California State Auditor

BUREAU OF STATE AUDITS

Investigations of Improper Activities by State Employees

February Through June 2001

September 2001
I2001-2

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CALIFORNIA STATE AUDITOR

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September 6, 2001 Investigative Report I2001-2

The Governor of California
President pro Tempore of the Senate
Speaker of the Assembly
State Capitol
Sacramento, California 95814

Dear Governor and Legislative Leaders:

Pursuant to the California Whistleblower Protection Act, the Bureau of State Audits presents its investigative report summarizing investigations of improper governmental activity completed from February through June 2001.

Respectfully submitted,

Elaine M. Howle

ELAINE M. HOWLE
State Auditor

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SUMMARY

Investigative Highlights . . .

State employees engaged in improper activities, including the following:

- ☑ *Circumvented state requirements and misled superiors when awarding contracts totaling more than $800,000.*
- ☑ *Used state time and resources to run and participate in an illegal gambling pool.*
- ☑ *Falsified records to avoid having to conduct a full investigation of a consumer complaint.*
- ☑ *Failed to take prompt formal action to terminate an employee who was doing no work and essentially gave her a $105,000 gift of public funds.*
- ☑ *Gave flawed legal advice to two state employees resulting in violations of the Political Reform Act.*
- ☑ *Improperly paid almost $3,000 for one employee's commuting expenses.*
- ☑ *Used state time, telephones, and vehicles to sell real estate.*

RESULTS IN BRIEF

The Bureau of State Audits (bureau), in accordance with the California Whistleblower Protection Act (act) contained in the California Government Code, beginning with Section 8547, receives and investigates complaints of improper governmental activities. The act defines "improper governmental activity" as any action by a state agency or employee during the performance of official duties that violates any state or federal law or regulation; that is economically wasteful; or that involves gross misconduct, incompetence, or inefficiency. To enable state employees and the public to report these activities, the bureau maintains the toll-free Whistleblower Hotline (hotline). The hotline number is (800) 952-5665.

If the bureau finds reasonable evidence of improper governmental activity, it confidentially reports the details to the head of the employing agency or the appropriate appointing authority. The employer or appointing authority is required to notify the bureau of any corrective action taken, including disciplinary action, no later than 30 days after transmittal of the confidential investigative report and monthly thereafter until the corrective action concludes.

This report details the results of the eight investigations completed by the bureau and other state agencies on our behalf between February 1 and June 30, 2001, that substantiated complaints. Following are examples of the substantiated improper activities and actions taken to date.

DEPARTMENT OF GENERAL SERVICES

A manager in the Office of Small Business Certification and Resources made verbal agreements with a consultant hired to perform information technology services costing $665,103 instead of following the State's formal contracting procedures, which require advertising the work, seeking competitive bids, and entering into formal contracts. She also improperly used

CAL-Cards assigned to five of her subordinates to pay $463,444 to the consultant. CAL-Cards are state procurement cards intended for small purchases. Although she prepared purchase orders so she could pay the consultant the other $201,659, she did not actually issue them to the consultant, an action that would have established a formal, enforceable agreement. Finally, the manager did not notify the appropriate office within the Department of General Services (DGS) of the payments made through the purchasing cards so that office could report the payments to federal and state tax authorities. The manager took another job in state government before DGS discovered her activities. Consequently, DGS could not take action against her.

DEPARTMENT OF TRANSPORTATION

Several employees in the Department of Transportation's Sacramento warehouse used state time and resources to run and participate in an illegal gambling pool on the outcome of professional football games. The warehouse manager warned the employees to stop.

CONTRACTORS STATE LICENSE BOARD

A Contractors State License Board (license board) investigator falsified investigative records to avoid having to conduct a more in-depth investigation of a consumer complaint against a construction contractor. Because the investigator retired, neither the license board nor the Department of Consumer Affairs was able to take action against the investigator.

GOVERNOR'S OFFICE OF EMERGENCY SERVICES

An executive and contract manager in the Disaster Assistance Division of the Governor's Office of Emergency Services (OES) engaged in the following improper activities:

- Falsely claimed that they had made reasonable attempts to identify alternative and competitive sources of training services and that they had verified references for their preselected contractor. Ultimately, this improperly awarded contract totaled $77,500, and OES paid the contractor for some work not provided.

- Apparently misled their deputy director about the subject matter of training to be provided on a $36,985 contract to obtain her approval. Then they exceeded their authority by changing the scope of the contract without proper approval. Ultimately, the contact was amended to total $90,588.

OES also made payments under at least one contract for expenses not allowed under state regulations and entered into other contracts lacking sufficient specificity. OES does not agree that its executive and contract manager made false claims concerning their efforts to identify alternative contractors or that they misled their deputy director. However, OES is reviewing its contractor's bills and will recover overpayments or seek additional training if it concludes they made payments in error. Also, OES agrees that it improperly paid for some expenses and has taken action to ensure it does not happen again.

SAN JOSE STATE UNIVERSITY

San Jose State University (university) gave one employee $129,304 in full pay and benefits from February 1, 1999, through May 31, 2000, without requiring her to report to work or to provide any services to the university. Because the university was only required to pay the employee for three months after notice of termination, $105,308 of the amount it paid her for no services amounts to a gift of public funds in violation of the California Constitution. In addition, the university paid five consultants $380,519 to perform some of the employee's duties in her absence. At least a portion of the cost for the consultants was a waste of state funds. If the university had promptly terminated the employee, it could have hired a regular employee to do her work.

The university disagrees that its payments constitute a gift of public funds and believes that it acted prudently in light of an unresolved lawsuit the employee had against it. The university also disagrees that any of its payments to the consultants were a waste of funds.

DEPARTMENT OF EDUCATION

Employees of the Department of Education (education) engaged in the following improper activities:

- One supervisor, who helped administer a $3.8 million child development contract with a company, violated conflict-of-interest prohibitions when she left her job at education to go to work for the company and then communicated with other education employees on behalf of her new employer. She also improperly advised and assisted her new employer with the same contract.

- Another supervisor appeared to violate conflict-of-interest prohibitions by communicating with education officials within 12 months of leaving his job at education to go to work for a private company. His communications with education officials concerned his new employer's applications for new state contracts.

- Education's legal office gave the two supervisors flawed legal advice concerning restrictions on what they could do in their new jobs.

Because the two supervisors relied on the legal office's advice, the Fair Political Practices Commission decided not to take formal enforcement action against them.

OFFICE OF THE STATE PUBLIC DEFENDER

The Office of the State Public Defender (public defender) inappropriately paid an employee $2,987 in commuting expenses. The Department of Personnel Administration directed the public defender to stop paying for the employee's commuting expenses.

DEPARTMENT OF TRANSPORTATION

An employee of the Department of Transportation (Caltrans) Division of Highways in Oakland used state time, telephones, and vehicles for his real estate business. Caltrans issued a letter of warning to the employee.

This report also summarizes actions taken by state entities as a result of investigations presented here or reported previously by the bureau.

Appendix A contains statistics on the complaints received by the bureau from February 1 through June 30, 2001, and summarizes our actions on those and other complaints pending as of January 31, 2001. It also provides information on the cost of improper activities substantiated since 1993 and the corrective actions taken as a result of our investigations.

Appendix B details the laws, regulations, and policies that govern the improper activities discussed in this report.

Appendix C provides information on actual or suspected acts of fraud, theft, or other irregularities identified by other state entities. Section 20080 of the State Administrative Manual requires state agencies to notify the bureau and the Department of Finance of actual or suspected acts. It is our intention to inform the public of the State's awareness of such activities and to publicize that agencies are acting against wrongdoers and working to prevent improper activities.

See the Index for an alphabetical listing of all agencies addressed in this report. ■

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CHAPTER 1

Department of General Services: Improper Contracting and Contract Payments

ALLEGATION I2000-779

A manager in the Office of Small Business Certification and Resources (office of small business) at the Department of General Services (DGS) improperly hired a consultant. Additionally, the manager improperly paid for the consultant's services by using state purchasing cards assigned to five of her subordinates.

RESULTS AND METHOD OF INVESTIGATION

DGS was already conducting an investigation into the same issues, and we asked that it report its findings to our office. DGS reported that it substantiated the allegations. The manager hired an information technology consultant through verbal agreements instead of using the State's formal contracting procedures, which require advertising the work, seeking competitive bids, and entering into a formal contract.[1] Additionally, DGS found that the manager used her subordinates' CAL-Cards to pay $463,444 (70 percent) of the $665,103 total cost of the consultant's services. CAL-Cards are procurement cards for state employees to use when making small purchases.

The manager paid the remaining cost by submitting purchase orders internally to encumber the required funds, but because she never sent the purchase orders to the consultant, she failed to establish an enforceable contractual relationship. Furthermore, DGS found that the improper payment process resulted in its failure to issue the required 1099 tax forms to the Internal Revenue Service and the Franchise Tax Board (1099s report

[1] For a more complete description of the laws and policies covering state contracts, see Appendix B.

payments made to consultants). Despite these improper governmental activities, the consultant's records supported the charges on the invoices and the hourly rates were reasonable.

To investigate the allegations, DGS interviewed the manager, the former and current chiefs of the office of small business, the consultant, the five subordinates whose CAL-Cards were used for the payments, and information technology support staff. Additionally, DGS reviewed all the invoices the consultant submitted and analyzed the available supporting data. DGS also reviewed the consultant's employee time-keeping records to validate charges on the invoices.

BACKGROUND

The manager responsible for the improper governmental activities left her position with the office of small business in May 2000 to take a position with another state agency. On July 1, 2000, DGS reorganized the office of small business under the procurement division, reducing its operations to a single function and distributing responsibility for the remainder of its operations to other existing programs. Soon after the reorganization, the new staff members assigned to process payments to the consultant realized that previous payments were unusual and brought their concerns to the attention of the division's acting deputy director.

MANAGER IMPROPERLY CONTRACTED FOR SERVICES

A manager verbally committed more than $650,000 in state funds to a consultant, bypassing the State's contracting process.

The manager did not seek competitive bids and improperly made verbal agreements with the consultant for services instead of complying with the State's formal requirements for information technology contracting. The total cost of these agreements from November 19, 1998, to June 30, 2000, was $665,103. The consultant's primary responsibility was maintaining the Web site and various databases of the office of small business, but he also worked on a number of special projects. Because the manager bypassed the standard contracting process, she denied other contractors the opportunity to compete for the State's business. Furthermore, because the contract was not in writing, the State could not verify critical contracting elements, such as the scope of work, the cost, and the period allowed for completing the

contract. The manager said that she engaged the consultant verbally because she needed the services quickly. She also said that she did not realize the significance of her failure to comply with contracting requirements.

MANAGER CIRCUMVENTED NORMAL PAYMENT PROCESSES

A DGS manager directed a consultant to split charges onto multiple invoices to keep costs below certain limits and improperly used state credit cards to pay the invoices.

