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FISCAL IMPACT REPORT

SPONSOR: Altamirano DATE TYPED: 03/11/01 HB _____
 SHORT TITLE: Performance Contracting Act SB 166/aSFC/aSFL#1/aHGUAC
 ANALYST: Padilla

APPROPRIATION

Appropriation Contained		Estimated Additional Impact		Recurring or Non-Rec	Fund Affected
FY01	FY02	FY01	FY02		
		See Narrative		Recurring	General Fund

(Parenthesis () Indicate Expenditure Decreases)

Duplicates House Bill 230

SOURCES OF INFORMATION

LFC Files
 Attorney General
 Department of Finance and Administration (DFA)
 Public Employees Retirement Association (PERA)
 State Investment Council (SIC)
 Public Regulation Commission (PRC)
 Department of Tourism
 Division of Vocational Rehabilitation (DVR)
 State Department of Education (SDE)
 State Agency on Aging
 Health Policy Commission
 Energy, Minerals and Natural Resources Department (EMNRD)
 Department of Health (DOH)
 General Services Department (GSD)
 Public Defender Department (PDD)
 Department of Public Safety
 State Highway and Transportation Department

SUMMARY

Synopsis of HGUAC Amendment

1. It eliminates the Senate Finance Committee amendment that limited “professional services” to private for-profit or non-profit services.

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2. It eliminates the Senate Floor Amendment entirely. This means that attorney contracts *are* subject to the act.
3. It requires a performance contract to tie a portion of the payment OR the contract extension to performance. (The original bill required both.)
4. It emphasizes that DFA should use federal Office of Management and Budget principles when providing guidance to state agencies on performing cost-benefit analysis.
5. It instructs DFA to use its judgement in prescribing different standards for cost-benefit analysis depending on the type and size of contract.
6. It exempts certain health care and hospital services that are purchased through a network. The language used is similar to language in the Procurement Code.
7. It allows state agencies to be transitioned into performance contracting according to a schedule developed by DFA.

Synopsis of Senate Floor Amendment #1

The Senate Floor amendment changes the definition of “litigation expenses” that was added as part of the SFC amendment and may have the effect of exempting attorney contracts from the Performance Contracting Act. The SFC amendment exempted certain litigation expenses, such as expert witnesses and mediators, from the provisions of the act with the SFC amendment, *but not attorney contracts*. In other words, attorney contracts were still subject to the Act. The Senate Floor Amendment deletes the language that specifically excluded attorney contracts from the definition of litigation expenses.

Synopsis of SFC Amendment

The Senate Finance Committee amendment does the following:

1. It changes the definition of “professional services” to limit it to services from private for-profit or non-profit entities. This definition will exclude services from government entities.
2. It exempts litigation expenses, including expert witness services but not attorney contracts, from the provisions of the bill. This exemption is similar to a Procurement Code exemption.
3. It states that the Performance Contracting Act cannot be applied if, by doing so, a legally protected right would be directly impaired. This addresses several concerns raised by the Public Defenders Department.
4. It moves back the effective date of the bill by one year to July 1, 2002. A number of agencies believed the July 1, 2001 date was unrealistic if DFA is to have time to develop new policies and to train agencies in performance contracting.

Synopsis of Bill

Senate Bill 166 adds a new section of law to require the Department of Finance and Administration (DFA) to implement a comprehensive system of managing the development and oversight of professional services contracts that are entered into by state agencies. It requires agencies that enter into professional services contracts to improve the decision making process they use when determining whether to contract out government services and to prepare cost-benefit analyses. Agencies must certify to DFA that they have completed the cost-benefit analysis. The bill requires agencies to review professional services contracts for legal sufficiency.

The bill requires that professional services contracts be “performance contracts” which means that they must include elements designed to improve accountability, including performance measures, provisions to use against contractors who do not meet performance standards; and provisions to monitor the contractor’s performance.

The bill applies to all state, legislative and judicial agencies and to post-secondary institutions. Legislative and judicial agencies and post-secondary institutions could formulate their own policies to meet the goals of the bill.

The bill exempts emergency procurements and those entities exempted by DFA rule or order.

Significant Issues

LFC staff studies in 1999 and 2000 have shown that New Mexico state government’s contract management and accountability system needs improvement. The 1999 study noted that the state’s expenditures for contract services have grown by \$1.6 billion from FY95 to FY00. The 2000 study reviewed six state agencies’ contract policies and procedures and found they are generally inadequate for financial accountability or quality control. A joint study by Governing magazine and Rutgers University study released in January 2001 noted that contracting in New Mexico is “very decentralized, leaving problems with the potential to fester unnoticed.”

This bill would require DFA to implement a management system for professional services contracts by state agencies that would include:

- Training for agencies on contract development and management;
- Policies and procedures for contract management;
- A role for DFA in the development of major contracts
- Selective monitoring of contract procedures;
- Guidelines for state agencies on preparing cost-benefit analyses; and
- Guidelines for state agencies on performance contracting and monitoring.

Enactment of this bill would provide greater accountability for the use of taxpayer dollars to fund professional services contracts entered into by state agencies. Expanding DFA’s role in the management of professional services contracts would potentially improve accountability in two areas: at the decision-making stage, by helping agencies to determine the benefits of contracting out, and in the ongoing management of contracts, by supporting agencies to use performance contracting.

