#329

Report To

The Mississippi Legislature

A Review of the Department of Finance and Administration's Process for Procuring Personal Services Contracts

September 12, 1995

The Department of Finance and Administration (DFA) contracts out some accounting and computer services, as well as third-party administrator and actuarial services for the state health insurance plans. From FY 1992 through FY 1994, DFA did not use a competitive selection process for fifty-seven percent of its contractual services contracts over $5,000. Further, DFA violated state law by not submitting third-party administrator contracts to the State Personnel Director for review and approval.

DFA also uses personal services contractors to help provide administrative support to the State Agencies' Workers' Compensation Pool and the Tort Claims Board. In selecting a third party-administrator for the Workers' Compensation Pool, DFA did not execute a written contract with the third-party administrator selected until six months after selection of the contractor.

As to Tort Claims Board contracts, the board and DFA failed to use a formal request for proposals when soliciting third-party administrators in 1993, confusing at least one bidder on how to respond. Also, a consultant hired by DFA made an error in analyzing third-party administrators' proposals. Although PEER found no evidence that any consultant erred purposely in order to influence the outcome of the selection process, the error caused delays and compromised the integrity of the selection process.

The PEER Committee

PEER: The Mississippi Legislature's Oversight Agency

The Mississippi Legislature created the Joint Legislative Committee on Performance Evaluation and Expenditure Review (PEER Committee) by statute in 1973. A standing joint committee, the PEER Committee is composed of five members of the House of Representatives appointed by the Speaker and five members of the Senate appointed by the Lieutenant Governor. Appointments are made for four-year terms with one Senator and one Representative appointed from each of the U. S. Congressional Districts. Committee officers are elected by the membership with officers alternating annually between the two houses. All Committee actions by statute require a majority vote of three Representatives and three Senators voting in the affirmative.

Mississippi's constitution gives the Legislature broad power to conduct examinations and investigations. PEER is authorized by law to review any public entity, including contractors supported in whole or in part by public funds, and to address any issues which may require legislative action. PEER has statutory access to all state and local records and has subpoena power to compel testimony or the production of documents.

PEER provides a variety of services to the Legislature, including program evaluations, economy and efficiency reviews, financial audits, limited scope evaluations, fiscal notes, special investigations, briefings to individual legislators, testimony, and other governmental research and assistance. The Committee identifies inefficiency or ineffectiveness or a failure to accomplish legislative objectives, and makes recommendations for redefinition, redirection, redistribution and/or restructuring of Mississippi government. As directed by and subject to the prior approval of the PEER Committee, the Committee's professional staff executes audit and evaluation projects obtaining information and developing options for consideration by the Committee. The PEER Committee releases reports to the Legislature, Governor, Lieutenant Governor, and the agency examined.

The Committee assigns top priority to written requests from individual legislators and legislative committees. The Committee also considers PEER staff proposals and written requests from state officials and others.

A Review of the Department of Finance and Administration's Process for Procuring Personal Services Contracts

September 12, 1995

The PEER Committee

Mississippi Legislature

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Joint Committee on Performance Evaluation and Expenditure Review

PEER Committee

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September 12, 1995

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At its meeting of September 12, 1995, the PEER Committee authorized release of the report entitled **A Review of the Department of Finance and Administration's Process for Procuring Personal Services Contracts.**

Representative Alyce Clarke, Chairman

This report does not recommend increased funding or additional staff.

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A Review of the Department of Finance and Administration's Process for Procuring Personal Services Contracts

September 12, 1995

Executive Summary

Introduction

The Department of Finance and Administration (DFA) provides Mississippi state government with a broad range of financial services including claims pre-audit, administration of employees' health insurance plans, management of office buildings, and executive budget preparation and oversight. DFA also provides support to the Tort Claims Board and the State Agencies' Workers' Compensation Pool.

DFA has chosen to contract out some of its activities, including actuarial services, some accounting services, and third-party administrator's services for health insurance, workers' compensation, and tort claims administration.

To assess DFA's contracting practices, PEER evaluated DFA's personal services contracts for fiscal years 1992, 1993, and 1994 with annual expenditures of more than $5,000. PEER excluded from its review service and repair contracts, as well as contracts for architectural and engineering service. DFA had procured forty-six contracts that met these review criteria.

Because personal services contracting in Mississippi is not a highly regulated activity and few statutes address the process, PEER evaluated DFA's personal services contracts against eight criteria determined to be elements of fair and efficient contracting:

- documentation of need;
- preparation of a formal request for proposals;
- notice of intent;
- formal proposal review;
- approval of competitive selection;
- development of a written contract;
- contract monitoring; and,
- contract evaluation.

Findings

Of the forty-six contracts reviewed by PEER, the Department of Finance and Administration did not use a competitive process to procure twenty-six, or fifty-seven percent, of the contracts. (See page 12.)

The Department of Finance and Administration has a general, but unwritten, policy that requires the department to procure personal services through a competitive process. DFA also periodically extends personal services contracts beyond their initial period, usually through amendments to the original contract. Failure to select contractors competitively could deprive the state of potential savings.

The Department of Finance and Administration failed to comply with MISS. CODE ANN. Section 25-9-107 because it did not submit some contracts for third-party administrator and utilization review services to the State Personnel Director for approval. (See page 14.)

State law requires agencies to obtain approval of the State Personnel Director for personal services contracts (excluding those for physicians, dentists, architects, engineers, veterinarians, and attorneys). DFA did not obtain approval for third-party administrator and utilization review contracts for the state and public school employees' health plans. While PEER does not contend that state employees could perform the functions of a third-party administrator or of the utilization review organizations, the department should not be allowed to bypass obtaining contract approval.

DFA did not execute a written contract with the third-party administrator selected for the State Agencies' Workers' Compensation Pool until six months after the effective date of the contract. (See page 16.)

In early 1994, the State Agencies' Workers' Compensation Pool commenced the process of selecting a new third-party administrator. Although DFA and the pool followed fair and efficient contracting procedures in selecting a contractor, the department did not prepare and execute a written contract until December 1994, even though the new contract was to become effective July 1, 1994.

Lack of a written contract could confuse the parties involved as to their respective tasks and responsibilities. In this instance, the department's failure to formalize its agreement in written form resulted in a six-month delay in payment to the contractor.

The Tort Claims Board did not develop a formal request for proposals to procure third-party administrator services. (See page 17.)

The Tort Claims Board never developed a formal request for proposals to solicit potential bidders for its third-party administrator contract. The board alerted potential bidders through newspaper advertisements, then sent out a letter to interested parties that requested information from them, but that did not state the evaluation factors the board would use when analyzing proposals.

The lack of a formal request for proposals caused confusion for one bidder with respect to exactly what he should bid. DFA and the Tort Claims Board could have avoided such a problem by using a more formalized selection process.

A contract consultant's error delayed selection of a third-party administrator for the Tort Claims Board and cast doubt on the integrity of the board's selection process, because one of the firms that bid on the Tort Claims Board contract subsequently employed that consultant. (See page 18.)

PEER could find no evidence that any employee of the firm involved committed or intended to commit any wrong that could result in a claim against the employee or the firm. However, the sequence of events that took place caused some bidders and others to question the integrity of the board's process in obtaining this contract because a person involved in evaluating proposals ultimately was employed by one of the bidders, albeit an unsuccessful bidder.

Recommendations (see page 21)

1. The Department of Finance and Administration should abide by its internal policy regarding the competitive selection of contractors. This policy should be expanded to require that the department issue a formal invitation or request for proposals, and that this request be advertised. Further, the request should inform the potential respondents of the job to be performed, the criteria that will be used for evaluating respondents, and any other material provisions.

2. The Department of Finance and Administration should comply with state laws regarding the State Personnel Director's approval of personal services contracts unless the Legislature specifically chooses to exempt the department.

3. The Department of Finance and Administration should exercise due diligence in preparing a written contract that parties can agree to prior to the intended date for service commencement. The parties should have a signed contract on or about the effective date of the service agreement.

4. The Department of Finance and Administration should require that any consultant or professional who contracts with the department to provide services to also agree in the contract that the consultant or professional service provider shall not contract with any person or firm upon whose work the consultant or professional has been required by the department to review or give advice. This prohibition should be effective during the term of the contract and for one year thereafter.

5. The Department of Finance and Administration should limit extensions to personal services contracts to a period not to exceed two years.

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A Review of the Department of Finance and Administration's Process for Procuring Personal Services Contracts

Introduction

The responsibilities of the Department of Finance and Administration, the state's fiscal pre-audit and budgetary control agency, include management of the self-insured health insurance program for state employees and personnel of school districts and community/junior college districts. In discharging these responsibilities, DFA often uses personal services contractors to provide accounting services to develop indirect cost allocation plans for federal grants, third-party administrator services and actuarial services for the health insurance plans, and computer assistance with further development of the Statewide Automated Accounting System.

The Department of Finance and Administration also uses personal services contractors to help provide administrative support to the State Agencies' Workers' Compensation Pool and the Tort Claims Board. The department contracts out the claims administration responsibilities of these entities to third-party administrators, and also uses a contract consultant to rank candidates and recommend the third-party administrator for the Tort Claims Board.

Personal services contracting by state agencies and institutions in Mississippi is not a highly regulated activity. Unlike state service positions, under control of the State Personnel Board, personal services contracts are subject to few pre-audit requirements. Thus state agencies and institutions have a great deal of flexibility in the utilization, selection, and monitoring of personal services contractors.

Authority

In accordance with MISS. CODE ANN. Section 5-3-57 (1972), the PEER Committee examined the processes by which the Department of Finance and Administration (DFA), the State Agencies' Workers' Compensation Pool, and the Tort Claims Board selected certain personal services contractors.

Scope and Purpose

PEER conducted this review in response to complaints from legislators and contractors that DFA did not use competitive procurement procedures when selecting personal services contractors for itself and for

two legal entities for which the department is responsible for providing administrative support--the State Agencies' Workers' Compensation Pool and the Tort Claims Board.

