



# STATE OF NORTH CAROLINA

**PERFORMANCE AUDIT**

**STATE AGENCY USE OF  
TEMPORARY STAFFING VENDORS**

**JANUARY 2009**

**OFFICE OF THE STATE AUDITOR**

**LESLIE W. MERRITT, JR., CPA, CFP**

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January 6, 2009

The Honorable Michael F. Easley, Governor  
Members of the North Carolina General Assembly  
Mr. Dempsey Benton, Secretary, Department of Health and Human Services  
Honorable Richard Moore, State Treasurer, Department of the State Treasurer  
Mr. Gordon Myers, Executive Director, Wildlife Resources Commission  
Mr. Lyndo Tippet, Secretary, Department of Transportation  
Mr. George Bakolia, State Chief Information Officer,  
Office of Information Technology Services

Ladies and Gentlemen:

We are pleased to submit this performance audit titled *State Agency Use of Temporary Staffing Vendors*. The audit objectives were to determine if state agencies pay too much for commercial temporary staffing services, if state agencies manage the general business and legal risks associated with temporary staffing arrangements, and if retirees returning to work for the State through temporary staffing vendors complied with return-to-work laws. Each of the engaged agency heads listed above reviewed a draft copy of this report. Their written comments are included in the appendix.

The State Auditor initiated this audit to identify cost-savings and mitigate business risks.

We wish to express our appreciation to the staff of the Office of Information Technology Services, the Department of Health and Human Services, the Department of the State Treasurer, the Wildlife Resource Commission, and the Department of Transportation for the courtesy, cooperation, and assistance provided us during the audit.

Respectfully submitted,

A handwritten signature in cursive script that reads "Leslie Merritt".

Leslie W. Merritt, Jr., CPA, CFP  
State Auditor

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# **PERFORMANCE AUDIT**

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## **SUMMARY**

### **PURPOSE**

The purpose of our audit was to determine if state agencies pay too much for commercial temporary staffing services, if state agencies manage business and legal risks of temporary staffing arrangements, and if retirees returning to work for the State through temporary staffing vendors comply with return-to-work laws. This audit report contains recommendations so that agency managers and state oversight agencies can take appropriate corrective action.

### **RESULTS**

State agencies are paying too much for temporary staffing services. In general, state agencies are not using open and competitive bidding practices when seeking temporary staffing services from vendors. By using an open and competitive bidding process to control the administrative mark-up rate, the five state agencies<sup>1</sup> audited could have saved approximately \$3.5 million in administrative costs between July 1, 2005, and January 31, 2008.

State agencies do not manage temporary staffing arrangements in ways that minimize the business and legal risks associated with those services. The lack of written contracts between state agencies and temporary staffing vendors and the nature of some working arrangements increase the risk of dispute, litigation, and liability to the State.

Retirees returning to work for the State through temporary staffing vendors are sometimes out of compliance with the State's return-to-work laws. Unknowingly, the Retirement Systems Division paid approximately \$633,000 in retirement payments to 27 retirees who were out of compliance with the State's return-to-work laws.

### **RECOMMENDATIONS**

State agencies should use open competition and competitive pricing in order to control costs when seeking temporary staffing services. Procurement managers should coordinate with area managers to estimate temporary staffing usage and needs and solicit bid proposals that include hourly wage ranges and administrative mark-up rates.

State agencies should use written contracts to clarify terms, conditions, and responsibilities when procuring temporary staffing services. These contracts should be reviewed by legal counsel experienced in employment law in order to minimize the unique business and legal risks associated with temporary staffing services. Upper level managers should evaluate their agencies use of temporary staffing workers and develop appropriate guidance, training, and policy in order to minimize the risk of legal challenges.

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<sup>1</sup> See the objective, scope, and methodology section of this report for an explanation of how the state agencies and temporary staffing vendors in this audit were selected.

## **PERFORMANCE AUDIT**

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State agencies need to develop and structure temporary staffing arrangements so that the risks associated with violations of return-to-work laws are minimized. Contracts with the temporary staffing vendors should have terms and conditions that require temporary staffing vendors to screen for state retirees and report assignments to state agencies. The Retirement Systems Division should determine if ineligible retirement benefits were paid that should be recovered.

The Office of State Personnel and the Attorney General's Office should collaborate to educate state agency managers about areas of risk and appropriate methods to manage temporary staffing workers.

To increase efficiency for all state agencies, subject matter experts from the Division of Purchase and Contract, the Office of Information Technology Services, the Office of State Personnel, the Retirement Systems Division, and the Attorney General's Office should collaborate with a group of managers from key state agencies to establish statewide convenience contracts or other statewide contracting methods for temporary staffing services. The outcome of the work group should be a system or program that enables state agency managers to use the State's collective buying power to keep temporary staffing wage and administrative costs competitive while providing the speed and flexibility needed by agency managers to quickly fill unexpected and critical vacancies on a temporary basis. This work group should focus initial efforts on general temporary staffing categories and progress to more specialized categories as feasible or needed.

