



State of New Jersey
Commission of Investigation

The Gifting of New Jersey Tax Officials

December 2005

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Commission of Investigation



**The Gifting of
New Jersey
Tax Officials**

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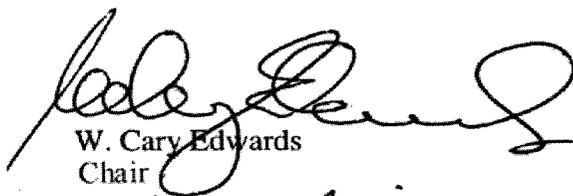
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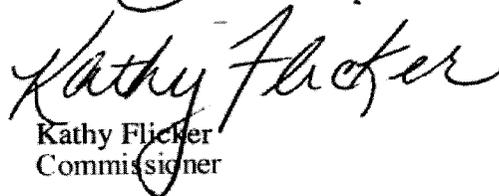
December 2005

Acting Governor Richard J. Codey
The President and Members of the Senate
The Speaker and Members of the General Assembly

The State Commission of Investigation, pursuant to N.J.S.A. 52:9M, herewith formally submits the final report of findings and recommendations stemming from an investigation of abuses in the privatized collection of back taxes.

Respectfully,


W. Cary Edwards
Chair


Kathy Flicker
Commissioner


Joseph R. Mariniello, Jr.
Commissioner

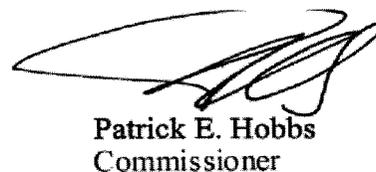

Patrick E. Hobbs
Commissioner

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EXECUTIVE SUMMARY

The Commission uncovered a corrosive vein within the Department of the Treasury [Treasury] that arose out of the relationship between certain of its officials and one of its outsourcing vendors. What began as an effort to privatize the collection of tax debt 12 years ago has evolved into a corrupt association whereby high and mid-level managers in the Divisions of Taxation [Taxation] and Revenue [Revenue] compromised their integrity and that of the department. As officials were lavished with gifts and entertainment by their outsourcing vendor, they turned a blind eye as their benefactor padded the billings. The gifting and entertaining were not isolated events aimed at a few individuals, but spawned a culture that swept through two major divisions within the department. Taxation and Revenue officials violated the public trust, flouted Treasury's Code of Ethics and ignored their responsibilities to ensure the accuracy of the billings.

Beginning in 1990, in the face of looming budget deficits, the State explored the privatization of government functions as a cost-saving measure. One area identified for outsourcing was the increasing backlog of uncollected tax liabilities, then estimated in excess of \$1 billion. As a result, the Department of the Treasury embarked upon a program of contracting with outside collection agencies and attorneys. The outsourcing commenced with the collection of personal income tax deficiencies and grew to encompass the collection of a variety of other back taxes, the identification and collection of tax delinquencies, and the collection of delinquent fees, fines and penalties assessed by other state agencies. Payco General American Credit Corp. [Payco] won the initial

contract award in 1993 and continued to obtain numerous contracts thereafter. In 1996, Outsourcing Solutions, Inc., [OSI] purchased Payco, renamed it OSI Collection Services, Inc., and essentially retained the New Jersey staff. Established in 1995 and acquired by Madison Dearborn Partners in 1999, OSI is a multi-million dollar, national corporation that provides outsourcing services to government and private entities. The company is headquartered in Chesterfield, St. Louis County, Missouri. In May 2003, OSI filed for bankruptcy protection, from which it emerged the following December. Today, OSI Collection Services has four competitively awarded contracts and several related non-competitively awarded agreements with the Department of the Treasury. It remains the primary outsourcing vendor for the Division of Taxation.

The Commission examined two contracts awarded to OSI for the collection of tax debt, one on behalf of the Division of Taxation and the other on behalf of the Division of Revenue. The two contracts comprise three separate collection projects, *viz.* deficient individual accounts, tax deficient business accounts and tax delinquent business accounts. Both contracts stipulate payment on the basis of fee for services, as opposed to a contingent fee basis.¹ The hourly rates, which are for the positions of manager, supervisor, collector and clerical, are all-inclusive, encompassing direct and indirect costs. The Taxation contract is for the time period of August 2004 through July 2007. The Revenue contract began in March 1999. The portion of the contract relating to the

¹ The contract for the Division of Revenue specified the collection of two types of debt, *viz.* back taxes, which is generated from income, sales and other taxes administered by the Division of Taxation, and non-tax debt, which includes fines, fees and assessments owed to other state agencies, namely the Departments of Corrections, Environmental Protection, Law and Public Safety (Division of Consumer Affairs) and Transportation (Division of Motor Vehicles). For the collection of back taxes, Treasury paid OSI an hourly rate. In contrast, for the collection of fines, fees and assessments owed to other state agencies, Treasury paid OSI on a contingency fee basis. In performing its analysis, the Commission focused only on OSI's hourly rate charges and did not include the contingency fees paid to OSI.

collection of back taxes was transferred from Revenue to Taxation in May 2004 and, as a result of four extensions, will expire on February 28, 2006.² Each contract was preceded by similar contracts that also were awarded to OSI or its predecessor and each contract spawned numerous separate, non-competitively awarded agreements with OSI. From January 1999 through June 2005, under the hourly rates of the contracts, OSI collected \$538,356,397 in revenue for the State and was paid \$70,280,690, or 13 percent of the revenue. From January 2000 through September 2005, OSI received more than \$8,000,000 for the additional projects.

OSI's internal documents exposed a pattern of gifting and entertaining not only of New Jersey's Taxation and Revenue officials, but also officials with the federal government and government agencies in other states. Because the initial stages of the Commission's investigation revealed conduct that may constitute violations of the criminal and/or civil laws of this State and of the federal government, referrals were made in a timely manner to the New Jersey Office of the Attorney General, Division of Criminal Justice, and the US Attorney for the District of New Jersey. In deference to their examinations of the issues, the Commission suspended further investigative activities and, thereby, limited the scope of its investigation. Nevertheless, the Commission's findings to date are of such a serious nature that its exposure of them and recommendations for change are compelled. This report is based upon an analysis of the documents received as of this date. Upon the conclusion of the other investigations, the

² On July 29, 2005, in advance of the expiration of the third extension on August 31, 2005, the Department of the Treasury issued a Request for Proposals. On September 15, 2005, the department announced that it was extending the contract for a fourth time to February 28, 2006. As of the printing of this report, no contract has been awarded.

Commission will determine whether to re-open its investigation and whether a supplemental report is appropriate.

THE GIFTING OF STATE OFFICIALS

Stringent laws and codes of ethics exist to prohibit the types of gifting and entertaining of State officials and employees that occurred in this matter. They also make it clear that the avoidance of an appearance of impropriety is as important as avoiding the actual conflict. Nevertheless, officials and employees of the Divisions of Taxation and Revenue violated every provision proscribing the receipt of gifts and other things of value. They engaged in the systematic acceptance of gifts, meals and entertainment and never reported any item to the department's Ethics Liaison Officer. Their actions not only created the appearance of a conflict of interest, but constituted a conflict in fact.

