A CALIFORNIA LOCAL PUBLIC AGENCY’S GUIDE TO LAWFUL OUTSOURCING

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In the aftermath of a recession and lower property and sales tax revenues, local public agencies have been forced to operate on slimmer budgets. Some have saved costs by contracting out agency services, such as road repair and wastewater treatment, to private companies or other public agencies.

However, some agencies have found themselves embroiled in litigation following an outsourcing decision. The risks of improper outsourcing include litigation concerning the lawfulness of the decision, injunctions and reinstatements, unfair labor practice charges, arbitration costs, and claims for pension benefits. However, if done properly, outsourcing need not be a legal minefield.

Public agencies wishing to outsource must first determine:

- Which statutes apply?
- Which full-time public agency staff positions can be outsourced?
- What Labor issues and other risks are involved in doing so, and how can they be avoided?

THE LAW GOVERNING OUTSOURCING

A public agency cannot contract out to the private sector services which are expressly required by law to be performed by a designated public official. (Jaynes v. Stockton (1961) 193 Cal.App.2d 47, 54.) However, under Government Code section 54981, a local agency “may contract with any other local agency for the performance . . . of municipal services or functions.”

The California Government Code contains two other key statutory limits on outsourcing. The first restricts the types of positions that may be outsourced to “special services” positions. The second requires a good faith economic reason for the elimination of a non-department-head city position.¹

¹ These statutes are not applicable to charter cities which have “nearly complete control over [their] municipal affairs and [are] not bound by the general laws of the state.” (San Francisco v. Boyd (1941) 17 Cal.2d 606.) Charter cities have “plenary authority to provide for the `compensation, method of appointment, qualifications, tenure of office and removal’ of their employees.” (Riveros v. City of Los Angeles (1996) 41 Cal.App.4th 1342, 1359, fn. 16.)
The Government Code’s “Special Services” Statutes Place Limits on Outsourcing

Under Government Code section 53060, applicable to public and municipal corporations and districts, only “special service” positions can be eliminated then outsourced to a contractor. Positions may be outsourced if they require “special services and advice in financial, economic, accounting, engineering, legal, or administrative matters if such persons are specially trained, experienced and competent to perform the special services required.” (Govt. Code § 53060; see also Govt. Code § 37103.)

Similarly, under Government Code section 37103, applicable to cities, an agency may “contract with any specially trained and experienced person, firm, or corporation for special services and advice in financial, economic, accounting, engineering, legal, or administrative.” (See also Gov’t Code § 31000 [applicable to counties].)

“Non-special” positions may be eliminated for good faith budgetary reasons—but not outsourced. The question of whether a position is sufficiently “special” to allow it to be outsourced is a question of fact. (California School Employees Ass’n v. Sunnyvale Elementary School District of Santa Clara County (1973) 36 Cal.App.3d 46, 61.) Factors considered are the “nature of the services; the necessary qualifications required of a person furnishing the services; and the availability of the services from public sources.” (Service Employees Intern. Union, Local 715, AFL-CIO v. Board of Trustees of West Valley/Mission Community College District (1996) 47 Cal.App.4th 1661, 1673.)

Courts have held public agencies can contract out a number of functions, including the following:

- Legal services. (19 Ops. Atty.Gen. 153 (1952) [outside legal counsel o.k. where unique or special skills are necessary to render services or where district counsel is disqualified or refuses the case].)
- Research and development. (Cal. School Emp. Ass’n v. Sunnyvale Elem. Dist. of Santa Clara County (1973) 36 Cal.App.3d 46, 62-64 [outsourcing research and development of new and improved techniques, methods and systems for the management and control of school property and equipment].)
- Services that cannot be performed by the public agency. (Ibid.)
- Grounds-keeping/grounds-maintenance. (See California School Employees Association v. Kern Community College District Board of Trustees (1996) 41 Cal.App.4th 1003, 1009-1012 [non-merit school district’s outsourcing of grounds-keeping does not violate Education Code].)
The California Attorney General has issued opinions stating if a position does not require specialized services and is currently being performed by public employees, it cannot be outsourced. (85 Ops.Cal. Atty.Gen. 83, 86 (2002); 76 Ops.Cal. Atty.Gen. 86 (1993).) In a pending case in Orange County, City of Costa Mesa argued any positions may be outsourced, provided they are not required by law to be performed “in-house” by a public agency employee. (Costa Mesa City Employees Ass’n v. City of Costa Mesa (2012) 209 Cal.App.4th 298, 315.)