Members of the Legislature were also concerned that the Tort Claims Board's procurement of a third-party administrator may have been influenced by contract consultants who had a pecuniary interest in insuring that a certain prospective contractor receive the contract for third-party administrator's services.

Method

In conducting this review, PEER:

- interviewed Department of Finance and Administration personnel regarding selected contracts;
- reviewed files of the Department of Finance and Administration, the State Agencies' Workers' Compensation Pool, and the Tort Claims Board;
- reviewed state laws of the states contiguous to Mississippi, as well as Wisconsin, Minnesota, and Virginia; American Bar Association publications; and federal regulations regarding accepted standards for procurement of personal services contracts;
- reviewed applicable Mississippi laws related to contracting and ethics; and,
- reviewed State Personnel Board records.

For the period FY 1992 through FY 1994, PEER reviewed DFA's procurement of forty-six personal services contracts that had annual expenditures of more than $5,000. PEER used the $5,000 benchmark because the Legislature established this amount when passing commodities bid laws requiring that purchases over $5,000 be made only through a competitive bid process. PEER excluded from its review service and repair contracts, as well as contracts for architectural and engineering services for DFA's Bureau of Building, Grounds, and Real Property Management. (PEER addressed DFA's procurement of architectural and engineering services in its October 12, 1993, report entitled *A Review of the Bureau of Building's Selection of Architectural and Engineering Firms*.)

The types of services provided by the contracts reviewed included accounting and actuarial services, third-party administrator services, data processing consulting, insurance, memberships in organizations such as the Governmental Accounting Standards Board, utilization review

organizations that monitor health insurance plan members' utilization of inpatient services, and training consultants.

Relationship of DFA to the State Agencies' Workers' Compensation Pool and the Tort Claims Board

In 1988 the Legislature authorized state agencies to become self-insurers for workers' compensation purposes. In 1990 the Legislature mandated state agencies to provide workers' compensation coverage and created a self-insured pool that agencies could join. The State Agencies' Workers' Compensation Pool is a corporation created to provide those agencies that choose to join with a workers' compensation self-insurance pool. The pool is governed by a board consisting of state agency personnel. Bylaws of the State Agencies' Workers' Compensation Pool designate the Department of Finance and Administration as the pool's administrator, and DFA contracts out the claims administration responsibilities of the pool to a third-party administrator.

In 1993 the Legislature established the Tort Claims Board to provide an administrative body for the resolution of tort claims against the state and the payment of such claims. CODE Section 11-46-18 makes the executive director of the Department of Finance and Administration a member of the Tort Claims Board and makes DFA responsible for the board's administrative functions. As in the case of the workers' compensation pool, DFA contracts out claims administration responsibilities to a third-party administrator.

Overview

The Department of Finance and Administration has not used competitive methods of selecting personal services contractors consistently in FY 1992 through FY 1994, failing to use competitive methods in fifty-seven percent of all cases reviewed. Although extending existing contracts could serve as an incentive to contractors to do business with the state, it deprives other service providers of opportunity. Such contract extensions are attributable to the department's failure to adhere to its own policy calling for the bidding of contracts for personal services.

In some cases, DFA has failed to obtain approval of contracts from the State Personnel Director. The contracts not approved in accordance with law were Blue Cross/Blue Shield third-party administrator contracts and Cost Care contracts for state health plan utilization review. Because these contracts called for the provision of labor to the state, they qualify as personal services contracts that should be sent to the State Personnel Director for review.

With assistance from the Department of Finance and Administration, the State Agencies' Workers' Compensation Pool selected a third-party administrator to begin services effective July 1, 1994, but DFA, as administrator of the pool, did not prepare a written contract until December 1994. The lack of a written contract prevented the contractor from receiving payment for services rendered from July 1994 through December 1994, until after the document was signed. The lack of a written contract violates good business practices and could lead to confusion regarding duties and responsibilities.

Regarding the third-party administrator's contracting process for the Tort Claims Board, DFA and the board did not develop a formal request for proposals to be distributed to interested firms. This created confusion on the part of one interested firm, causing it to bid on more services than necessary. A consultant working for the Department of Finance and Administration erred in evaluating the proposals submitted for third-party administrators' services, which made one proposal appear to be more expensive than it actually was. Because the board detected this error and took corrective action in time for the proposal to be considered at its correct price along with other proposals, no harm resulted from the error. PEER found no evidence that any consultant erred purposely in order to influence the outcome of the contractor selection process.

Elements of Fair and Efficient Personal Services Contracting

Personal services contracting by state agencies and institutions in Mississippi is not a highly regulated activity. Unlike position recruitment, selection, classification, and compensation, which must comply with State Personnel Board pre-audit controls to determine whether persons are hired, compensated, and classified in a manner reflective of their job skills and job worth, few pre-audit requirements exist in the area of personal services contracts. MISS. CODE ANN. Section 25-9-107(c)(x) requires that agencies hiring state service personnel obtain approval of the State Personnel Director prior to entering into contracts for personal services. The statutory basis for the State Personnel Director's disapproval of such contracts is limited to those cases in which the tasks to be performed by the contractor could be performed by a state service employee in an authorized position.

Since Mississippi law provides no procedural controls on personal services contracting except for review by the State Personnel Director, PEER reviewed other states' laws and the recommendations of other entities such as federal law and publications of the American Bar Association to determine the procedural steps that should be found in a personal services contracting process. Generally, an effective contracting process ensures that an agency procures services that it cannot produce for itself with authorized staff, solicits and selects contractors competitively, and monitors the performance of contractors to insure that the contract deliverables are provided on a timely basis and are of sufficient quality to meet the expectations of the contracting agency.

Needs Assessment

To obtain the State Personnel Director's approval for a personal services contract, state agencies must complete a standard form explaining why they need the contract, what impact failure to procure the service would have on the agency, and why a staff member in an employment position cannot carry out the responsibilities that are to be contracted out. These matters should be addressed by a needs assessment. Presently, Mississippi law does not require that agencies document methods used to arrive at the conclusions of need that they report to the State Personnel Director.

Other states specifically require that agencies provide documentation with respect to the establishment of need. In Wisconsin, WIS. STAT. ANN. § 16:705 requires that agencies seeking approval of a personal services contract provide the Department of Administration with a statement of need and an explanation of why another state agency cannot perform the services that are the subject of the contract. Arkansas requires that all

contracts be reviewed by the State Fiscal Officer. Agencies submitting contracts for review must include an explanation of why the contract is necessary for the agency to fulfill its legal responsibilities (see ARK. STAT. ANN. § 19-4-1712).

Although not binding upon the states, federal procurement standards require that federal agencies determine need before entering into contracts for consulting services. Federal regulations do not outline the procedure an agency must follow in order to make a determination of need for such services (see 48 C.F.R. § 37.205). However, implicit in any requirement of a statement of need is that the requesting entity use some rational method for arriving at the conclusion that it needs a personal service, whether it be for consultants or for janitors.

Competitive Selection

Competitive selection methods help insure that agencies benefit from forces of the marketplace. The underlying assumption behind such methods of selecting contractors is that the agency can obtain a lower price for the service or product it requires if it seeks offers from a broad range of sellers, each with a desire to obtain the agency's business.

Mississippi law does not require agencies to use any form of competitive selection method, such as the use of sealed bids, in obtaining personal services contracts. However, bid laws make competitive selection mandatory for state agencies' and local governing authorities' acquisition of equipment when the purchase exceeds $5,000 (see MISS. CODE ANN. § 31-7-1 et. seq).

Other states have imposed more procedural controls over personal services contracting than has Mississippi. While none of the laws in the seven states PEER researched require that all personal services contracts be procured through a competitive bid process, many require that agencies attempt to obtain proposals from more than one possible contractor before selecting a contractor. Following are brief descriptions of the efforts of the seven states PEER reviewed to place controls on service contracting.

Minnesota: MINN. STAT. ANN. § 15:061 and 16B:17 allow selection of consultants or technical services contractors without the use of competitive bidding. This method of selection may be allowed only with the approval of the State Commissioner of Administration. When consultants or technical service providers are so hired, the agency must be able to document that it made reasonable efforts to publicize the availability of the contract and obtain a contractor through the competitive market before selecting a contractor without using bids.

Virginia: VA. CODE § 11-41 requires that government contracts for services be procured through competitive sealed bidding or through

competitive negotiation. A public body may use competitive negotiation when it has made a formal determination that competitive bidding is not practicable. Regardless of whether a public body uses competitive bidding or competitive negotiation, the law requires public bodies to prepare and issue written invitations to bid, including evaluation criteria as well as other terms that the public body must include in a contract between itself and the party selected to enter into the contract. Under both methods, the public body must publish notice of the request for proposals so that potential service providers may have the opportunity to respond to the request. (See definitions in VA. CODE § 11-37.)

Wisconsin: Wisconsin requires competitive sealed bids for personal services contracts for $20,000 or more. When the Secretary of the Department of Administration determines that the use of such procedures is not advantageous, the Secretary may require competitive sealed proposals. (See WIS. STAT. ANN. § 16:75.) While state law does not define competitive sealed proposals, the law does provide that such a method will include the development of evaluation criteria and the dissemination of such criteria to interested parties with no selection of a successful proponent until seven days have elapsed since the last published notice to interested parties.

Alabama: ALA. CODE § 41-16-50 requires that contractors providing services with a value of $7,500 or more be selected through a competitive bid and bid evaluation process. An exception in § 41-16-51 excludes contracts for professional services from the bidding requirement. "Professional services" includes contracts for attorneys, engineers, physicians, teachers, and others who must possess a high degree of professional skill and in which the personality of the individual pays a decisive part.