DGS's policies for using CAL-Cards limit the amount that can be charged for a single transaction and for a 30-day period. Therefore, the manager advised the consultant to split his invoices to stay below the individual card limits and used CAL-Cards assigned to five of her subordinates to pay the invoices. The consultant charged a total of $463,444 to these five cards for 164 invoices dated from November 19, 1998, to June 30, 2000. Because the manager had given the CAL-Card numbers to the consultant, he continued to submit charges incurred after the manager's departure in May 2000. The charges appearing after the manager's departure alerted the office of small business to the problem and led to the internal investigation. This misuse of CAL-Cards, coupled with the manager's improper contracting practices, violates acceptable internal control procedures that require separation of duties. The manager alone authorized the consultant to perform the services, certified that the department received the services, and authorized the payment of invoices.

The manager explained that she directed the consultant to split invoices and used the CAL-Cards to make payments because the department's accounting system did not meet her need to expedite payments. However, she acknowledged that she knew her use of the cards was improper. Although her subordinates were not involved in obtaining the services of the consultant and were not aware of the services provided, they deferred to the manager's judgment in allowing their cards to be used for the payments. These employees did not know that DGS policies do not allow another person to use their cards because the department did not train them regarding those policies.

The manager also made improper payments to the consultant through the use of incomplete purchase orders. Instead of using the purchase orders as a contractual vehicle, she used them only to encumber funds that could be used to make payments through the

State's normal payment process. The manager did not send the purchase orders to the consultant to authorize and describe the scope of his work, as required. The manager used this technique to authorize payments to the consultant totaling $201,659.

In addition to making these improper payments, the manager did not notify the DGS Office of Fiscal Services (fiscal services) that she made payments to the consultant using CAL-Cards. Consequently, fiscal services did not notify federal and state tax authorities about these payments, which are taxable income to the consultant.

CONSULTANT'S RECORDS SUPPORT INVOICES

Due to weaknesses in the internal controls of its contracting and payment processes, DGS had some concerns regarding the propriety of the hours and rates charged by the consultant. Therefore, DGS auditors performed tests of the consultant's time-keeping records and found them adequate to support the charges on the invoices. The auditors also interviewed the acting chief of the office of small business, who has extensive experience in the information technology field, and confirmed that the contractor's rates were reasonable and significantly lower than those allowed under the current California Multiple Award Schedule, a contract awarded to multiple contractors for the same and similar products and costs.

AGENCY RESPONSE

Because the manager left her position at the office of small business in May 2000, before DGS began its investigation, it took no adverse action against her. DGS reported that its reorganization of the office of small business corrected the improper use of CAL-Cards and other contracting weaknesses; the procurement division now oversees the use of the cards. Furthermore, DGS canceled the five cards used for the improper payments and stopped paying the contractor with CAL-Cards.

Finally, DGS stated that it reported the consultant payments to fiscal services, which will take the required action to notify tax authorities of the payments. ■

CHAPTER 2

Department of Transportation: Illegal Gambling

ALLEGATION I2000-801

Employees at the Sacramento warehouse of the Department of Transportation (Caltrans) used state time and resources to run and participate in an illegal gambling pool.[2]

RESULTS AND METHOD OF INVESTIGATION

Caltrans investigated and substantiated that several warehouse employees participated in an illegal gambling pool. To investigate the allegation, Caltrans interviewed warehouse employees and reviewed documents we provided.

We gave Caltrans documents related to gambling pools on professional football games that had been faxed to or from Caltrans and asked the agency to investigate the allegation on our behalf. These documents included wager tickets on which bettors would mark the teams they believed would win professional football games during a one-week period. Bettors would also indicate the total number of points they believed would be scored during the Monday Night Football game. Another document we provided to Caltrans appeared to be a compilation of all the wagers placed on the results of one week of professional football games. According to those documents, nearly 30 individuals participated in this pool. We were unable to determine how many of the individuals worked for Caltrans or other state agencies.

AGENCY RESPONSE

After beginning its investigation, Caltrans learned that the warehouse manager had earlier become aware of these activities and warned the employees to stop. Caltrans reported that there has been no recurrence of the gambling activities since. ■

[2] For a description of the state law prohibiting the activities described here, see Appendix B.

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CHAPTER 3

Contractors State License Board: Falsification of Investigative Records

ALLEGATION I2000-670

A Contractors State License Board (license board) investigator filed a report containing false information about a contractor that resulted in improper closure of the case.

RESULTS AND METHOD OF INVESTIGATION

We referred the allegation to the Department of Consumer Affairs (consumer affairs) for investigation on our behalf, because the license board is part of consumer affairs. In turn, consumer affairs referred the investigation to the California Highway Patrol (highway patrol). The highway patrol substantiated the allegation, concluding that the investigator intentionally falsified a report to avoid having to conduct a more in-depth investigation of a consumer complaint concerning the contractor.

To investigate the allegation, the highway patrol interviewed various license board employees. It also reviewed correspondence between the consumer who filed the complaint against the contractor and the license board, a copy of the consumer's original complaint, copies of the license board investigation records and organizational charts, the license board investigator's personnel file, and internal correspondence related to the license board investigator's professional behavior in other instances.

BACKGROUND

The license board was established in 1929 at the request of the building industry to protect consumers by regulating the construction industry. Its field office staff investigate consumer complaints against contractors, and the license board initiates disciplinary actions against contractors guilty of violating the law or other established guidelines.

The license board assigned an investigator to a consumer's complaint charging a contractor—contractor A—with abandonment, faulty construction, breach of contract, fraud, and misrepresentation related to an addition to and remodeling of her home. The investigator reported that he interviewed another contractor—contractor B—who took over the complainant's project after the alleged abandonment by contractor A. The investigator reported that he asked contractor B to provide a statement of the condition of the project at the time he took it over, but contractor B refused to cooperate. The investigator relied on this alleged refusal to conclude that the case should be closed with no legal action against contractor A because of insufficient evidence.

INVESTIGATOR FALSIFIED A REPORT

The highway patrol found that the preponderance of evidence suggested that the investigator intentionally falsified the report to avoid conducting a more in-depth investigation. The supervisor of the license board's eight investigative centers told the highway patrol that he had interviewed contractor B. According to the supervisor, contractor B told him that the license board's investigator said that he was "retiring soon and wanted this complaint to go away." The same supervisor told the highway patrol that contractor B denied refusing to cooperate with the investigator. Contractor B confirmed to us that he did not tell the investigator that he would not cooperate with the investigation.

The investigator told one witness that he was retiring soon and wanted the consumer complaint to go away.

The highway patrol concluded that contractor B advised the license board's investigator that he would cooperate and, therefore, the investigator's statement to the contrary in his report was clearly false. According to the highway patrol, the investigator's purported desire for "this complaint to go away" lent credibility to the view that the investigator intentionally placed a false statement in the report. Further, the highway patrol found that a legal action deputy who reviewed the case file after it was closed believed that the investigator should not be working for the license board because he was not thorough in his investigations. The legal action deputy held the opinion that the investigator made every effort to settle cases and close them without taking any actions, even in the presence of clear violations. Therefore, the highway patrol concluded the evidence strongly suggested that the investigator intentionally

falsified his report. Furthermore, the highway patrol concluded that the investigator's claim that contractor B refused to cooperate was the central basis for the otherwise premature closure of the case. However, the highway patrol concluded that the investigator's actions did not constitute criminal violations.

AGENCY RESPONSE

The license board reopened the consumer's original case. Consumer affairs reported that it took no punitive or corrective action against the investigator because he retired before it could do so. Nevertheless, to avoid similar occurrences in the future, the license board has instituted semiannual quality control audits. ■

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CHAPTER 4

Office of Emergency Services: Contracting Improprieties

ALLEGATION I990186

The Governor's Office of Emergency Services (OES) improperly awarded a sole-source contract and failed to follow proper contracting procedures.

RESULTS AND METHOD OF INVESTIGATION

We investigated and substantiated the allegation and other improprieties. In fact, we found that an executive and a contract manager in OES's Disaster Assistance Division (division) frequently circumvented state requirements for contracting for services. In one instance (contract 1), the two employees misrepresented their efforts to identify alternative and competitive sources of training services to obtain approval by the Department of General Services (DGS) for a $37,500 training contract. The executive and the contract manager falsely claimed that they had considered training services provided by state departments and that they had verified references for their preselected contractor. Because of the actions of these employees, OES neither advertised the work nor solicited competitive proposals. Consequently, it denied others the opportunity to compete for the State's business and may have paid more than necessary. OES later amended the contract, raising the total to $77,500. Further, OES paid the contractor for some services not provided.

In another instance (contract 2), the same executive and contract manager misled their deputy director about the subject matter of a training program to obtain her approval on a $36,985 contract request. The executive and contract manager then exceeded their authority by changing the scope of the contracted services, which, after amendments, increased the contract amount to $90,588. We believe OES paid too much for the training provided under this contract.

As a further demonstration of OES' mismanagement of contracts, we found that it paid for meals in violation of state regulations and paid a vendor too much to perform administrative tasks. OES also entered into contracts that lacked specificity. Thus, the individuals approving the contracts and payments did not have appropriate information to make informed decisions.

To investigate the allegations, we reviewed contract files, invoices, and claim schedules. In addition, we obtained information from contractors and interviewed OES contract managers and other personnel.

OES IMPROPERLY AWARDED A SOLE-SOURCE CONTRACT

OES unfairly limited competition and has no assurance it obtained the best price or services.

In violation of state rules, OES improperly awarded a sole-source contract for training services, denying other entities an opportunity to compete for the work.[3] Although the contract file documentation indicates OES researched other state sources for providing the training, we do not believe it made a good faith effort to find alternatives. Without obtaining competing proposals, OES could not be sure that it obtained the best price for the best services. In fact, OES paid for some services this contractor did not provide.

Statutes, regulations, and policies governing the State's contracting process are designed to protect the State's interests. Therefore, it is not appropriate to create artificial exceptions to contracting requirements or seek loopholes. In particular, as noted in the State Contracting Manual, circumvention of required competitive bidding or contract approval is illegal.

BACKGROUND—CONTRACT 1

During the winter of 1997-98, OES responded to El Niño storms that caused severe flooding in many California counties. According to an OES executive, although OES had several hundred employees in the field, they were unable, either by inclination or skill, to adequately represent OES to the media or other interested parties. The executive further stated that OES's

[3] For a more detailed description of the state laws, regulations, and policies discussed in this chapter, see Appendix B.

experiences during the El Niño disaster made it very clear that having only a few people who could speak to the media was not realistic. Consequently, he wanted to offer training to OES employees on how to deal with the media; the public; and government officials, such as members of the Legislature, in case of a disaster. The executive told us his goal in offering this type of training to OES employees was to give them practical exercises and help change organizational thinking, not simply to have an instructor make a noninteractive presentation. Also, he wanted to be able to customize such a class.

The executive discussed his desire to offer this type of training with a public information officer hired by OES on an emergency basis during the El Niño storms.[4] The public information officer was also the owner of a private company, company A, that provides public speaking and media training. The executive and public information officer agreed to discuss such training when the public information officer's temporary employment at OES ended. After the public information officer was no longer working for OES, the executive further discussed with him the possibility of presenting a class to OES employees. The executive informed the owner of company A that he would request a sole-source authorization; if the request failed, he would send the proposal out to bid. In a sole-source transaction, only a single business enterprise is afforded the opportunity to offer the State a price for the specified goods or services.

On May 11, 1998, approximately one month after the public information officer ceased to be an OES employee, he submitted a proposal to OES, including a general course outline and cost information indicating how much company A would charge to provide the services described.

