineers, 97 Daily Journal D.A.R. at 6201. Similarly, City Charter section 117 provides that "[e]mployment in the City shall be divided into the Unclassified and Classified service." It goes on to say, "the Classified Service shall include all positions not specifically included by this section in the Unclassified Service." The state civil service system provides appointments and promotions in the service shall be made "on the basis of merit, efficiency and fitness ascertained by competitive examination." Id. at 6201. In a similar fashion, the City Charter provides that the Personnel Director, under the auspices of the Civil Service Commission, shall make assignments to classified positions on the basis of competitive tests and that no person shall be certified to an eligible list absent such competitive examination.

The language of both the Charter and the Constitution make clear the purpose of the civil service system is "to promote efficiency and economy in . . . government by prohibiting appointments and promotion in the service except on the basis of merit, efficiency, and fitness ascertained by competitive examination." Id. at 6201. Since the two civil service provisions are remarkably similar in construction with respect to employment policies, it is reasonable to analogize the tests enunciated in the Professional Engineers case for state employees to City employees, and to believe courts could find such an analogy compelling. The courts have made clear that "within its scope, such a charter is to a city what the state Constitution is to the state." Grimm v. City of San Diego, 94 Cal. App. 3d 33, 37 (1979). The courts have, in fact, previously applied state civil service interpretations to city charter provisions. Kennedy v. Ross, 28 Cal. 2d at 571-74; San Francisco v. Boyd, 17 Cal. 2d at 618-20. On that basis, we analyze the Professional Engineers case and its applicability to the City's Competition Program.

In the Professional Engineers case, the court exhaustively addresses each of the tests previously articulated by various courts in reaching decisions on whether certain state civil service functions were amenable to "contracting out." We review those tests to determine when and under what circumstances the City may subject civil service functions to a competitive bid process.

I. The Nature of Services Test

The first case to address the "largely implicit nature of the private contracting restriction" was State Compensation Ins. Fund v. Riley, 9 Cal. 2d 126, 134-36 (1937). In Riley, the Supreme Court pointed out that the civil service scheme is very inclusive and applies to all employees except those specifically exempted, and "that the appointing power in all cases not excepted or exempted 'shall fill the positions by appointment' . . . in strict accordance with the provisions of this act . . . ." Id. at 133. The court explained the true test as:

> whether the services contracted for, whether temporary or permanent, are of such a nature that they could be performed by one selected under the provisions of civil service. If the services could be so performed then in our opinion it is mandatory upon such appointing power to proceed in accordance with the provisions of the Constitution and the statute . . . .

Id. at 135 (emphasis added).

In determining whether the services could be performed by a civil service employee, the court said: "in the absence of a showing to the contrary we must assume that such services could be adequately and competently performed by one selected in accordance with the mandate of the Constitution." Id. at 135.

Implicit in the "nature of services test" is the conclusion that government functions can be performed adequately and competently by civil service employees. To date, services scheduled for possible "contracting out" through the Competition Program are being performed by City employees. No showing has been made that the services have not in the past nor cannot in the future be adequately and competently performed by City employees appointed under the civil service provisions of the City Charter.

Absent such a showing, no factual underpinning exists to justify the need to contract out services previously performed by City employees. Conversely, if such a showing is made the contracting out of services would meet the "nature of services" test requirements.

II. New Function Test

While the regular standard implies most government functions can be performed by civil service employees, the courts have recognized that governmental agencies are continually growing and expanding their range of duties. Mindful of the ever changing nature of governmental duties the courts have indicated that "civil service coverage restricts but does not prohibit the performance of government work by independent contractors." California State Employees' Ass'n. v. Williams, 7 Cal. App. 3d 390, 395 (1970). For example, the courts have said new functions, those not traditionally and historically performed by government employees, may be subjected to the competitive bid process. For example, in the Williams case, the state was implementing its new Medi-Cal program. The underlying statutory framework for the Medi-Cal program permitted the services to be provided, to the fullest extent possible, by private entities. When state employees challenged the program, the court upheld the statutory scheme fashioned by the legislature. The court found the functions to be significantly new and different from any services previously performed by state employees. On that basis the court allowed the private contracting provisions of the legislation to stand. In doing so, the court said:

> [T]he constitutional policy of a merit employment system within the system of state agencies engenders no demand for achieving expansions of state functions exclusively through the traditional modes of direct administration. It does not prohibit legislative experimentation in new forms to fit new functions. It compels expansion of civil service with expansions of state agency structure but does not force expansions of state agency structure to match extensions of state functions.

Id. at 399.

Thus, to the extent the City is entering into new areas of services, such as the newly developed co-generation plants, an argument can be made that services performed as a result of the new functions need not be subject to the civil service provisions of the City Charter and may be subject to a competitive bid process.