Ethics standards have been established by the State for its employees and vendors and by OSI for its personnel. The Code of Ethics of the Department of the Treasury, promulgated pursuant to the New Jersey Conflicts of Interest Law (*N.J.S.A. 52:13D-23*), prohibits an officer's or employee's acceptance or solicitation of any gift, favor or other thing of value "*which he knows or has reason to believe is offered to him with intent to influence him in the performance of his public duties and responsibilities*" or "*under circumstances from which it might be reasonably inferred [that the same] was given or offered for the purpose of influencing him in the discharge of his official duties.*" Code of Ethics, Section V., "*Acceptance of Gifts,*" quoting *N.J.S.A. 52:13D-14* and *-23(e)(6)*, respectively. Further, the department's Code states that the acceptance of any gifts, gratuities or anything of value "*from a person or organization doing business with the Department, or the granting of special treatment or favors to such person or organization*

for the purpose of obtaining personal gain, is a conflict of interest.” Included as examples of prohibited gifts are cash, liquor, entertainment tickets, personal goods “*and other favored treatment.*” Section V. A.

Citing the *Guidelines Governing Receipt of Gifts and Favors by State Officers and Employees* issued by the Executive Commission on Ethical Standards, Treasury’s Code of Ethics mandates that all officers and employees report “*immediately to the Ethics Liaison Officer*” any gift or other thing of value received “*from a person or corporation with whom they have had contact in their official capacity.*” The Ethics Liaison Officer will determine whether the thing of value was “*given or offered with the intent to influence or reward the performance of the recipient’s public duties and responsibilities, or whether it may be reasonably inferred to have been given or offered with the intent to influence the performance of his or her public duties and responsibilities, or whether the use of the item will create an impression of a conflict of interest or a violation of the public trust.*” An officer or employee may retain “*unsolicited gifts or benefits of trivial or nominal value*” only “*if such use does not create an impression of a conflict of interest or a violation of the public trust.*” Section V. B. Any invitation to a “*business-related function,*” including a meal or “*other social function,*” must also be reported to the division director and Ethics Liaison Officer, who will determine whether acceptance “*will present any problems of conflict with the code, and whether the Department might wish to underwrite the costs incurred.*” Moreover, “*employees are responsible for full payment for the costs of their meals, beverages, travel, lodging and entertainment and may not accept the same from any person, partnership or corporation doing business*

with the Department, contemplating such business, or seeking to influence official actions.” Section V. C.

Specifically, employees of the Division of Taxation “*may not accept a gift or favor from an organization, company or individual . . . that is engaged in a contract with the Division of Taxation.*” Section V. F. In addition, no employee may “*act in any way that might reasonably create an impression or suspicion, among the public having knowledge of the employee’s acts, that the public trust is being violated.*” Section VI. A.1.

After identifying the sanctions to which a violating employee may be subject, Treasury’s Code of Ethics concludes:

Given the severe consequences of violating this code, all employees are advised to strictly adhere to it and to seek advice from the Treasurer, the Treasury’s Ethics Liaison Officer or the Executive Commission on Ethical Standards if they have any questions concerning their obligations under this code. [Section IX.]

In addition to the foregoing provisions, Treasury’s Purchase Bureau developed *Instructions for Agency Participation on an Evaluation Committee*, which was provided to the individuals selected to evaluate the proposals for the contracts ultimately awarded to OSI. The document speaks to the “*the role of the Evaluation Committee in the procurement process*” and the responsibilities of committee members. It addresses conflicts of interest as follows:

Individuals who have a known or perceived conflict of interest with any potential bidder, or with any potential subcontractor of a potential bidder, should not be

recommended to serve on the Evaluation Committee. Individuals who are aware of an actual, perceived or possible conflict of interest should notify the Director prior to accepting our appointment to an Evaluation Committee.

* * *

Evaluation Committee members must immediately make known to the Purchase Bureau member of the Evaluation Committee any real or perceived conflict of interest of any party involved in the procurement process, particularly with bidders, including proposed subcontractors of bidders.

* * *

Evaluation Committee members must not act in any way that might reasonably be expected to create an impression or suspicion among bidders or the general public that his/her judgment is biased, including but not limited to any inappropriate contact with any bidder or subcontractor.

The document also contains an acknowledgement and certification to be signed by each member attesting that he or she has “received, understand[s] and will abide by the rules relating to service on the committee.” The acknowledgement and certification states:

I have agreed to become a member of the Evaluation Committee formed to evaluate bid proposals received in response to the above-referenced Request for Proposals (RFP). As an Evaluation Committee member, I am aware that I am charged with being objective, impartial, unbiased and fair in all aspects of the evaluation process. As an Evaluation Committee member, I am charged with adherence to all of these instructions set forth in the attached “Instructions for Participation on an Evaluation Committee” and the State laws, regulations and policies governing public procurement and ethics. Further, I understand that my strict adherence to these instructions is critical in safeguarding the integrity of the procurement process.

My signature acknowledges that I have read, understand and will abide by the attached “Instructions for Participation on an Evaluation Committee.”

If I have any questions or concerns, either now or at any time in the future, relating to the attached “Instructions for Participation on an Evaluation Committee,” I will immediately bring them to the attention of the Purchase Bureau buyer assigned to the Evaluation Committee or to the Assistant, Deputy or Director of the Purchase Bureau and will resign from the Evaluation Committee, if that is deemed necessary.

I certify that the foregoing statements made by me are true. I am aware that if any of the foregoing statements made by me are willfully false, I am subject to punishment.

The State also has addressed the other side of the gift equation by prohibiting vendors from offering or giving items of value to State employees. Provisions in both contracts awarded to OSI contain “*STANDARDS PROHIBITING CONFLICTS OF INTEREST*” governing “*vendor activities [that] shall apply to all contracts or purchase agreements made with the State of New Jersey.*” Specific standards proscribe vendors from (1) paying or offering to pay gifts or other things of value to a State officer or employee; (2) influencing or attempting to influence any State officer or employee “*in his official capacity in any manner which might tend to impair [his] objectivity or independence,*” and (3) causing or influencing, or attempting to cause or influence, any State officer or employee “*to use, or attempt to use, his official position to secure unwarranted privileges or advantages.*” In addition, a vendor must report to the Attorney General and the Executive Commission on Ethical Standards any solicitation of a gift or other thing of value by a State officer or employee.

OSI has established policies governing the ethical conduct of its employees. **OSI Leader’s Guide**, *Human Resources Policies and Procedures*, contains a chapter on “*Ethical Behavior & Conflict of Interest.*” Its purpose is articulated as follows:

OSI’s reputation for trustworthiness is crucial to its success and growth in a competitive industry. OSI will never tolerate unethical or unlawful business conduct or behavior from any associate. No business or financial purpose could ever justify improper or unethical associate conduct. In many instances, the appearance of impropriety can be just as damaging to the Company and the associate as actual impropriety. Therefore, it too, is unacceptable and will not be tolerated.