Arkansas: ARK. STAT. ANN. § 19-11-201 regulates service contracts and requires that these be bid as commodity contracts. Contracts between state agencies and professionals or consultants are exempt from the operation of these provisions. For consultants and professionals, state law sets no bid requirements, but does require pre-approval of contracts by the state's chief fiscal officer. Subsequent to his approval, all consultant and professional services contracts must be approved by the Arkansas Legislature's Joint Budget Committee.

Louisiana: LA. REV. STAT. ANN. § 39:1496 requires state agency consulting service contracts of $50,000 or more to be procured through either a competitive process bid process or a competitive negotiation process. Competitive bidding requires that the agency advertise the contract and select the lowest and best proponent. Competitive negotiation requires that the agency negotiate with a contractor after issuing a request for proposals from interested parties (see § 39:1484). Personal services and professional services do not have to be procured through the use of such competitive processes (see § 39:1494 and 39:1495). Consequently, only those services that fit within the definition of consulting (the application of

specialized knowledge, experience, and expertise to problem solving) would be subject to competitive negotiation or bidding. Because professional services also require such applications of knowledge, skill, and expertise, it is not clear when a service falls in one category rather than the other. Services of licensed professionals such as attorneys, physicians, and accountants are specifically included in the definition of professional services (see § 39:1484).

Tennessee: While Tennessee does not specifically require bids for professional or other contractual services, it does require that the state's Commissioner of Administration develop regulations requiring state agencies and departments to consider the following before entering into service contracts:

- costs of the contractor proposal and the qualifications of the proponent;
- a solicitation document with evaluation criteria;
- reasonable notice and time for proponents to respond to the solicitation; and,
- review by the state and interested parties of any models and formulas to be used in the evaluation of proposals.

Contracts for engineers whose employment is to be associated with specific construction projects, firms selected to market bonds, and attorneys' contracts are exempt from the provisions of this section (see TENN. CODE ANN. § 12-4-109).

Summary: The states discussed above have placed some controls on the processes state agencies must follow when they enter into contracts. Most require that agencies bid or competitively negotiate service contracts. Most allow agencies to escape formal bid requirements when seeking the services of consultants or licensed professionals. While states usually give agencies more flexibility in seeking professional or consultant services, the states of Minnesota, Tennessee, and Virginia require agencies to solicit proposals from interested parties before making any decision regarding the selection of a contractor. Tennessee and Virginia also require that formal evaluation criteria be used in the selection process. Wisconsin requires formal bids if the service sought will cost $20,000 or more.

Federal law requires the use of competitive selection methods for federal agencies and, in some instances, for state recipients of grants. The American Bar Association also recommends competitive selection procedures for use by entities that plan to acquire personal services by contract.

Monitoring and Evaluation

Post-contract evaluation is a means of determining how well a contractor performed assigned tasks. While Mississippi law does not require post-contract evaluation of contractor performance, other states do require that agencies engage in such post-contract monitoring of contractor performance. Minnesota law requires that contracting agencies file evaluation reports with the Department of Administration that address contractor tasks to be performed and the agency's monitoring of these tasks. Wisconsin, Arkansas, and Louisiana require that the agency hiring a personal services contractor establish evaluation standards to assess the performance of the contractor. In Louisiana and Wisconsin, evaluation standards must be submitted to the Department of Administration (Wisconsin) or the Office of Contract Review (Louisiana) as a pre-condition to the contract's becoming effective.

Federal agencies also use evaluations to determine whether contractors have met contract requirements. 48 C.F.R. § 37.205 specifically requires that when federal agencies contract for personal services of an advisory nature, such as consulting, the agency must conduct an evaluation at the conclusion of the contract to:

> *. . .assess the utility of the deliverables to the agency, and the performance of the contractor.*

Such evaluations could help an agency determine whether such contracts should be sought in the future.

Findings

Overall Assessment of Department of Finance and Administration's Contracting Practices

To assess DFA's contracting practices, PEER evaluated DFA's personal services contracts for fiscal years 1992, 1993, and 1994 against eight criteria PEER concluded to be elements of fair and efficient contracting:

- documentation of need;
- preparation of a formal request for proposals;
- notice of intent;
- formal proposal review;
- approval of competitive selection;
- development of a written contract;
- contract monitoring; and,
- contract evaluation.

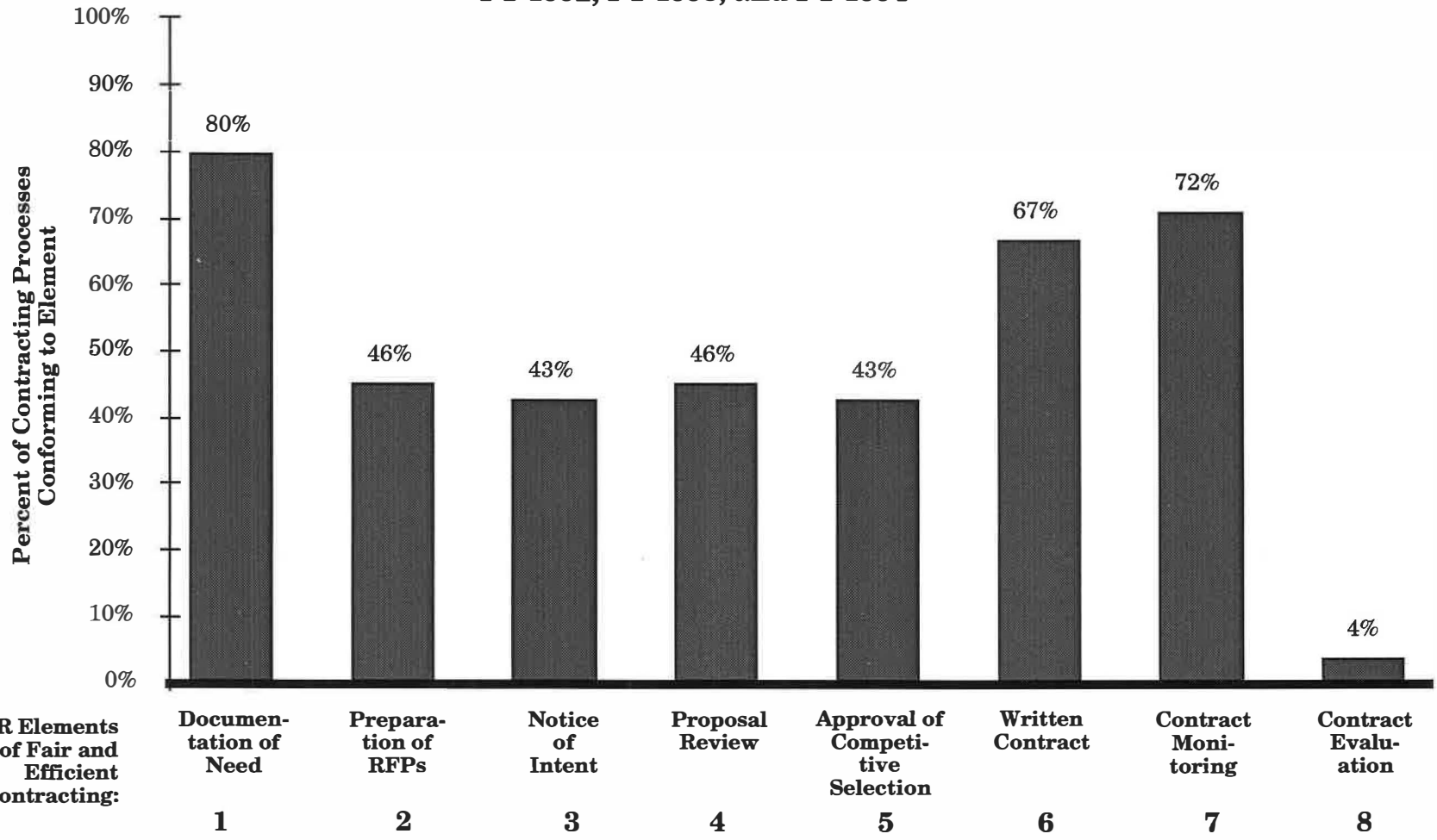
Exhibit 1, page 11, depicts graphically PEER's evaluation of the department's contracting practices.

The Department of Finance and Administration has met most of the criteria PEER considers to be essential to an effective system of service procurement. Generally the department has performed necessary steps with respect to determining need for a contract. On average, the department has performed needs assessments approximately eighty percent of the time over the past three years. In most cases the agency has also obtained written contracts. In compliance with State Personnel Board procedures, most contracts have a contract monitor.

However, the Department of Finance and Administration's contracts for consulting services entered into during or extended into the period under review lacked the components for effectiveness noted in the following findings. Regarding contractor selection, during the period under review, DFA went through the steps of preparing a request for proposals (RFP), distributing the RFP to interested persons, analyzing results, and failing to select a contractor competitively in fifty-seven percent of all cases reviewed. This is contrary to the department's own policy for competitively selecting contractors. In some cases, DFA contracted with third-party administrators without prior approval of the State Personnel Board.

Exhibit 1

Percent of DFA Contracts Awarded Using Procedures Consistent with PEER Elements of Fair and Efficient Contracting: FY 1992, FY 1993, and FY 1994



DFA used competitive bidding (Steps 2 through 5 above) in securing fewer than half of the DFA contracts PEER reviewed.

SOURCE: PEER Analysis of DFA Contracting files.

DFA Does Not Consistently Use a Competitive Selection Process

Of the forty-six contracts reviewed by PEER, the Department of Finance and Administration did not use a competitive process to procure twenty-six, or fifty-seven percent, of the contracts.

Competitive selection methods allow entities to benefit from the forces of the marketplace. The underlying assumption is that entities can obtain lower prices for services or products if they obtain prices from a broad range of sellers, each with a desire to obtain the entities' business. While Mississippi law does not require competitive selection of personal services contractors, most states require that agencies bid or competitively negotiate service contracts unless seeking the services of consultants or licensed professionals (see page 6). (Mississippi law makes competitive selection mandatory only for state agencies and local governing authorities when acquiring commodities and equipment in excess of $5,000.)