III. Experimental Programs

The courts have also recognized exceptions in instances when a program is experimental. In Professional Engineers v. Department of Transportation, 13 Cal. App. 4th 585 (1993) ("Engineers I"), the court approved the contracting out of a number of services traditionally and historically performed by Caltrans engineers. In Engineers I the design and construction of roads, which the court admitted could and had previously been performed by Caltrans engineers

and construction workers, was contracted out through a competitive bid process. As with the Medi-Cal process, the new program was developed by legislative enactment and was supported by an underlying statutory scheme. The court upheld the validity of the contracts because the program enlisted private financing, design, construction and operation of transportation facilities to solve state transportation needs that could not be met with available public revenue. The court noted that "the novelty of the contracts and legislation lies in the privatization of project financing and management. After all, the private sector, not the state, will pay for the services engaged pursuant to the exclusive franchise agreements." Id. at 593.

Following this reasoning, the City could conceivably contract out even existing services if the complete program envisions a novel or experimental process in the financing or delivery of the service.

IV. Cost Savings

Finally, and perhaps most importantly, the courts have indicated that services traditionally performed by government employees may be contracted out for purposes of cost effectiveness and efficiency if a number of specific criteria are met. Courts specifically allow cost effectiveness to be considered in determining whether contracting out is appropriate. However, such contracts must provide substantial cost savings and not undercut government pay rates, cause the displacement of civil service employees, or adversely affect affirmative action efforts.[1] Additionally, the contracts must insure there are specific provisions regarding the qualifications of the staff to be performing the work and demonstrate that hiring standards meet applicable nondiscrimination standards. Finally, the contract must be awarded through a competitive bidding process, and the potential economic advantage of contracting must not be outweighed by the public's interest in having a particular function performed by the government. California State Employees' Ass'n. v. State of California, 199 Cal. App. 3d 840, 844 (1988).

The majority of the enumerated criteria can be met through the simple expedient of requiring specific detail in the RFP concerning wages, experience, etc. However, whether the public interest is protected by having the functions performed by government employees or private sector employees, is not easily determined by any bright line test. There are those who would argue that it is imperative for the City to retain the responsibility for performing certain functions, for example, police and fire services. Indeed, the City Charter supports this interpretation by providing that the respective chiefs shall have supervision over the personnel of the department and all members of the departments shall be subject to the civil service provisions. Similarly, the City Charter provides that subordinates of the City Auditor and

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[1]Affirmative actions efforts may be a nonessential factor in light of Proposition 209, however we do not need to address that issue for purposes of this discussion.

Comptroller, and the City Attorney (except deputy city attorneys) be appointed under the auspices of the civil service provisions.

Other City departments do not have the clear Charter mandate that all personnel be subject to the civil service provisions of the City Charter, although City Charter section 26.1 obligates the City "to provide public works services, water services, building inspection services, public health services, park and recreation services, library services, and such other services and programs as may be desired." The Charter language, however, does not specifically state that City forces must actually perform these functions. Arguably, if the City carefully selects the provider and oversees the performance of the services, its obligations under Charter section 26.1 are met.[2]

This interpretation must be reconciled with the court's consistent acknowledgment of the validity of the proposition that certain services are best performed by the governmental entity and their support of the maintenance of strong civil service systems. "Early on the California Supreme Court recognized that the civil service provisions will not work if the merit appointment system can be circumvented by simply contracting out civil service jobs." Professional Engineers, 97 Daily Journal D.A.R. at 6206. Thus, while the California State Employees' Ass'n. case allows some latitude for the introduction of the Competition Program into some areas of City services, previous case law and the City's own Charter limit the areas in which contracting out is appropriate. In making a determination to contract with the private sector for the provision of services, the City should carefully evaluate all the surrounding circumstances.

CONCLUSION

The Professional Engineers case is not directly applicable to, nor binding on, the City's civil service employees. However, the similarity between state and City civil service provisions suggests the analysis of the civil service provisions in Professional Engineers could be persuasive to courts interpreting the City's civil service provisions. Thus, while the Professional Engineers case does not prohibit all contracting out of government services, such contracting out would likely be subject to the restrictions imposed by the tests discussed by the Court.

We recommend RFPs be drafted with each of the criteria set forth above carefully considered and addressed. A factual basis supporting the need for contracting out should be included as part of the RFP. As the court has carefully pointed out, the purpose of civil service

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[2]The City cannot maintain too much control over the contractor lest the contractor's employees be considered City employees, but that, too, is an issue for another memorandum of law.

systems is to promote efficiency and economy in government and to avoid favoritism. A carefully drafted RFP and award process, with the appropriate factual basis, can be proof that the contracting out process is an attempt to meet both those goals.

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