The chapter's stated policies include (1) the responsibility of every OSI employee for his or her "*own actions with respect to proper business conduct and behavior. Proper business conduct and ethical behavior are fundamental conditions of employment.*"; (2) the exercise of "*good judgment, common sense and high level of integrity in all dealings and relationships with OSI's customers,*" and (3) the requirement that the employee disclose to OSI Senior Management "*the existence of any actual or potential conflict of interest*" arising from "*a relationship with outside firms*" where the employee has "*any influence on transactions involving . . . contracts.*" In addition, all OSI employees, "*regardless of job or title,*" must report to the General Counsel any suspected violation of the ethics policy.

The Taxation and Revenue employees who compromised their positions were not new to state government. Most are longtime public servants, having spent the majority of their careers in the department. Contrary to the statement contained in a 2001 OSI internal memorandum that "*[a] sound relationship based on trust created the partnership that exists today between OSI and the State of New Jersey,*" the relationship was grounded in gifts. Although there is no evidence that personnel with Taxation and Revenue received anything of value during the periods when they sat on evaluation committees for the awards of contracts, they routinely accepted benefits prior to and after the procurement processes. In addition, Taxation officials took meals during the procurement process of the contract to be administered by Revenue and low-level employees in both divisions accepted lunches during the procurement process of each contract. Benefits also were accepted during periods when decisions were being made to

extend OSI's contracts or to assign additional projects to the vendor. The expense report for one OSI official contained the following notation for August 27, 2004: "*Trenton submitted call center maintenance proposal*" – "*lunch with decision makers.*"

The detailed expense reports submitted by OSI personnel, together with internal e-mails and memoranda, provide a unique glimpse into the special relationship that they cultivated with Taxation and Revenue officials and employees. These documents evince a design to influence public officials. Between February 1999 and March 2005, OSI expended \$65,902 on gifts, meals, alcohol and entertainment³ for 20 officials and employees in the Divisions of Taxation and Revenue.

OSI spent its money in proportion to the benefit that it realized. Because its contract for the Division of Taxation offered the greater potential for income and additional projects, the company spent \$38,924 on that division and only \$24,969 on the Division of Revenue. An additional \$2,009 in expenditures for meals, alcohol and gifts was categorized for personnel in both divisions and cannot be separated by division. After the tax debt portion of the contract, originally administered by Revenue, was transferred to Taxation in May 2004, OSI's gifting and entertaining pattern shifted away from Revenue personnel and in favor of Taxation officials. In addition, OSI established a hierarchy of gifting and entertaining within each division. The level of gifts, meals and entertainment depended upon the level of employee. For example, higher-placed officials usually were treated to late-afternoon lunches, dinners, accompanied by alcohol

³ The monetary figures for meals, alcohol and entertainment include the cost for OSI officials who were present.

on occasion, and cocktails, while lower ones were the recipients primarily of lunches. Of the \$30,363 spent on Taxation officials and employees for meals and alcohol, more than \$20,000 was directed to three high-level officials, in contrast to the approximately \$5,000 expended for a couple of lower-level employees. For the Division of Revenue, the majority of the \$19,517 spent on meals and alcohol was targeted at those at the higher levels.

OSI's arsenal of largess included a variety of personal gifts and forms of entertainment, such as golf outings, a leather portfolio, gourmet chocolates, a set of custom golf balls, expensive imported cigars, and fruit baskets, some costing in excess of \$100 each. In this regard, OSI expended \$8,561 on Taxation officials and \$5,451 on Revenue personnel. Opportunities for gifting included birthdays, Christmastime, the appointment of one official to his position and the retirement of another official, who received two \$100 gift certificates. OSI spent close to \$7,000 on golf outings alone. Of this figure, \$3,814 was for separate golf outings for two officials, one from Taxation and the other from Revenue, and, of that figure, \$1,600 was for the same two officials and two OSI officials to attend a charity golf outing. At an out-of-state conference, detailed below, OSI indulged select officials from both divisions with spa treatments at a cost of \$1,019.

OSI was particularly generous with two officials in Taxation. In addition to spending close to \$17,000 on them for meals and alcohol, the vendor also entertained and gifted them. OSI officials, usually accompanied by their wives, treated the one official

and his wife to dinner and a theater performance in New Jersey; dinner and a concert in New Jersey, and a Broadway musical, together with limousine service, dinner and a soundtrack of the show. OSI spent \$2,028 on the New York City excursion. On yet another occasion, at a cost of \$461, an OSI official and his spouse and a second OSI official treated the Taxation official and his wife to dinner, followed by “[a]fter dinner drinks and cigars” for an additional \$66. Noted on the OSI expense report was “discussed new opportunities.” The same official also received \$781 in personal gifts and contributions to the liquor and entertainment for parties at his home. In addition to meals and cocktails, the second Taxation official received gifts totaling \$452, which included a \$200 gift certificate to a premier golf club, and was taken on nine golf outings costing \$3,077. The OSI official’s expense report indicates that on one of the golf outings, they “discussed expanding contract.”

OSI’s internal documents chronicle its generosity with Taxation and Revenue officials. In an October 2001 memorandum to sales people dealing with government agencies, a high-level manager in New Jersey announced the “2001 Holiday Gift Program”:

We are adopting a new policy for gift giving to clients and prospects for this holiday season. We are enabling each of you to purchase your own gifts and will rely on you having them shipped or personally delivered. Attached is a list of the people you sent gifts to last year along with the size of the gift you sent. The total dollars spent by you is listed at the bottom of the print out [sic].

Below are listed the guidelines you must adhere to for this holiday season. If you are not sure of policy or wish to ask a question or discuss a particular client/prospect[,] please call me at once. Do not assume anything:

- ◆ *You are to spend no more than you did last year on total gifts[.]*

- ◆ *No matter how small or large the gift, you must have a receipt when expensing.*
- ◆ *Where you can't send a gift to an individual, it might be a good idea to send something to the department or division. Food items (popcorn, candy, etc.) are generally thought to be ok.*
- ◆ *Stay "holiday-neutral" and avoid any religious or [sic] themes or messages.*
- ◆ *Make sure all gift tags say "From Your Friends at OSI". [sic] Do not just sign your name.*
- ◆ *Where multiple people are calling on a client/prospect, the person who [sic] territory the client falls in will be responsible to send the gift. You should coordinate this with the "other" sales person prior to ordering[.]*
- ◆ *Ordering quickly will insure proper and on-time delivery. Make sure all presents being sent by mail are shipped early.*
- ◆ *Costco or Sams Warehouse type of super discount stores are excellent places to pick up gifts. Shop early as their supplies run out quickly. With this new policy it will be easy to pick up items such as decorative candles to give to non-decision makers that previously didn't warrant our least expensive gift (\$32)[.]*
- ◆ *It is not necessary to overspend or spend all your budgeted monies. Let's keep in mind our not so great year and be more creative and selective when purchasing gifts.*

An attachment to a November 29, 2004, e-mail from one New Jersey OSI official to an individual in the corporate finance department not only exemplified OSI's pattern of gifting Taxation and Revenue officials, but also revealed the underlying motive:

Holiday Gift Giving

CONFIDENTIAL

My Holiday Expenses (with the exception of Cards) is usually limited to the State of New Jersey:

I personally shop for gifts for the top decision makers of both the Taxation and Revenue Agencies. I normally hand deliver these items to the recipients at a Holiday lunch or dinner or if I attend an affair at their home. I clearly notate that the gift is from everyone at OSI.

