

# Secretary of State Audit Report

Kate Brown, Secretary of State

Gary Blackmer, Director, Audits Division



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## Agencies Ensured Contracts With Former State Employees Were Properly Awarded

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### Summary

In early 2011 a highly-publicized instance of questionable contracting practices involving a former state employee led to the reassignment of one state agency manager and the dismissal of another. Later that year, at the request of the Oregon Department of Administrative Services, we began an audit of personal services contracts awarded to former state employees. While this audit was requested in response to the discovery of the questionable contracting practices, the topic of contracting for services has become more important as state agencies, boards, and commissions seek ways to deliver services with reduced budgets and fewer employees.

The objective of this audit was to determine whether state agencies, boards, and commissions awarded personal services contracts to former state employees in accordance with contracting laws, rules and best practices.

Personal services contracts are used to acquire specialized skills, knowledge, technical or scientific expertise, and professional management or judgment. Oregon statutes and administrative rules govern the process of creating and awarding personal services contracts. They require transparency and impartial competition when awarding state contracts in order to promote the efficient use of state resources and ensure that the state receives the best value.

We reviewed personal services contracts with former state employees at 10 agencies, as well as personal services contracting practices at a board and a commission. All of the contracts we reviewed were awarded in accordance with state contracting laws and rules. Additionally, we did not find evidence that former state employees were given an unfair advantage over other potential contractors, nor did we identify instances where contractors appeared to be working more as an employee than a contractor.

During our audit, we also found that the agencies we visited have adopted contracting best practices and have implemented many of

our prior audit recommendations relating to personal services contracting.

While we have no statewide recommendations, we did identify and discuss opportunities to improve personal services contracting practices at individual agencies.

## **Agency Response**

The agency response is attached at the end of the report.

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## Background

In June 2011, at the request of the Oregon Department of Administrative Services we began an audit of personal services contracts awarded to former state employees. The request came after one agency manager was reassigned and another dismissed after a highly-publicized instance of questionable contracting practices involving a former state employee. This incident raised concerns about whether former state employees are provided an unfair advantage over other potential contractors.

The objective of this audit was to determine whether state agencies, boards, and commissions awarded personal services contracts to former state employees in accordance with contracting laws, rules, and best practices.

### Personal Services Contracts

Personal services contracts are used to acquire specialized skills, knowledge, technical or scientific expertise, and professional management or judgment. Specific examples include project managers, physicians, engineers, and consultants. Personal services contracts are used for limited duration projects and often supplement an agency's workforce during temporary periods of heavy workloads, or to fulfill the duties of employee positions an agency is unable to fill.

As shown in the diagram below, various state laws and rules govern how the state procures services with personal services contracts. The Public Contracting Code, which establishes methods of awarding public contracts and provides general guidance to both contractors and state agencies, is implemented through two sets of administrative rules - the Department of Administrative Services' (DAS) Public Contracting Rules and the Department of Justice's (DOJ) Model Rules. Many state agencies are explicitly assigned to either the DAS Public Contracting Rules or the DOJ Model Rules. Those that are not must adopt one of the rule sets, or create their own rules within agency policies.

