

Statement of Prof. Gordon Lafer

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Thank you for the opportunity to submit testimony.

My name is Gordon Lafer, and I am an Associate Professor at the University of Oregon's Labor Education and Research Center. I hold a PhD in Political Science from Yale University, and have been called to testify as an expert witness before the U.S. Congress and several state legislatures. In 2009-10, I was on leave from the UO to serve as Senior Policy Advisor for the U.S. House of Representatives' Committee on Education and Labor.

Over the past fifteen years, I have studied multiple cases of school districts contracting out food service, custodial and bus drivers. I want to tell you today about some of the disturbing facts uncovered during the course of that research, that may be useful in determining how best to safeguard taxpayer dollars when making decisions regarding contracting-out.

Before describing what we found, I'd like to make two things clear:

- I have not made a cent in my pocket from any of this research, and therefore I have no financial incentive whatsoever on this issue. I am paid one salary – by the generous taxpayers of the state of Oregon – and one salary only. As UO faculty, we are held to only one standard – that our research be impartial and rigorous.
- Not all, but most of what I want to share comes a study of the Central Point School District's decision to contract out school transportation to the First Student corporation. This is the first case of contracting-out in the state since the adoption of ORS 279. Because it was subject to litigation, a lot of information has come out in public that is not normally available on these type of contracts, so it's a good case to learn from.
 - When my analysis of that contract was completed – but before it was published – I sent a copy to the financial and HR directors of Central Point School District. At their request, I also allowed them to share the pre-publication copy with the District's consultant, who also has worked for First Student. I asked them to please identify any statements in the report they believed were factually incorrect, so that I could correct them before publication. They asked for six weeks to

review the report, which I agreed to. After six weeks, they did not identify a single number in the report as factually incorrect.

As you think about how to make sure the law is functioning the way you want, there are four issues I think are critical to consider, that have come up in our research:

- Making sure all costs are included, including the state. In transportation, the state reimburses 70% of all district costs. But I have seen cost-benefit analyses where a school district announces some level of guaranteed savings – based only on the district’s expenses but not the state’s. Current law does not specify that the state share of costs has to be taken into account – it’s common sense, but it’s not specified in the law. But “cost-benefit” should include all costs to Oregon taxpayers.
- Current law says that agencies must show two things: that contracting out will produce a net cost savings, and that that savings won’t come simply from wage and benefit cuts. We need to make sure all information is available to make that calculation.
- Some costs don’t show up until several years down the road. I’ve seen cost-benefit analyses that look only at Year 1, and therefore include a one-time infusion of cash from selling off a bus fleet, but do not include the long-term costs of buying many more new buses (as demanded by a private contractor) than the District would have done if it kept transportation in-house. The analysis has to go far enough out to capture a realistic balance of the financial pro’s and con’s of contracting out.
- There must be some mechanism to effectively monitor and enforce the requirements written into law. In the past there has been exactly one person in the state of OR responsible for school transportation. This means that requirements that exist on paper may be ignored in reality. If legislators don’t want to fund a huge enforcement staff, which I assume they do not, then some other mechanism is needed to make sure the legislature’s wishes are carried out.
- I will give examples of each of these issues.

Problem 1: Cost-Benefit analyses that ignore the state's share of transportation costs and treat state tax dollars as "free money." The Lake Oswego school district contracted with First Student on terms that included what was essentially a one-time \$400,000 loan from the company to the District. The repayment of this loan was tacked on to the per-mile charge for bus service and submitted to the state as "transportation costs." Thus the state picked up 70% of the cost for repaying this loan. The result was a cost-saving for the district – but at the expense of state taxpayers. Because this cost was not included in the cost-benefit analysis, it produced a seemingly positive result.

SLIDE - INFORMATION NEEDED FOR COST-BENEFIT ANALYSIS

Problem 2: Insuring there's enough information to make the needed comparisons. According to the language of ORS 279B.033, contractors must provide

- "Actual salary or wage and benefit costs for ... employees"
- "Material costs, including ... space, energy, transportation... equipment and supplies"
- "Miscellaneous costs... including ... reasonably foreseeable fluctuations in the costs for the items identified" above.

But in the case of Central Point, none of this was provided. And critically – when the Central Point-First Student was challenged in court, at least at the District level, the court ruled that it was ok for none of this information to be provided. So additional legislative language must be needed to clarify that districts are, indeed, required to produce this information.

It turns out that, after contracting out, wages and benefits of employees providing bus service in Central Point fell by 47%. This information was discovered by a team of investigators at the UO who worked intensively to piece together details of this case. But the state obviously needs a much simpler, transparent process to get information quickly and easily, without having teams of people investigate each contract.

So if Central Point cut employee compensation by 50%, how could they still generate net savings that was NOT from wage and benefit cuts? They couldn't. Our team at UO analyzed the actual costs of this contract in extensive detail,

using four different methodologies. By some calculations, they district ended up with small net savings; others show that there is a net financial loss from contracting out. But *all* of them show that if there's any net gain, it comes entirely from wage and benefit cuts.

The District simply provided some fictional information to the state, and in other cases omitted information. Because there is no strict oversight mechanism, this was possible.

Problem 3: Cost-benefit analysis must be conducted by projecting costs out over a reasonable time period. The biggest problems in the Central Point cost-benefit analysis was the omission of key costs that occur after year 1:

- First Student insists on replacing buses much sooner than the District would. The cost-benefit analysis assumed that the District would buy the same number of buses either way – but this is false.
- First Student's fees were contracted to rise faster than the rate of inflation, therefore changing the cost-benefit analysis over time.
- First Student bought the District's fleet – but then built the purchase price into their per-mile charges so that over the five-year contract, the District would pay for 100% of the purchase price. But – if the District had retained ownership of the buses, at the end of this five-year contract it would have owned assets worth \$875,000 – even after depreciation. One of the costs of contracting-out was giving up this asset. But this was never included in the calculation.

If you add up everything, you see that contracting-out resulted in a large net loss to the District – except for being made up by huge cuts in wages and benefits.

But the language in statute is apparently not clear enough to require contractors, Districts or Court officials to demand sufficiently clear information to reveal all these facts. And there is no cost-effective oversight or enforcement mechanism to police this.

Problem 4: the need for more effective oversight and enforcement.

When school buses are not being used to transport students, First Student uses them to operate a private charter company, renting out buses to weddings, corporate outings, or transportation to casinos. This happens at Central Point and in other Oregon school districts – sometimes in direct violation of a contract. Furthermore, the increased costs of wear and tear on the buses are paid for entirely by the public. Gas, maintenance and repair costs may be as well.

Currently, neither districts nor the state has an effective way of monitoring such practices.

The schedule of bus purchases in a district should be based on one thing only: what's good for the kids. And if companies want to run private charter business with taxpayer-bought buses, then taxpayers should be compensated by the same rate per mile that school districts otherwise pay.

In conclusion, it seems that stronger language might go a long way toward ensuring that legislators' intent is carried out in reality.

I hope that our research may be of some help in formulating a way forward on this issue.

Thank you again for the opportunity to contribute to the legislature's consideration of this topic.