



## **National Employment Law Project**

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Members of the Office of Management and Budget, thank you for this opportunity to testify on reforming the federal contracting process.

My organization, the National Employment Law Project (NELP), is a non-profit policy and advocacy center that works with national and grassroots partners across the country on new policies for creating good jobs.

President Obama's directive to modernize the federal acquisition system to improve accountability and results is badly needed. It also represents an important opportunity to address another national priority: rebuilding America's middle class by creating more good jobs across our economy.

NELP has just completed a comprehensive report on the experiences of state and local governments over the last fifteen years with contracting reforms seeking to create good jobs and deliver better quality services. Often referred to as "responsible contracting" policies, the experiences of states and cities with these reforms demonstrate that promoting purchasing from responsible employers that create good jobs is a "win-win" for workers and taxpayers alike. States and cities have generally found that promoting purchasing from employers that invest in their workforces with living wages and benefits, and that comply with workplace, tax and other laws, delivers higher quality, more reliable services, and minimizes the hidden costs to taxpayers that result when employers pay low wages.

The experiences of states and cities with these reforms have been overwhelmingly successful and provide a roadmap for reforming the federal contracting process. Moreover, translating such reform to the federal level requires no new legislative authority since the federal

procurement laws already instruct the government to purchase from responsible vendors that offer the best value for the government.

I will briefly outline some of the key findings that have emerged from the state and city experiences with responsible contracting reforms. They highlight the advantages that this approach offers not just for working families but for the taxpayers and the government as well.

## **1. Responsible Contracting Factors in the Hidden Public Costs of Low-Wages and Benefits**

First, states and cities have found that evaluating bidders' proposals based simply on bid price without factoring in wages and benefits skews the evaluation and selection process. This is because contractors that pay low wages and do not provide quality, affordable health benefits to their workers generate substantial indirect costs to the government as their employees are forced to rely on taxpayer-funded safety net programs for support. As Maryland Delegate Tom Hucker, the sponsor of Maryland's Living Wage Law explains in our forthcoming report, "Before the passage of the living wage law, we effectively had a policy of subsidizing low road employers. This distorted the state's contracting and budgeting processes."

There is a growing body of research quantifying the indirect costs of such low-wage work. The costs are chiefly generated by Earned Income Tax Credit payments, health benefits under Medicaid, and other benefits and income supports that the government provides to workers whose employers pay them low wages and provide limited benefits. In California, for example, the University of California found that \$10.1 billion that federal and state taxpayers spent in 2002 on public assistance programs went to families of low-wage workers but that this cost would have been slashed to \$3.2 billion if the employers had paid a living wage and provided quality, affordable health benefits. Other studies have calculated the corresponding figures for other states.

To ensure a more accurate assessment process, states and cities have adopted reforms that factor into the evaluation process the wages and benefits that contractors provide. One state (Maryland) and more than 140 municipalities have done this by adopting living wage policies. Other states and cities have adopted policies that factor in the type, quality and affordability of contractors' health benefits into the bid evaluation process. While the specific approaches vary, the key innovation here is making wages and benefits a consideration in the contracting process.

## **2. Responsible Contracting Enhances Competition**

A second important lesson from the states and cities is that responsible contracting reforms that factor into the selection process contractors' wages, benefits, and records of complying with workplace, tax and other laws can actually enhance competition by leading more vendors to submit bids for government contracts.

For example, Maryland found that the average number of bidders for state contracts increased from 3.7 bidders to 4.7 bidders after it adopted its living wage policy. Where employment practices are not made part of the evaluation process and bids are assessed chiefly based on low price, responsible employers are often unwilling to go to the expense of submitting bids, knowing that they will be at an inherent disadvantage on account of their higher labor costs. Almost half of the vendors interviewed by Maryland's Department of Legislative Services said that the living wage law encouraged them to bid on state contracts because it leveled the playing field with regard to labor costs. Several vendors reported that in the future, they would only bid on living wage contracts because of "the leveling effect it has on competition."

Many of the procurement officials that NELP has spoken to at the state and local level report similar experiences with their responsible contracting policies. As Carol Isen, Director of Labor Relations for the San Francisco Public Utilities Commission explained, "In order to encourage bidders possessing the requisite experience to spend the resources necessary to prepare bids for a large public workers construction project, it is paramount to eliminate the prospect of low bids from contractors whose qualifications to perform the work have not been examined by the owner."

### **3. Responsible Contracting Provide Higher Quality Services**

A third key lesson from state and local experiences with responsible contracting reforms is that vendors that provide good wages and benefits and that respect workplace laws deliver better results for government agencies and the taxpayers by providing higher quality and more reliable services.

For example, studies of living wage policies have found that when government agencies shift from low-wage contractors to those that provide living wages and quality benefits, the results include reduced turnover and improvements in service quality. In a leading case study, the San Francisco Airport saw annual turnover for security screeners plummet from 94.7 percent to 18.7 percent when their hourly wage rose from \$6.45 an hour to \$10 an hour under a living wage policy. In addition, 35 percent of employers reported improvements in work performance, 47 percent reported better employee morale, and 45 percent reported improvements in customer service.

The benefits of this reduced workforce turnover can be substantial. Recruitment and training costs for replacing employees are significant, typically estimated at 25 percent of the annual salary costs for a position each time it must be filled. In the San Francisco Airport study, the reduced turnover saved employers about \$4,275 per employee in turnover costs.

Improved screening out of contractors with records of significant workplace law violations has also been found to be a key strategy for improving the quality of contracted services. As early as the 1980's, an audit by the Department of Housing and Urban Development of HUD sites found a "direct correlation between labor law violations and poor quality construction" on seventeen HUD projects, and noted further that poor quality work would lead to excessive

maintenance costs. More recently, a survey of New York City construction contractors by New York's Fiscal Policy Institute found that contractors with workplace law violations were more than five times as likely to have a low performance rating than contractors with no workplace law violations.

In response, over the past decade, increasing numbers of states have adopted responsible contracting reforms that include enhanced review to screen out contractors with records of significant violations of workplace, tax and other laws. The best systems use model questionnaires and publicly announced weighting formulas, developed with input from all relevant stakeholders, to put prospective bidders on notice of the process and provide a fair means of evaluating individual firms' information. To date, states including California, Illinois, Ohio, Massachusetts and Connecticut have adopted versions of these model reforms.

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These state and local experiences highlight how responsible contracting reforms offer important advantages for government and working families alike. By modernizing the contractor selection process to take into account workplace practices such as wages, benefits and compliance with workplace laws, the government can improve competition, reduce the indirect public costs of low-wage work, and deliver higher quality services for federal agencies and the taxpayers.

Thank you for your time and attention. We would be delighted to work with OMB and the federal government going forward on specific approaches for incorporating these reforms into the federal acquisition system.

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Attachment:

Paul K. Sonn and Tsedeye Gebreselassie, *The Road to Responsible Contracting: Lessons from States and Cities for Ensuring that Federal Contracting Delivers Good Jobs and Quality Services* (New York, NY: National Employment Law Project, June 2009).