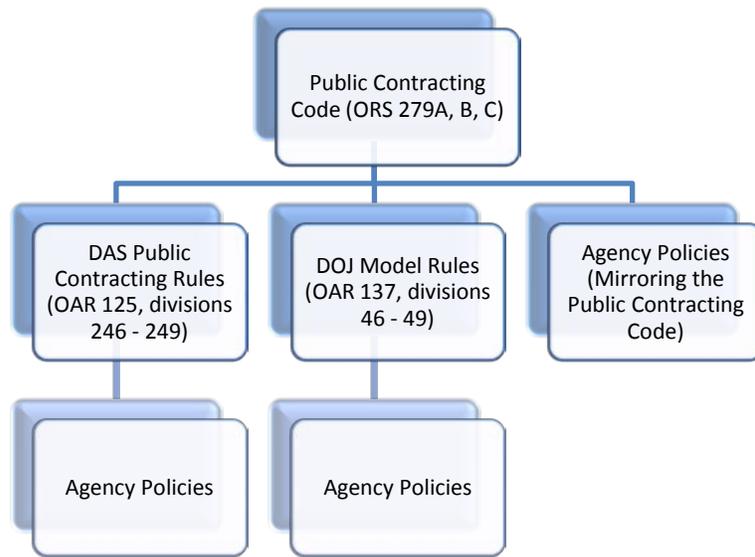


Figure 1 Hierarchy of Procurement and Contracting Regulations in Oregon

### ***Former State Employees as Contractors***

It is not uncommon for former state employees, including retirees, to return to state service as personal services contractors. In fact, agencies can benefit from the knowledge and understanding that former employees have about the agencies and their programs, clients, etc. Specific experience and training in state agency programs can make a former state employee highly qualified and effective at performing the work required under a personal services contract.

The laws and rules described above do not specifically address former state employees acting as contractors. However, like all potential contractors, former state employees are subject to the laws and rules regarding competitive selection. This means they must submit the same materials, within the same timeframes, and be evaluated by the same criteria as would anyone who competes for a state contract.

In addition, state ethics laws generally prohibit state employees from using their position to obtain a financial gain for themselves, a relative or member of their household, or a business with which any of them may be associated. State ethics laws also prohibit former state employees from attempting to further the gain of any person by using confidential information obtained during the course of, or by reason of, their position as a public official. Last, the ethics laws prohibit former employees who served on contract selection committees or similar groups from having a personal financial interest in those contracts for two years after the date the contract was authorized.

Agency policies regarding former employees acting as contractors range from not allowing it at all, to requiring a period of time where former employees are unable to bid on contracts associated with their former agencies. Most agencies with such policies expand on the conflict of interest statutes. A typical policy would require employees serving on a selection committee to disclose any relationships with potential contractors and to provide a signature acknowledging and agreeing to adhere to ethical requirements. The goal of these policies is to identify any issue that could influence the objectivity of someone evaluating bid proposals or even create the appearance of a biased evaluation. Identified conflicts of interest must be mitigated or the employee cannot serve on the selection committee. The Oregon Department of Transportation (ODOT) goes a step further by requiring contractors submitting proposals to disclose any relationships with ODOT employees and agree to adhere to ODOT's conflict of interest policies.

### *The Role of the Department of Administrative Services*

In addition to developing the Public Contracting Rules for agencies subject to their authority, the State Procurement Office within DAS also operates several programs that facilitate various aspects of contracting across the state. These include:

- Oregon Procurement Information Network (ORPIN) – This program is an online resource to help connect suppliers of goods and services with contracting opportunities posted by Oregon state agencies and local governments.
- Oregon Cooperative Procurement Program – This program is a fee-for-service program that allows local governments and other qualified organizations access to a wide variety of state contracts for goods and services.
- Procurement Transactions Unit - The Procurement Transaction Unit provides procurement guidance to agencies and suppliers. It is also responsible for soliciting and negotiating statewide price

agreements for use by Oregon state agencies and local governments.

- State Procurement Office Training Program – This program provides training and credentialing for state agencies and local government personnel to improve state procurement practices.

### *The Role of the Department of Justice*

In addition to developing the DOJ Model Rules for agencies subject to its authority, the DOJ is responsible for reviewing public contracts over certain dollar thresholds for legal sufficiency. This is to ensure that the contract language meets all the requirements of the Oregon statutes and rules; that it does not conflict with the Oregon constitution; that it contains the components to be a legally binding contract; that the scope of work to be completed is clear and enforceable; and that the agency has the authority to enter into the contract. DOJ does not determine if the contract is a good business deal for the agency, although it may provide advice regarding significant risks and other issues in the transaction.

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## Audit Results

The purpose of our audit was to determine whether state agencies, boards, and commissions awarded personal services contracts to former state employees in accordance with contracting laws, rules, and best practices.

By using about 3.4 million records of current and former state employees, we identified about 35,000 former employees who left state services between June 1, 2005 and June 1, 2011. We then matched that information to payments made to contractors in the last six years, and identified payments to former state employees. Next, we compared this information to about 4.5 million active and inactive business registry records, providing us with additional information on some of the former state employees who did business with the state. We then selected 81 personal services contracts with former state employees for testing, which totaled about \$6.5 million, as well as another \$3.7 million with non-state employees. The contracts covered 10 agencies, a board and a commission. The contracts were for personal services such as management consulting, emergency medical preparedness, educational screening and assessment, and inmate rehabilitation.