I have listed the recipients and the anticipated spending below:

The document then identified three officials with Taxation, together with “Taxation Admin[.] Staff,” and four officials with Revenue. It estimated Taxation’s 2004 revenue under OSI’s contracts and projects at \$13.5 million and projected Revenue’s income to be \$1.85 million. The cost of the gift was \$125 or \$150 for each Taxation official and \$40 for each administrative staff person, while the gift for each Revenue official was valued at \$30 or \$50.

The confidential e-mail continued:

Scheduled Dinners/Luncheons with operation management and key NJ contacts:

<i>Dept[.] of Revenue – Upper Management</i>	<i>6 people</i>	<i>200.00</i>
<i>Taxation; Contract auditors & liaisons</i>	<i>10 people</i>	<i>600.00</i>
<i>Taxation Decision Makers & Upper management</i>	<i>12</i>	<i>1400.00</i>

I would really like to take [the first names of two Taxation officials] into the city for a show (we’d take the train). With tickets and dinner this cost might be between \$7-800.00. [The first names of these individuals] contributed largely to our NJ new client revenue this year. Let me know your thoughts.

The OSI official concluded the e-mail with the reasons for treating Taxation and Revenue officials in this manner, with the second and third points focusing not only upon extant contracts, but also future ones:

Things worth considering when you’re contemplating the amount of spending you’ll approve:

- *There are next to no travel expense or lodging cost associated with entertaining this client. (Right off the top an average visit to a client can be close to \$1,000.00!) [Emphasis in original.]*
- *Largest revenue producing client and largest “new client revenue” opportunity for Government in 2005. [Emphasis in original.]*
- *Re-bid for the largest portion of this client will be in July 05.*
- *These spending are in line with previous years. (May even be a bit shy considering the former SVP’s [Senior Vice-President’s] focus on indulging this customer & spouses.)*

OSI did not provide the Commission with any responding e-mail.

Other OSI documents also recorded the holiday gifting of Revenue and Taxation officials:

1. Computer print-outs entitled “*Holiday Gift List*” for particular OSI personnel, by year, contained the following completed categories:
 - *Gift Level;*
 - *Quantity;*
 - *Client Name [NJ Division of Revenue or NJ Division of Taxation];*
 - *Contact Name [name of Revenue or Taxation official];*
 - *Title;*
 - *Annual Revenue;*
 - *Ship To [“Client’s House” or “OSI”];*
 - *Address, and*
 - *City.*
2. In computer print-outs labeled “*Holiday Gift Order*,” local OSI officials detailed their annual gift orders for Revenue and Taxation employees, from high-level managers to secretaries. The forms included the type of gift and its cost, the name of the client and the location for delivery. Included on one order was the name of a retired official who became a consultant for OSI. In one year, three Taxation and Revenue officials each received not only a gift costing \$64.95, but also a \$49.99 bottle of Grey Goose Vodka delivered at “*Xmas parties*.”
3. An undated, computer-generated document for one New Jersey-based OSI official was marked “**CONFIDENTIAL**” and contained three headings, viz. “*Client (Name & Contract)*,” “*Type of Gift*” and “*Approximate spending*.” It listed the names of nine officials in Taxation and Revenue

together with their corresponding gifts, which included “*Book series & book ends*,” “*Home Goods Basket*,” “*Fondue Kit w/wine*,” “*X-Wreath & wine*,” “*Wine & glasses*,” wine and “*FL Candle stand & liquor*.” The cost of the gifts totaled \$642, ranging from \$13 to \$242 each.

4. Computer print-outs titled “*Total Govt Holiday Gift Order*” included the completed categories for:
 - *OSI sender*;
 - *Gift level [denoted as “1,” “2,” “3” or “4”]*;
 - *Qty.*;
 - *Client*;
 - *Contact name*;
 - *Contact title*;
 - *Annual revenue*;
 - *Ship to client or OSI?*;
 - *Ship address, with City[,] State and Zip*;
 - *Residence?, and*
 - *Phone.*

The wining and dining of Taxation and Revenue officials was not limited to New Jersey locales. According to e-mails in September 2002, OSI officials in corporate headquarters in Missouri prepared for the visit of a high-ranking Taxation official, together with several New Jersey-based OSI officials. The Taxation official, whose office was referred to as OSI Government Division’s “*largest client*,” was invited to address OSI’s Executive Management Team on “*The Role of Today’s Manager in Government*.” On the day of his arrival, he was taken to dinner. The itinerary showed that the topics for dinner discussion included “*Scoring & Segmentation*” and “*marketing*.” On the next day, the official was treated to a St. Louis Cardinal Baseball Game and lunch, following which he was driven to the airport for his return flight home.

In 2004, Taxation and Revenue officials attended a regional conference of tax officials held in Maine. OSI, one of the exhibiting vendors, “*treated*” eight of them to

spa services totaling \$1,019. The OSI official expending the money for the spa treatments, as well as other forms of entertainment, listed the following on the expense report:

- 9/26/2004 *Treated NJ Clients (NJDOT [New Jersey Division of Revenue]) to spa treatments [number of persons was five at a cost of \$788.80]*
- Dinner w/existing clients & prospects [“Clients from NJ” was listed in addition to unnamed officials of another state and OSI officials, totaling nine, for a cost of \$492.74]*
- 9/27/2004 *OSI hosted hospitality suite [for \$45.76]*
- 9/28/2004 *Treated NJ Clients (NJDOT) [New Jersey Division of Taxation] to spa services [number of persons was two at a cost of \$136]*
- 9/29/04 *NJDOR [New Jersey Division of Revenue] spa service [one person at a cost of \$95]*

The easygoing, unprofessional relationship that developed between OSI and Taxation and Revenue officials is reflected further in March 2004 e-mails between a top-level Taxation official and a local OSI official concerning the upcoming arrival of a corporate official in New Jersey. The OSI official advised:

I can't thank you enough for taking time out to meet with our [corporate official] and for speaking with our collections staff. I spoke with [him] about dinner on Thursday evening, most likely [names of two local OSI officials] will join us. As soon as I know [his] flight arrival I can confirm a dinner time and restaurant.

Our staff will be thrilled to have you speak. I [sic] did just occur to me though, that our East Windsor's office would feel very left out if we didn't acknowledge them. I don't want to monopolize your entire day but, but . . . I could suggest the following: Meet at East Windsor in the morning. Head to Edison around lunch time. Talk to the staff – [the corporate officer] has a very short presentation on his role and the direction of the company etc. . . he leaves by 2pm. [sic] We are at Clydz enjoying martini's [sic] by 3:30 ish. If your schedule won't allow – we can get everything done in a morning.

It goes without saying that should you wish to bring any members of your illustrious staff, their company is always welcomed and most enjoyable.

Thanks a million.

The Taxation official responded:

I would like to revisit an offer you made about picking [another Taxation official] and I [sic] up on Friday. If you could pick up yup [sic] at the Trenton train station we could travel with your gang all day and take the train home from New Brunswick when we stumble out of Clydz's. If it still works for you just tellme [sic] what time. Thanks, [first name of official] . . . I am getting pumped!!!!