Though leaders of these central service agencies may act on this recommendation on their own, the General Assembly or Governor should assign responsibility for this project to the Division of Purchase and Contract and direct other agencies to contribute subject matter expertise to ensure that an effective statewide solution for general temporary staffing needs is developed in a timely manner.

### **AGENCY'S RESPONSE**

The Agency's responses are included in the appendix.

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## **INTRODUCTION**

### **BACKGROUND**

Managers of state agencies use the services of temporary staffing vendors to meet agency and program needs that can not be met by the existing workforce. The need for temporary workers can arise from a variety of reasons, ranging from an unexpected and extended absence of a critical employee, a planned strategy for meeting agency service level requirements, or acquiring the services of subject matter experts.

State agency managers can obtain temporary staffing services through a State administered program or through commercial temporary staffing vendors. The Office of State Personnel administers a temporary staffing program known as Temporary Solutions. The program maintains a pool of temporary workers of various job classifications that are available to fill temporary needs at state agencies. Temporary Solutions imposes restrictions on the duration of full-time employment and limits the number of hours for workers that are retired from the State. State agencies are not required to use Temporary Solutions and may seek the services of commercial temporary staffing vendors to meet temporary staffing needs.

This audit focused on approximately \$28 million in temporary staffing services purchased from eight commercial vendors by five state agencies (*see chart 1*).

### **OBJECTIVES, SCOPE, AND METHODOLOGY**

The audit objectives were to determine if state agencies pay too much for commercial temporary staffing services, if state agencies manage the business and legal risks of temporary staffing arrangements, and if retirees returning to work for the State comply with the State's return-to-work laws.

The State Auditor initiated this audit to identify cost-savings opportunities and mitigate business risks.

The audit scope included temporary staffing services purchased from eight commercial vendors by five state agencies between July 1, 2005, and January 31, 2008. We conducted the fieldwork for this audit from March 2008 to August 2008.

Four of the temporary staffing vendors were identified during 2007 Single Audit work at the Department of Health and Human Services Division of Medical Assistance (DMA). Office of the State Auditor financial auditors found that DMA procured personal consulting services totaling \$2.5 million from four temporary employment service agencies without entering into formal contractual agreements.

Performance auditors searched the accounting records of all state agencies that use the North Carolina Accounting System (NCAS) for the period of July 1, 2005, to January 31, 2008, for payment activity associated with the four temporary staffing vendors and noted four additional temporary staffing vendors that received significant payments. Based on the level of payments made to the eight vendors, the Department of Health and Human Services, the