The Department of Finance and Administration has a general, but unwritten, policy that requires the department to procure personal services through a competitive process. Consequently, there is no formal requirement for:

- formal development of a request for proposals;
- dissemination of the RFP to interested parties after advertising;
- evaluation of responses to the RFP; or,
- formal selection of the governing authority based on evaluations.

The department's only written policies regarding procurement of personal services relate to contracts for DFA's Mississippi Management and Reporting System (computerized accounting services for state agencies) and architects and engineers.

Contrary to DFA's general policy favoring the bidding of personal services contracts, the department has been inconsistent in the use of bidding as a means of selecting contractors. Of the department's forty-six personal services contracts reviewed by PEER, DFA did not use a competitive process in procuring twenty-six, or fifty-seven percent, of the contracts.

Between FY 1992 and FY 1994, the number of contracts that DFA bid competitively (or extended contracts originally bid) increased from twenty percent in FY 1992 (three of fifteen contracts reviewed) to fifty percent in FY 1993 (eight of sixteen contracts reviewed) to sixty percent in FY 1994 (nine of

fifteen contracts reviewed). This trend of increase shows that personal services contracts that were not bid in fiscal years 1992 or 1993 were bid in FY 1994. Examples of such contracts include:

- *a contract with an accounting firm to audit the State Agencies' Workers' Compensation Pool.* During FY 1992 and FY 1993, DFA procured this contract by informally seeking an offer from the company, rather than through a competitive process.

- *a contract for actuarial services in FY 1994 for the Office of Insurance.* DFA procured this same contract in FY 1993 without using a competitive process.

- *a contract for consulting services in FY 1994 relative to the operations of the MMRS.* DFA treated earlier contracts for such services as extensions or continuations of previous contracts, and did not use a competitive process.

- *a consulting contract with a national accounting firm to help devise request for proposals materials for an upcoming bid of the state health insurance third-party administrator contract.* In the past, DFA used national firms to devise specifications or give actuarial advice regarding state insurance matters, but these contracts had not been bid.

Regardless of this trend favoring the use of competitive bids, the department failed to bid other professional and personal services contracts during FY 1994. Examples of these contracts include:

- *a contract to develop an indirect cost allocation plan for the state.* During the period reviewed by PEER, DFA did not select the contractor through a competitive process. During this period, the agency expended $82,850 on three contracts with this firm.

- *a training contract for the department's MMRS services.* During FY 1994 the agency expended $8,848 on a contract with this firm.

- *a FY 1994 contract with a firm hired to perform actuarial services for the State Agencies' Workers' Compensation Pool.* During FY 1994, the agency expended $11,674 on a contract with this firm.

In addition to inconsistent use of a competitive process, DFA periodically extends personal services contracts beyond their initial period, usually through amendments to the original contract. Evidence of an extension usually consists of a letter to the effect that the contract has been extended. Examples of extensions include:

- *Blue Cross/Blue Shield third-party administrator contracts for the state health insurance plan for fiscal years 1992, 1993, and 1994.*

These were extensions of a contract originally bid in 1988. During the three years under review, the agency expended $6,556,145 on this contractor without seeking competitive bids.

- *Lamar Life Insurance Company third-party administrator contracts for the state life insurance plan for fiscal years 1992, 1993, and 1994.* During the three years under review, the agency expended $375,199 on this contractor without seeking competitive bids.

- *selected American Management Systems contracts for fiscal years 1992, 1993, and 1994 to provide DFA with services relative to the development of management reporting databases for the state.* During the three years under review, the agency expended $543,780 on this contractor without seeking competitive bids.

While the contracts in question allowed amendments and extensions, DFA has no written policy defining the conditions under which extensions, rather than a competitive procurement process, should be used.

While it is impossible to determine just how much the department might have saved from using competitive selection methods, the failure to utilize such methods has deprived the state of potential savings that could be realized from competition. A further effect of this weakness is that without defined statements of work to be performed by the contractor, usually found in an RFP, the agency has no mutually-agreed-upon basis for evaluations of the contractor. This could explain the agency's lack of post-contract evaluation exhibited in column 8 of Exhibit 1 on page 11.

DFA Has Not Submitted All Service Contracts to the State Personnel Director for Approval

The Department of Finance and Administration failed to comply with MISS. CODE ANN. Section 25-9-107 because it did not submit some contracts for third-party administrator and utilization review services to the State Personnel Director for approval.

MISS. CODE ANN. § 25-9-107 (c) (x) states that ". . .any agency which employs state service employees may enter into contracts for personal and professional services only with the prior written approval of the State Personnel Director." The section further states:

> *Prior to paying any warrant for such contractual services, the Auditor of Public Accounts, or the successor to those duties* [DFA], *shall determine whether the contract involved was for personal or professional services, and, if so, shall determine whether it was properly submitted to the State Personnel Director and approved.*

(The section exempts from the State Personnel Director's approval contracts involving physicians, dentists, architects, engineers, veterinarians, attorneys, utility rate experts, and specialized technical services related to facilities maintenance.)

According to State Personnel Board records, DFA did not obtain the State Personnel Director's approval for contracts with Blue Cross Blue Shield of Mississippi or Cost Care, third-party administrator and utilization review contractors, respectively, for the state and public employees' health plans administered by DFA. Department staff contend that because state law does not define "contract personnel," the department's third-party administrator and utilization review contracts were not subject to the approval provisions of Section 25-9-107 (c) (x).

This section further provides that the auditor of public accounts, or its successor (the Department of Finance and Administration) determine prior to paying a warrant for contractual services whether the contract was for personal or professional services, and if for such services, whether it was approved by the State Personnel Director. (See the Appendix, page 23, for a detailed explanation of this analysis.)

The Department of Finance and Administration has avoided the State Personnel Director's limited review of third-party administrator and utilization review organization contracts, the only check existing in law to ensure that agencies do not use contractors unnecessarily. If agencies become accustomed to entering into personal services contacts without first getting approval of the State Personnel Director, contracts could be executed for services that could have been performed by employees of the contracting agency, thus causing unnecessary expenditures of state funds.

The practice of bypassing State Personnel Director approval also results in some contracts not being included in the State Personnel Board's data bases, which provide information regarding the availability of information on personal services spending. Lack of contractual information in data bases means budgetary authorities such as the Legislative Budget Committee have no information on the contracts and how much agencies spend on them. Such information is important to the appropriations process, as the Legislature must appropriate funds to agencies to cover the costs of health care for state employees, and should be provided with the information needed to determine how these appropriated funds are expended, even though the appropriations process does not specifically extend to DFA's management of the premium funds.

DFA Executed an After-the-Fact Contract with the Third-Party Administrator for the Workers' Compensation Pool

DFA did not execute a written contract with the third-party administrator selected for the State Agencies' Workers' Compensation Pool until six months after the effective date of the contract.

In early 1994, the State Agencies' Workers' Compensation Pool commenced the process of selecting a new third-party administrator. The department used fair and efficient contracting procedures in selecting the contractor. With assistance from consultants, DFA developed and disseminated a request for proposals and analyzed responses based on criteria made available to bidders in the request for proposals. Results of the analysis were made available to the pool's board for consideration. At its meeting of April 21, 1994, the pool selected Sedgwick, James of Mississippi to serve as third-party administrator. No written contract was prepared and signed by the parties until December 30, 1994. However, Sedgwick, James continued to provide services to the State Agencies Workers' Compensation Pool.

One fundamental of generally accepted business practices is that a contract between parties should be in writing. DFA generally follows this practice for its agreements. No provision of law in Mississippi specifies when a contract document is to be delivered to the parties to the contract; however, federal regulations provide a persuasive standard as to when written contracts should be used and delivered to parties even though these regulations are not binding upon the state with respect to the execution of a workers' compensation pool contract.

Federal rules regarding performance presume the existence of a written contract when delivery or performance of services is to commence (see 48 C.F.R. § 12.103). Regulations specifically require that contracts be distributed to interested parties within ten days of execution. Such rules regarding prompt delivery of contracts to interested parties insure that all will have the complete statement of contractual duties and responsibilities upon which to base expectations and reliance. While these are not binding on the state in this particular matter, federal regulations provide a persuasive standard as to when a document should be written and delivered to the parties.

According to the Department of Finance and Administration, the delay in obtaining a written contract in this instance has been attributable to the department's consideration of possibly performing the risk management function through the Tort Claims Board and using the third-party administrator for claims management only. The department could have taken on the responsibilities that are currently being performed by the contractor. Regardless of the department's motives, delays in the preparation and execution of a written contract could cause confusion between the parties as to their respective duties and responsibilities.

The service contract signed on December 30, 1994, provides a lengthy statement of responsibilities for the contractor. Most of these are duties normally associated with performing the function of a third-party administrator--claims review and processing, premium collection, case investigation and settlement, and assistance in litigation.

In this specific instance, the effect of the department's failure to formalize its agreement in written form resulted in delays in payments made to the contractor. According to personnel of Sedgwick, James, all functions assigned to the contractor were performed, including risk control and claims processing, but the contractor did not receive payment for services rendered until after the written contract was executed. Thus, the contractor performed services for approximately six months before receiving payment.

DFA Did Not Ensure that the Tort Claims Board Use a Formal RFP in Selecting its Third-Party Administrator

The Tort Claims Board did not develop a formal request for proposals to procure third-party administrator services.

The Tort Claims Board never developed a formal request for proposals to solicit potential bidders for the third-party administrator contract. The board informed potential bidders through newspaper advertisements for three weeks in the *Clarion-Ledger* in March and April of 1993. The advertisement simply noted that the state was seeking a third-party administrator for its Tort Claims Fund and requested interested parties to seek information from the actuaries assisting the state in selecting a third-party administrator. According to one bidder, the actuaries sent out a letter to interested parties dated April 13, 1993, informing them that the board sought a third-party administrator for claims management, safety and loss control management. The letter further informed the parties that they should provide information on the staffing they would assign to the third-party administrator functions, including the time they would spend on these functions, the agencies they would visit for safety management, their priorities on agencies they would visit, and how they would track their activities and results. The letter never informed interested parties concerning the evaluation factors the board would use when analyzing the proposals.