CONTRARY TO ITS REPRESENTATIONS, OES DID NOT SEEK AN ALTERNATIVE SOURCE

A governor's order prohibits the use of sole-source contracts or procurements except in a state emergency when required for public health and safety. To obtain an exemption to enter into a sole-source transaction, a department must submit a request for exemption to DGS. The form must include either of the

[4] The public information officer worked as an OES employee for approximately six weeks during March and April 1998.

following: (1) a survey of the marketplace, if possible, or a narrative of the efforts made to identify similar appropriate services (including a summary of how the agency came to the conclusion that such alternatives are either inappropriate or unavailable) or (2) an explanation about why the survey or other effort was not done.

The OES official told us he was in a hurry to plan and schedule the training before another disaster occurred.

The executive told us he was in a hurry to plan and schedule the training before another disaster occurred. Contrary to his statement, however, the need for these services did not constitute a state emergency, and OES did not present it as an emergency in its documentation. In fact, in its request for exemption, OES claimed to have looked for other sources in state government to provide the training. Prepared at least in part by the contract manager, the request for exemption implied OES had researched the courses offered by the State Training Center (STC) as an alternative. Before submitting the request for exemption to DGS, OES employees prepared an internal contract request form. One of the items on this form instructs the preparer to "document efforts made to determine why OES personnel or other state agencies cannot do this work. List names of agencies contacted, and explain why they cannot provide the requested service."[5] The form completed for this contract states that staff researched training alternatives, including classes offered by the STC and the California Specialized Training Institute (CSTI). Although the form indicates it was submitted by the contract liaison, she told us she believes that the contract manager provided her with the information because no one else was substantially involved with the request.

It seems evident that, contrary to its claims, OES did not make a good faith effort to find alternative sources for the training. Specifically, no one at OES actually spoke with anyone at the CSTI or the STC. The executive told us he was aware that the CSTI offered a five-day course on dealing with the media during emergencies. He did not find it acceptable because the course was geared toward media professionals or staff who might be called on to fill the role of public information officer and was not intended to cover the incidental types of contacts included in company A's proposal. Further, the contract manager said he reviewed CSTI course listings and did not remember seeing any

[5] State law allows agencies to contract for personal services to achieve cost savings if they can demonstrate that it would cost less to contract for the services than it would to have state civil service employees perform the work as part of their jobs.

course that matched the depth of training OES was looking for; therefore, he did not see the need to contact the CSTI directly for further information. The CSTI is OES's training arm and, according to the OES Web site, is responsible for coordinating all OES training.

The executive said he considered the STC but had concerns about its ability to provide this type of highly customized training course. However, in its schedule of classes, the STC states that it realizes customers have unique needs and that it can customize its classes accordingly.

The contract manager said he reviewed the STC schedule of classes to determine whether it offered any comparable courses. He told us that, based on his review, OES employees would have had to take three separate courses to obtain the same training offered by company A: Media Skills Workshop, Effective Presentations, and Legislative Process. This information was included in OES's request for exemption. However, we question whether these three classes were all relevant to what the executive said he wanted to achieve with the training. Specifically, the Legislative Process class is an overview to help participants follow the path of a bill from its introduction in the Assembly to its signature by the governor. In our opinion, the path of a bill is not necessary knowledge for employees to disseminate information regarding emergencies or disasters to legislators or their staff. The contract manager initially provided us with an explanation as to why he thought the Legislative Process class was relevant, saying he thought it was useful for employees to know how legislators work and to have a better understanding of the environment in which the legislators operate. When we attempted to clarify with him our understanding of his explanation, he neither confirmed nor elaborated on his initial response. The contract manager simply said that he was not aware that the STC could customize courses and that he did not contact the STC about possibilities beyond its advertised classes.

It appears that the executive and contract manager made their decision to hire the contractor before they even nominally researched alternatives.

We have no confidence in the research efforts of either the executive or the contract manager. Based on their comments, it appears they made their decision to hire company A before they even nominally researched alternatives. The executive told us that, although other private companies might have been able to offer services similar to the training obtained from company A, he was not sure if it was worth the time and effort to check with

them. However, OES spent a substantial amount of time and effort obtaining its sole-source contract with company A. From the time the contractor submitted his proposal in May 1998, it took one year to obtain the required approvals on OES's request for exemption. Much of this time was spent responding to questions raised internally and by DGS and revising the request for exemption and the contract. We doubt OES achieved any efficiencies by seeking a sole-source contract. Moreover, OES denied other entities the right to compete for this business and may not have received the best training at the best price.

OES AMENDED THE CONTRACT TO $77,500 AND PAID FOR SERVICES NOT PROVIDED

According to the attendance sheets for the classes, it appears that 96 OES employees attended the training course under the original $37,500 contract at a cost of approximately $390 each. Attendees included program managers, emergency services coordinators, disaster assistance program specialists, engineers, analysts, and office assistants. The evaluations indicate the attendees felt the course was valuable and they would recommend it to others.

Effective September 20, 2000, OES amended the original contract with company A, increasing the total to $77,500. The amendment called for company A to provide the same basic training course to an additional 40 employees at a cost of $375 each, advanced training to 20 employees at $975 each, and individual training to 4 employees at $1,000 each. An additional $1,500 covered supplies and travel expenses. Although the amendment did not indicate the length of the courses, according to the attendance sheets, the basic course was one day, the advanced course was two days plus an individual 45-minute meeting with the instructor, and the individual course was two days.

Even though only two of four employees attended the entire course and one of the four completed half of it, OES paid the consultant as if all four employees completed the training.

OES planned to have four employees attend the individual course; however, due to scheduling problems, three employees attended the first day of the course and only two of those three attended the second day. Although the contract amendment specified the costs were per person, company A billed OES for four people, the maximum allowed under the contract, and OES approved the invoice for payment. Since only two people completed the individual course and a third person only completed

half of it, we do not believe company A was entitled to the full $4,000 it charged OES. Also, as mentioned previously, by awarding this contract and amendment the way it did, OES denied other entities the opportunity to compete for its business.

OES Had Other Inaccurate and Incomplete Documentation Regarding Contract 1

State law requires each state agency to maintain effective systems of internal accounting and administrative control as an integral part of its management practices. Elements of a satisfactory system of control include an established system of practices to be followed in performance of duties and functions in each of the state agencies and an effective system of internal review. State law also specifies that dishonesty, incompetency, and inefficiency are all causes for disciplining state employees.

Although OES has a system to assess the competency of potential contractors, it appears that at least some OES employees are not following the procedures. Specifically, the OES contractor competency assessment form asks the preparer whether the company has provided at least three references and says the references must be verified. Although the response on the assessment form indicates company A provided the references and OES verified them, according to the contract manager and the division's contract liaison who completed the form, they did not verify the references.[6] Moreover, this form indicates the company history or a consultant's resume was received and experience was verified; however, we could not locate either the company history or the consultant's resume in the contract file or any documentation other than the form itself to indicate that the information was verified. Although it is unclear whether the employees falsified the form intentionally or inadvertently, the result is inaccurate information in the contract file. Therefore, the individuals responsible for approving contracts, including those at DGS, may be making decisions based on misleading information.

Although OES employees claimed they had reviewed the consultant's history and verified his experience, they did not.

[6] Although the division's contract liaison's electronic signature appears on the form, she told us she electronically prepares the form based on a handwritten version completed by the contract manager.

IT APPEARS OES EMPLOYEES MISLED THE DEPUTY DIRECTOR TO OBTAIN CONTRACT APPROVAL AND THEN CHANGED THE TERMS OF THE CONTRACT

The same OES executive and contract manager apparently misled their deputy director about the nature of training being purchased through a contract because they believed she would not approve the training they wanted to offer. After the deputy director approved the $36,985 contract request, the employees changed the training from the specified course to another that was part of a longer certification program. Although OES told us that its practice is to allow someone at the executive's level to change the scope of a contract as long as it does not change the dollar amount, the executive did not have specific authority to approve contracts. Further, it appears that OES paid more for the training than necessary.

BACKGROUND—CONTRACT 2

The executive told us he had helped develop a training plan for the division that ultimately would include offering Total Quality Management (TQM) training to OES staff. He thought it was important for division employees to adopt a quality management philosophy, especially in light of issues raised in various Bureau of State Audits reports that he says chided the division for failing to update or make improvements to various administrative processes and procedures. Further, he chose to contract with Los Rios Community College (Los Rios) because of its regional reputation regarding TQM training and certification.[7] According to the contract manager, OES employees earned the TQM certification by completing five semester-length classes. The classes normally met once a week at OES facilities for three to four hours during the workday, totaling 54 hours each, or 270 hours for all five classes.

The executive believed the semester-long courses were the best way to accomplish the organizational transformation he felt was necessary. He also told us it was never his intent to put his entire staff through the certification program, but he wanted to ensure that every staff member attended at least the introductory course, Management 1. Further, he wanted to provide the

[7] Contracts between state agencies and local agencies, including California community colleges, are exempt from competitive bidding requirements.

opportunity to take advanced courses to employees who showed interest and promise. He hoped to train approximately 180 staff in the introductory course and certify about 20 staff through the TQM certification program.

The Executive and Contract Manager Apparently Misled Their Deputy Director

The contract manager told us he and the executive did not think the deputy director would approve a contract for the TQM certification program they wanted.[8] Consequently, they sought her approval for a contract with Los Rios for 100 OES staff to attend a course titled Applying Quality Tools, which was not part of the Los Rios TQM certification program. In July 1998 OES entered into a $36,985 contract with Los Rios for that purpose.

Because they believed their deputy director would not approve the type of training they wanted to provide, an executive and contract manager told her they were providing some other kind of training.

We asked the contract manager to clarify why OES contracted for a class that was not part of the TQM certification program if he and the executive selected Los Rios because it offered the program. He replied that he and the executive were not sure about the response they would get from the deputy director when they proposed the contract. He also told us the deputy director had not promoted any kind of training in the past and was not a person who easily accepted new thinking of any kind, especially that represented by the TQM certification program. He said they did not want to propose a training program only to have it denied by the deputy director, so they started with one class, Management 1. He did not explain why the contract specified Applying Quality Tools instead of Management 1. After the success of the first sessions of the Management 1 class, they augmented the contract to allow for the full range of TQM courses so division staff could earn TQM certification.

The Executive and the Contract Manager Exceeded Their Authority

By changing the scope of services specified in the Los Rios contract, and doing so without obtaining formal approval, the executive and the contract manager exceeded their authority. State policy specifies that contract managers cannot change the description or scope of work in contracts. Although OES told us

[8] We spoke with the deputy director who now works for a different state agency. She told us that the contract manager and the executive were correct in thinking she would not have approved a TQM certification program. She supported the TQM concept, but she was very concerned about the time commitment and cost involved in a certification program.

it allows someone at the executive's level to change the scope of a contract as long as the dollar amounts do not change, the executive did not have specific authority to approve contracts. Moreover, the contract file contained no documentation or authorization of the change in the scope of work.

The executive and contract manager changed the scope of the contract and raised the price from $36,985 to $90,588.

The original contract amount was $36,985. Three contract amendments to cover the additional classes offered were executed after the deputy director no longer worked for OES and raised the total amount to $90,588. Both the executive and the director approved the contract request forms for the first two amendments. However, the executive improperly approved the contract request form for the third amendment by signing two levels of approval himself.