Recently, the Court of Appeal rejected Costa Mesa’s broad reading of the law, and rejected the City’s reliance on the following cases:

- California School Employees Association v. Kern Community College District Board of Trustees (1996) 41 Cal.App.4th 1003 addressed whether a local agency could contract with a private vendor to provide grounds-keeping services that, at the time, were being performed by the local agency’s classified employees. The Kern court held this contract was proper because the local agency was not “required by law” to have its own employees perform this function. (Id., at p. 1006.) The Court of Appeal said this case is inapplicable to Costa Mesa’s situation because it does not address the “special services” statute. (Costa Mesa City Employees Ass’n, supra, 209 Cal.App.4th at p. 314, fn 7.)

- The Court in Service Employees International Union, Local 715, AFL-CIO v. Board of Trustees of the West Valley/Mission Community College District (1996) 47 Cal.App.4th 1661 (“SEIU”), held an agency was permitted to contract with a private vendor to replace its bookstore clerks. The court reasoned the law “does not require that all work be performed by the classified employees” of a local agency. (Id. at pp. 1666, 1672.) The court emphasized the move would save money. Further, the private book store could provide expertise in bookstore management and operation which the District lacked; thus, the services were sufficiently “specialized.” However, the Court of Appeal, in Costa Mesa, distinguished the SEIU case from Costa Mesa because in SEIU, the scope of outsourcing was smaller and all employees kept their jobs. (Costa Mesa City Employees Ass’n, supra, 209 Cal.App.4th at p. 313.)

The Court of Appeal disagreed with Costa Mesa’s reading of these cases, emphasizing some of the cases cited by Costa Mesa did not discuss the “special services” statute at all. The Court upheld a preliminary injunction to stop Costa Mesa’s outsourcing plan, stating there is a likelihood of union success on the merits. (Costa Mesa City Employees Ass’n, supra, 209 Cal.App.4th at pp. 309-316.) The court stated, at the final trial on the merits, the court must examine each position to ascertain whether it is “special.” Thus, the most cautious approach is to examine job duties and only outsource positions that are “special,” i.e. those that require particular training and experience and are not required to be performed by a city employee.

**Government Code Section 45007 Limits Elimination of Civil Service Positions**

The second important statute on outsourcing is Government Code section 45007 which prohibits a city from re-designating permanent civil service positions as at-will exempt city positions—absent a vote of electors. Government Code Section 45007 states:

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2 The Court of Appeal was reviewing the trial court’s granting of a preliminary injunction against the outsourcing of certain positions.
“After inclusion in the civil service system, any departments or appointive officers or employees shall not be withdrawn, either by an outright repeal of the Civil Service ordinance or otherwise, unless the withdrawal has been submitted to the city electors at a special or regular municipal election and approved by 2/3 of those voting on the proposition, except that regular full-time city department heads, may be withdrawn by a majority vote of the city council.”

Courts have interpreted section 45007 as allowing positions to be eliminated due to budgetary constraints, provided such action is taken in good faith. (See Cal.Jur. §§ 354, 359; Rains v. County of Contra Costa (1951) 37 Cal.2d 263; Placer County Employees Assn. v. Board of Supervisors (1965) 233 Cal.App.2d 555, 559.) Where the action taken is truly a “sham attempt” to abolish civil service through piecemeal dissolution of permanent city positions, or an attempt to get rid of a particular employee, courts invalidate the action. If it appears the city is “laying-off” certain employees it dislikes and hiring others, such action will be invalidated by the courts. California case law provides guidance on what types of actions are considered “bad faith” or “sham.”