DFA has stated that agency contract management and accountability needs improvement. DFA believes individual agencies should bear principal responsibility for ensuring accountability. DFA also believes that any changes to contracting processes for professional services should apply to all branches of government.

Performance contracting, which the bill mandates, is becoming more widely practiced in the public sector, especially in the areas of health and human services. Performance contracts focus on the outputs, quality and outcomes of service provision and may tie at least a portion of a contractor's payment as well as any contract extension or renewal to the achievement of those goals. In several recent studies, the need for adequately trained contract managers has been highlighted as one of the principal challenges of moving to performance contracting.

FISCAL IMPLICATIONS

The bill contains no appropriations.

In order for the Department of Finance and Administration to adequately carry out the provisions of the bill, several additional FTE are likely to be required. LFC analyst estimates one FTE. DFA did not address this issue.

Fiscal implications for other agencies are indeterminate. Some agencies, including the SIC, the PRC, DOH, and EMNRD argue that additional performance requirements would increase the cost of professional services contracts because of the additional reporting and monitoring requirements. The Public Defender Department provided the most extreme estimate of fiscal impact, stating that they would need 9 additional FTE to implement the provisions of the bill. Other agencies believe that the bill would have positive fiscal implications by ensuring that all contracts contribute in a measurable way to their overall missions.

Positive long-term fiscal implications of the bill deriving from better management of the contracting process and improved accountability are indeterminate. Better management of professional services contracts, both the initial decision to contract out services and the ongoing oversight of contracts, would likely have significant positive fiscal impact. Performance contracts should provide a means to ensure that deliverables are of high quality and are related to the overall performance goals and targets of the contracting agency.

PERFORMANCE IMPLICATIONS

As New Mexico state government moves to performance-based budgeting as required by the Accountability in Government Act of 1999, integration of professional services contracts into a results-oriented management structure is, for many agencies, a logical next step. The SIC, for example, says that the bill would help agencies tie their overall performance to the performance of contractors. The Department of Tourism notes that the bill would set standards for professional services contracts and that "this will help agencies tie the professional services that were provided to the agency's budget based on performance measures." The Health Policy Commission notes that the bill would help it "to monitor achievement of outcomes under the upcoming performance-based budgeting system."

ADMINISTRATIVE IMPLICATIONS

The bill does not add FTE to DFA, but would likely require DFA to increase staffing as the bill expands DFA's role in contracts management. DFA did not address this potential impact.

Several agencies believe that the bill would require additional staff time to perform the required cost-benefit analysis. EMNRD, for example, says that they would have to employ two FTE to meet the requirements of the bill. GSD estimates four FTE and the Public Defender Department estimated nine FTE. Other agencies, however, such as the Department of Tourism say that additional staff time or FTEs would not be needed to comply with the act. Instead, staff would need to integrate new processes into their regular work. The bill also anticipates DFA's resources being available to contracting agencies so the agencies themselves would not need to add additional staff.

TECHNICAL ISSUES

The bill goes into effect July 1, 2001. A number of agencies question whether this would give adequate time for DFA to provide training and develop guidelines for agencies. DFA did not address this issue.

OTHER SUBSTANTIVE ISSUES

Several agencies raised concerns about the effect of the bill on contractors. SIC, for example, asked whether the number of potential bidders might be reduced to new requirements of performance contracting.

Several agencies raised concerns about the bill's requirement in Section 4. D. that they submit contracts for DFA review at least 30 days prior to their effective date. Current statute, however, requires that DFA approve certain professional services contracts, including those of EMNRD. Because many agencies do not provide enough lead time, DFA often approves contracts retroactively. This section of the bill is designed to help prevent retroactive approvals.

The Public Defender Department raised a number of concerns about how the bill's provisions would affect the PDD's constitutional obligation to serve its clients and the constitutional right to counsel. The PDD pointed out that the Procurement Code exempts litigation costs, which means that the PDD's contracts for expert witness services are exempt.

AMENDMENTS

To address the technical issue addressed above, replace lines 16 and 17 on page 6 to read "EFFECTIVE DATE – The effective date of the provisions of this act is July 1, 2002."

To address the concerns of some agencies about additional FTE needed to implement performance contracting, amend the bill to phase in a transition to performance contracting.

To address the concerns of some agencies about additional FTE needed to implement the provisions of the bill, amend the bill to require cost-benefit analysis only for professional services contracts over a certain dollar amount.

POSSIBLE QUESTIONS

1. Will the costs that might accrue to agencies, particularly in the beginning stages of performance contracting, outweigh the benefits of improved accountability, especially in regard to small contracts?

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2. What would it mean in practice for DFA to actively participate in the development of major requests for proposals and contracts? Could Section 5.F. be changed to allow DFA to act as a resource instead of requiring direct participation.?
3. The bill requires state agencies to review contract decisions and the RFP process for form and legal sufficiency. A review of this type is currently performed by the Contracts Review Bureau at DFA, per Section 13-1-118 NMSA 1978. Is this duplication necessary to ensure good management of professional services contracting?

LMP/ar/njw