Another State Agency Contracted for Similar Training at a Substantially Lower Cost

We believe OES paid more for the training than necessary. In 2000, another state agency, the Board of Control, entered into a contract with Los Rios for a Management 1 class at a rate substantially below what OES paid for the same class.[9] State law declares that waste and inefficiency in state government undermine Californians' confidence in government and reduce the State's ability to adequately address vital public needs.

In fall 2000 the Board of Control contracted with Los Rios to pay $2,510 for approximately 20 people to attend a Management 1 course. The course for which the Board of Control contracted was open to the public, so Los Rios was able to offer the three-unit course at the state-subsidized rate of $33 per person. The Board of Control's agreement with Los Rios included a $350 coordination fee and an estimated $1,500 for books. In contrast, OES paid $381 per person for 21 employees to attend the spring 2000 Management 1 course, plus about $598 for books, for a total of $8,594. This course was not open to the public, so OES was not eligible for the state-subsidized rate.

Both agencies were able to have the course held at their offices. OES said its course was customized with OES-specific content. Although OES may have received some added value from the

[9] The Board of Control is now named the California Victim Compensation and Government Claims Board.

OES paid approximately $6,000 more than another state agency paid for similar training.

customization, the idea behind college courses is that students are able to apply the concepts they learn to their own situations; therefore, we question whether the added value OES might have received as a result of the course customization was worth the additional price it paid.

The Training Course Cost OES Additional Money

In addition to the cost of the Management 1 course and the books, OES had to pay the salaries of employees attending the course on state time. Of the 21 employees who attended the spring 2000 Management 1 course, 5 are classified as workweek group E employees. According to state regulations, the salaries these employees receive are based on the premise that they work as many hours as needed to perform the duties of their positions. As a result, we were unable to conclude that these 5 employees attended the course on "state time." However, we estimate that the salary expense for the remaining 16 employees to attend the 54-hour course on state time was $20,493, bringing the cost of this one course to roughly $29,087.

OES PAID FOR IMPROPER CONTRACT EXPENDITURES

OES violated state regulations when it provided meals at a three-day conference for 40 managers in the division at a cost of $3,827. In addition, OES made a questionable decision when it agreed to pay a contractor more than $1,300 for an estimated 20 hours of work. California regulations state that reimbursement of per diem expenses, such as meals, is not allowed if the expenses are incurred within 25 miles of the state employees' headquarters. Both state regulations and the division's Travel Reimbursement Guide specify that the maximum allowable lunch reimbursement amount for an employee on travel status is $10 per day.

On January 12, 2000, OES entered into a contract for $8,375 with the California State University, Sacramento Foundation (foundation) for education, consulting, and research services related to the conference. Actually, the foundation oversaw facilities arrangements.

OES paid the foundation a total of $8,173, including direct costs of $7,107 and $1,066 as a 15 percent administrative fee. The direct costs included $5,939 ambiguously classified on the

foundation invoices as "other costs." We asked the foundation for details and determined that $3,827 (64 percent) of the "other costs" were actually for lunches and refreshments. The other $2,112 covered room and equipment rentals provided by the hotel where OES held the conference. In addition, OES paid the foundation $891 in administrative fees for expenses related to room and equipment rentals and food at the hotel.

OES improperly paid for lunches and refreshments for its employees.

According to the information OES provided us, only 9 of the approximately 40 attendees were on travel status from outside the Sacramento area, where the conference was held, and therefore entitled to reimbursement for meal expenses. None of the 9 individuals requested reimbursement on their travel expense claims because they did not pay for the lunches. However, since they were on travel status, at $10 per day, they would have been eligible to have the State pay a combined total of $270 for lunches on the three days, or $30 per person. Nevertheless, OES spent $3,827 on lunches and refreshments, an average of approximately $96 for each of the 40 attendees. OES told us that to condense the conference to three days, the schedule necessitated working lunches to cover all the critical issues and meet established deadlines.

In addition to the amount paid for food, OES paid the foundation more than $1,300 for approximately 20 hours of work by foundation employees to manage and coordinate the conference, including ordering food. The foundation charged personnel costs of $1,000, an average of $50 per hour, and additional overhead fees totaling more than $300. We believe an hourly rate of $50 is high enough to cover a share of benefits and other overhead costs, so the total amount charged by the foundation and paid by OES seems excessive.

OES MISMANAGED OTHER CONTRACTS

Some OES contracts lack relevant details, which could lead to misunderstandings or disputes between the parties over contract terms. Clear definition of contract terms is an important administrative control. Also, some contract files did not contain sufficient information to allow individuals reviewing and approving the contracts to make an informed decision about the need for or quality of the services being purchased. According to state policy, each contract must

contain, among other things, the dates or duration covered by the contract; the maximum amount to be paid to the contractor and the basis on which payment is to be made; and the scope of the work, service, or product to be performed, rendered, or provided. Clear and concise language must be used to describe the scope. For example, when a contractor is to provide a particular training session, the length of which may be open to interpretation, the contract should define the term *session*.

The following table illustrates the lack of specificity we noted in several OES contracts.

TABLE 1

Contracts for Which OES Had Insufficient Information

Contract Date	Contractor	Purpose	Cost	Missing Detail
June 1997	California Polytechnic State University Foundation	Training, instructional consultants, student and research assistants	$4,614,000*	Length of training sessions and number of attendees at each session
March 1998	Private company	Transition plan, facilitation of two management meetings, and out-placement workshops for 100 limited-term employees	$73,500	Amendment extended the term of the contract to September 30, 1998, from June 30, 1998, without explanation; employees' jobs were scheduled to end on June 30
March 1999	California State University, Sacramento, Regional and Continuing Education	One-hour presentation on risk communication	$6,750	Identity and qualifications of speaker and number of attendees

* Under this contract, OES and the contractor were to prepare a mutually acceptable memorandum of understanding (MOU) for each specific training event. We reviewed four MOUs totaling $1,625,000.

OES also allowed the contractors to begin work before the 1998 and 1999 contracts were fully approved. State law prohibits consultants from starting work before formal contract approval, except in an emergency.

AGENCY RESPONSE

OES disagrees that its executive and contract manager misrepresented their efforts to identify alternative sources of training or misled their deputy director. OES contends that any mistakes that occurred probably occurred because of an imperfect understanding of state contracting rules, a lack of formal contract management training, and an incomplete contract tracking system. However, OES will review contractor A's bills to determine if billing errors occurred. If so, OES will recover any overpayments or seek additional training.

OES also disagrees that it paid more for some training than was necessary, but agrees that it should not have paid for meals for employees within 25 miles of their headquarters. OES stated that the payment occurred because of the contracting method used, and the approving official did not realize that meals were included. OES no longer uses this method of contracting.

OES reported that it has established a process that involves both its deputy director and director in approving all service contracts. ■

CHAPTER 5

San Jose State University: Gift of Public Funds

ALLEGATION I990204

San Jose State University (university) paid an employee full salary and benefits for more than a year but did not require her to report to work or to provide any services to the university for the entire time.

RESULTS AND METHOD OF INVESTIGATION

We investigated and substantiated the allegation and other improper governmental activities. The employee took industrial disability leave for surgery in September 1998. Although her doctor lifted her medical restrictions in November 1998, she never returned to the campus and provided only minimal services from her home through January 1999. Nevertheless, the university continued to pay her full salary and benefits, including vacation credits, from February 1, 1999, through May 31, 2000. In addition, the university paid five consultants to perform some of the employee's duties in her absence. Of the $129,304 the employee received in salary and benefits, $105,308 amounts to a gift of public funds in violation of the California Constitution, while at least a portion of the cost for the consultants is a waste of state funds.

To investigate the allegation, we interviewed the campus president, the vice president for administration, university legal counsel, the employee's supervisor, and the employee. We also interviewed one of the consultants engaged to perform some of the employee's duties during her absence. Additionally, we reviewed records in the campus payroll, procurement, and accounting offices. Finally, we reviewed sections of the California Code of Regulations and the California Constitution.

BACKGROUND

The employee took industrial disability leave from September 4, 1998, through September 18, 1998, for surgery due to a work-related injury. After the surgery, her supervisor allowed her to work from her home due to temporary worker's compensation restrictions. However, even after the doctor lifted her medical restrictions on November 24, 1998, the employee did not return to the campus to work. Although the supervisor learned by December 15, 1998, that the employee had not returned to work, he did not contact her until January 29, 1999, when he sent her a letter requesting her to return to work. He sent another written request on February 15, 1999. The employee responded in writing to both requests, stating she had medical conditions that precluded her from returning to work. However, according to the supervisor, the employee never presented acceptable medical evidence that she should not return to work, and he considered her self-reports insufficient to justify her absence.

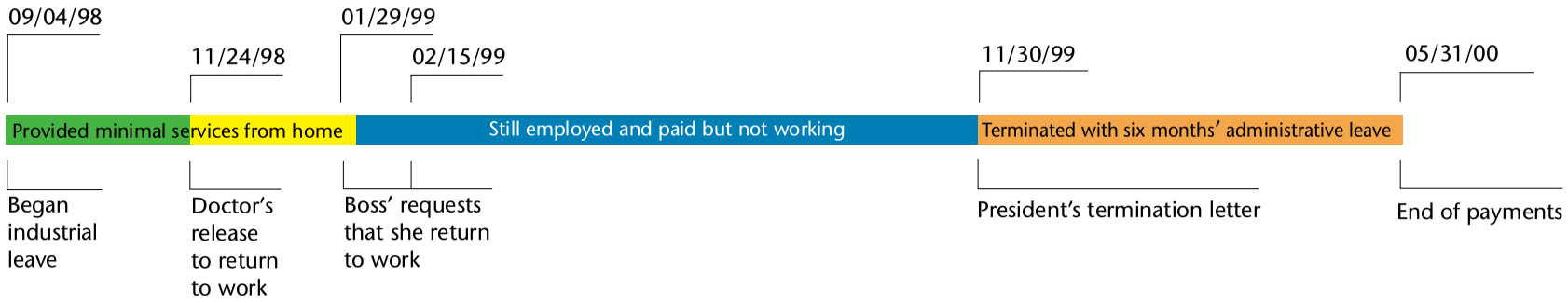
Despite the employee's refusal to return to work, the campus took no further action to compel her to return. The employee's supervisor told us he spoke with her on the telephone on March 1, 1999, informing her that university legal counsel was reviewing her status. Although he also told her he would contact her at a later date, he admitted to us that he never did. The employee confirmed that she had this conversation with her supervisor and that she never heard from him again. The supervisor also told us that the employee provided minimal services from her home through January 1999 but provided no services to the university after February 1, 1999. Nevertheless, the university continued to provide full salary and benefits through May 31, 2000. Figure 1 illustrates the timing of the events described here.