It was extremely rare for a Revenue or Taxation employee to refuse a gift or free entertainment. Indeed, the Commission discovered only two such incidents. The first occurred in 2002, when a local, high-level OSI manager saw a Revenue official at a Titanic Exposition. He purchased a “*Titanic Acrylic 8x10 gift*” and later gave it to his co-worker to bestow upon the Revenue employee, who refused it. The second incident took place when another Revenue employee decided to reimburse OSI for the spa services she had received at the aforementioned regional tax conference in Maine. According to the e-mail from the “*treat[ing]*” local OSI official to corporate headquarters regarding “*Client reimbursement,*”

I am forwarding you a check for \$285.00 made payable to me, which I have endorsed back to OSI. The check was sent to me by a client who [sic] I treated to spa services during a tax conference. Because she works for the government[,] she's uncomfortable accepting a gift of this size from OSI.

Despite this spurt of ethical conscientiousness, both Revenue officials accepted meals from OSI.

In June 2004, an e-mail emanated from the corporate finance department concerning the company's "requirements for expense reports." Emphasizing that "[t]he new expense policy requires detail," it stated:

If you are entertaining a client, include name, titles, discussion and any dollar amount involved in the entertainment.

The e-mail concluded:

I have always believed that we need to spend money to make money, but spend the money wisely. We need to get the biggest bang for our buck!

In a responding e-mail, an OSI official in New Jersey revealed a personal gifting pattern:

It has been a standard practice for me not to include the names of individuals I entertain in NJ.

(There are a few other branches of NJ government who have faced tremendous public scrutiny for accepting gifts and meals from vendors who's [sic] records were subpoenaed.)

In the past I have simply told [my supervisor] who [sic] I've entertained or attached a note to the report that he'll keep separate or toss. Since OSI has relationships with various levels of each department and our 3 separate contracts are managed by different teams of people, I try to have lunch or dinner with someone from either Taxation or Revenue twice per month. If I plan to spend more than \$125-175.00 I would normally talk to [my supervisor] about it in advance. [Emphasis in original.]

We have always been a bit more generous with NJ then [sic] other clients. They are the [Government] Division's largest client, we have 4 separate contract [sic] between Revenue & Taxation as well as 5 State Agencies. (Also worth mentioning: [my predecessor] spoiled the hell out of the Directors, so although I don't try to compete, I am conscious of the special treatment they [sic] used to.) The good thing is, at the end of the day, there is never a plane ticket or hotel expense!

Please let me know your thoughts and how you & [another OSI officer] would like to handle this situation going forward.

Although the local official sought direction, OSI was unable to produce a reply e-mail.

OSI's deliberative program of gifting and entertaining extended into the political arena. According to a series of e-mails in early 2004, OSI supported a US Senator in a neighboring state in connection with proposed legislation. In response to a directive to attend a fund-raising luncheon for the Senator (*"Although we have had a minor setback this week in the Senate, it is even more important that we have a good showing of support – both physically (next Wednesday) and most importantly, financially for the Senator from [the neighboring state]."*), a New Jersey-based OSI official sought approval from corporate headquarters to contribute to the \$1,000 fund-raiser, even though he was unable to attend. Initially, it was agreed that a \$500 corporate check would be mailed. However, according to an e-mail by the local official to a corporate officer,

I got a call from the folks running the fund raiser [sic]. They need a personal check, not a corporate check.

[An individual in the corporate finance department] said he will stop payment on the corporate check and that I should send my own personal check for \$500 and submit it on my next expense report.

The OSI official submitted the item on his expense report and attached a copy of his personal check for \$500, which was made payable to the US Senator's campaign.

INFLATED BILLINGS

As stated above, OSI's billings were based upon hourly rates for the positions of manager, supervisor, collector and clerical.⁴ According to the contracts, as confirmed by Taxation and Revenue officials, administrative overhead was encompassed in the hourly rates and was not to be billed separately. OSI violated the terms of the contracts when it failed to bill the State in strict accordance with the hourly rates and task categories. In the absence of a vigorous watchdog, OSI took license to enhance its profits. Based upon the Commission's limited investigation, it is estimated that for each year from 2000 through 2004, OSI over-billed the State by hundreds of thousands of dollars that totaled more than \$1 million for the five-year period. For example, from January 2000 to February 2004, OSI billed approximately \$237,000 for the regular and overtime hours of a longtime employee as a collector and then as a supervisor when, in fact, she performed an administrative function on Treasury and other matters.

According to documents, the issue of questionable billings was raised three times, once by a Revenue official and twice by OSI personnel. In a February 2002 e-mail, a Revenue official alerted other officials that the January bills contained hourly charges at a manager's rate for two OSI employees who were assigned to Information Technology, positions that constituted administrative overhead and were not to be billed. Noting that there may have been "*a discussion or agreement to this effect*" between OSI and Revenue officials, she asserted:

⁴ It appears that OSI has this billing arrangement only with the New Jersey Department of the Treasury and not with government agencies of any other state or the federal government.

I don't know what your feeling is[,] but these guys are not collecting money for us. Under our additional work section, our categories are clerical, @ \$19.00, imaging/scanning operators @ \$22.95 and customer service reps @ \$28.50. These guys are coming in above \$32 an hour.

Although no responding e-mails were provided to the Commission to indicate how the issue was resolved, OSI resubmitted the January bills, but without any supporting documentation. The resubmitted bills showed the names of the two OSI employees moved from the manager category to the collector category and contained a reduction in the total number of manager hours, but an increase in the number of collector hours by the same number of disallowed manager hours. Apparently, in approving the bills, Revenue officials did not question the re-listing of the names or the sudden increase in collector hours. From that time to early 2005,⁵ the billings submitted by OSI continued to list the two individuals as collectors at a cost to the State of more than \$400,000. If, in fact, Taxation or Revenue officials had advised OSI personnel that they approved the billing of administrative overhead at the collector's hourly rate, they contravened the clear terms of the contract, violated their responsibilities, and concealed the fact during interviews conducted by Commission staff.

On two separate occasions, OSI employees charged that OSI was over-billing the State of New Jersey. In December 2002, a former employee sent Revenue an e-mail captioned "*The Bilking of Taxpayers.*" Taxation and Revenue provided no records to the Commission to indicate that the allegations triggered any internal audit or investigation. The failure to conduct an examination is all the more startling because Revenue officials had previously determined that OSI's January 2002 billings were improper. However,

⁵ The Commission subpoenaed records from OSI through February 2005.

the e-mail was turned over to OSI for its assessment. An internal OSI document responded to the allegations. Although the record provided to the Commission does not identify the author, the recipient, the date or its form, it was an attachment to an e-mail sent from a local OSI official to an official in Revenue. On the day before OSI sent the e-mail, another local OSI official took a Taxation official to lunch, at a cost of \$117. On his expense report, the OSI official noted that they discussed “*employee complaint.*” In the OSI document forwarded to Revenue, OSI offered the following on the allegation of “*billing a tax collector as a manager*”:

OSI is not aware of any situation in which a collector was billed to the State as a manager. Our invoices are heavily scrutinized internally to ensure all employees are categorized correctly and billed at the agreed upon rates.