Although we identified some opportunities for state agencies, boards, and commissions to improve contracting practices, we found that personal services contracts with former state employees were in accordance with state contracting laws and rules. Furthermore, we did not find evidence that former state employees were provided an unfair advantage over other bidders or that agency staff had circumvented the competitive selection process.

The testing we performed showed that former state employees, as with other proposers, were required to submit proposals that were evaluated against established criteria and against other proposals before being awarded. Additionally, we found that contracting opportunities were publically advertised, as were the award notifications.

### *Rules Encourage Competition*

Oregon statutes and administrative rules governing procurement require state agencies to encourage competition when acquiring personal services. Open and fair competition in the procurement process provides many benefits to the public.

Competition helps ensure state agencies, boards, commissions, and others subject to procurement rules, acquire services of the requisite

quality within the time frame needed and at the lowest reasonable cost. Open and fair competition also promotes fair dealings and equitable relationships among the parties involved in the contracting process, and allows vendors an opportunity to obtain business from the state.

Agencies authorized to contract for personal services must award using one of the following seven methods:

Method	Contract Amount	Description
<b>Competitive Sealed Bid</b>	Greater than \$150,000	Competitive selection is based on price.
<b>Competitive Sealed Proposal</b>	Greater than \$150,000	Competitive selection is based on a combination of price and qualifications.
<b>Intermediate Procurement</b>	\$5,001 - \$150,000	Selection is based on obtaining three competitive quotes or can be formally selected as described above.
<b>Small Procurement</b>	\$5,000 and Below	Direct award to contractor. Competitive selection not required. <sup>1</sup>
<b>Sole Source Procurement</b>	Any Amount	Direct award to contractor when only one contractor is known to provide the service.
<b>Emergency Procurement</b>	Any Amount	Direct award to contractor in case of a defined emergency.
<b>Special Procurement</b>	Any Amount	Direct award to contractor based on a special class of procurement authorized by DAS.

***Personal Services Contracts with Former State Employees Appropriately Awarded***

We reviewed personal services contracts with former state employees at the 10 state agencies listed below. The contracts totaled approximately \$6.5 million.

- Oregon Community Colleges and Workforce Development
- Oregon Department of Corrections
- Oregon Department of Education
- Oregon Department of Fish and Wildlife
- Oregon Department of Forestry
- Oregon Department of Housing and Community Services
- Oregon Department of Human Services

<sup>1</sup> OAR 580.0062, which relates to the Oregon University System, authorizes direct award for contracts up to \$25,000.

- Oregon Department of the Military
- Oregon Department of Transportation
- Oregon University System:
  - Portland State University
  - Oregon State University
  - University of Oregon

We found that personal services contracts with former state employees at these agencies were appropriately awarded in accordance with state contracting laws and rules. Additionally, we did not find evidence that former state employees were given an unfair advantage over other potential contractors.

We also reviewed personal services contracting practices at the Oregon Construction Contractors Board and the Oregon Public Utilities Commission totaling approximately \$3.7 million and found them to also be in accordance with contracting laws, rules and best practices. Because their personal services contracts with former employees were under the threshold requiring competitive selection, we reviewed other personal services contracts of greater value in order to evaluate the contracting practices of the board and the commission.

#### *Contracting Exceptions Were Used Appropriately*

We analyzed personal services contracts with former state employees that were let using a sole-source, emergency or class special procurement in order to determine if agencies had complied with the requirements of the sourcing method. These three types of procurements allow an agency to directly award a contract without a formal, competitive selection process. However, the process for these contracts must still be open and advantageous to the state. For example, the Department of Human Services is authorized to use a special procurement to obtain client services such as in-home care or living skills training.

In prior audits, we found misuse of sole-source contracts. However, during this review we found that very few personal services contracts were let using a sole-source justification. Upon examination, they were all let in accordance with the requirements to determine in writing that the services are available from only one source.