CAMPUS OFFICIALS DID NOT TAKE PROMPT ACTION

When the employee refused to return to work after her supervisor sent her the second letter on February 15, 1999, campus officials met to consider whether to recommend that the president terminate her employment with the university. The fact that the employee had a current lawsuit against the university alleging various forms of discrimination influenced their deliberations. One of the officials told us they wanted to proceed with the utmost caution to ensure that their decision was based on legitimate

FIGURE 1

Timing of Events From the Beginning of the Manager's Industrial Leave Until the University Stopped Paying Her



business considerations and was not and could not be viewed as retaliatory. Additionally, the officials did not want the employee to return to her normal duties because of the sensitive nature of her work and their concern that she may not be impartial in the performance of those duties in light of her lawsuit against the university. Although they decided to assign her alternative duties if she returned to the campus, they failed to find any suitable work. Finally, in November 1999, a campus official recommended to the president that he terminate the employee.

THE UNIVERSITY CONTINUED TO PAY THE EMPLOYEE FULL SALARY AND BENEFITS

The university paid the employee her full salary and the full costs for all benefit entitlements from February 1, 1999, through November 30, 1999, even though it had not placed her on paid administrative leave. Additionally, the university allowed her to continue to accrue vacation credit throughout this period. The value of the salary, benefits, and accrued vacation was $81,312. We believe that this constitutes a gift of public funds in violation of the California Constitution.[10]

Although the employee's supervisor told us the employee did not report to work after the surgery in September 1998, he said she performed at least minimal work from her home through January 1999. However, both the supervisor and the employee admit she did not perform any services for the university after February 1, 1999. Nonetheless, the university continued to pay her full salary and benefits and allowed her to continue to accrue vacation credit. The cost to the State for the period from February 1, 1999, until the date of the president's termination letter, November 30, 1999, is composed of the following:

[10] For a more detailed description of the constitutional provision, see Appendix B.

Salary	$62,880
Benefits*	8,002
Social Security and Medicare	4,626
Value of accrued vacation†	5,804
Total	$81,312

* Benefits include the State's contribution to the Public Employees' Retirement System, health, dental, vision, and life insurance premiums.

† Because the university did not require the employee to use leave to cover her absences, it paid her in cash for accrued vacation credit.

We interviewed the president to determine if he was aware of the employee's work history from the time she went on industrial disability leave in September 1998 until he sent the termination letter. He told us he was aware of the supervisor's efforts to get the employee to return to work and of the employee's contention that medical necessity precluded her from returning. He said he was also aware of the campus officials' effort to find alternative duties for the employee. However, he said he did not know if the employee provided any services to the university after February 1, 1999, although he told us he believed that she was available to provide services and consultation from her home.

THE PRESIDENT PLACED THE EMPLOYEE ON PAID ADMINISTRATIVE LEAVE LONGER THAN NECESSARY

In addition to paying the employee for the time she did not report to work, the president gave her paid leave of six months following notice of her termination. In the employee's termination letter dated November 30, 1999, the president stated he was placing her on administrative leave with pay for six months, thus extending her pay, benefits, and vacation credits to May 31, 2000. According to California regulations, the president was required to provide the employee at least three months' notice of termination or corresponding pay in lieu of notice. However, the employee had already been paid full salary and benefits for 10 months without performing any services for the university. Therefore, we believe that providing full pay, benefits, and vacation credit for more than the required minimum of 3 months was unjustified, wasteful, and a gift of

public funds in violation of the California Constitution. The 6-month administrative leave that cost the State $47,992 is broken down as follows:

Salary	$37,728
Benefits*	2,743
Social Security and Medicare	2,878
Value of accrued vacation†	4,643
Total	$47,992

* Benefits include the State's contribution to the Public Employee's Retirement System, health, dental, vision, and life insurance premiums.

† Because the university did not require the employee to use leave to cover her absences, it paid her in cash for accrued vacation credit.

Because the university was required to pay the employee salary and benefits for only three months after notice of termination, we believe that half of this cost—$23,996—in addition to the $81,312 discussed previously, represents a gift of public funds.

THE UNIVERSITY INCURRED ADDITIONAL COSTS TO ADMINISTER A PROGRAM IN THE EMPLOYEE'S ABSENCE

The campus paid over a half million dollars to manage a program that normally would cost $134,342.

The university paid not only the employee's salary and benefits but also fees for consultants it had to hire to perform some of the employee's duties in her absence. The employee's supervisor told us the university engaged consultants to perform her duties to avoid the possibility of litigation over not providing required services promptly. From January 4, 1999, to May 24, 1999, four of the five consultants hired by the university provided services for short periods. Charges for these services ranged from $2,438 to $5,250 and totaled $16,838. The fifth consultant provided services for 18 months beginning in December 1998 at a cost of $363,681. The total cost for all five consultants was $380,519, not including the university's overhead costs for administering these contracts. Including the employee's salary, benefits, and accrued vacation, the university paid $525,308 to manage the program that was the employee's primary responsibility from December 1, 1998, to May 31, 2000.[11] This is $390,966 more than the $134,342 it would normally cost just for the employee's

[11] We calculated the cost from December 1, 1998, because that was the first full month the employee failed to return to work after her doctor released her to return to work.

pay and benefits. The university likely would have incurred some of this additional cost even if it had taken prudent action to terminate the employee when it became obvious that she refused to return to work after her medical clearance to do so. However, the university's failure to take prompt action cost the State hundreds of thousands of dollars.

AGENCY RESPONSE

Neither the university nor its parent organization, California State University, agrees that the payments to the employee were gifts of public funds or that the payments to the consultants were a waste of state funds. However, the university reported that it has taken or intends to take action to protect against similar situations in the future.

The university does not agree that its costs were a gift or a waste of public funds. It believes instead that it avoided increased risks in the employee's pending lawsuit.

The university stated that the circumstances surrounding the employee's situation were complex and that by not precipitously removing her from the payroll, it was appropriately protecting the State from increased risks associated with her lawsuit against the university. The university also contends that it was further justified in removing her from a university position in which she could inflict considerable damage. It attempted to find an alternative position for her but was unable to, primarily because of her high rank, according to the university. However, the university did not explain why, if the employee was able to do work from home between November 1998 and January 1999, she was no longer able to do it after that point.

The university stated that the employee had long had an acrimonious relationship with the president and had agreed much earlier to seek employment elsewhere. Ultimately, it was that earlier agreement that was the basis for the university terminating her in November 1999. However, the university believes that its ability to successfully settle her lawsuit and any other claims she might have had against the university in February 2001 would likely have been impaired if it had put her on unpaid leave or terminated her earlier.

The university also told us the amounts it paid to five consultants did not represent a waste of funds. It contends that the first four consultants finished work that the employee had not completed. It also reported that only 40 percent of the fifth consultant's time

was devoted to the employee's duties and that the other work this consultant did was beyond what the employee would have done. However, we believe that the other work the university told us the fifth consultant did was within the employee's range of responsibilities. Moreover, as we have stated in this report, the amount the university paid the consultant was far more than it would have paid if it had filled the employee's position and paid that person an appropriate salary.

Nevertheless, the university told us that it has acted to avoid any similar situations in the future. For example, it reported that any future separation agreements will be in writing and will specify the final date of employment. It also will formalize the status of employees who are off work for any sustained period and communicate at least once every 45 days with employees who have been advised that their status is under review. When any employee is off work for 10 working days or more, the university will formally classify the status of the employee and inform the employee of that status. The university also reported that it has restructured the department where the employee worked and that consultants are no longer performing the department's work. ■

Despite the university's disagreement, it will take several actions to avoid similar situations in the future.

CHAPTER 6

Department of Education: Conflicts of Interest and Flawed Legal Advice

ALLEGATION I990003

We received an allegation that two former supervisors in the Child Development Division (child development) of the Department of Education (education) violated conflict-of-interest laws after they left education to work for organizations that had contracts with the State.[12]

RESULTS AND METHOD OF INVESTIGATION

We investigated and substantiated these allegations. After we completed our investigation, we forwarded our findings to the Fair Political Practices Commission (FPPC) for further investigation. As a state employee, supervisor A helped administer a $3.8 million contract with contractor 1. Within 12 months of leaving education and going to work for contractor 1, supervisor A communicated with departmental employees regarding the contract. She also advised and assisted her new employer with this same contract's administration. The FPPC concluded that supervisor A's actions violated the State's conflict-of-interest provisions and issued a warning to her, at which time she agreed to stop working on the contract.

Supervisor B began working for contractor 2 after leaving his job at education, and within 12 months he communicated with departmental officials regarding his new employer's applications for state contracts. The FPPC concluded that his actions appeared to violate conflict-of-interest laws. Only after the FPPC came to this conclusion did supervisor B stop communicating with department officials.

[12] For a more detailed description of the conflict-of-interest laws relevant to this chapter, see Appendix B.

However, the FPPC decided not to take formal enforcement action against the former supervisors for three reasons. First, the FPPC concluded that both supervisors received inaccurate legal advice from education's legal office regarding their prospective employment. Second, both supervisors fully cooperated with the FPPC. Third, the FPPC concluded their actions caused minimal harm to the State.

We also determined that supervisor B engaged in other incompatible activities. For example, he personally benefited when he flew to Southern California to interview for a job with contractor 2 at the same time he was purportedly participating in a technical assistance review of contractor 2's operations. In addition, it appears that supervisor B planned to use state resources to provide an unprecedented level of technical assistance to contractor 2. Both before and during the review, education conducted an investigation of allegations concerning contractor 2. Although investigators expressed concern that supervisor B lacked impartiality and could compromise the ongoing investigation, he remained involved with the contractor. At the very least, supervisor B's continued involvement with contractor 2 created the appearance of a conflict of interest, and we found some evidence that his involvement interfered with education's investigation.

To investigate the allegations concerning supervisors A and B, we interviewed them, other education staff, and representatives from the FPPC. We reviewed contracts between education and contractors 1 and 2 and related documents. We also reviewed work products produced by the supervisors on behalf of their new employers. Finally, we reviewed laws and regulations governing the activities of individuals who leave state employment.

BACKGROUND

Both former supervisors discussed in this report worked in child development while employed by education. Child development's mission is to provide leadership and support to all individuals and organizations concerned with children and families by promoting child development programs. It offers education programs to the

public, including departmental contractors, about appropriate practices for infants, toddlers, preschoolers, and school-age children in a variety of child care and development settings.

TWO FORMER SUPERVISORS VIOLATED OR APPEARED TO VIOLATE CONFLICT-OF-INTEREST LAWS

According to the FPPC, supervisor A violated and supervisor B appeared to violate conflict-of-interest laws intended to regulate the activity of former government officials who leave state service and enter the private sector. Under state law, an individual who participated in a contract while employed by a state agency is banned for life from contacting anyone in the agency to influence that contract. State law also indefinitely prohibits such an individual from receiving compensation for aiding, advising, counseling, consulting, or assisting any other person with the contract. In addition, by law, a former employee of a state agency cannot receive compensation for appearing before or communicating with the agency to influence contract awards within 12 months of leaving state employment.

Supervisor A Had a Conflict of Interest

The FPPC warned the supervisor that her actions violated conflict-of-interest laws.

Supervisor A left state employment on December 30, 1998, and began working for contractor 1 on January 11, 1999. Despite the prohibitions previously noted, supervisor A improperly communicated with departmental employees on behalf of contractor 1 within 12 months of leaving education regarding a $3.8 million contract she helped oversee while employed by the State. One of the departmental employees she contacted was the contract monitor, who reported to supervisor A before her departure from state employment. The FPPC also confirmed that supervisor A violated conflict-of-interest laws when she advised and assisted contractor 1 with the same contract. The contract and related amendments covered the period December 1, 1997, through November 30, 1999.