It concluded with the statement:

The State audits our invoices upon receipt; any items in question are discussed and explained openly. The DOR’s [Division of Revenue’s] liaison, who works one day per week in the EW [East Windsor] office coordinates this effort.

Contrary to the assertion regarding the auditing of OSI’s invoices, both Revenue and Taxation officials admitted to Commission staff in interviews that no such audits were done, either on a routine or sampling basis. Further, no documents were produced by either division evidencing that any audits were performed. Apparently, Revenue and Taxation officials were satisfied with OSI’s perfunctory handling of the matter.

In March 2004, allegations of over-billing surfaced again when an administrative employee made oral and written complaints to both local and corporate officials. The

complaints were not addressed internally until May 2004. Contrary to the requirements of the contracts, there is no documentation to indicate that OSI notified Taxation or Revenue officials of the allegations. The issue was conspicuously absent from OSI's monthly reports to both Taxation and Revenue, viz. the Fiscal Monthly Report, which included the categories of "*Problem Areas*," "*Highlights*," "*Unusual Situations*" and "*Matters of Significance*."

Two separate documents presented the allegations of over-billing to a high-level corporate officer in Missouri. In an e-mail dated May 26, 2004, a New Jersey-based official advised that an employee had alleged that her time and that of "*our recruiter, time and attendance admin [administrator] and trainer*" were improperly billed to New Jersey on "*the hourly rate project*." The local official dismissed the allegations on the grounds that (1) the complaining employee was the assistant to an administrative supervisor and "*took her calls and messages most often from NJ Tax*," and (2) the other employees "*spend the overwhelming amount of time working on NJ Tax*." It is noted that with respect to the hours of the complaining employee, OSI never billed for the hours of her supervisor, whose responsibilities constituted administrative overhead. Clearly, then, her assistant should not have been billed. With respect to the other employees, their titles fell outside of the categories permitted for billing.

The May 26, 2004, e-mail noted that "*another disgruntled employee*" had complained to the State several years ago "*about this same subject*" and that after two high-level local OSI managers, both of whom generously had gifted Taxation and

Revenue officials, *“met with the client, all was explained and resolved satisfactorily.”* Any favorable resolution rendered by Revenue or Taxation officials is highly suspect in light of the permissive atmosphere fostered by OSI. The same suspicion attaches to the e-mail’s assertion that *“the client requested that we put”* two information technology employees on the billings as collectors. If the statement is accurate, the official’s directive ran counter to the mandates of the contract.

The same e-mail also contained an admission by the local official regarding the billing categories:

Thought there are only four billing categories – manager, supervisor, account rep and support. We have included other functions within the four categories.

In an e-mail to the same corporate official on May 28, 2004, another local OSI official advised, *“Per your request, I have detailed at a summary level the billing exceptions areas.”* The summary was the subject of an internal memorandum of the same date to the corporate official. After reciting that the contract allows OSI to bill Revenue and Taxation for the job categories of manager, assistant manager, supervisor, collectors and clerical support, the author noted that OSI billed for all of the categories except assistant manger and also *“billed for three employees whose job titles do not fall under”* any of the permitted job titles. He named the three employees and identified their job titles as well as the ones under which they were billed. Specifically, the human resources assistant and the recruiter were each billed as clerical support and the technical trainer was billed as a collector. His attempted justification for billing them under different titles is strained at best:

While the contract does not expressly define their roles, the Assistant Manger job description in our 1998 proposal included the responsibilities for Human Resources, Payroll Administration as well as collector training.

The fact remains that, although its proposal included the position of assistant manager, OSI never billed these three employees or anyone else under that title.

With respect to the complaining employee's allegation that her time also was improperly billed, the local official presented the following rationalization:

We are of the opinion that the billing of 100% of her time was not inappropriate since [the individual] who manages the Edison tax operation was never billed under the contract.

However, the duties of the individual "who manages the Edison tax operation" constituted administrative overhead and her hours properly were never billed to the State. Moreover, if OSI perceived any errors in prior billings, it should have submitted corrected billings.

After advising that the complainant had "threatened" to "complain to the State about our billing practices," the memorandum's author concluded:

In light of this development, hindsight would suggest that a different course of action would have been more appropriate. I believe with the exception of the eight-month period referenced above [when the complainant spent only a little time working on statistics for the NJ Tax project, but 100 percent of her time was billed to the State], our billing activities can withstand any scrutiny. I also believe that if we explain our rationale for billing 100% of [the complainant's] time to NJ Tax, it will be acceptable to the client.

Even though the OSI official drew an “*exception of the eight-month period,*” OSI did not reimburse the State for the employee’s hours during this period. Further, it bears emphasis that Taxation and Revenue officials were adamant that only OSI employees performing the specific billable jobs could be billed. Despite the “*hindsight*” of the memorandum’s author, OSI officials continued the billing schemes. Significantly, neither the monthly fiscal reports filed by OSI with Taxation and Revenue nor the minutes of monthly meetings between OSI and Revenue contained any mention of the employee’s allegations of over-billing. It is noted that during this time period, OSI was attempting to secure a renewal of its contract for the collection of delinquent tax debt. On May 10, 2004, Treasury issued Requests for Proposals and, on June 25, 2004, awarded the contract to OSI.

The memorandum also advised that the complainant’s threat was discussed with a high-ranking Taxation official, who allegedly opined that “*this is an OSI matter and should be dealt with internally.*” If such an allegation had been brought to this official’s attention, then his blasé attitude may only be attributed to his having been compromised by the routine acceptance of gifts, entertainment, meals and alcohol.

The corporate officer who received the May 28, 2004, e-mail and internal memorandum forwarded the communications the same date to a higher-level corporate official, who shot back:

This is a BS response. I think we need an objective person to interview [the employee making the allegations] and get hard details ASAP.

However, little was done to examine the serious allegations; there was no interview of the complaining employee, and the resultant report was a flawed and unconvincing recital of findings.

As reflected in internal e-mails in July 2004, the administrative employee's allegations of improper billings triggered a review by the Corporate Review department, which produced an "*audit report for the NJ Department of Tax project.*" It concluded that "*the billings were well supported by the time and attendance system and the billings are in accordance with the contract.*" The audit report, a one and one-quarter-page memorandum dated July 9, 2004, is little more than a conclusory statement that avoids the substance of the allegations of over-billing. Although claiming to be "*an internal examination of the billing practices,*" the scope of the examination was limited to the five-month period of January through May 2004 and the conclusions were based solely upon a review of hours performed. The report ignored any analysis of the job functions of the employees billed to the State. The issue was not whether the employees in question worked the hours documented, but whether their titles were misrepresented on the billing documents and whether their true titles and duties constituted administrative overhead. According to the report, the only employee interviewed was the local official who had authored the May 28, 2004, memorandum attempting to justify the billings. The report relied, in part, on his bald opinions:

[The local official] believes that all work has been performed in accordance with the contract and invoicing has been performed on a timely and accurate basis. [He] also mentioned that the client has been very pleased with our work over the years as evidenced by the continued renewal of the contract and addition of new projects. . . .