Similarly, our review of contracts let using an emergency or special procurement found that they were also done in accordance with established contracting rules. However, we did note regarding the use of emergency and special procurements, that agencies did not always document how the contract price was determined or the basis for the total price. These types of contracts, as with those based on a

competitive process, must be advantageous to the state, which includes the price paid for services.

### ***Contractors Did Not Appear to be Working as Employees***

All contractors entering into a personal services contract must qualify as an independent contractor. The purpose of this qualification is to clearly identify that this is not an employer-employee relationship. Generally, to qualify means the contracting agency only has control over the results of the contractor's work and not what will be done or how it will be done. For example, a personal services contract may require a contractor to conduct research and create a final report covering certain aspects of the results. However, it should not specify how the contractor uses time to meet this final deliverable. Control over how a contractor spends time is one of several indications the contractor may actually be working as an agency employee.

The Internal Revenue Service (IRS) and Oregon Revised Statutes have established guidelines regarding the difference between an employee and an independent contractor. The IRS provides guidance for evaluating relationships with contractors and suggests looking at the entire relationship since there is no single determining factor. One of the key guidelines states contractors should be free from the direction and control of the employer.

Our review of contracts with former employees did not identify any instances where personal services contractors appeared to be working more as employees than as contractors. We found that although some contractors had a state telephone number or state email address, they were not under the agency's direct control.

For example, the Department of Corrections contracts with chaplains for ecumenical services and provides a state email address so the chaplains can correspond with the families of inmates. These chaplains are not under the Department's control simply because they have a state email address.

### ***Professional Contracting Staff Were Key to Ensuring Open and Competitive Contracting***

As part of our review, we conducted interviews with contracting staff and management to evaluate whether each agency utilizes a fair, open and competitive contractor selection process. Based on our interviews and review of contractor selection documentation, we found that contracting staff were the main drivers for ensuring that personal services contractors were competitively selected in accordance with state contracting rules and laws, or that contracting exceptions were correctly used. Given the variability of needs at each agency and the complexity of the contracting laws and rules, we

concluded that the proactive involvement of agency contracting professionals was largely responsible for the transparency and adherence to contracting requirements we observed.

We also found that almost all agencies have state or federally certified contracting staff and management within Contracts and Procurement departments. These certifications are earned after passing exams following significant coursework. The annual continuing professional education requirements of these certifications, helps agency contracting staff remain abreast of changes in contracting rules and best practices.

The contracting files showed that broad involvement by agency contracts departments throughout the contracting process led to the enforcement of rules and policies. We noted examples of contracting staff guiding program staff through the contracting process and, when needed, questioning decision points. For example, contracting staff notified program staff and contract administrators when contracts were nearing expiration dates, which alerted program staff that they needed to decide whether or not to amend the contracts.

Contracting departments also provided contracting training to agency program staff on issues such as how to determine whether they need to hire an employee or contract for a service, how to request a personal services contractor, how to write a detailed scope of work, information about hiring former employees, contract administration, and ethics associated with contracting. Some agencies strongly encourage program staff involved with contracting to attend the state's contracting classes.

We also asked whether contracting staff felt as though agency management and staff outside the contracting department had the ability to override or circumvent the contracting process and rules in order to select contractors they prefer. We were told that the contracting department had the full support of agency management in upholding contracting rules and requirements for competitive selection.

Several agencies indicated they are still improving contract administration, such as documenting vendor performance and verifying that services were provided in accordance with contract terms and conditions. Typically, a contract administrator is assigned from within the program to ensure contract monitoring is occurring. We did find, however, that a few agencies also include contract monitoring activities as part of the contracting function.

For example, the Oregon Department of Education requires its contract administrators to complete an "Evaluation of Services and

Request for Final Payment” document prior to final payment to the contractor. In addition, the Oregon Department of Transportation has an oversight unit within its Contracting Department that is responsible for administering personal services contracts and small non-construction contracts. This includes invoice approval and processing; negotiating, setting, and maintaining consultant billing rates; and administering the contract closeout process.

### *Significant Improvements Have Been Made in Contracting Practices*

The Audits Division has issued several audits of contracting practices over the past few years with numerous recommendations on how agencies, boards, commissions, and education services districts can improve personal services contracting practices. Our recommendations addressed issues such as competitive screening and selection processes, adequate administration and monitoring, and not treating contractors as employees.