On June 28, 2000, the FPPC issued a warning letter to supervisor A, informing her that she was banned under conflict-of-interest laws from contacting anyone at education to influence the contract. It also informed her that she was prohibited from aiding, advising, counseling, consulting, or assisting any other person, including her new employer, with the contract.

Supervisor B Had an Apparent Conflict of Interest

Supervisor B left state employment on October 16, 1998, and three days later began work for contractor 2—one of the same contractors he was responsible for monitoring and assisting during his employment with the State. Some of the duties that supervisor B and his staff performed during his employment with the State included program monitoring, management reviews, technical assistance, and reviews of applications of state contractors under his jurisdiction. The FPPC found that supervisor B made inappropriate contact with education on behalf of contractor 2 within 12 months of leaving state employment. The contact concerned contractor 2's applications for new funds. Supervisor B had not worked on these applications during his employment with education. However, the FPPC said his communication with that department, which occurred within the 12-month ban, appeared to violate conflict-of-interest laws, which are concerned with not only what actually happens but also with what might happen.

Education's Flawed Advice to the Supervisors Contributed to Conflicts of Interest

The Department of Education's legal analysis overlooked conflict-of-interest laws that regulate the activity of former state employees who enter the private sector.

In October 1998, when it became aware of the two supervisors' plans to accept employment with private companies that contracted with education, the department conducted a legal analysis that focused narrowly on whether provisions of the California Education Code (education code) would prohibit the supervisors' acceptance of such employment. However, the FPPC concluded this analysis was incomplete because it overlooked additional conflict-of-interest laws that regulate the activity of former state employees who enter the private sector.

Education's counsel restricted its October 1998 analysis of supervisor A to one section of the education code and state contracting laws and determined that these laws did not preclude supervisor A from accepting her new job. Similarly, education's review of supervisor B focused on provisions in the education code that prohibit departmental employees from accepting jobs with contractors for a period of 12 months following their retirement, dismissal, or separation from state service if, while employed by education, the individuals engaged in any negotiations, transactions, planning, arrangements, or

any part of the decision-making process relevant to state contracts held by those companies. The counsel's analysis indicated no legal problems existed for either of the supervisors and even suggested that education, rather than enforcing the provisions of the education code, seek to remove them. Education's arguments against the application of these provisions included the following:

- Dozens of former departmental staff now work for entities over which they had direct program responsibility, and education either concluded that the provisions did not apply to these individuals or responded in a manner that would suggest it made no difference since the individuals no longer worked for the State.

- Suddenly enforcing these provisions, given past failures to do so, might subject education to claims of disparate treatment.

- Checks and balances now exist in the processes leading to contract awards. Individuals cannot make contract decisions, as they could in the past.

- The provisions should be consistent with other conflict-of-interest provisions, but the education code is actually more restrictive in that it includes employment as a prohibited economic interest. Other conflict-of-interest laws do not prohibit officials from leaving the State and assuming positions with the source of the economic interest, in this case the new employer.

In a letter dated May 18, 2000, the FPPC informed education that its legal office may have been giving employees incomplete advice regarding post-employment restrictions of state law and, more specifically, that the advice offered to supervisors A and B did not consider "revolving door" sections of the Political Reform Act. Relying on education's flawed advice, both supervisors began their new jobs with the understanding that no legal problems existed. Thus, education contributed to the violations carried out by these former supervisors.

Because of Mitigating Factors, the FPPC Took No Formal Action

Although the FPPC confirmed that both supervisors either violated or appeared to violate conflict-of-interest laws, it decided to close both cases and not to take any formal enforcement action because of the following mitigating factors:

Relying on the Department of Education's flawed advice, both employees began their new jobs with the understanding that no legal problems existed.

- Both supervisors relied on the faulty legal advice they received from education before they took their jobs with their new employers.
- Both supervisors cooperated fully with the FPPC's investigation.
- The FPPC found the activities of the former supervisors resulted in little or no harm to the State.

However, the two individuals did not cease these activities until after the FPPC informed them that they violated or appeared to violate conflict-of-interest laws. Had they been allowed to continue to rely on the flawed advice afforded them, we cannot say what damages the State may have incurred.

SUPERVISOR B ENGAGED IN INCOMPATIBLE ACTIVITIES

Between June and November 1997, several employees of contractor 2 sent letters to education alleging a variety of improprieties. Copies of these letters were forwarded to supervisor B, who was responsible for monitoring and assisting that contractor. In December 1997 supervisor B traveled to Southern California to meet with six employees of contractor 2 who were prepared to provide evidence of misconduct by the contractor. According to at least some of these employees, they provided confidential information to supervisor B. Although supervisor B promised the employees that he would not give that information to contractor 2, they said he did.

On January 20, 1998, education's Office of Special Investigations opened an investigation into the allegations concerning contractor 2. During the initial stages of the investigation, witnesses told investigators they were reluctant to speak out as long as supervisor B remained involved because he had given contractor 2 confidential information that could compromise both the witnesses and the investigation. In response to concerns regarding his lack of impartiality, education's investigators were assured that supervisor B would not be involved in any activity with contractor 2 until the investigation was completed.

However, in a July 10, 1998, memo to the manager of education's external audits, one of the investigators expressed concern that supervisor B remained actively involved with

A department supervisor interviewed for a job with the contractor, the same day he purportedly began a review of the contractor's operation for the department.

contractor 2. In fact, on June 12, 1998, contractor 2 had asked education to conduct a technical assistance review of the child care and development programs it operated to assess its performance and capacity to expand in light of increased funding for these programs. Contractor 2 specifically asked to meet with supervisor B on June 23 and June 24, 1998, to discuss the scope of the requested review. Supervisor B traveled to Southern California at the State's expense to meet with contractor 2. However, supervisor B and contractor 2's vice president of operations admitted that supervisor B interviewed for a job with the contractor on June 23, 1998, the same day he purportedly began work on the review of contractor 2 on behalf of education. Supervisor B continued to be involved with contractor 2 in his state role and did not formally remove himself until September 25, 1998, when he informed education that he had disassociated himself from the review and planned to leave state employment to work for contractor 2.

Both the State and education have incompatible activity prohibitions against employees using state equipment, travel, time, or prestige for private gain or advantage or the private gain of another. One of education's investigative reports indicated that the technical assistance that supervisor B planned to give contractor 2 exceeded any technical assistance ever provided by education. Therefore, it appears that supervisor B planned to use state resources in an unprecedented way to benefit contractor 2.

We also found some indication that supervisor B interfered with education's investigation. In fact, one of the investigators reported that, in spite of numerous requests for information from supervisor B's initial investigation into allegations concerning contractor 2, he never provided the information. Education ultimately closed the investigation of contractor 2 on April 1, 1999, citing it lacked sufficient corroborating information to support prosecution of the case. We cannot know whether there would have been a different outcome to the investigation if education had ensured that supervisor B had no further interaction with contractor 2. However, the fact that witnesses perceived him to be biased and believed that he gave privileged information to contractor 2 certainly raises questions concerning what effect supervisor B's relationship with contractor 2 had on education's ability to obtain evidence.

We further believe that supervisor B should have immediately removed himself from any involvement as a state employee with contractor 2 at the point he perceived that contractor 2 was a potential employer. Although supervisor B may have conducted legitimate state business during the period he claimed to be working on the review, we believe he scheduled his trip on June 23, 1998, in part, as a convenient means of having the State pay for his travel expenses to interview with his future employer.

AGENCY RESPONSE

Education agrees that its legal office provided flawed advice in 1998 to the two supervisors and that they appear to have violated conflict-of-interest laws. The attorney who provided the flawed advice is no longer an education employee and there is a new general counsel. Education's legal staff are aware of the conflict-of-interest laws and education revised its incompatible activities policy to ensure that all employees clearly understand what activities are not allowed. Further, education offers training to its managers on conflict-of-interest and incompatibility requirements to ensure that the managers are conducting their activities in accordance with the law and to enable them to monitor and guide the activities of their staff. Finally, education gives all employees who leave state employment a memorandum reminding them of the restrictions on their post-employment activities. ■

CHAPTER 7

Office of the State Public Defender: Improper Payment of Transportation Costs

ALLEGATION I990145

The California Office of the State Public Defender (public defender) paid the transportation expenses of an employee who primarily telecommutes but sometimes travels to her headquarters in Sacramento. This employee lived in Los Angeles and subsequently moved out of the State.

RESULTS AND METHOD OF INVESTIGATION

We asked the Department of Personnel Administration (DPA) to investigate the allegation on our behalf. DPA concluded that the public defender inappropriately paid the employee's transportation costs between her home and the Sacramento headquarters. According to our calculations, these costs totaled $2,987.

To investigate the allegation, DPA reviewed the public defender's telecommuting policy, as well as applicable statutes, policies, and regulations. DPA also held discussions with public defender management, reviewed the director's response to the allegations, and examined travel expense claims submitted by the employee.

THE PUBLIC DEFENDER INAPPROPRIATELY PAID AN EMPLOYEE'S TRAVEL EXPENSES

State regulations prohibit payment of expenses arising from travel between an employee's home and headquarters.[13] Further, regulations do not allow payment of per diem expenses, such as meals, if incurred within 25 miles of headquarters. The employee submitted travel expense claims for the cost of airfare between her home and public defender headquarters in Sacramento. On one occasion, the employee also submitted claims for rental cars in

[13] For more specific references to the regulations mentioned in this chapter, see Appendix B.

Sacramento as well as meals and parking associated with her trips to headquarters. In some cases, the public defender paid for the employee's expenses directly. These travel-related expenses totaled $2,987 for the period between July 1998 and March 2000.

AGENCY RESPONSE

DPA instructed the public defender to stop paying for the employee's commuting expenses, and the public defender agreed to do so. The public defender ordered the employee to report to the Sacramento office and cease telecommuting. ■

CHAPTER 8

Department of Transportation: Improper Use of State Time and Equipment

ALLEGATION I2000-690

A Department of Transportation (Caltrans) employee at the Division of Highways in Oakland used state time and a state vehicle on several occasions from March through May 1999 for his private real estate business.

RESULTS AND METHOD OF INVESTIGATION

We asked Caltrans to investigate the complaint on our behalf. It substantiated the allegation, finding that the employee used a state vehicle to meet with sellers of a residence in Campbell during hours for which he was paid by the State, which is contrary to the law.[14] Caltrans also found that the employee used his state telephone to call these real estate clients during his state work hours.

To investigate the allegation, Caltrans staff reviewed the employee's state telephone bills, vehicle logs, and time sheets for the dates in question. They also interviewed the employee and his supervisor.

In addition to being a licensed real estate agent, the employee is a transportation engineer in the Caltrans Division of Highways in Oakland. Because his job involves travel throughout several counties in the San Francisco Bay Area, Caltrans has assigned him a state vehicle for his use in conducting Caltrans business. Although it confirmed that he had possession of a state vehicle on the days he met with his clients in Campbell, the employee denied that he had used the vehicle or state time to meet with the clients. Similarly, although Caltrans confirmed that the employee used his state telephone to call these real estate clients

[14] For a more detailed description of the law discussed in this chapter, see Appendix B.

on at least three occasions during normal state business hours, the employee denied that he used state time or equipment in conducting his real estate business.