- In Trujillo v. City of Los Angeles (1969) 276 Cal.App.2d 333, 337-339, the Court did not cite 45007 but found an employee’s removal to be in bad faith where a civil service position was eliminated and the position was given to the employee’s assistant.
- In Rexstrew v. City of Huntington Park (1942) 20 Cal.2d 630, 632-634, the court found an elimination of positions was not taken in good faith where 9 police officers and firemen were discharged by resolution for economic reasons, when in fact, the city treasurer admitted there was “plenty of money to pay these salaries.”
- In Hanley v. Murphy (1947) 40 Cal.2d 572, superintendents of jails were improperly laid off when their department head omitted their positions from the annual budget, gave their duties to others, and did not notify the civil service commission of these actions—in violation of the civil service regulations and charter. Evidence also showed the two eliminated positions were necessary to the functioning of the jails. Thus, the lay-offs were taken in bad faith.
- In Childress v. Peterson (1941) 18 Cal.2d 636, lay-off notices to “policewomen” were defective. Despite the city’s allegation there were insufficient funds for two positions and despite the city’s statement the positions were eliminated, evidence showed the opposite. Whether the defective notice was due to bad faith or error, it could not support the lay-offs.
- In Charamuga v. Cox (1962) 207 Cal.App.2d 853, Charamuga’s position was “eliminated” on paper, but was, in fact, filled by two others who were not qualified under civil service rules. There were sufficient funds for the position; no position re-survey was conducted, and the two individuals who replaced Charamuga made twice his salary. Therefore, his position was not eliminated in good faith, and he was reinstated.
- In Placer County Employees Assn. v. Board of Supervisors (1965) 233 Cal.App.2d 555, 559, the county established a central servicing bureau to perform data services using new tabulating and processing machines. Two ordinances abolished the positions of Addressograph Operator and Duplicating Supervisor. A new position, Supervisor of Central Services, was added. A county ordinance required voter approval for repeal of
civil service or for an amendment that nullifies civil service. However, the court found 
the lay-offs did not nullify civil service.

- In *Rains v. County of Contra Costa* (1951) 37 Cal.2d 263, the board of supervisors 
removed all physicians from the county civil service and placed them in exempt status. 
The county civil service ordinance required voter approval to repeal the civil service 
ordinance. The court found there was no outright repeal of civil service and upheld the 
change.

A claim brought for bad faith elimination of a civil service position is one of the few cases 
where a court can inquire into the motives of legislators. (See *Trujillo v. City of Los Angeles* 
(1969) 276 Cal.App.2d 333, 337-339; *Rexstrew v. City of Huntington Park* (1942) 20 Cal.2d 630, 
632-634.) For example, a court may consider a city’s failure to conduct an efficiency study as 
evidence of bad faith. (*Trujillo, supra*, 276 Cal.App.2d at pp. 337-339.) Courts will consider 
whether the city actually had a budgetary problem that required reorganization. (*Rexstrew, supra*, 
20 Cal.2d at pp. 632-634.)

**The Health and Safety Code Allows Outsourcing of Certain Positions**

Health and Safety Code section 34144(a), applicable to community development 
commissions, states in part:

“A commission may select, appoint, and employ such permanent and temporary 
officers, agents, counsel, and employees as it requires, and determine their 
qualifications, duties, benefits, and compensation, subject only to the conditions 
and restrictions imposed by the legislative body on the expenditure or 
encumbrance of the budgetary funds appropriated to the commission.”

Health and Safety Code section 34145(a) states in part:

“In addition to all other powers and authorities of the commission, the 
commission may hire, employ, or contract for staff, contractors, and consultants, 
or the commission may use community staff, contractors or consultants under 
contract or other arrangements with the community at the expense of the 
commission, the community, the redevelopment agency, or the housing 
authority.”

In *SEIU Local 1021, AFL-CIO v. County of Sonoma* (July 11, 2014) 2014 DJDAR 9061, 
the court applied Health & Safety Code section 34144 and 34145 to hold a county community 
development commission could lawfully contract out overflow housing inspection to achieve 
cost savings. More broadly, the court held housing inspection may be outsourced, and 
Government Code 53060 is not an impediment because the more specific provisions of Sections 
34144 and 34145 control.
EMPLOYEES INCORRECTLY DESIGNATED “CONTRACTORS” MAY CLAIM PENSION BENEFITS

Agencies must ensure independent contractors are truly independent and are not misclassified employees. Otherwise, contractors may attempt to claim an entitlement to public pension benefits. (Metropolitan Water District v. Superior Court (Cargill) (2004) 32 Cal.4th 491, 508-509.) For example, if there are long-term contractors performing the same job, in the same office, with the same level of supervision and accountability to the agency, at the same number of hours as employees, contractors may claim they are truly common law employees entitled to CalPERS enrollment. (See ibid.) Agencies may negotiate an exception to CalPERS contracts for long-term project workers. (Govt. Code § 20502.)

LABOR ISSUES RELATED TO OUTSOURCING

If contracting out is based on an agency’s desire to save labor costs, the decision itself requires negotiations. An employer wishing to outsource work performed by represented employees should negotiate the decision and the effects with timely notice to the employees’ association.