Fundamental to a sound contracting process is a formal request for proposals. Most of the states' contracting laws PEER reviewed required formal requests for proposals. The American Bar Association has recommended that such requests contain:

- instructions and information to bidders concerning delivery of bids;

- a description of the goods/services and evaluation factors, as well as delivery and performance schedules; and,

- contract terms and conditions.

These components would clearly inform interested parties of what they would be required to provide in the way of services or goods, and on what criteria their offer would be evaluated.

Tort Claims Board personnel are not certain as to why no formal RFP was used, but explains that the process was "hurried" to try to find a contractor to begin operations as soon after July 1, 1993, as possible.

The lack of a formal request for proposals could result in bidder confusion because no clear guidance exists on how to structure a response. In discussing the process with one bidder, PEER determined that the bidder was uncertain as to how it should respond to the board in preparing a proposal. Under conditions where no clear statement of bidder responsibilities was available and no statement of evaluation points was provided, the bidder could only guess at what it should provide to the board for review. This bidder essentially offered more to the board than other bidders. Specifically, this bidder offered a law enforcement risk control program upon which other parties did not bid, and had no clear idea of which claims level scenario to assume when preparing its response. Because it offered more, the bidder was more expensive than other bidders.

When bidders are not certain as to how they should bid and how they will be evaluated, the process of competitively selecting the lowest and best bidder is frustrated because no two bidders will be able to interpret agency needs in the same way and make their best offer in response to these needs.

A Consultant's Error Delayed and Compromised Integrity of the Tort Claims Board's Third-Party Administrator Selection

A contract consultant's error delayed selection of a third-party administrator for the Tort Claims Board and cast doubt on the integrity of the board's selection process, because one of the firms that bid on the Tort Claims Board contract subsequently employed that consultant.

As noted above, the Tort Claims Board used consultants from the Mclean, Oddy actuarial firm in selecting a third-party administrator. According to the June 3, 1993, board minutes, several firms responded to a newspaper advertisement regarding administrative services. The minutes from June 22, 1993, show that the board considered Executive Risk Consultants (ERC) and Adjustco as finalists for consideration. Board minutes show that there had been an error in the evaluation of the

Sedgwick, James proposal. Mr. Rick Alford of Mclean, Oddy noted the error, and upon motion of the Attorney General, a member of the board, Sedgwick, James was added as a finalist at the July 13, 1994, meeting. Specifically, this error made the Sedgwick, James risk control proposal appear to be $50,000 more expensive that it actually was.

This error was not initially detected and reported to the board by board personnel or contractors, but by the bidder injured by the error. This bidder, Sedgwick, James, after learning from an undisclosed source the substance of the Mclean, Oddy evaluation, complained to the Chairman of the Tort Claims Board, Frank Montague, of the error. The board agreed to allow Sedgwick, James back into consideration along with Adjustco and ERC.

Subsequent to the detection of the error by Sedgwick, James and the admission of error by the consultants, the Tort Claims Board allowed Sedgwick, James to compete with the other two finalists, ERC and Adjustco. Ultimately, Sedgwick, James was selected as the third-party administrator. The contract between the board and the administrator was executed on August 11, 1993, for a three-year term. The Mclean, Oddy employee (Mr. Alford) later became an employee of ERC, an unsuccessful bidder for the administrator's contract.

PEER could find no evidence that any employee of Mclean, Oddy committed any wrong that could result in a claim against the employee or the firm, or ever intended to commit a wrong. All information PEER obtained shows that the change in employment occurred after the Tort Claims contract analysis was initially conducted and corrected. However, the occurrences noted above have caused some bidders and others to question the integrity of the Tort Claims Board's process in obtaining this contract because a person involved in the sensitive role of evaluating proposals ultimately was employed by one of the bidders, albeit an unsuccessful bidder.

The American Bar Association has recommended that states prohibit contractors from hiring former employees of the state and doing business with the state for a period of one year after the state employee has ceased to be an employee of the state. While persons who work for independent contractors such as the actuarial firm used by the Tort Claims Board are not state employees, an argument could be made that such persons have the potential to do as much harm to the state agency as could a former employee, as contractors can influence decisions made by state agencies just as employees can. When contractors ultimately go to work for a firm that could have been benefited by the contractor's mistake in analysis, bidders and the public at large may lose confidence in the contracting process just as they might if a state employee made an error that could have benefited a firm with which that employee was soon employed.

State law at present does not touch this matter. According to the Executive Director of the Ethics Commission, an independent contractor may not fall within the definition of a public servant found in CODE Section 25-4-101. Further, because no one achieved a pecuniary benefit from the mistake in analysis, the transaction would not fall within the scope of Section 25-4-105.

Recommendations

1. The Department of Finance and Administration should abide by its internal policy regarding the competitive selection of contractors. This policy should be expanded to require that the department always issue an invitation or request for proposals, and that this request be advertised in a publication that will reach persons or firms who might be interested in doing business with the department. Further, the request should inform the potential respondents of the job to be performed, the criteria that will be used for evaluating respondents, and any other material provisions that the department will include in a contract between itself and the successful firm or person.

2. The Department of Finance and Administration should comply with state laws regarding State Personnel Director's approval of personal services contracts unless the Legislature specifically chooses to exempt the department from Section 25-9-107(c)(x).

3. In the future, the Department of Finance and Administration should exercise due diligence in preparing a contract that parties can agree to prior to the intended date for service commencement. The parties should have a signed contract on or about the effective date of the service agreement.

4. The Department of Finance and Administration should require that any consultant or professional who contracts with the department to provide services to also agree in the contract that the consultant or professional service provider shall not contract with any person or firm upon whose work the consultant or professional has been required by the department to review or give advice. This prohibition should be effective during the term of the contract and for one year thereafter.

5. The Department of Finance and Administration should limit extensions to personal services contracts to a period not to exceed two years.

Appendix

Why Third-Party Administrator and Utilization Review Organization Contracts Fall Within the Scope of MISS. CODE ANN. Section 25-9-107 (c) (x)

While the provisions of the CODE cited in this report do not define the terms "contract personnel," "personal services," or "professional services," Section 25-9-107 (c)(x) treats professional and personal services as subsets of the term "contract personnel." The State Personnel Board defines *personal services contract* as a contract between a state service agency and outside party for personal or professional services which cannot be performed by an agency employee in an authorized position. The contractors in this report whose contracts were not submitted to the State Personnel Board for approval provide personal services to the Department of Finance and Administration insofar as they provide the agency with claims processing functions and utilization review activities which are not functions of any personnel at the Department of Finance and Administration.

As to what constitutes a service, state statute law is silent. The Mississippi Supreme Court has, however, defined the term *service* for purposes of matters other than those arising out of the Statewide Personnel System Law. In *Mississippi Theaters Corporation v. Hattiesburg Local Union No 615,* 164 So 887 (Miss, 1936), the Mississippi Supreme Court, in determining whether it was an error to deny the dissolution of an injunction requiring the use of certain persons to provide theater projection services, determined that service is:

> *. . .being employed to serve another; duty or labor to be rendered by one person to another, the former to submit his will to the direction and control of the latter, Supra, at 890.*

Because claims processing and inpatient service screening, are forms of labor rendered by providers to the state, PEER concludes that contracts for these services fall within the scope of Section 25-9-107(c)(x).

Agency Response

STATE OF MISSISSIPPI

DEPARTMENT OF FINANCE AND ADMINISTRATION

EDWARD L. RANCK
EXECUTIVE DIRECTOR

August 3, 1995

Mr. John Turcotte
Executive Director
PEER Committee
222 N. President Street
Jackson, MS 39201

Dear Mr. Turcotte:

Enclosed is the Department of Finance and Administration's response to the PEER draft report on contracting for personal and professional services. Needless to say we are disappointed in this report. As we point out in the attached response it is, in our opinion, inadequately researched, poorly reasoned and out of date.

I hope that you will give careful consideration to our response. It is incumbent upon you to provide the best possible analysis of those matters that you address. We feel that your draft report seriously falls short of that goal.

Sincerely,

Edward L. Ranck, Ph.D.

DFA Response to PEER Committee Draft Report on Contracts for Service

This report purports to address the issue of competitive bidding for professional and personal services by the Department of Finance and Administration (DFA). However, because it contains incomplete information, inaccuracies, and misunderstanding of the law, its usefulness is seriously undermined. The report apparently concludes that the Department of Finance and Administration uses a competitive bidding process to select most of its contractors. This is found to be the case despite the fact that Mississippi law does not require such a process for service contracts. We essentially concur in this conclusion with the qualification that the report seriously and substantially understates the heightened degree to which DFA uses a competitive bid process to select its contractors. The report also provides a survey of bid laws in selected other states. We find this interesting and think that it might be useful and recommend that it be provided to the appropriate committees of the legislature for their consideration. However, the report seems to imply that the laws of Wisconsin, Arkansas, and Alabama, among other states, are the standard by which agencies in Mississippi should be judged. In fact, the record indicates that the Mississippi Legislature has struggled for years over this issue without clear resolve. Meanwhile, this department will continue to competitively bid its contracts.

This report contains serious errors and oversights which cannot be allowed to go uncorrected. In the following paragraphs we describe more accurately the relationship between the Tort Claims Board and DFA, cite and describe the legal environment regarding State Personnel Board approval of contracts, correct the erroneous conclusion regarding the contact with Blue Cross Blue Shield of Mississippi, recalculate the percentage of contracts awarded competitively in FY 94 and provide similar data for FY 95. Also, attached is an article from the Wall Street Journal which we strongly recommend as suggested reading for the PEER staff (Attachment 1).