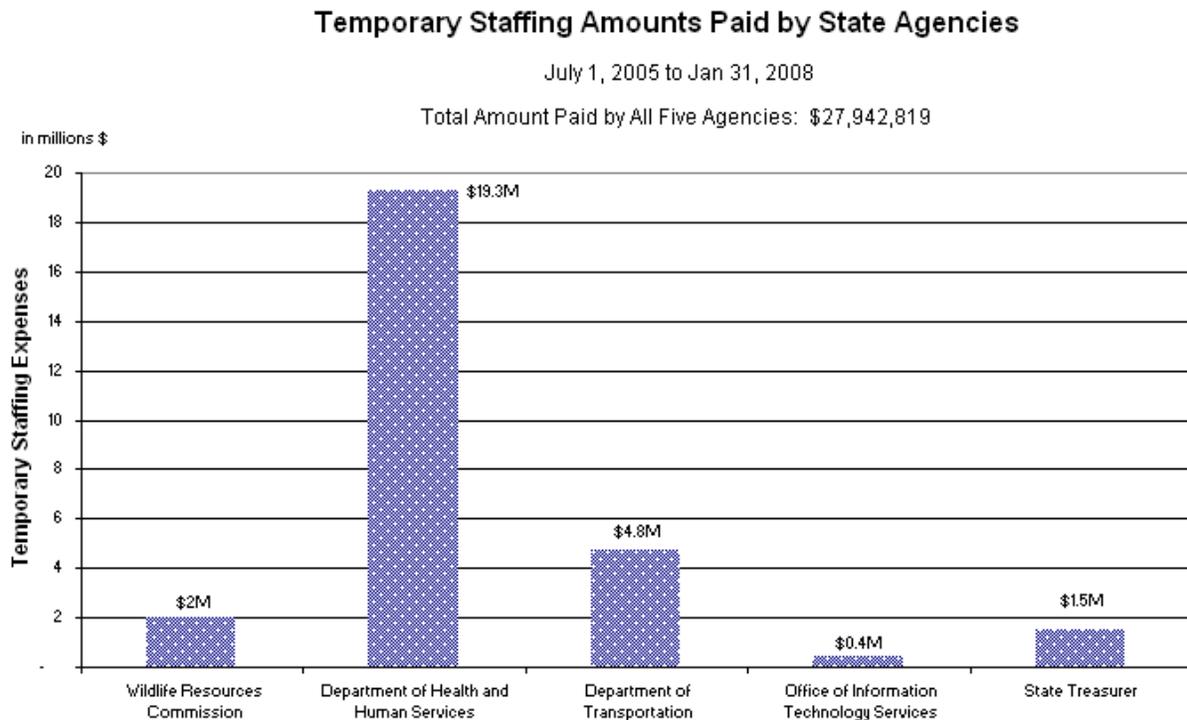
## PERFORMANCE AUDIT

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Wildlife Resources Commission, the Department of State Treasurer, and the Office of Information Technology Services were included in this audit.

The Department of Transportation (DOT) does not use NCAS for its financial accounting system. Auditors asked DOT to provide electronic transactions of any payment activity with the same eight vendors during the same period. Based on the level of activity reported, DOT was added to the list of agencies for this audit. In total, the five state agencies paid approximately \$28 million to the eight vendors between July 1, 2005, and January 31, 2008 (see chart 1).

*Chart 1 shows temporary staffing expenses, by agency, paid to the eight temporary staffing vendors.*



source: NCAS, SAP and vendor supplied data

To determine if state agencies pay too much for temporary staffing services purchased from commercial vendors, we identified State purchasing regulations designed to foster open competition and competitive bidding. We then met with agency managers to determine how temporary staffing services are obtained at the individual agencies and compared those processes to State regulations. We confirmed the number of contracts awarded to the eight vendors with officials from the Division of Purchase and Contract and the Office of Information Technology Services, as well as agency managers. We reviewed details of worker assignments, wages paid to individuals, and total billings from the eight vendors for the period of July 1, 2005, to January 31, 2008. To determine the completeness of the vendor data, we compared summary billing data to agency transactions. We then made calculations

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to determine the administrative mark-up rate<sup>2</sup> charged by each vendor, noting the lowest administrative rate paid. We then calculated the amount of administrative cost paid to each vendor and compared that amount to the administrative cost that would have been paid if each vendor had applied the lowest mark-up rate offered by one of the vendors. We conducted telephone interviews with procurement managers from other states to determine other methods for purchasing temporary staffing services.

To determine if state agencies manage general business and legal risks, we conducted research to ascertain the business and legal risks associated with temporary and contingent workers and management best practices to minimize those risks. We met with agency managers to determine how temporary workers are assigned and used within the agency and to determine if written contracts are used for temporary staffing services. We collected information about the duties and length of service for a selection of temporary staffing workers. We also verified with two vendors our understanding of how a specific category of temporary worker is identified and assigned to state agencies. We consulted an official with the Department of Insurance to understand the risks with this distinct category of temporary worker. We analyzed agency practices and compared them to documented risks and best practices.

To determine if retirees returning to work for the State comply with return-to-work laws, we reviewed the State's return-to-work laws and Retirement Systems Division (RSD) guidance for return-to-work situations. We met with RSD officials to confirm applicability of return-to-work laws with temporary staffing assignments at state agencies. We then compared the vendors' listing of temporary workers assigned to the five state agencies to the RSD database of retirees receiving retirement benefits. We compared the RSD date of retirement and 2006 and 2007 earnings limitation to the vendor supplied employment and earnings history for each retiree that returned to work for the State. We then applied return-to-work laws to specific situations to determine the amount of ineligible retirement benefits received.

Because of the test nature and other inherent limitations of an audit, together with limitations of any system of internal and management controls, this audit would not necessarily disclose all instances of performance weaknesses or lack of compliance.

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

We conducted this audit under the authority vested in the State Auditor of North Carolina by *North Carolina General Statute 147-64*.

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<sup>2</sup> The administrative mark-up rate is the percent of cost (e.g. employment taxes, benefits, overhead, and profit) that exceeds the wages paid to workers.

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## FINDINGS AND RECOMMENDATIONS

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### 1. STATE AGENCIES PAY TOO MUCH FOR TEMPORARY STAFFING SERVICES

State agencies are paying too much for temporary staffing services. In general, state agencies are not using open and competitive bidding practices when seeking temporary staffing services from vendors. By using an open and competitive bidding process to control the administrative mark-up rate, the five state agencies<sup>3</sup> audited could have saved approximately \$3.5 million in administrative costs between July 1, 2005, and January 31, 2008.