AGENCY RESPONSE

Caltrans reported that the employee had no previous instances of discipline for similar offenses. Therefore, it issued him a letter of warning. ■

CHAPTER 9

Update on Previously Reported Issues

CHAPTER SUMMARY

The California Whistleblower Protection Act, formerly known as the Reporting of Improper Governmental Activities Act, requires an employing agency or appointing authority to report to the Bureau of State Audits (bureau) any corrective action, including disciplinary action, it takes in response to an investigative report not later than 30 days after the report is issued. If it has not completed its corrective action within 30 days, the agency or authority must report to the bureau monthly until it completes that action. This chapter summarizes corrective actions taken by one state agency related to investigative findings since we last reported them.

DEPARTMENT OF CORRECTIONS CASE I990136

On April 3, 2001, we reported that employees of the Southern Transportation Unit (STU) of the Department of Corrections (corrections) had their privately owned vehicles repaired by a vendor who also repaired the STU's state vehicles and that employees improperly received benefits from the vendor. Specifically, one employee of the STU, employee A, improperly received a gift in the form of reduced vehicle registration fees when he purchased a car from a business whose owners also owned an automotive repair shop that the STU uses to repair its vehicles. The Department of Motor Vehicles assessed employee A less for registration fees than what should have been charged because the sales price reported to the Department of Motor Vehicles was less than what was actually paid. Employee A and three other STU employees used the same vendor to repair their personal vehicles while they held state positions that enabled them to authorize or influence significant increases in the amount of business the vendor received from the State. For instance, in fiscal year 1996-97, the STU paid the vendor only $11,287. The manager of the STU—who had stopped using the vendor because of concerns with his work and her knowledge that certain employees were taking their personal vehicles to

him for repair and possibly receiving discounts—left the unit in July 1997. Following her departure, the STU's payments to the vendor increased to $71,971 in fiscal year 1997-98 and $113,273 in fiscal year 1998-99. In addition, STU employees circumvented controls over high-cost repairs and vehicle modifications made by the vendor by allowing the vendor to split the cost of repairs onto multiple invoices and did not exercise due diligence in making sure the State paid only for necessary costs. All these factors contributed to the appearance of conflicts of interest.

UPDATED INFORMATION

Corrections did a follow-up investigation on the issues we reported. Corrections agreed that employee A received a gift in the form of reduced vehicle registration fees. However, it could not develop a preponderance of evidence that employee A was responsible for reporting a lower sales price to the Department of Motor Vehicles. In addition, Corrections concluded that those employees who used the state vendor for personal repairs had not inappropriately authorized or influenced the increase in the amount of state business the vendor received. Corrections did substantiate that STU employees circumvented controls over repairs made by the vendor by allowing invoices to be split. Corrections' investigative report has been forwarded to the appropriate hiring authority within corrections to determine what action should be taken. ■

We conducted this review under the authority vested in the California State Auditor by Section 8547 et seq. of the California Government Code and applicable investigative and auditing standards. We limited our review to those areas specified in the audit scope sections of this report.

Respectfully submitted,

ELAINE M. HOWLE
State Auditor

Date: September 6, 2001

Staff: Ann K. Campbell, Director, CFE
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APPENDIX A

Activity Report

The Bureau of State Audits (bureau), headed by the state auditor, has identified improper governmental activities totaling $10.7 million since July 1993 when it reactivated the Whistleblower Hotline (hotline), formerly administered by the Office of the Auditor General. These improper activities include theft of state property, false claims, conflicts of interest, and personal use of state resources. The state auditor's investigations also have substantiated improper activities that cannot be quantified in dollars but have had a negative social impact. Examples include violations of fiduciary trust, failure to perform mandated duties, and abuse of authority.

Although the bureau investigates improper governmental activities, it does not have enforcement powers. When it substantiates allegations, the bureau reports the details to the head of the state entity or to the appointing authority responsible for taking corrective action. The California Whistleblower Protection Act (act) also empowers the state auditor to report these activities to other authorities, such as law enforcement agencies or other entities with jurisdiction over the activities, when the state auditor deems it appropriate.

Corrective actions taken on cases contained in this report are described in the individual chapters. Table 2 on the following page summarizes all the corrective actions taken by agencies since the bureau reactivated the hotline. In addition, dozens of agencies modified or reiterated their policies and procedures to prevent future improper activities.

TABLE 2

Corrective Actions Taken July 1993 Through June 2001

Type of Corrective Action	Instances
Referrals for criminal prosecution	73
Convictions	5
Job terminations	42
Demotions	8
Pay reductions	9
Suspensions without pay	12
Reprimands	119

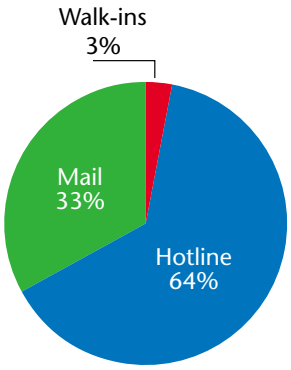
New Cases Opened February Through June 2001

From February 1 through June 30, 2001, we opened 145 new cases.

We receive allegations of improper governmental activities in several ways. Callers to the hotline at (800) 952-5665 reported 93 (64 percent) of our new cases.[15] We also opened 48 new cases based on complaints received in the mail and 4 based on complaints from individuals who visited our office. Figure 2 shows the sources of all cases opened from February through June 2001.

FIGURE 2

Sources of 145 New Cases Opened February Through June 2001



[15] In total, we received 1,995 calls on the hotline from February through June 2001. However, 1,445 (72 percent) of the calls were about issues outside our jurisdiction. In these cases, we attempted to refer the caller to the appropriate entity. Another 457 (23 percent) were related to previously established case files.

Work on Investigative Cases February Through June 2001

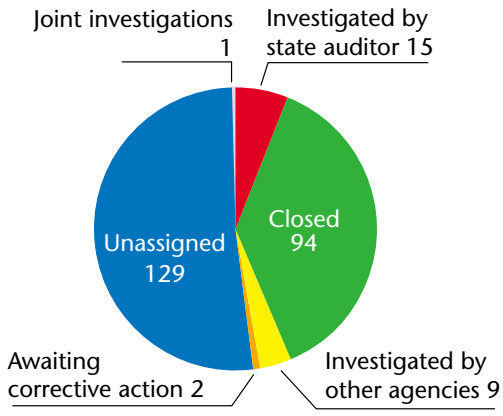
In addition to the 145 new cases we opened during this five-month period, 65 previous cases were awaiting review or assignment as of January 31, 2001, and 39 were still under investigation, either by this office or by other state agencies, or were awaiting completion of corrective action. Consequently, 249 cases required some review during this period.

After reviewing the information provided by complainants and conducting preliminary reviews, we concluded that 94 cases did not warrant complete investigation because of lack of evidence.

The act specifies that the state auditor can request the assistance of any state entity or employee in conducting an investigation. From February 1 through June 30, 2001, state agencies investigated 9 cases on our behalf and substantiated allegations on 5 (83 percent) of the 6 cases they completed during the period. In addition, we independently investigated 15 cases and substantiated allegations on 2 (40 percent) of the 5 cases we completed during the period. As of June 30, 2001, 129 cases were awaiting review or assignment. With the Fair Political Practices Commission, we jointly investigated and substantiated allegations on another case. Figure 3 shows the disposition of the 249 cases worked on from February through June 2001.

FIGURE 3

Disposition of 249 Cases
February Through June 2001



APPENDIX B

State Laws, Regulations, and Policies

This appendix provides more detailed descriptions of state laws, regulations, and policies that govern employee conduct and prohibit the types of improper governmental activities described in this report.

CAUSES FOR DISCIPLINING STATE EMPLOYEES

The California Government Code, Section 19572, enumerates the various causes for disciplining state civil service employees. These causes include incompetency, inefficiency, inexcusable neglect of duty, insubordination, dishonesty, misuse of state property, and other failure of good behavior either during or outside of duty hours which is of such a nature that it causes discredit to the appointing authority or the person's employment.

CRITERIA CONCERNING CONTRACTING

Chapters 1 and 4 report contracting improprieties.

Competitive procurement requirements

State policy requires contracts to be competitively bid except under specific circumstances as set forth by law or as determined to be in the best interests of the State. The governor's Executive Order W-103-94 prohibits the use of sole-source contracts and procurements except in a state emergency when required for public health and safety. A sole-source transaction is defined as a procurement or contract for goods or services or both when only a single business enterprise is afforded the opportunity to offer the State a price for the specified goods or services.

The State Contracting Manual outlines the procedures for requesting a sole-source exemption. One of the requirements for obtaining approval of a sole-source exemption is to submit a Request for Exemption From Contract Advertising form to the Department of General Services (DGS). The request must include one of the following: (1) a survey of the marketplace, if possible, or a narrative of the efforts made to identify other similar

appropriate services (including a summary of how the agency came to the conclusion that such alternatives are either inappropriate or unavailable); or (2) an explanation about why the survey or other effort was not done.

Public Contract Code, Section 12102(a), states that the acquisition of information technology services shall be conducted through competitive means, except when the director of the DGS determines one of the following:

- The services proposed for acquisition are the only services that can meet the State's need.

- The services are needed in cases of emergency, where immediate acquisition is necessary for the protection of the public health, welfare, or safety.

According to Chapter 4800 of the State Information Management Principles, when acquiring services involving information technology, state agencies must seek maximum economic advantage to the State.

Use of private contractors to perform services instead of civil service employees

The California Government Code allows state agencies to contract for personal services, but only under certain conditions. For example, Section 19130(a) states that personal-services contracting is permissible to achieve cost savings when all the following conditions are met:

- The contracting agency clearly demonstrates that the proposed contract will result in actual overall cost savings to the State. (This section also establishes criteria for comparing the cost of having the work done by civil service employees to the cost of having the work performed by a contractor.)

- Proposals to contract out work are not approved solely on the basis that savings will result from lower contractor pay rates or benefits. Proposals to contract out work are eligible for approval if the contractor's wages are at the industry's level and do not significantly undercut state pay rates.

- The contract does not cause the displacement of civil service employees. The term *displacement* includes layoff, demotion, involuntary transfer to a new class, involuntary transfer to a

new location requiring a change of residence, and time base reductions. Displacement does not include changes in shifts or days off, nor does it include reassignment to other positions within the same class and general location.

- The contract does not adversely affect the State's affirmative action efforts.

- The savings is large enough to ensure that it will not be eliminated by private sector and state cost fluctuations that could normally be expected during the contracting period.

- The savings clearly justifies the size and duration of the contracting agreement.

- The contract is awarded through a publicized, competitive bidding process.

- The contract includes specific provisions pertaining to the qualifications of the staff that will perform the work under the contract, as well as assurance that the contractor's hiring practices meet applicable nondiscrimination, affirmative-action standards.

- The potential for future economic risk to the State from possible contractor rate increases is minimal.

- The contract is with a firm, which is defined as a corporation, partnership, nonprofit organization, or sole proprietorship.

- The potential economic advantage of contracting is not outweighed by the public's interest in having a particular function performed directly by state government.

Authority to change a contract's scope of work
According to the State Contracting Manual, contract managers are not authorized to change the description or scope of work in the contract.