The Tort Claims Board was established in 1994 by the Mississippi Legislature. It is a board comprised of six ex-officio members and a chair appointed by the Governor. The ex-officio members are the Attorney General, the State Treasurer, the Insurance Commissioner, the Commissioner of Public Safety, the Executive Director of the Department of Environmental Quality and the Executive Director of the Department of Finance and Administration. The Chair is Mr. Frank Montague, former president of the Mississippi Bar. At the time that the third party administrator was chosen, the Tort Claims Board had no staff and Mr. Tommy Campbell, former member of the Mississippi Legislature and former State Fiscal Officer was engaged (with State Personnel Board approval) to initiate the business of the board. All policies, procedures and actions were those of the board. The Department of Finance and Administration, as a state agency had no role whatsoever in setting policy or otherwise determining the board's course of action on any matter. The process utilized for selecting the third party administrator was fair, open, competitive and appropriate to the circumstances as determined by this board and recorded in its minutes. The board's intent to hire a third party administrator was published in area newspapers. Seven firms responded or were contacted and all of them submitted proposals and were formally interviewed by the board. A detailed comparison of fees and an examination of credentials was conducted and reviewed by the entire board. Three finalists were selected who

were each interviewed again on two separate occasions before the lowest and best bidder was selected. This process was also necessary because this board had only 90 days to organize and assume the responsibilities assigned to it by law. While there are certain advantages to the use of "formal" RFP's as demonstrated by the track record of this agency, there are also circumstances where other processes are more appropriate. This was clearly one such situation and exception is taken to the suggestion to the contrary (see Attachment 1).

With respect to matters of State Personnel Board authority regarding contracts, the report is incomplete and misleading. Section 25-9-133 (2) of the Mississippi Code of 1972, as amended, provides that no person shall be employed by an agency for any period for any purpose except in an employment position authorized by legislative appropriation or by the body authorized by law to escalate budgets and approve employment positions under the guidelines established by the Legislature.

An exception to this provision lies currently in Section 25-9-107 (c) (x), as interpreted by the attached Attorney General's Opinion (Attachment 2), which states that any agency that employs state service employees may enter into contracts for personal and professional services only with the prior written approval of the state personnel director. It further states that prior to paying any warrant for such contractual services, the auditor of public accounts, or the successor to those duties, shall determine whether the contract involved was for personal or professional services, and if so, shall determine whether it was properly submitted to the state personnel director and approved; provided, however, that physicians, dentists, architects, engineers, veterinarians, attorneys and utility rate experts who are employed for the purposes of professional services, and other specialized technical services related to facilities maintenance, shall be excluded from the provisions of this paragraph. Section 25-9-107 (c) (x) was previously amended by Laws, 1984, Ch. 488, to allow the State Fiscal Officer oversight authority for determination and payment of personal service contracts. Personal service contracts are not otherwise defined by statutory law in Mississippi.

The Attorney General, in the opinion dated May 18, 1990, determined that successor to the Auditor of Public Accounts, is solely charged with determining whether a contract is for personal service, and therefore subject to State Personnel Board Approval (Attachment 2). If and only if the State Fiscal Officer determines that the contract in question is for personal services, should he authorize payment for the service. Due to the volume of requests for approval and at the behest of the State Personnel Board, the State Fiscal Officer historically has issued a memorandum each year that specifically addressed implementation of Section 25-9-107 (c) (x) as it relates to

personal service contracts. This practice became effective April 6, 1989. A memorandum from the State Fiscal Officer dated April 6, 1989 (Attachment 3) states, in part, that...

> "Conversely, the following contracts will not require the prior approval of the State Personnel Director for payment of warrants. . .
>
> (3) Those which are properly charged to object codes 165 and 169, as follows: (This list is not exhaustive and can be expanded as necessary with approval of the State Fiscal Officer.)"

By legislative mandate, in accordance with the opinion of the Attorney General and in cooperation with the State Personnel Board, the State Fiscal Officer since 1989 has implemented a policy for determination of what constitutes personal service contracts. This policy applies to personal service contracts of the Department of Finance and Administration as well as all other agencies. However, beginning in FY 95, such exclusions from State Personnel Board approval have been by State Personnel Board memorandum, rather than by determination of the State Fiscal Officer. DFA recognizes that the entire area of personal service contracts is problematic. This agency's approach, since 1989, has been to assist in solving the problem at hand and not to circumvent the law.

It is noted that § 31-7-13 - the purchasing statute - fails to recite that personal service contracts must be bid. Such was admitted in the PEER draft report. The laws of other states and generally of the American Bar Association are not legal standards or policies of this state. We must follow our own legislation.

The PEER draft report makes reference to the renewal of the Blue Cross Blue Shield of Mississippi (BCBSM) third party administrator contract. The third party administrator contract in question was originally signed in 1989 for three years with a two year renewal solely at the option of BCBSM (Attachment 4). DFA had no right under the contract to reject that renewal. No contract entered into by DFA subsequently has contained such a provision. The third party administrator contract in question was later extended for six months at DFA request in order to facilitate awarding a single contract for administration of state employee and public school employee health plans in accordance with the law and good management practice. In summary, the citation of this particular contract renewal as an example of the absence of competitive bidding is inaccurate and misleading and exception is taken.

Finally the report cites a very favorable trend of increasing the use of competitive bidding in awarding contracts by DFA. In fact, the record is far better than is cited. The basis for calculation selectively omits some parts of DFA and in particular omits the Bond Advisory Division which introduced competitive bidding for services in FY 93.

Of the FY 94 contracts reviewed by PEER, 9 out of 15 were competitively bid. The dollar value of these 9 contracts was 82% of the total dollar value of the 15 contracts selected for review. Included in the 6 which were not bid was a one year extension on a contract which had been in place for a three year period. Extension of this contract allowed us to develop a request for proposal during FY 94 and the contract was competitively bid for FY 95. Another one of the 6 contracts cited in this report as not bid for FY 94 had been competitively bid the previous year. The contractor selected was the same firm that has prepared the statewide cost allocation plan for approximately ten years; therefore, we did not feel it necessary to re-bid this contract in FY 94. Without including the costs for these two contracts, the total dollar value of contracts not bid would equal only 1.4% of those contracts selected for review in the PEER draft report.
Using the same criteria used for the PEER review (excluding repair and service contracts, amounts under $5,000, temporary day laborers, etc.), new contracts entered into during FY 94 and FY 95 by the Department of Finance and Administration, the Tort Claims Board, and the State Bond Commission were competitively bid for 95% of the dollar value of total contracts. Contracts not entered into through a competitively bid process were primarily through the State Bond Commission. Excluding the State Bond Commission's contracts, the total dollar value of new contracts let through a competitively bid process was 98%. The only contracts that were not bid by the State Bond Commission involved a very complicated debt restructuring which netted the state over $3 million in profit. Bidding this restructuring was considered carefully and only rejected as the preferred option after the State Bond Commission, not DFA, determined conclusively that a competitive bid was not feasible to accomplish the goal.

In summary, this agency has demonstrated a commitment above and beyond the stipulation of the law to competitive bidding and has established a verifiable and enviable record of that commitment. We are disappointed that the PEER staff in an inadequately researched and poorly reasoned report has failed to recognize that effort. We would wholeheartedly support in any way possible an initiative by the PEER Committee to increase the level of competitiveness in bidding for services throughout state government.

ATTACHMENT 1

Cut the Dead Wood

By PHILIP K. HOWARD

In the next few weeks, Congress will take up legislation that claims to streamline government contracting. Congress will lose a historic opportunity if it does not seize the moment finally to destroy the most wasteful part of modern American government.

A story about dead wood is a good place to start. For years, San Francisco has hired outside contractors to remove the dead trees in Golden Gate Park, at about $50,000 a shot. This year, a park bureaucrat noted a flier from a sawmill owner looking to buy logs. One thing led to another, and the sawmill owner offered to pay San Francisco about $40,000 for the privilege of taking away the dead wood. A bonanza of small proportions, to be sure, but every tax dollar counts.

The proposal, unfortunately, was unthinkable. Accepting a bid from one contractor, in the strange world of government contracts, would have been considered "favoritism." OK, how about calling up a few other lumber mills and getting some quotes? Out of the question: What about the unfairness to those not called? Or the unfairness to budding entrepreneurs who might form a new business to exploit the dead wood removal opportunities? No, the rules are clear: The dead wood contract must be published and made available to the world. Everyone interested can then engage in a formal process, generally taking a year or more, that promises "complete objectivity." The contract will be awarded to the low bidder who has understood and mastered the detailed contract specifications (including a certification of no dealings with unfriendly foreign states).

Someone sensible might observe that San Francisco's dead wood needs to be removed this year. Why not take the money now, and worry about procedural niceties later? But being practical is not what this is about. Government officials are too busy filling out forms in triplicate and chanting this mandatory refrain: "Government must always be fair." *Fair*? Fair to whom? Is it fair to San Francisco taxpayers to throw away $90,000? Why does government give a hoot about the other sawmills? It's just a contract, after all, not the exercise of regulatory power.

A Lot at Stake

How government lets contracts is not nearly as exciting as arguing over what government spends money on, like whether to fund "Sesame Street" or the Seawolf submarine. But the way government spends money is an established system across all levels of government. "Full and open competition" is its credo, a principle so high-sounding that Congress hasn't re-examined the basic premise of this bureaucratic utopia since it was unveiled over the past few decades.

A lot is at stake. Of America's gross domestic product, about 10%—or close to $500 billion per year (including $280 billion in federal funds)—gets spent through these procurement processes. The waste is staggering and completely unnecessary. The waste is not caused by bad management or human inefficiency, but by a defective idea: The rigid procedures designed to prevent squandering of public money, as it turns out, function almost perfectly to guarantee that the money gets squandered.

