



State of Connecticut

OFFICE OF POLICY AND MANAGEMENT

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**COST-EFFECTIVENESS EVALUATION OF NEW OR RENEWED PRIVITIZATION CONTRACTS  
Policies and Procedures Manual**

*Subsection (p) of C.G.S. Section 4e-16*

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**Benjamin Barnes  
Secretary  
Office of Policy and Management  
450 Capitol Avenue  
Hartford, Connecticut 06106**

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## I. Introduction

### A. Authority and OPM's Responsibilities

This document provides guidelines and instructions related to the use of the template the must be prescribed by the Secretary of the Office of Policy and Management (OPM) in accordance with Section (p) of C.G.S. Section 4e-16. Section (p) reads as follows:

(p) Prior to entering into or renewing any privatization contract that is not subject to the provisions of subsection (a) of this section\*, the state contracting agency shall evaluate such contract to determine if entering into or renewing such contract is the most cost-effective method of delivering the service, by determining the costs, as defined in subsection (b) of this section, of such service. The state contracting agency shall perform such evaluation in accordance with a template prescribed by the Secretary of the Office of Policy and Management and such evaluation shall be subject to verification by the secretary. The secretary may waive the requirement for an evaluation of cost-effectiveness under this subsection upon a finding by the secretary that exigent or emergent circumstances necessitate such waiver.

\*Note: Section (a) of C.G.S. 4e-16 indicates that entering into any privatization contract for the privatization of a state service that is not currently privatized, the state contracting agency shall develop a cost-benefit analysis in accordance with the provisions of subsection (b) of this section. Such requirement shall not apply to a privatization contract for a service currently provided, in whole or in part, by a non-state entity.

As defined by C.G.S. Section 4e-1, "State contracting agency" means any executive branch agency, board, commission, department, office, institution, council, or constituent unit of the State system of higher education. "State contracting agency" does not include the judicial branch, the legislative branch, the offices of the Secretary of the State, State Comptroller, Attorney General, state Treasurer with respect to their constitutional functions, or any State agency with respect to contracts specific to the constitutional and statutory functions of the Office of the State Treasurer.

As defined by C.G.S. Section 4e-1, "privatization contract" means an agreement or series of agreements between a State contracting agency and a person or entity in which such person or entity agrees to provide services that are substantially similar to and in lieu of services provided, in whole or in part, by State employees. The term "privatization contract" does **not** include contracts with a nonprofit agency which were in effect as of January 1, 2009 and which through a renewal, modification, extension, or rebidding of contracts continue to be provided by a nonprofit agency.

As defined in According to Subsection (b) of CGS 4e-16, "Costs" means all reasonable, relevant and verifiable expenses, including salary, materials, supplies, services, equipment, capital depreciation, rent, maintenance, repairs, utilities, insurance, travel, overhead, interim and final payments and the normal cost of fringe benefits, as calculated by the Comptroller. **Note:** The concept of "Normal Cost" related to retiree benefits will be described more fully in this manual.

## **B. Amendments**

The Secretary of OPM reserves the right to amend these procedures, in whole or in part, to maintain consistency with the authorizing State law or when it is determined to be in the best interest of the State of Connecticut.

## **C. Required State Contracting Agency Actions**

As required by Subsection (p) of C.G.S. Section 4e-16, prior to entering into a new or renewed privatization contract that is not subject to the provisions of (a) of 4e-16, a State contracting agency must evaluate such contract to determine if entering or renewing the contract is the most cost-effective method of delivering a service. Such evaluation shall be done using the template to be described in this manual. The evaluation shall be completed before contracting out the subject services, in order to make such determination, and shall be subject to verification by the Secretary of OPM. If a State agency is seeking to procure a service through a statewide privatization contract that is available for use by more than one agency, such agency shall, as appropriate, undertake any evaluation required by Subsection (p) prior to issuing a purchase order for use of such privatization contract.

State contracting agencies may have or utilize a number of contracts that are substantially similar to one another. In such cases, the cost evaluation required by Subsection (p) may, as appropriate, be done on such contracts as a group or with respect to one or more representative contracts. Such an approach, however, may only be taken to the extent that it provides a reasonable method of comparing if privatization contracts are the most cost effective method of delivering the service. In addition, such cost evaluations must have been completed no more than 12 months prior to the proposed start date of the new or renewed contract.