Contracts between state and local agencies
Section 10356(c)(4) of the Public Contract Code exempts certain consulting-services contracts from advertising and bidding requirements, including contracts for the services of one local agency by a state agency. Community colleges are local agencies.

Requirement for contract specificity
The Financial Integrity and State Manager's Accountability Act of 1983, California Government Code, Section 13400, and following declares that it is the policy of the State for each agency to maintain effective systems of internal accounting and administrative control as an integral part of its management practices. The clear definition of contract terms is an important administrative control.

According to Section 2.05 of the State Contracting Manual, each contract must contain, among other terms, all of the following: the term for the performance or completion of the contract (dates or length of time); a clear statement of the maximum amount to be paid and the basis on which payment is to be made; and the scope of work, service, or product to be performed, rendered, or provided described in clear and concise language.

Requirement that contracts be approved before consultants begin work
The Public Contract Code, Section 10371, prohibits consultants from starting work before formal contract approval, except in an emergency. According to the State Contracting Manual, when it is necessary for a consultant to start work before approval of the contract, the circumstances must be noted in the contract file as an emergency as defined in the Public Contracts Code.

CRITERIA GOVERNING STATE MANAGERS' RESPONSIBILITIES

Chapters 1, 4, 5, and 8 report weaknesses in management controls.

The Financial Integrity and State Manager's Accountability Act of 1983 (act) contained in the California Government Code, beginning with Section 13400, requires each state agency to establish and maintain a system or systems of internal accounting and administrative controls. Internal controls are necessary to provide public accountability and are designed to minimize fraud, abuse, and waste of government funds. In addition, by maintaining these controls, agencies gain reasonable assurance that those measures they have adopted protect state assets, provide reliable accounting data, promote operational efficiency, and encourage adherence to managerial policies. The act also states that elements of a satisfactory system

of internal accounting and administrative control should include a system of authorization and record-keeping procedures adequate to provide effective accounting control over assets, liabilities, revenues, and expenditures. Further, this act requires that, when detected, weaknesses must be corrected promptly.

In addition, the California Government Code, Section 11813, declares that waste and inefficiency in state government undermine the confidence of Californians in government and reduce the state government's ability to adequately address vital public needs.

PROHIBITIONS AGAINST GAMBLING POOLS

Chapter 2 reports an illegal gambling pool.

Section 337a of the Penal Code states that every person who engages in pool selling or bookmaking, with or without writing, at any time or place is punishable by imprisonment in the county jail for a period of not more than one year, or in the state prison.

INCOMPATIBLE ACTIVITIES DEFINED

Chapters 2, 3, 7, and 8 report incompatible activities.

Incompatible activity prohibitions exist to prevent state employees from being influenced in the performance of their official duties or from being rewarded by outside entities for any official actions. Section 19990 of the California Government Code prohibits a state employee from engaging in any employment, activity, or enterprise that is clearly inconsistent, incompatible, in conflict with, or inimical to his or her duties as a state officer or employee. This law specifically identifies certain incompatible activities, including using state time, facilities, equipment, or supplies for private gain or advantage.

It also includes using the prestige or influence of the State for one's own private gain or advantage, or the private gain of another. In addition, state employees are prohibited from receiving or accepting, directly or indirectly, any gift, including money, or any service, gratuity, favor, entertainment, hospitality, loan, or any other thing of value from anyone who is doing or is seeking to do business of any kind with their department.

The same law requires state departments to define incompatible activities. The Department of Transportation (Caltrans) policy states that "Caltrans employees do not willfully engage in any other employment or activities which are illegal; which are or give the appearance of being incompatible or in conflict with their duties as state employees; discredit their profession, the Department, or the State; or have an adverse effect on the confidence of the public in the integrity of government." Further, the policy requires employees to perform their duties and responsibilities honestly and objectively and to use state resources, information, and positions only for the work of Caltrans, not for their private gain or the private gain of another.

PROHIBITIONS AGAINST USING STATE RESOURCES FOR PERSONAL GAIN

Chapters 2, 6, and 8 report personal use of state resources.

The California Government Code, Section 8314, prohibits state officers and employees from using state resources such as equipment, travel, or time for personal enjoyment, private gain, or personal advantage, or for an outside endeavor not related to state business. If the use of state resources is substantial enough to result in a gain or advantage to an officer or employee for which a monetary value may be estimated or a loss to the State for which a monetary value may be estimated, the officer or employee may be liable for a civil penalty not to exceed $1,000 for each day on which a violation occurs plus three times the value of the unlawful use of state resources.

SALARIES PAID TO WORKWEEK GROUP E EMPLOYEES

Chapter 4 refers to workweek group E employees.

According to the California Code of Regulations, Title 2, Section 599.703, the salaries that workweek group E employees receive from the State are based on the premise that they are expected to work as many hours as are necessary to perform the duties of their positions.

LAWS AND REGULATIONS COVERING TRAVEL EXPENSE REIMBURSEMENTS AND PAYMENT OF COMMUTING EXPENSES

Chapters 4 and 7 report improper payment of travel or commuting expenses.

The California Code of Regulations, Title 2, Section 599.616, states that no payment of per diem expenses, such as meals is allowed if incurred within 25 miles of headquarters. Section 599.619 and the Office of Emergency Services Disaster Assistance Division's travel reimbursement guide specify that the maximum allowable lunch reimbursement amount for an employee on travel status is $10 per day.

According to the California Code of Regulations, Title 2, Section 599.626.1(d), payment of expenses arising from travel between home and headquarters is not allowed.

THE PROHIBITION AGAINST MAKING GIFTS OF PUBLIC FUNDS

Chapter 5 reports what might have been a gift of public funds.

The California Constitution, Article XVI, Section 6, prohibits gifts of public funds. In determining whether an appropriation of public funds is to be considered a gift, the primary question is whether funds are to be used for a public or private purpose.

REGULATION CONCERNING CALIFORNIA STATE UNIVERSITY'S RESPONSIBILITY TO PROVIDE NOTICE OF TERMINATION TO MANAGEMENT EMPLOYEES

Chapter 5 discusses payments made in lieu of notice of termination.

According to the California Code of Regulations, Title 5, Section 42723(d), the university president is required to provide an employee at least three months notice of termination or corresponding pay in lieu of notice.

PROHIBITIONS AGAINST CONFLICTS OF INTEREST

Chapter 6 reports conflicts of interest.

Under the California Government Code, Section 87401, if an individual participated in a contract while employed by a state agency, that employee is banned for life from contacting anyone in the state agency for the purpose of influencing that contract. Section 87402 of the same code also indefinitely prohibits such individuals from aiding, advising, counseling, consulting, or assisting any other person with the contract if the individual is receiving compensation for such services. In addition, California Government Code, Section 87406 (d)(1), prohibits former employees from receiving compensation for appearing before or communicating with their former agencies for 12 months if the appearance or communication is for the purpose of influencing the awarding of a contract.

In addition to specific statutory prohibitions, according to the attorney general, common-law doctrines against conflicts of interest exist. Common law is a body of law made by decisions of the California Supreme Court and the California Appellate Courts. Both the courts and the attorney general have found conflicts of interest by public officials to violate both common-law and statutory prohibitions. For example, common-law doctrines state that a public officer is bound to exercise the powers invoked by that position with disinterested skill, zeal, and diligence, and primarily for the benefit of the public. Another judicial interpretation of common-law doctrine is that public officers are obligated to discharge their responsibilities with integrity and fidelity. According to the attorney general, where no conflict is found in statutory prohibitions, special situations still could constitute a conflict under the long-standing common-law doctrine. Consequently, situations that have the mere appearance of a financial conflict of interest may still be subject to common-law prohibitions.

LAWS AND REGULATIONS CONCERNING PERSONAL USE OF STATE VEHICLES

Chapter 8 reports misuse of state vehicles.

The California Government Code, Section 19993.1, requires that state-owned motor vehicles be used only in the conduct of state business. Section 19993.2(a) requires the Department of Personnel Administration (DPA) to define what constitutes use

of state-owned vehicles in the conduct of state business. In Section 599.800(e) of Title 2 of the California Code of Regulations, DPA defines use of a vehicle in the conduct of state business as driving the vehicle in the performance of or necessary to, or in the course of, the duties of state employment. The regulations permit employees to use a state vehicle to commute to work under certain approved circumstances, although both the DPA and the Office of the State Controller generally require employees who do so to report the value of this use as taxable income. In fact, Internal Revenue Service Regulation 1.61-21(a) states that gross income generally includes fringe benefits, such as the personal use of an employer-provided automobile.

APPENDIX C

Incidents Uncovered by Other Agencies

Section 20080 of the California State Administrative Manual requires state government departments to notify the Bureau of State Audits (bureau) and the Department of Finance of actual or suspected acts of fraud, theft, or other irregularities they have identified. What follows is a brief summary of incidents that involved state employees reported from February through June 2001. Although many state agencies do not yet report such irregularities as required, some agencies not only vigorously investigate such incidents but also put considerable effort into creating policies and procedures to prevent future occurrences. It is important to note that reported incidents have been brought to conclusion; we will not publish any reports that would interfere with or jeopardize any internal or criminal investigation.

Two state agencies notified the bureau of 25 instances of improper governmental activity they brought to conclusion from February through June 2001. Those agencies were the Department of Motor Vehicles (DMV) and three campuses of the California State University system. Of these 25 instances, 7 included financial irregularities such as embezzlement and loss of funds intended for deposit to a bank. The State lost $35,939 because of these financial irregularities. Further, as a result of DMV employees fraudulently issuing driver's licenses or other documents, individuals paid these DMV employees and their accomplices at least $43,567.

During the five-month period from February through June 2001, the DMV advised this office of 22 investigations completed by its staff that substantiated improper activities by DMV employees. Of these, 15 investigations involved the selling of fraudulent driver's licenses to 41 people of whom 39 were undocumented immigrants who paid dearly for the privilege of driving. Many of these immigrants did not take (or pass, if taken) written, vision, or driving tests. According to the DMV reports, of the $43,567 paid for fraudulent licenses, the

undocumented immigrants paid at least $43,400 to DMV employees and their accomplices. Additionally, the investigations uncovered the following improprieties:

- An employee waived vehicle registration fees and penalties for a friend.
- Two employees illegally accessed DMV records.
- One employee solicited sexual favors in exchange for a driver's license.
- An employee falsified records of a personally owned motor home to avoid full payment of use taxes.
- One employee embezzled vehicle registration fees.
- One employee misappropriated driver's license and vehicle registration fees.
- One employee fraudulently registered a vehicle.

Three California State University campuses reported improper governmental activities. One campus reported the loss of $28,935 it collected as parking fines and related charges. The campus investigation revealed that a former employee created the deposit documents and that the courier receipts had been forged, but it could not determine who forged them. The investigation cleared the transport service of any wrongdoing in the loss. Another campus terminated a temporary employee who misused state telephones and funds, and the matter has been turned over to campus police for possible criminal investigation. The third campus fired a lock technician for stealing $3,628 from a parking permit machine.

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cc: Members of the Legislature
Office of the Lieutenant Governor
Milton Marks Commission on California State Government Organization and Economy
Department of Finance
Attorney General
State Controller
State Treasurer
Legislative Analyst
Senate Office of Research
California Research Bureau
Capitol Press