The system almost seems designed to avoid sensible commercial decisions. Negotiations with vendors are hopelessly distorted, for example, by the vendors' right to sue for any trumped-up unfairness in the process. In 1991, the Air Force awarded a large contract for desk-top computers. As is typical, the losing bidders sued. The Board of Contract Appeals, a federal agency that presides over this odd species of litigation, disagreed with the Air Force's criteria and overturned the award. After going through the process again, the Air Force awarded the contract to someone else. Predictably, the new losers appealed, on the ground that the Air Force had "incorrectly evaluated" their bids. Once again, the decision was overturned. This time, however, the winner paid off some of the losers by cutting them into the deal. This was not considered illegal or even shocking. Indeed, the Board of Contract Appeals had encouraged it. In other situations, the winners openly pay off losers with cash. How else can contracts be finalized?

"Objectivity" means that government has to prove that every bidder is treated exactly the same. Contract specifications are thus written in stone, usually taking months or years to prepare. But without the ordinary give and take, government ends up getting the wrong products, or products that don't work.

The rigid procedures designed to prevent squandering of public money, as it turns out, function almost perfectly to guarantee that the money gets squandered.

Sometimes the results are comical. In one incident detailed by the Kennedy School of Government at Harvard, the Defense Department ordered a cold-weather suit, specifying exactly the shape of the pieces of fabric and the thread to be used. It turned out that the pieces of fabric didn't fit each other, and the zipper was too long. Then, when those problems were ironed out, the designated thread wasn't suitable, so the suits fell apart. This is the system that gave us the $600 toilet seat.

As originally conceived, all this fairness was supposed to encourage more competition and better prices. But the rigidities, the paperwork, the legalisms and the long delays are all anathema to effective commerce. A representative of the construction industry, testifying before Congress a few years ago, observed that because of the "confusing and often contradictory array of regulations," contractors "routinely bid 10% to 30% higher than [for] similar work in the private sector." This is only the bid price, and understates the real waste. The Federal Aviation Administration, for example, recently tried a radical experiment: It asked bidders to submit alternatives to FAA's detailed specifications for a transceiver. An idea came back that did the job at barely one-fourth the cost and half the time.

Attack this waste across the $500 billion of government contracts, and the fight over the National Endowment for the Arts seems almost laughably insignificant (a greater contract efficiency of 1/30th of 1% equals the NEA's total budget). Half of the budget deficit of about $200 billion would be eliminated by 20% less waste in federal and local contracting.

The Clinton administration, to its credit, has been trying hard to institute various reforms. But without a legislative overhaul, it is practically impossible. Congress has stayed away from serious reform mainly because it feared—and here is the richest irony of all—that it would be accused of being careless with public money. Politicians can't seem to get beyond the linguistic pretense of "full and open competition" to the reality that it has become a synonym for central planning.

Last month, Rep. William Clinger (R., Pa.) tried to delete the "full and open competition" standard, and got voted down. Here's what one member of Congress said in leading the defeat of the Clinger bill: "Full and open competition is at the heart of the free market system . . . it guarantees that the government gets the best value." Mr. Clinger is now preparing a bill that will allow some give-and-take in the front-end of the contracting process. But, as if in penance, his draft bill actually expands the vendor's rights to "protest" on the other end, and will chill the give-and-take it purports to foster. Sens. William Cohen (R., Maine) and Carl Levin (D., Mich.) are also reform-minded, and propose abolishing the Board of Contract Appeals. A great idea. Except that they would just shift the right of vendors to appeal, albeit in simpler hearings, to another agency.

Not Rocket Science

So, what to do?

Buying goods and services isn't rocket science. For starters, just compare prices, and have a little give and take. The traditional bugaboos—avoiding favoritism and corruption—are far better managed through audits. Practically every modern study has concluded that the complex procedures just end up masking accountability and giving cheats a place to hide.

In the dead wood episode, when the sawmill operator saw his original two-page agreement become a one-inch-thick "request for proposals," he decided to feed the file into the shredder. America would go far forward toward solving its budget crisis if it did the same thing with government contracting regulations. Changing a gear or two of this Rube Goldberg machine will do almost nothing. The machine needs to be consigned to the junk heap, and replaced by contracting professionals—mere mortals—who are willing to take responsibility and be held accountable for the job that they do. Being practical, after all, used to be what America was about.

Mr. Howard, a lawyer in New York, is author of "The Death of Common Sense" (Random House, 1995).

ATTACHMENT 2

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AUTH Denise Owens-Mounger

RQNM James Dunn

SUBJ Retirement-Public Employees

SBCD 170

Actual Text of Opinion

1 Mr. James H. Dunn
Acting Executive Secretary
Public Employees' Retirement System
429 Mississippi Street
Jackson, Mississippi 39201-1005

2 Dear Mr. Dunn:

3 Your request for an official opinion has been received by this office and has been assign to me for research and response. Your request is as follows:

4 "We hereby respectfully request an official Attorney General's Opinion regarding the approval process for which PERS can enter into contracts with an actuary to serve the Board of Trustees and evaluation services or other such services as determined by the Board to be necessary for the effective and efficient operation of the System.

5 Section 11-25-119, paragraph 8, states:

> Duties of Actuary. The Board of Trustees shall designate an actuary who shall be the technical advisor of the Board on matters regarding the operation of the System and shall perform such other duties as are required in connection therewith.

6 Section 25-11-121, paragraph 6, states:

> subject to the above terms, conditions, limitations, and restrictions, the Board shall have power to sell, assign, transfer, and dispose of any of the securities and investments of the System provided that said sale, assignment, or transfer has the majority approval of the entire Board. The Board may employ or contract with investment managers, evaluation services or other such services as determined by the Board to be necessary for the effective and efficient operation of the System.

7 Our specific question is: Is State Personnel Board approval required prior to PERS entering into contracts on the

aforementioned items.

8 Section 25-9-133 (2) of the Mississippi Code of 1972, as amended, provides that no person shall be employed by an agency for any period for any purpose except in an employment position authorized by legislative appropriation or by the body authorized by law to escalate budgets and approve employment positions under the guidelines established by the Legislature.

9 An exception to this provision lies in Section 25-9-107 (c)(x), which authorizes the employment of contract personnel for personal and professional services. This provision states that any agency that employs state service employees may enter into contracts for personal and professional services only with the prior written approval of the state personnel director. It further states that prior to paying any warrant for such contractual services, the auditor of public accounts, or the successor to those duties, shall determine whether the contract involved was for personal or professional services, and if so, shall determine whether it was properly submitted to the state personnel director and approved; provided, however, that physicians, dentists, architects, engineers, veterinarians, attorneys and utility rate experts who are employed for the purposes of professional services, and other specialized technical services related to facilities maintenance, shall be excluded from the provisions of this paragraph.

10 In making the above determination, the State Fiscal Officer issued a memorandum dated April 20, 1990, that specifically addresses the issue of implementation of Section 25-9-107 (c)(x) of the Mississippi Code of 1972, as amended. This memorandum states, in part, that...

11 "Conversely, the following contracts will NOT require the prior approval of the State Personnel Director for payment of warrants:

12 1) Those which are properly charged to object codes other than 61651, 61680, and 61690. (Each purchase order citing those other codes will be closely reviewed to ensure that it is properly coded for the services to be rendered.)"

13 Effective 7/1/89, the Fiscal Management Board established a revised chart of accounts. On this chart of accounts is account number 61625 which is for the payment of professional fees for investment managers and actuaries. Thus, since the two services in question would be paid under this object code and since it is specifically excluded by virtue of the memorandum dated April 20, 1990, it is the opinion of this office that it would not be necessary for the State Personnel Board to give approval prior to PERS entering into contracts for the aforementioned services.

14 Sincerely,

15 MIKE MOORE, ATTORNEY GENERAL

16 BY: Denise Owens-Mounger
Special Assistant Attorney General

"SECTION 4. The Attorney General of the State of Mississippi is hereby directed to submit appropriate sections of this act, immediately upon approval by the Governor, or upon approval by the Legislature subsequent to a veto, to the Attorney General of the United States or to the United States District Court for the District of Columbia in accordance with the provisions of the Voting Rights Act of 1965, as amended and extended.

SECTION 5. This act shall take effect and be in force from and after October 1, 1994, or the date they are effectuated under Section 5 of the Voting Rights Act of 1965, as amended and extended, whichever date occurs later.

Cross references—
Additional fees for court reporters, see §§ 9-13-1 et seq.

CHAPTER 9

Statewide Personnel System

PERSONNEL ADMINISTRATION SYSTEM

New Sections Added

SEC.
25-9-120. Contract personnel not state service or nonstate service employees of state.
25-9-153. Operator of state-owned vehicle must have valid state drivers license.
25-9-155. Nonstate service employees to be given preference for state jobs over general public.

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§ 25-9-107. Definitions.

The following terms, when used in this chapter, unless a different meaning is plainly required by the context, shall have the following meanings:

(a) "Board" shall mean the State Personnel Board created under the provisions of this chapter.

(b) "State service" shall mean all employees of state departments, agencies and institutions as defined herein, except those officers and employees excluded by this chapter.