In addition to the allegations of over-billing, an internal OSI e-mail, dated September 27, 2003, indicates that another type of liberty was considered with respect to billing the State:

*[W]ith the TGI section being so light on cases, this give [sic] us an opportunity to expand the upcoming account rep management training courses. I think we should give them additional material that they can work on at their desks, such as having them document a sample personnel dispute or case related problem or memo to the client. This way we can improve their written AND verbal communication skills. **We need something to fill their time and it will still be related to working accounts**, the better they learn to write and document, the better their casework will be. Just some ideas I'm thinking about. . . . [Emphasis in bold supplied.]*

LACK OF OVERSIGHT

The handling of the two OSI contracts depicts the failure of government to oversee its vendor's activities, not necessarily in the day-to-day operation, but in terms of ensuring the financial integrity of the billings. The system eroded because those responsible for the oversight compromised their personal integrity and abandoned their public duty. Taxation and Revenue officials operated in a milieu where receiving gifts and being entertained became the norm and the Code of Ethics irrelevant.

The areas of failure are numerous:

- **Audits and Quality Controls.** In startling admissions, officials stated that no quality controls have existed to determine the accuracy of OSI's billings. Officials in both Revenue and Taxation admitted that there has been no system in place to verify the titles or number of hours submitted for individual OSI employees, not even on a random or spot-check basis. In approving OSI's requests for payment, they perfunctorily certified the acceptance of work completed. One official, who was a recipient of OSI's generosity, cavalierly advised that he never had reason to doubt the accuracy of the billings. He admitted that in his role of reviewing OSI's payment vouchers, which included time sheets, he undertook no steps to ensure the accuracy of any of the billings, but simply conducted a "*cursory inspection*" and accepted the information presented by OSI.

Both contracts required OSI to maintain books, records and other evidence related to all of its administrative costs and expenses for review by Taxation and Revenue, and one contract specified the right to inspect all financial and accounting records supporting OSI's billings. In addition, during the procurement process for one of the contracts, the responses to bidders' questions included the statement, "*The State does reserve the right to review your payroll records to verify billable hours.*" Nevertheless, according to documents and interviews, neither Revenue nor Taxation personnel performed any audit of payroll records or administrative costs and expenses.

Although Revenue assigned an employee to visit one of OSI's collection facilities each week, it never assigned anyone to inspect OSI's other facility.

Meetings conducted by Taxation with OSI management rarely yielded minutes, in contrast to those conducted by Revenue. Nevertheless, none of the minutes compiled by Revenue indicated any notification or discussion of allegations of over-billing.

- **Passcodes.** In order for OSI collectors to access Taxation's computerized system of taxpayers' accounts, Taxation assigned passcode numbers to them. The assignment of the numbers and their deletion from the system were based on OSI's notification to Taxation of hirings, terminations and resignations. Despite the sensitivity of taxpayers' information and the potential for abuse of these numbers, Taxation officials conducted no audits of the usage of the numbers. They never matched numbers with the names of collectors listed on the billing documents or verified the deletion of numbers. The Commission found that some OSI employees whose names were billed as collectors either did not have passcodes assigned to them or, if they did, their passcodes showed no usage.
- **Notification regarding personnel.** Provisions in each contract addressed the movement of personnel by OSI. The vendor repeatedly ignored the requirements and Taxation and Revenue officials failed to enforce them.

Under the one contract, OSI must notify Taxation of proposed changes in managers or supervisors and obtain its written approval prior to any substitution. Although one official acknowledged that such changes in personnel have occurred, he was not aware of the contract provision mandating notice and approval and admitted that there is no "*process*" in place to address this requirement.

Contrary to the requirements of the other contract, OSI failed to provide Revenue "*on a monthly basis a detailed table of organization or list showing all employees by name and title that are assigned to the contract*" or to inform it of all new hires and terminations.

OSI also did not adhere to the provision in each contract to provide detailed resumé qualifications and justification for substitute management and supervisory personnel.

Although OSI submitted fiscal monthly reports that included categories for hires, terminations and transfers, it did not always note the transfer of personnel to, or from, the tax projects.

POST-EMPLOYMENT OF STATE OFFICIALS

In addition to addressing gifts and favors, the New Jersey Conflicts of Interest Law and the Department of the Treasury's Code of Ethics proscribe the acceptance by a State officer or employee of "*employment or offer of employment . . . which he knows or has reason to believe is offered to him with intent to influence him in the performance of his public duties and responsibilities.*" N.J.S.A. 52:13D-14. In addition, the department's Code of Ethics, Section VII.D., prohibits employees, "*who have direct and substantial contact with any consultants or vendors doing business with the Department of the Treasury,*" from actively "*seeking employment with those firms until such contact ceases.*" Any solicitation of the employee for potential employment must immediately be reported to the employee's management and to the Ethics Liaison Officer.

After lengthy careers with the Department of the Treasury, two high-ranking officials, who had been involved in the administration of the Payco/OSI contracts, became consultants for OSI. The Taxation official signed an agreement with OSI only 17 days after his retirement. He was hired as "*an independent contractor providing consulting and marketing support*" and, specifically, "*as a sales representative for OSI for the purpose of inducing certain clients and prospects to utilize the services of OSI.*" His duties include "*provision of administrative and consulting services such as advice as to better servicing existing clients, assistance with selling new products or services to existing clients, appointment setting with key decision makers, assistance in responses to*

RFP's and prospecting state and local government for sales opportunities." A 2004 OSI organizational chart showed him as the sole consultant for "*State Local Gov't.*"

Following the retirement of the Revenue official, who had been gifted and entertained by OSI officials, OSI hired him as a consultant for its Government Division in New Jersey. Although records indicated that a consulting agreement was executed approximately five months after his retirement from public service, OSI expense reports revealed that he commenced providing services much earlier. Only five days following his retirement date, OSI officials took him to dinner. Approximately one-and-one-half months after his retirement, he was taken to lunch, where, according to the expense report, "*consulting on State of NJ data*" occurred. Two weeks later, OSI officials took him out for cocktails and, one week after that, treated him to dinner. Approximately five weeks later, little more than three months following his retirement, the former official again was taken to dinner. The notation on the OSI official's expense report for this dinner disclosed that it was for the purpose of meeting "*w/NJ consultants re: pending contracts (date [sic] entry & processing).*" According to another OSI document, approximately six weeks later, but prior to the execution of an agreement, approval was sought for the payment of a \$500 "*Consulting Fee*" to him "*for his assistance and contribution to our response to the NJ Data Entry RFP.*"

In an internal e-mail recommending the hiring of the former Revenue employee, an OSI official stated, "*We believe he can open a few doors and add credence to presentations.*" The consulting agreement recited that "*OSI is engaged in the business of*

collecting retail, commercial, and government accounts throughout the United States,” that the individual is *“to act as a consultant for OSI for the purpose of inducing state agencies to utilize the services of OSI for either/or collections or outsourcing services,”* and that *“in furtherance”* of an executed agreement with a client agency, the individual *“will devote his best efforts to negotiating, arranging, and maintaining these exclusive collection/outsourcing contracts.”* Nothing in the consulting agreement excluded New Jersey government agencies.