## **D. Waivers**

As indicated in Sub-section (p), the Secretary may waive the requirement for an evaluation of cost-effectiveness upon a finding by the Secretary that exigent or emergent circumstances necessitate such waiver.

Such waiver requests may be submitted to the contact person indicated in Section F, below. Any waiver requests should fully describe of the circumstances involved with such request. To the extent feasible, such requests shall be submitted in a time and manner that will allow for the cost evaluation to be completed in the event that the Secretary rejects such request.

The Secretary shall approve or reject waiver requests and may add such conditions to such approval or rejection actions that he or she may deem appropriate.

## **E. Effective Date**

These policies and procedures are effective September 29, 2014.

**F. Inquiries & Contact Information** For further information concerning these policies and procedures, contact:  
Valerie Clark- Office of Finance  
Office of Policy and Management  
450 Capitol Avenue  
Hartford, CT 06106  
E-mail: [Valerie.clark@ct.gov](mailto:Valerie.clark@ct.gov) Telephone: (860) 418-6313

## II. Procedures for a Cost Effectiveness Evaluation of a New or Renewed Privatization Contract

When required by Subsection (p) of C.G.S. 4e-16 to undertake a cost-effectiveness evaluation of a new or renewed privatization contract, a State contracting agency shall complete the template created by OPM. This template can be found on OPM's website.

The information required in each of the sections of the Template are described below.

### A. Template Questionnaire

The template questionnaire provides background and other information needed to understand the scope and type of services being contracted out. The contract information to be provided includes: contract title and description of services; need for new contract or renewal; proposed term and amount of new contract or renewal; number of years the service has been contracted out with current contractor; method of procurement; and information regarding any prior renewals.

The questionnaire also seeks information regarding the approach, implementation actions and timeframes that would be involved with bringing the service in-house. Outlining these actions and timeframes, as well as the description of the services involved, should help in making valid comparisons between the costs of contracting out and the costs of in-house service delivery.

Finally, the questionnaire requests information regarding the benefits and risks, including both quantitative and qualitative measures, that are associated with the different service delivery methods (e.g. contracting out, in-house service delivery).

### B. Projecting the Costs of Contracting Out

1. Cost of Contract (Template Form A-100): Since the services are currently contracted out, prior actual and current estimated costs of these services should be known. In order provide a better understanding of these costs and to assist in making projections for the in-house delivery of services, Form A-100 requires State agencies to identify the number of units of services received (e.g. hours of service, number of FTE's, quantity received) and the cost for each of these units of service in the prior year, for year 1 and for years 2 and 3, as appropriate. These projections should include any projected inflationary increases.

**Please note:** Hourly rates for contractors may incorporate costs such as vacation and sick time, fringe benefits, overhead, and other costs.

2. Cost of In-House Contract Management (Template Form A-200): In addition to estimating the potential cost of the contract itself, the agency must also consider the cost of administering the contract. These costs include staffing and other costs associated with contract preparation and management, monitoring contractor performance, negotiating change orders, contractor evaluation, making payments and other related fiscal work. Below is a table that offers **a potential basis** for

determining the number of contract administration staff needed to manage the contract.

<u>In-house Staffing Requirements</u>	<u>Contract Administration Staff</u>
Less than 20 FTE's	1
21-42	2
43-65	3
66-91	4
92-119	5
120-150	6
More than 150	Use 2-4% of In-house requirements

Source: Office of the State Auditor, Commonwealth of Massachusetts, March 1994

An agency may create an in-house contract management rate by function or types of contract. Agencies should explain the basis for such rate.