The courts apply a three-part test to ascertain whether a management decision is within the scope of bargaining:

“First, we ask whether the management action has `a significant and adverse effect on the wages, hours, or working conditions of the bargaining-unit employees. . . . If not, there is no duty to meet and confer . . . Second, we ask whether the significant and adverse effect arises from the implementation of a fundamental managerial or policy decision. If not, then . . . the meet-and-confer requirement applies. . . . Third, if both factors are present—if an action taken to implement a fundamental managerial or policy decision has a significant and adverse effect on the wages, hours or working conditions of the employees---we apply a balancing test. The action is within the scope of representation only if the employer’s need for unencumbered decision making in managing its operations is outweighed by the benefit to employer-employee relations of bargaining about the action in question.’ . . . In balancing the interests to determine whether parties must meet and confer over a certain matter (§ 3505), a court may also consider whether the `transactional cost of the bargaining process outweighs its value.’” (Rialto Police Benefit Assn. v. City of Rialto (2007) 155 Cal.App.4th 1295, 1301 [quoting Claremont Police Officers Assn. v. City of Claremont (2006) 39 Cal.4th 623, 637-638 which applies a three-part test from Building Material & Construction Teamsters’ Union v. Farrell (1986) 41 Cal.3d 651, 663-665].)

Courts applying this test to outsourcing have held an employer wishing to outsource work performed by represented employees must negotiate both the decision to outsource and the effects. (Rialto Police Benefit Assn. v. City of Rialto (2007) 155 Cal.App.4th 1295, 1309; see
CRP v. NLRB (1981) 452 U.S. 666, 680 (must negotiate outsourcing decisions that are based on a desire to save money).\(^3\) Effects bargaining must occur at a meaningful time and in a meaningful manner, with timely notice to the union of the decision. Effects bargaining must occur sufficiently before actual implementation of the decision. (See *ibid.*) The union may consider whether the employer offers severance, transfers or retaining.

A Collective Bargaining Agreement may contain language on outsourcing which further restricts outsourcing. There may even be language allowing an employer to outsource subject to a notice and meet and consult requirement over process, order of layoffs, and impacts. For example, the MOU at issue in the *Costa Mesa* case states in part:

“It is recognized that as prudent professionals, the ongoing evaluation of costs should be a collective process of sharing information on a participative basis to develop sound decisions and appropriate practices. The City is interested in involving the employee associations to the greatest degree in this regard; and, as such, agrees to make them part of discussions regarding the contracting of services. . . . Should a decision be made to contract out for a specific service which is at the time being performed by employees covered by this MOU, the employees affected will be given sufficient notice (a minimum of six) months in which to evaluate their own situation and plan for their future. To this end, the City will make every effort to transfer and utilize regular attrition in making the necessary adjustments. The City will assist employees in this endeavor through training and through preferential treatment (under meritorious conditions) when [filling] vacancies . . . In the event a decision is made by the City to contract out for a specific service performed by City employees, the City will give the affected employees a minimum of six (6) months advance notification in which to evaluate their own situation and assist in planning for the future. The City shall meet and consult with CMCEA on which matters as the timing of the layoff and the number and identity of the employees affected by the layoff . . . Thirty (30) calendar days before the effective date of the layoff, the appointing authority shall notify the Administrative Services Director of the intended action with reasons therefor.”

In *Costa Mesa*, the court interpreted this language as follows:

“The MOU does not prohibit outsourcing altogether. Nor does it give CMCEA a veto over such plans. . . . It simply requires the City to include the CMCEA in the process of evaluating costs and developing effective work practices, which may include the contracting out of services.”

(*Costa Mesa, supra,* at pp. 309-310.)

**Conclusion**

In conclusion, public agencies can outsource special services. (Govt. Code § 53060; see also Govt. Code § 37103.) Civil Service positions may not be eliminated in bad faith or as a way of firing an unpopular employee. (Govt. Code § 45007.)

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\(^3\) A rare exception to bargaining is recognized for a significant change in the nature and direction of a company’s business where the purpose of outsourcing does not turn on labor costs but on an entrepreneurial decision. However, even in this case, the effects should be bargained.
Agencies should review their Collective Bargaining Agreements for language restricting outsourcing. An employer wishing to outsource work performed by represented employees must negotiate the decision to outsource and the effects. Effects bargaining must occur at a meaningful time and in a meaningful manner, sufficiently before implementation of the decision, with timely notice to the employee’s association of the decision.

Finally, ensure that “independent contractors” are truly independent and not employees; otherwise, these individuals may qualify for pension benefits.

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