During this audit, our review of personal services contracts with former employees let through a competitive selection process, demonstrated compliance with contracting laws and rules, and overall improvement in contracting practices. Specifically, we noted the following practices:

- A formal solicitation document, such as a request for proposals or an invitation to bid, was used and was publically advertised through ORPIN, which is the state’s electronic contracting system.
- The solicitation document clearly explained how proposals would be evaluated.
- The winning proposals were received prior to the closing date and time stated in the solicitation. For contracts that resulted from the receipt of more than one bid, proposals were evaluated based on the criteria outlined in the solicitation document.
- Most agencies had proposal evaluation team members complete conflict of interest statements prior to evaluating and scoring proposals.
- The winning proposal evaluation and scoring documents were maintained in the contract files and scores agreed to the winning proposal.
- Bidders were notified of the agency’s intent to award a personal services contract, either by letter or through a posting on ORPIN.
- Contracts contained a clearly defined scope of work to be performed by the contractor, and the contract not-to-exceed amount agreed with the winning proposal.

- As required by law, contracts calling for payment over a certain dollar threshold were reviewed for legal sufficiency.
- With the exception of one agency, all contracts were fully executed (signed) by all parties prior to the start of services as indicated in the contract. This was a significant improvement from past audits where we previously found that contracts often were not signed until after the start of services being provided.
- Contract files were generally well organized and contained information supporting the contractor selection. Some agency files also contained the following types of information, providing greater transparency of the process:
  - request from the program for personal services;
  - determination of the need to contract for personal services versus the use of an employee;
  - proposal or bid receipt log documenting the number of proposals or bids received and the date and time;
  - copies of all vendor proposals or bids, including the winning and non-winning proposals or bids;
  - correspondence with contractor during contract development, including a record of price negotiation when required; and
  - contract administration documentation such as information regarding service deliverables as required by the contract, payments to the contractor, and overall contractor performance.

Because we found that personal services contracts with former state employees were awarded in accordance with state contracting laws and rules, we do not have formal audit recommendations. We did identify and discuss with the applicable agency management, the following improvements that could be made in personal services contracting:

- documenting when only a single bid or proposal is received and the required evaluation;
- retaining all proposals or bids, and supporting materials submitted by contractors who are not awarded a contract;
- clearly documenting the process used for establishing or negotiating price for contracts let using an emergency or special procurement; and
- further promoting good contract management practices.

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## Objectives, Scope and Methodology

The objective of our audit was to determine whether state agencies, boards, and commissions awarded personal services contracts to former state employees in accordance with contracting laws, rules, and best practices.

The scope of our audit included a review of personal services contracts with former state employees let between January 2009 and July 2011 at 10 state agencies, one board, and one commission. We excluded information technology contracts and contracts for architectural/engineering services. As agreed with DAS, we provided DAS with all former employee and contractor matches at DAS for review by their internal auditor.

To answer our audit objective, we obtained the following data files:

- state personnel data from the Department of Administrative Services (DAS), which contained the majority of state employees' current and historical employment information, totaling about 3.42 million records;
- state email account information as of June 13, 2011 from the Department of Administrative Services' State Data Center, totaling about 44,600 records; and
- business registry information on active and inactive registered businesses as of June 1, 2011 from the Secretary of State's Corporation Division, totaling about 4.53 million records.

Using the personnel information from DAS, we identified about 35,600 former employees who left state service between June 1, 2005 and June 1, 2011. We then obtained vendor payment information from the state's financial system for payments made between July 1, 2006 and June 28, 2011, and matched that to the former state employee information. As a result, we identified former state employees who were paid as contractors.

We then compared this information to business registry information. This provided us with a combined list of both former state employees and former state employees associated with a business registered in Oregon.

In a few instances, we had to obtain former employee information and/or vendor payment information directly from an agency, such as with the Oregon University System and the Oregon Department of Transportation. Also, because separate agencies, boards, and

commissions entered their own contracting data into the state's financial system, contracting data was not uniform across files and databases. It is also possible that an individual had a name and/or address change after leaving state service, or may have a business that is not registered with the state or is registered without listing the former employee's name. As such, we may not have compiled a complete list of former state employees who had business with the state as personal services contractors. However, the resulting list was sufficiently complete for our purpose, which was to provide a basis for judgmentally selecting personal services contracts for testing. Specifically, we tested:

- 81 personal services contracts with former state employees at 10 state agencies totaling about \$6.5 million; and
- 8 personal services contracts at one board and one commission that were not with former state employees totaling about \$3.7 million.