The Sections of Form A-200 include:

- Section A- Payroll: Payroll costs are defined as salaries and wages for full-time, part-time and temporary state employees, including overtime, longevity payments, shift differential, hazardous duty pay and all similar payroll costs. The payroll costs related to the management of the contract that is the subject of this cost-effectiveness evaluation should be included in this section. **Costs related to agency overhead or indirect costs, as described in “Section D – Agency and Central Agency Overhead”, below, should not be included in this Section (nor in Sections B and C).**
- Section B – Fringe Benefits. The fringe benefit costs related to the State employee payroll costs included in Section A of the form are included in Section B. These figures will be automatically calculated by Form A-200 by multiplying the applicable fringe benefit percentage by the payroll amounts in Form A-100 for employees eligible for such benefits. Agencies may choose to override the automatic calculations made by the form. **Please see Appendix 1 of this manual for a more complete description of fringe benefit costs and calculations.**
- Section C- Other Expenses. Other expenses related to management of the contract should be included in this section. **Please see Section C of this Manual (i.e. “Projecting the Costs of In-House Service Delivery”) for a description of the types of other expenses that should be included in this section.**
- Section D – Agency and Central Agency Overhead. Agency overhead, or indirect costs, include agency leadership, business office, personnel and legal staff as well as items such as building and utility costs which are not directly attributable to the proposed privatized service. Central Agency Overhead are those costs incurred by support functions and activities, such as the Office of the State Comptroller, Auditors of Public Accounts, and the Office of Policy and Management that benefit all departments. Form A-200 will automatically calculate the overhead costs by multiplying an average of State agency indirect rates by contract management payroll costs. Some agencies have an approved indirect rate, mostly those receiving federal funds, which may be used in this template in lieu of the pre-filled percentage and calculations. **Please see Appendix 2 of this manual for a more complete description of agency and central agency indirect or overhead costs.**
- Section E – Total Contract Management Costs. This section will automatically calculate the cost of in-house contract management, with and without indirect costs included.
- Section F – Additional Comments and Information. This section provides a space for additional information and comments related to the other sections of the form.

3. Total Cost of Contracting Out (Template Form A-300): This form, by adding the costs in Forms A-100 and A-200, calculates the total cost of contracting out, with and without agency and central agency overhead.

### C. Projecting the Cost of In-House Service Delivery (Template Form B-100)

To project the cost of in-house service delivery, a State agency would need to determine the number and type of State employees and other resources it would need to provide the currently contracted service in-house. The resources deployed by the contractor would be one source of information in this regard, with an analysis of the in-house resources used to provide similar State services potentially being another.

The Sections of Form B-100 include:

- Section A- Payroll: Payroll costs are defined as salaries and wages for full-time, part-time and temporary state employees, including overtime, longevity payments, shift differential, hazardous duty pay and all similar payroll costs. The payroll costs of direct service in-house State employees needed to provide the service in lieu of a contract should be included in this section. **Costs reflected in agency overhead or indirect costs, as described in “Section E – Agency and Central Agency Overhead”, below, should not be included in this Section (nor in Sections B and C).**
- Section B – Fringe Benefits. The fringe benefit costs related to the State employee payroll costs included in Section A of the form are included in Section B. These figures will be calculated by Form B-100 by multiplying the applicable fringe benefit percentage by the payroll amounts in Form A-100 for employees eligible for such benefits. If your agency has specific fringe rates it would like to include, these values may be overridden to accommodate such changes. **Please see Appendix 1 of this manual for a more complete description of fringe benefit costs and calculations.**
- Section C- Other Expenses. Other expenses related in-house service delivery of the service in question should be included in this section. Definitions for the “Other Expense” line-items in the template are included below (**Please Note: Other Expense costs, like other direct costs, should be for those costs directly associated with the delivery of the service. Shared agency-wide costs should be included in your indirect rate**)

#### Line-Item Number

1. Contracted Services. Outside person or entity providing work or services under a contract or agreement.
2. Materials & Supplies. Printing and Postage. Commodities, goods or other consumables obtained from outside suppliers, including printing costs, along with software and other licenses.
3. Rent and Utilities. Rent is the cost of renting/ leasing of property, equipment or facilities directly used in performing the service. DAS would be able to provide information for properties or facilities within Hartford or other properties that they manage and pay for. Utilities includes fuel, electricity, water, and sewer, along with wire line and wireless telecommunications services, e-mail and internet services and cable costs.
4. Insurance. Insurance involves costs for the protection against potential financial loss that the organization is required to carry specifically for this service; or any other such protection that an organization maintains in connection with the general conduct of this service. This definition of insurance does not include fringe benefits for employees.
5. Maintenance and Repair. These costs are for the necessary preservation, care or upkeep of buildings or equipment directly related to this service that neither add to the permanent value



of the property nor appreciably prolong its intended life, but keep it in an efficient operating condition.

