Legislative Analysis

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BID OUT STATE PAYROLL

House Bill 4237 (as passed by the House
Sponsor: Rep. Philip LaJoy
Committee: Government Operations

Second Analysis (9-16-05)

BRIEF SUMMARY: The bill would require the Department of Management and Budget to determine the true cost of the state's payroll system and contract out the operation of that system if it receives bids that meet certain performance criteria and are less than 95 percent of that cost.

FISCAL IMPACT: The fiscal impact is indeterminate at this time.

THE APPARENT PROBLEM:

Given the state's persistent budget problems over the past few years, the governor and legislative leaders have recently adopted a budget approach that identifies the state's funding priorities, establishes the "price of government", and sets up a process that decides how to best provide services that meet those priorities at the determined price. One aspect of this "new" budgeting method is the idea of spending the state's (that is, the taxpayers') money more intelligently by receiving more value at lower cost. Some people believe that one way to achieve this is through competition, by requiring public agencies to compete with private entities to provide certain services. Services are then provided by the firm, whether public or private, that can provide them in the most cost-efficient and effective manner. One proposal is to open the operation and maintenance of the system to provide payroll to the state's 55,000 employees to competition and contract it out to a private entity if doing so is cost-efficient and effective.

THE CONTENT OF THE BILL:

The bill would amend the Management and Budget Act to require the Department of Management and Budget to do the following:

-- Solicit bids from vendors and award a contract to determine the true cost of operating and maintaining the state's payroll system within 120 days after the bill's effective date;

-- Solicit bids from vendors to operate and maintain the state's payroll system within 240 days after the bill's effective date; and

-- Enter into a contract with a vendor, if the DMB receives bids that are less than 95 percent of the department's true cost and include standards for security, accuracy, responsiveness, and timeliness that meet those standards currently set or provided by the department. (The vendor would also have to agree to reimburse the state the cost of the contract that determined the true cost of operating and maintaining the central payroll system.) In entering into a contract, the DMB would have to give preference to Michigan-based firms with a physical presence and employees in the state, if all other things are equal.

The bill defines "true cost" to mean the total monetary value of all personnel, equipment, software, hardware, supplies, services, utilities, postage, rent, and time and attendance collection of the department.

MCL 18.1283

ARGUMENTS:

For:

The bill is an important first step in ensuring that state services are provided effectively and efficiently as possible. Given the budget problems that have plagued the state over the past several years, the state must continue to find ways to provide services as best it can at the cheapest price possible. Any inefficient use of state spending is a waste of taxpayer dollars. To that end, any costs savings realized by this bill could be applied to other budgetary concerns, reducing the need for further programmatic cuts in arguably more important public programs. Note, moreover, that bill does not automatically privatize the state's payroll system; that would only happen if cost and effectiveness criteria were met.

For:

As provided in this notion of the "price of government" and elsewhere, opening the operation and maintenance of the state's payroll system to competition improves the efficiency of providing the service, forces the service provider to be more responsive to the needs of the service recipient, rewards innovation in the provision of that service, improves the general public's faith in government, and improves the quality of the service provided.

For:

At the very least, the bill gets the state to actually assess the true cost of providing services, in this case the state's payroll system. This does not simply include the cost of providing a check or electronic statement, but also costs for time and attendance collections, software and hardware required, and other related costs. This, it could be argued, better enables the state to know how taxpayer dollars are being spent and, with that, how the state should prioritize its spending.

Against:

The bill seems to be predicated on two assumptions, neither of which hold when scrutinized more closely. Governments typically look to contract out its services (1) when the service is not provided efficiently or effectively, or (2) when the system (such as technology) is outdated and the costs of upgrading the service do not necessarily outweigh the cost of privatizing it. Thus far, there has been no finding that the state's payroll system is not operating in a cost-efficient and effective manner. Moreover, representatives from the department and the Office of the State Employer testified that the state's payroll system, which is integrated into the larger Human Resources Management Network (HRMN), has proven to be very accurate, effective, and responsive, particularly given the sheer complexity of the state's various payroll requirements, including recent changes regarding banked leave time and furlough days. There would be a greater justification for change and for this bill if there had been a showing that the payroll system does not operate properly.

In addition, over the past few years, the state has spent $40.5 million in hardware and software for the HRMN system – the state's integrated system for administering human resources, payroll, and employee benefits system. The HRMN system replaced, improved, and streamlined several outdated human resources systems, and bidding out and removing the payroll function from that integrated system does not seem to be an effective and efficient use of taxpayer money given the massive investment the state has already poured into the system.

In addition, representatives from the DMB and the Office of the State Employer also testified about the apparent difficulty and impracticality of de-coupling (or dis-integrating) the payroll function from the HRMN system. Removing the payroll function would require an additional set of complex interfaces with existing benefits and human resources functions as well as the state's accounting system. These changes would likely negate and possibly outweigh any other potential cost savings derived from simply contracting out the payroll system. Moreover, there is great concern about the responsiveness and cost-efficiency of an outside vendor when the state's payroll system must be changed quickly to reflect any new agreements between the state and the several bargaining units. The state was able implement recent changes such as banked leave time and furlough days relatively quickly and with no additional costs within a relatively short period of time. It is not clear that an outside vendor would be able to do the same, particularly after the contract has been entered into. (The bill does establish certain performance criteria that bids must meet before the payroll system is contracted out, but as a practical matter it may not be apparent at the time the contract is entered into whether the vendor can meet those performance standards. A vendor may be able to meet the general task of providing payroll services, but would it be able to meet any changing payroll requirements, such as the implementation of banked leave and furlough days, that occur well after the contract is finalized?)

Response:

The bill now requires that bids include standards for responsiveness. This should ease concern that the privatized service could not respond as quickly as the department when changes to the payroll system must be made. If a bidder cannot provide the same response standards as those provided by the department, in theory, that bidder would not receive a contract, even if it met the other standards.

Additionally, one representative of a firm that provides payroll services for numerous companies questions the apparent inability of the state to separate payroll functions from the other aspects of the HRMN system, and notes that one company it works with operates an HR system similar to the state's.

Against:

The bill targets the operations of the Department of Management and Budget with such great specificity that it meddles in the affairs and administration of the executive branch and trends closely to violating the constitutional separation of powers between the legislative and executive branches.

Response:

The Management and Budget Act already includes numerous other legislative directives on the operations of the department, including a requirement that nonclassified state employees be paid by electronic funds transfer (EFT).

POSITIONS:

The Michigan Chamber of Commerce testified in support of the bill. (2-22-05)

Automatic Data Processing (ADP) testified in support of the bill. (2-22-05)

The Office of the State Employer testified in opposition to the bill (2-22-05 and 3-1-05)

The Department of Management and Budget testified in opposition to the bill. (2-22-05)

The Michigan Association of Governmental Employees indicated that it opposes the bill. (2-22-05)

The Service Employees International Union (SEIU) indicated that it opposes the bill. (2-22-05)

The AFL-CIO indicated that it opposes the bill. (2-22-05)

The International Union-UAW indicated that it opposes the bill. (2-22-05)

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