REFERRALS AND RECOMMENDATIONS

In addition to the referrals previously made to the New Jersey Office of the Attorney General and the United States Attorney for the District of New Jersey, the Commission also refers its findings to the Office of the New Jersey State Treasurer, the New Jersey Executive Commission on Ethical Standards, the New Jersey Election Law Enforcement Commission and the United States Internal Revenue Service.

* * *

The Commission's investigation underscores not only weaknesses in the character of individual public servants, but also in the ethics system designed to maintain the highest degree of integrity in government. In addition, the findings of this inquiry highlight defects in the administration of contracts for the privatization of government services. On a broader scale, these findings exemplify the need for an entity dedicated to the provision of effective and ongoing fiscal and programmatic oversight of government operations, particularly with respect to contract management and administration. Therefore, the Commission makes the following recommendations for systemic reform:

1. SEVER THE RELATIONSHIP BETWEEN OSI AND THE RECIPIENTS OF BENEFITS IN THE DIVISIONS OF TAXATION AND REVENUE

The Commission's investigation revealed the widespread, unethical relationship that has developed between officials and employees within the Divisions of Taxation and

Revenue and their outsourcing vendor. The actions of these individuals undermine the integrity of government and besmirch the good name of public service. At the very least, Taxation and Revenue personnel have violated ethics rules by accepting things of value. At the most, they have abdicated their responsibilities in overseeing OSI's contractual obligations. Accordingly, the Commission urges that immediate action be taken to sever their involvement with the administration of OSI's contracts and agreements. In addition, disciplinary proceedings against the offending officials and employees must be initiated in order to demonstrate to the public and other government employees that such conduct will not be tolerated. Further, department-wide ethics training should occur to reinforce in every employee the importance of strict adherence to the Code of Ethics.

At the same time, the Department of the Treasury must take appropriate action against OSI for violating the standards governing the activities of State vendors. In light of the longstanding and deliberative pattern of gifting and entertaining Taxation and Revenue officials by OSI employees, the Commission recommends that, pending a resolution of the issues identified in this report, the department commence an orderly transfer of responsibilities under the OSI contracts and then temporarily debar OSI from performing its contractual obligations.

2. AUDIT OSI CONTRACTS AND AGREEMENTS

The Department of the Treasury should immediately conduct a detailed financial and internal control or systems audit of all contracts and agreements with OSI and correct

any deficiencies. The department should initiate proceedings to recover amounts owing to the State. In addition, the department must determine whether OSI has been complying with all of the terms of each contract and agreement.

3. *ESTABLISH INDEPENDENT ENTITY FOR FISCAL AND PROGRAMMATIC OVERSIGHT*

This matter presents another example of the failure of State government oversight with respect to the administration and performance of contractual arrangements with private vendors. Earlier Commission investigations laid bare various related aspects of the State's inability to monitor and root out threats to the integrity of the contract procurement process and to ensure acceptable operational performance.⁶

Therefore, the Commission reiterates its recommendation that the Governor and Legislature should undertake a review of the State's current fragmented oversight structure and either reorganize it or establish an independent entity to consolidate and expand fiscal and compliance oversight functions. This entity could take any number of forms, including an appointed or elected state auditor or auditor general, or an appointed or elected state comptroller or controller. Whatever the form it takes, the need for such a centralized mechanism is critical given the vast sweep of government operations and the sheer number of agencies and departments that engage in procurements and administration of contracts.

⁶ See Commission reports, *E-ZPass: The Making of a Procurement Disaster* (June 2004) and *N.J. Enhanced Motor Vehicle Inspection Contract* (March 2002).

4. ESTABLISH AN INTERNAL TREASURY UNIT TO AUDIT CONTRACTS

In order to ensure that routine financial audits and internal control reviews of contracts are conducted by the Department of the Treasury and its various divisions, the Commission recommends that a special oversight unit be established within the confines of that agency. This unit would have no involvement in the administration of the contracts. With respect to the privatization of tax debt collections, the functions of this office should include:

1. Reconciliation of amounts owed by taxpayers with the monies collected to determine whether the vendor is collecting appropriate amounts in relation to the debt;
2. Reconciliation of the monies collected by the vendor with the funds transmitted to the State;
3. Auditing of the vendor's billings and supporting documentation to ensure the accuracy of the billings under the parameters of the contract or agreement, and
4. Examination of whether the State is receiving the services for which it contracted and assessment of the relative value of the products being delivered.

5. STRENGTHEN PROCEDURES FOR THE AWARD AND OVERSIGHT OF PRIVATIZATION CONTRACTS

In light of the trend toward increased privatization of services traditionally restricted to the exclusive domain of government, it is imperative that the State institute comprehensive procedures to ensure that the use of private contractors, in other than *de*

minimis situations, is in the best interest of the public. Accordingly, procedures for the award, extension or renewal of a contract or agreement should include the following:

1. Prior to the initial award, periodically during the term of a multi-year contract, and prior to any extension or renewal of the contract, an analysis should be performed to determine whether the cost saving or benefit to the State is sufficiently substantial to justify the privatization of the services. Such analysis should be reviewed and approved by an independent government office.
2. Following the conclusion of a contract, its extension or its renewal, an analysis should be performed to assess the cost-effectiveness or benefit of the outsourcing program. The audit report should be prepared by a qualified internal auditor and should be reviewed by an independent government office.
3. State employees who participate in the procurement process, including evaluation committees utilized in deciding the award of contracts, should have no involvement in the administration of the contracts.
4. Upon the award, extension or renewal of a contract, State employees involved in these processes should sign an attestation, under penalty of perjury, that he or she has not received anything of value, either directly or indirectly, from anyone representing or associated with the vendor.
5. Where a contract is extended or renewed with the same vendor, employees of the vendor in management or supervisory positions should attest, in writing, to compliance with the standards governing conflicts of interest for State vendors. The attestation, under penalty of perjury, should include a statement that the person did not offer or give any State employee, directly or indirectly, anything of value, has no knowledge of such conduct by another employee of the vendor, and has received no solicitation by any State employee for anything of value.
6. Where contracts permit the government agency to assign additional work to the vendor, a comparative analysis should be performed to ensure that the lowest priced and responsible contractor is obtained.

6. *STRENGTHEN THE NEW JERSEY CONFLICTS OF INTEREST LAW*

The existence of the New Jersey Conflicts of Interest Law and a departmental Code of Ethics did not prevent the extensive and routine gifting and entertaining of State officials and employees in this matter. Also highlighted is the fact that two high-ranking officials, who had involvement in the administration of the Payco/OSI contracts, accepted employment with OSI. Accordingly, the Commission urges the following additional safeguards and renews its call for measures to place controls on the revolving door between government and the private sector:

1. At the beginning of each year, every State employee should acknowledge, in writing, that he or she possesses a copy of the Code of Ethics and understands its provisions, has not violated its provisions, and knows of no violation of them.
2. At the conclusion of each year, every State employee and official, who had substantial responsibilities in administering a contract with a vendor, should complete a form attesting, under penalty of perjury, to the fact that he or she neither accepted nor was offered anything of value by a vendor's representative.
3. State employees, who have had substantial contact with a vendor, should be barred from seeking or taking employment with such vendor for a period of at least two years.