6. Depreciation. Under the concept of the conversion of expenditures to expenses, capital equipment or improvement costs (defined as equipment or capital improvements costing over \$5,000) must be allocated over the period of benefit to reflect consumption of resources. This amount should be included in the Depreciation line-item. Depreciation should be calculated by dividing the depreciable basis or current cost by the estimated life or remaining life of the asset. Depreciable basis is defined as acquisition cost plus transportation and installation costs. Real property (buildings, land, etc.) often have an estimated life of up to 20 years, while equipment may be in the 5 to 7 year range.
  7. Non-capital Equipment (under \$5,000). Equipment is defined as nonexpendable, tangible personal (non-real estate) property with a normal useful life of at least one year. **NOTE: Expenditures for equipment with an acquisition cost of \$5,000 or greater are considered capital expenditures and should be amortized using the Depreciation line-item.**
  8. Travel and Training. Travel and transportation costs include vehicle costs, including leases and rentals, gasoline and vehicle repairs, mileage costs, air or train transportation, and, lodging, meal and other expenses associated with non-training related travel. Cost of training for personnel along with any registration fees, transportation, meals and other costs associated with training.
  9. Other. Other expenses, not otherwise listed, should be specified.
  10. One-time Start-up Costs. These costs would include the one-time training and other costs associated getting the service established and set up in-house.
- Section D – Transition Costs Related to Bringing the Service In-House. Transition costs are those contract-related costs, both one time and recurring, that are associated with moving from contracting the service to bringing it in-house. Examples of such costs include costs related to termination provisions in the contract or the need to have an overlap of contractor and in-house costs during the transition period. **Please note: One-time start-up costs for the State to deliver the service should be included in the direct cost portion of the template (i.e. Section C, above)**
  - Section E - Agency and Central Agency Overhead. Agency overhead, or indirect costs, include agency leadership, business office, personnel and legal staff as well as items such as building and utility costs which are not directly attributable to the proposed privatized service. Central Agency Overhead are those costs incurred by support functions and activities, such as the Office of the State Comptroller, Auditors of Public Accounts, and the Office of Policy and Management that benefit all departments. Form B-100 will calculate the overhead costs by multiplying an average of State agency indirect rates by contract management payroll costs. Some agencies have an approved indirect rate, mostly those receiving federal funds, which may be used in this template. **Please see Appendix 2 of this manual for a more complete description of agency and central agency indirect or overhead costs.**
  - Section F – Total Costs. This section will automatically calculate the cost of in-house service delivery, with and without indirect costs included.
  - Section G –Additional Comments and Information. This section provides a space for additional information and comments related to the other sections of the form.

#### **D. Summary of Costs: Contracting Out and In-House Delivery** *(Template Form C-100)*

This form summarizes and compares the costs of contracting out and delivering the services in-house. The form automatically calculates the (costs) or savings related to contracting out the service compared to in-house delivery of the service.

### III. Appendices

#### **Appendix 1-Description of Fringe Benefits**

The Office of the State Comptroller annually issues a memorandum at the beginning of the fiscal year to the heads of all state agencies which outlines the Fringe Benefit Cost Recovery Rates for that fiscal year. The memorandum can be found at: <http://www.osc.ct.gov/2014memos/index.html>. These rates are generally in the form of a percentage of payroll. When doing an evaluation, these percentages should be applied to the total payroll amounts found in Sections A of the Template. **NOTE: These percentages are pre-populated and calculated in the template for your convenience. State agencies can, however, choose to override these calculations.**

The fringe benefit categories included in the Comptroller's memorandum include:

- i. Unemployment Compensation
- ii. Retirement Employer Normal Cost of pension and Retiree Health Insurance: Guidance on rates for the normal cost of the State Employee Retirement System (SERS) for both regular and hazardous duty SERS employees can be found in the Office of the State Comptroller's Fringe Benefit Cost Recovery Rates Memorandum. Please note that the unfunded liability related to the SERS retirement plan has been removed from the rate. The current regular SERS employee and the hazardous duty SERS employee has been prefilled in the template.
- iii. Social Security. Federal percentage of salaries/wages up to the federal wage maximum
- iv. Medicare. Federal rate
- v. Employer Portion. Life Insurance: State Share Premium\*
- vi. Employer Portion. Medical & Dental: State Share Premiums for Medical, Dental and Prescription Coverage.\*
- vii. Worker's Compensation. The cost of Workers' Compensation at your agency may be centrally managed by DAS. If it is, please refer to the Office of the State Comptroller's memorandum pertaining to this topic (<http://www.osc.ct.gov/2013memos/numbered/201317.htm>) and use the "general agency" rate as listed. If your agency budgets its own Workers' Compensation, please locate the rate assigned to your agency as listed in the aforementioned memo.

\* Note: Since November 2003, with the implementation of the Core-CT HRMS module, the state share of certain fringe benefits has been charged to agencies on an actual cost basis. This includes group life insurance and medical insurance, which are calculated based on the actual cost of the state's share of insurance premiums, including for each individual employee. If you are making projections for new or vacant positions, please estimate based on actual costs associated with those for your agency as a whole. When there are vacant positions, some assumptions as to salary levels, number of dependents, etc., may need to be made. **The provided template is pre-populated using a statewide average of the State's share of employee medical and dental benefit costs as a percent of salaries.**

Definition of Normal Cost for Pension and OPEB: The Normal Cost, also known as the annual benefit cost, generally represents the portion of the cost of projected benefits allocated to the current plan year. The Normal Cost does not include the portion of the Actuarially Required (ARC) contribution that addresses a pension or OPEB plans unfunded liability. The unfunded liability portion of the ARC relates to funding issues associated with prior years and does not relate to the cost of benefits being earned in the current year. Section 4e-16 requires the use of the Normal Cost for retirement benefits when doing an evaluation.

## **Appendix 2-Description of Overhead (or Indirect) Costs**

Also known as overhead costs, these items include those that benefit two or more direct services or functions. There are generally two types of indirect costs: agency overhead and central services overhead.

- A. Agency Indirect Costs. Agency indirect costs, or overhead, include agency leadership, business office, personnel and legal staff as well as items such as building/utility costs which are not directly attributable to the proposed privatized service. To recover indirect costs associated with a federal grant, a number of state agencies have developed an indirect cost rate. This rate has to be approved by the federal government in order for it to be used to recover indirect costs through a federal grant. The indirect cost rate is a ratio (expressed as a percentage) that is multiplied by the direct salary base of the federal grant to arrive at the amount of indirect costs, or direct salaries plus fringe benefits and other expenses in some agencies, depending on the indirect cost methodology used. When doing a cost evaluation of a privatization contract, the indirect rate would be applied to the applicable cost base of the direct in-house service costs and to the cost of in-house contract management.
- B. Central Services Overhead. These costs are those incurred by support functions and activities, such as the Office of the State Comptroller, Auditors of Public Accounts, and the Office of Policy and Management that benefit all departments. The Office of the State Comptroller, as required by the federal government, develops the Statewide Cost Allocation Plan (SWCAP), which allocates the cost of these central services to twenty or so state agencies.  
(<http://www.osc.ct.gov/2013memos/numbered/201319.htm>)

The allocation of these costs to twenty state agencies account for approximately 93 percent of the total central agency costs, with the remaining amount being for services provided to all other state agencies. State agencies having an agency overhead indirect cost can add the SWCAP amount to their indirect costs to arrive at a percentage of costs (i.e. indirect rate) that includes the central agency indirect costs.

**Again, the template calculates these indirect costs based on an average of state agency indirect cost percentages, which percentage is multiplied by total payroll costs. If your agency has an indirect rate, you would be able to override the percentages and the calculations included in the template.**