Our audit included reviewing contractor solicitation documents (e.g. an invitation to bid or request for proposal), public notice of the solicitation, contractor bids or proposals and their receipting, the processes used to evaluate and score bids or proposals, the awarding process, the contractor selection notification process, and the contract terms and conditions. We also compared contractor payments to the contract not-to-exceed amount and the contract execution (signed) date. Additionally, if a contractor had a state email account or phone number, we checked to see if the contractor appeared to be working more as an employee.

To determine whether agencies complied with requirements for non-competitive procurements, our review included personal services contracts with former state employees let using sole-source, emergency, and special procurements.

We also interviewed contracting department management and staff, other agency management and internal auditors to gain an understanding of each agency's personal services contracting practices. To determine whether contracts with former state employees were awarded in accordance with state contracting laws and rules, we reviewed the agencies' practices relating to solicitation and selection of personal services contractors.

We considered the following criteria for our review:

- ORS 279A Public Contracting General Provisions
- ORS 279B Public Contracting General Provisions
- OAR 137, Divisions 46 and 47 Attorney General's Contracting Rules
- OAR 580, Division 62 Oregon University System Purchasing and Contracting for Personal or Professional Services and Goods and Services
- IRS Publications regarding independent contractors

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient and appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.



# Oregon

John A. Kitzhaber, MD, Governor

## Department of Administrative Services

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February 10, 2012

Gary Blackmer, Director  
Audits Division  
Office of the Secretary of State  
255 Capitol Street NE, Suite 500  
Salem, OR 97310

RE: Audit report entitled, *Agencies Ensured Contracts with Former State Employees were Properly Awarded*

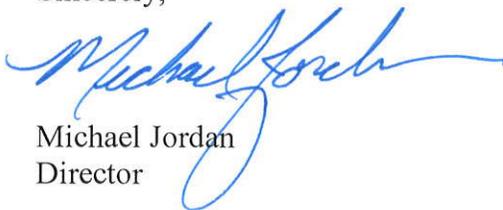
Thank you for providing the Department of Administrative Services (Department) with the audit report noted above. The Department requested a statewide audit on this topic be performed in June 2011 due to the discovery of a contractor being treated as an employee within the agency.

We appreciate the work of the Oregon Audits Division staff and are pleased to see that there are no formal findings in the audit report. The Department acknowledges the opportunities for improvement presented in the report and generally agrees with them.

We also appreciate your willingness to share the list of former employees that are contractors with our agency as we were not part of the audit work performed. We hope you will be willing to share that information with any agency that requests it.

Thank you for your audit team's effort over the past seven months to address the Department's request for this work. If you have any questions about this response, please don't hesitate to contact Pamela J. Stroebel, Chief Audit Executive, at 503-378-4037.

Sincerely,



Michael Jordan  
Director

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## About the Secretary of State Audits Division

The Oregon Constitution provides that the Secretary of State shall be, by virtue of her office, Auditor of Public Accounts. The Audits Division exists to carry out this duty. The division reports to the elected Secretary of State and is independent of the Executive, Legislative, and Judicial branches of Oregon government. The division audits all state officers, agencies, boards, and commissions and oversees audits and financial reporting for local governments.

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### Audit Team

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Deputy Director William K Garber, MPA, CGFM

Audit Manager Sandra Hilton, CPA

Principal Auditor Sheronne Blasi, MPA

Staff Auditor Larry Stafford, MBA

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This report, a public record, is intended to promote the best possible management of public resources. Copies may be obtained from:

internet: <http://www.sos.state.or.us/audits/index.html>

phone: 503-986-2255

mail: Oregon Audits Division  
255 Capitol Street NE, Suite 500  
Salem, OR 97310

During the course of this audit, the courtesies and cooperation extended by officials and employees of the state agencies included in our review were commendable and sincerely appreciated.