(c) "Nonstate service" shall mean the following officers and employees excluded from the state service by this chapter. The following are excluded from the state service:

(i) Members of the state Legislature, their staffs and other employees of the legislative branch;

(ii) The Governor and staff members of the immediate office of the Governor;

(iii) Justices and judges of the judicial branch or members of appeals boards on a per diem basis;

(iv) The Lieutenant Governor, staff members of the immediate office of the Lieutenant Governor and officers and employees directly appointed by the Lieutenant Governor;

(v) Officers and officials elected by popular vote and persons appointed to fill vacancies in elective offices;

(vi) Members of boards and commissioners appointed by the Governor, Lieutenant Governor or the state Legislature;

(vii) All academic officials, members of the teaching staffs and employ-

ees of the state institutions of higher learning, the State Board for Community and Junior Colleges, and community and junior colleges;

(viii) Officers and enlisted members of the National Guard of the state;

(ix) Prisoners, inmates, student or patient help working in or about institutions;

(x) Contract personnel; provided, that any agency which employs state service employees may enter into contracts for personal and professional services only with the prior written approval of the State Personnel Director. The State Personnel Director shall disapprove such contracts where the services to be provided could reasonably be performed by an employee in an authorized employment position. Prior to paying any warrant or such contractual services, the Auditor of Public Accounts, or the successor to the duties, shall determine whether the contract involved was for personal or professional services and if so, shall determine whether it was properly approved by the State Personnel Director and approved; provided, however, that physicians, dentists, architects, engineers, veterinarians, attorneys and utility rate experts who are employed for the purposes of professional services, and other specialized technical services related to facilities maintenance, shall be excluded from the provisions of this paragraph;

(xi) Part-time employees; provided, however, part-time employees shall only be hired into authorized employment positions classified by the board, shall meet minimum qualifications as set by the board, and shall be paid in accordance with the Variable Compensation Plan as certified by the board;

(xii) Persons appointed on an emergency basis for the duration of the emergency; the effective date of the emergency appointments shall not be earlier than the date approved by the State Personnel Director, and shall be limited to thirty (30) working days. Emergency appointments may be extended to sixty (60) working days by the State Personnel Board;

(xiii) Physicians, dentists, veterinarians, nurse practitioners and attorneys, while serving in their professional capacities in authorized employment positions who are required by statute to be licensed, registered or otherwise certified as such, provided that the State Personnel Director shall verify that the statutory qualifications are met prior to issuance of a payroll warrant by the auditor;

(xiv) Personnel who are employed and paid from funds received from a federal grant program which has been approved by the Legislature or the Department of Finance and Administration whose length of employment has been determined to be time-limited in nature. This subparagraph shall apply to personnel employed under the provisions of the Comprehensive Employment and Training Act of 1973, as amended, and other special federal grant programs which are not a part of regular federally funded programs wherein appropriations and employment positions are appropriated by the Legislature. Such employees shall be paid in accordance with the Variable Compensation Plan and shall meet all qualifications required by federal statutes or by the Mississippi Classification Plan;

(xv) The administrative head who is in charge of any state department, agency, institution, board or commission, wherein the statute

specifically authorizes the Governor, board, commission or other authority to appoint said administrative head; provided, however, that the salary of such administrative head shall be determined by the State Personnel Board in accordance with the Variable Compensation Plan unless otherwise fixed by statute;

(xvi) The State Personnel Board shall exclude top level positions if the incumbents determine and publicly advocate substantive program policy and report directly to the agency head, or the incumbents are required to maintain a direct confidential working relationship with a key excluded official. Provided further, a written job classification shall be approved by the board for each such position, and positions so excluded shall be paid in conformity with the Variable Compensation Plan;

(xvii) Employees whose employment is solely in connection with an agency's contract to produce, store or transport goods, and whose compensation is derived therefrom;

(xviii) Personnel employed by the State Prison Emergency Construction and Management Board, paid from funds from the "Correctional Facilities Emergency Construction Fund," or employed under contracts let or approved by the board for the construction, acquisition, lease, lease-purchase or operation of prison facilities. This subparagraph shall stand repealed from and after July 1, 1996.

(d) "Agency" means any state board, commission, committee, council, department or unit thereof created by the Constitution or statutes if such board, commission, committee, council, department, unit or the head thereof, is authorized to appoint subordinate staff by the Constitution or statute, except a legislative or judicial board, commission, committee, council, department or unit thereof.

SOURCES: Laws, 1994, ch. 377, § 1, eff from and after July 1, 1994; 1994 Ex Sess, ch. 26, § 18, eff from and after passage (approved August 23, 1994).

Amendment Note—

The first 1994 amendment provided that licensed nurse practitioners in authorized state employment positions shall not be considered state service employees.

The second 1994 amendment in the definition "Nonstate service" added paragraph (c), subparagraph (xviii), relating to personnel employed by the State Prison Emergency Construction and Management Board.

Cross references—

Preference for nonstate service employees for state jobs, see § 25-9-153.

§ 25-9-115. Specific duties and functions of board.

It shall be the specific duty and function of the State Personnel Board to:

(a) Represent the public interest in the improvement of personnel administration in the state departments, agencies and institutions covered by the State Personnel System;

(b) Determine appropriate goals and objectives for the State Personnel System and prescribe policies for their accomplishment, with the assistance of the Mississippi Personnel Advisory Council;

(c) Adopt and amend policies, rules and regulations establishing and maintaining the State Personnel System. Such rules and regulations shall not be applicable to the emergency hiring of employees by the Public Employees' Retirement System pursuant to Section 25-11-15(7). The rules and regulations of the Mississippi Classification Commission and the Missis-

ATTACHMENT 3

STATE OF MISSISSIPPI

RAY MABUS
GOVERNOR

MEMORANDUM

TO: State Agencies

FROM: Cecil C. Brown
State Fiscal Officer

SUBJ: Implementation of Sec. 25-9-107(c)(x), Ms Code Ann. (1972)

DATE: April 6, 1989

Effective immediately your Department must use the guidelines contained herein when determining whether or not a particular requisition for issuance of warrant requires the prior approval of the State Personnel Director before issuance of the warrant.

Section 25-9-107(c)(x) excludes contract personnel from the definition of "state service" within the statewide personnel system and further requires that certain contracts for personal and professional services be approved by the State Personnel Director. This Code section reads, in pertinent part, as follows:

> ...provided that any agency which employs state service employees may enter into contracts for personal and professional services only with the prior written approval of the state personnel director. The state personnel director shall disapprove such contracts where the services to be provided could reasonably be performed by an employee in an authorized employment position. Prior to paying any warrant for such contractual services, the auditor of public accounts, or the successor to those duties, shall determine whether the contract involved was for personal or professional services, and, if so, shall determine whether it was properly submitted to the state personnel director and approved; provided, however, that physicians, dentists, architects, engineers, veterinarians, attorneys and utility rate experts who are employed for the purposes of professional services, and other specialized technical services related to facilities maintenance, shall be excluded from the provisions of this paragraph.

Pursuant to the authority granted in this Code section, only those contracts properly chargeable to object codes 165 (Professional Fees, Other) and 169 (Other Fees and Services), with the exception of those identified below, will require the prior approval of the State Personnel Director for the payment of warrants.

Conversely, the following contracts will NOT require the prior approval of the State Personnel Director for payment of warrants:

1) Those which are properly charged to object codes: 160, DPW fees; 161, Engineering; 162, Architectural; 163, Legal; 164, Medical; 166, Court costs, Notaries; 167, Laboratory, Testing; and 168, Appraisers, Witnesses. (Each purchase order citing these codes will be closely reviewed to ensure that it is properly coded for the services to be rendered.)

2) Those contracts with a total annual cost of $400.00 or less.

3) Those services chargeable to object codes 165 and 169, as follows: (This list is not exhaustive and can be expanded as necessary, with the approval of the State Fiscal Officer.)

   Department of Audit fees
   State Personnel Board fees
   Funeral and/or mortuary services
   Facilities maintenance services as described in SPB Policy Memorandum No. 3-FY 1990
   Tower observers
   Election task force
   Land surveyors
   Polygraph services
   Art evaluators
   Student interns
   Microfilming services
   Home health care services ordered by a physician
   Entertainers/craftsmen/panelist for specific, limited engagements in state parks, or for Archives and History, or public radio and TV
   Temporary day laborers
   Interpreters for the deaf
   Institutional food services
   Land appraisers
   Flying service - spraying
   Officials - athletic events
   Newspaper clipping services

I am designating James Sanders, Director of FMB's Financial Control Division, as the individual responsible for responding to all inquiries.

Once it has been determined that prior approval of the State Personnel Director is necessary, you should insure that you have complied with the requirements of the State Personnel Board contained in Policy Memorandum No. 3 - FY 1990, Contract Personnel Services Policies and Administrative Procedures.

CCB:SMS:tj

ATTACHMENT 4

1. EFFECTIVE DATE OF CONTRACT.

The Effective Date is January 1, 1989.

2. TERM OF THE CONTRACT.

The term of the Contract extends from the Effective Date through December 31, 1991. The Administrator may extend the term of the Contract for an additional two-year period at the end of the initial term without rebidding if the parties reach agreement on the Administrator's adjusted fee schedule at least six months prior to December 31, 1991.

3. COMPENSATION.

In consideration of the Administrator's services under this Contract, SFMB will pay the Administrator a set monthly administrative fee for each active and retired employee enrolled under the state employees health insurance plan. Effective January 1, 1990, SFMB will pay the Administrator a fee per contract per month of $3.04. It is understood and agreed that the monthly fee includes a claims administration service fee of $2.86 and a billing and eligibility file fee of $.18. In addition, effective February 1, 1989, SFMB will pay the Administrator a monthly fee of $.05 for each active and retired employee enrolled under the state employees health insurance plan for implementation of pre-certification and re-certification of private duty nursing care under this Contract. SFMB will make payment by the fifteenth day of each month based on enrollment data as of the first day of the month.

4. FEE ADJUSTMENTS.

Unilateral adjustments by the Administrator of its fee for services can take place no more often than annually and upon six months' notice of intent to adjust. Any annual increase will be limited to no more than the posted adjustment in the Social Security wage index.

5. TERMINATION OF CONTRACT.

The Contract may be terminated by either party without cause upon (6) six months' prior notice of intent to terminate. SFMB may give notice of intent to terminate on shorter notice

PEER Staff

Director

John W. Turcotte
Merrin Morgan, Intern

Administrative Division

Steve Miller, General Counsel and Controller

Shirley Anderson
Ann Hutcherson
Mary McNeill

Planning and Support Division

Max Arinder, Chief Analyst

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Larry Landrum
Kathleen Sullivan
Bonita Sutton
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Operations Division

James Barber, Chief Analyst

Mitchell Adcock
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Barbara Hamilton
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Katherine Stark
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Linda Triplett
Larry Whiting