#### **Open Competition and Competitive Bidding is Beneficial**

State agency managers are responsible for carrying out public functions efficiently, economically, and effectively while achieving desired agency and program objectives. In this context, economy refers to the acquisition of resources at the lowest cost while considering the objectives of the government agency or program.

Key tools for acquiring resources economically within the purchasing function of any organization are open competition and competitive bidding by capable vendors. Open competition provides all capable vendors the opportunity to bid on state business. Competitive bidding compels vendors to improve efficiency and lower costs in order to successfully win state business. Without open competition and competitive bidding, state agencies may pay too much for temporary staffing services, and managers may fall short of their fiduciary responsibilities.

The North Carolina Administrative Code (01 NCAC 05B) requires competitive quotes for most purchases over \$5,000. Generally, purchases of goods or services above \$10,000 require competitive bidding proposals to ensure open competition and best overall value to the State. The State Purchasing Officer, who is responsible for adopting procurement rules and administering the State's procurement program, confirmed that temporary staffing services acquired from commercial vendors are subject to competitive bidding regulations.

The purchase of information technology (IT) oriented services are regulated separately (09 NCAC 06B), but still require the elements of open competition and competitive bidding. The Office of Information Technology Services (ITS) is responsible for establishing rules for IT procurement. ITS established an IT procurement program for state government and preapproved numerous vendors to competitively bid on state agencies' IT temporary staffing needs through statewide convenience contracts.

#### **Lack of Competitive Bidding**

Approximately \$18.25 million, or 65%, of the \$28 million spent by the five state agencies on commercial temporary staffing services was expended outside of competitive bidding regulations.

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<sup>3</sup> See the objective, scope, and methodology section of this report for an explanation of how the state agencies and temporary staffing vendors in this audit were selected.

## FINDINGS AND RECOMMENDATIONS

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Each of the five state agencies audited has its own process for obtaining non-IT temporary staffing services. The processes include formal contracts and guidelines for medical service contracts at the Department of Health and Human Services (DHHS) and formal contracts for rail station workers at the Department of Transportation. Most often, agencies use informal agreements for temporary staffing situations. It is common practice for area managers to simply contact one or two temporary staffing vendors successfully used in the past to obtain needed temporary staffing services. When multiple vendors are contacted, the decision to use one vendor over another may be influenced by availability of workers, quality of candidates, and total cost. Managers could not, however, provide documentation to support their decisions.

Agency managers should use competitive bidding because even a single temporary staffing assignment can exceed competitive bidding thresholds in a relatively short period. At a rate of \$20 per hour, the estimated cost of a single full-time assignment would exceed \$10,000 in three months<sup>4</sup>. When multiple temporary staffing workers are used, competitive bidding thresholds are surpassed even faster. In fact, 342 (or 6%) of invoices paid for temporary staffing services obtained outside of procurement rules were for amounts over \$10,000. The total of the 342 invoices alone was over \$4.5 million, or 25% of the more than \$18.25 million spent outside competitive bidding rules.

The combined temporary staffing expenses within an agency or division is large enough that managers should recognize their fiduciary responsibility to seek open competition and competitive bidding even if the anticipated cost of a particular temporary staffing need does not exceed the competitive bidding threshold. For example, the DHHS Division of Central Administration and the Division of Medical Assistance paid invoices totaling \$1,256,002 and \$464,127, respectively, to the same temporary staffing vendor during the fiscal year ending June 30, 2006. Similarly, sections within the State Treasurer and Wildlife Resources Commission paid invoices totaling \$458,360 and \$507,472, respectively, to two separate temporary vendors during the fiscal year ending June 30, 2007. Clearly, this level of activity would benefit from open competition and competitive bidding. Nevertheless, the Division of Purchase and Contract and ITS, the two agencies that oversee the bidding for larger (\$25,000 and up) contracts have no record of contracts awarded to seven of the eight vendors<sup>5</sup>.

### **Paying Too Much**

The five state agencies do not negotiate for a lower administrative mark-up rate (the cost above the wages paid to the individual) in any temporary staffing situations. By using an open and competitive bidding process to control the administrative mark-up rate, the five state agencies could have reduced costs.

The rate charged for each individual worker is comprised of two components, the amount paid to the worker (i.e. the individual's gross hourly pay) and the administrative mark-up rate charged by the temporary staffing vendor. The administrative mark-up rate covers

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<sup>4</sup> \$20 x 168 hours a month (21 work days) x 3 months = \$10,080

<sup>5</sup> The eighth vendor provided primarily temporary staffing services to all five agencies through an ITS statewide convenience contract.

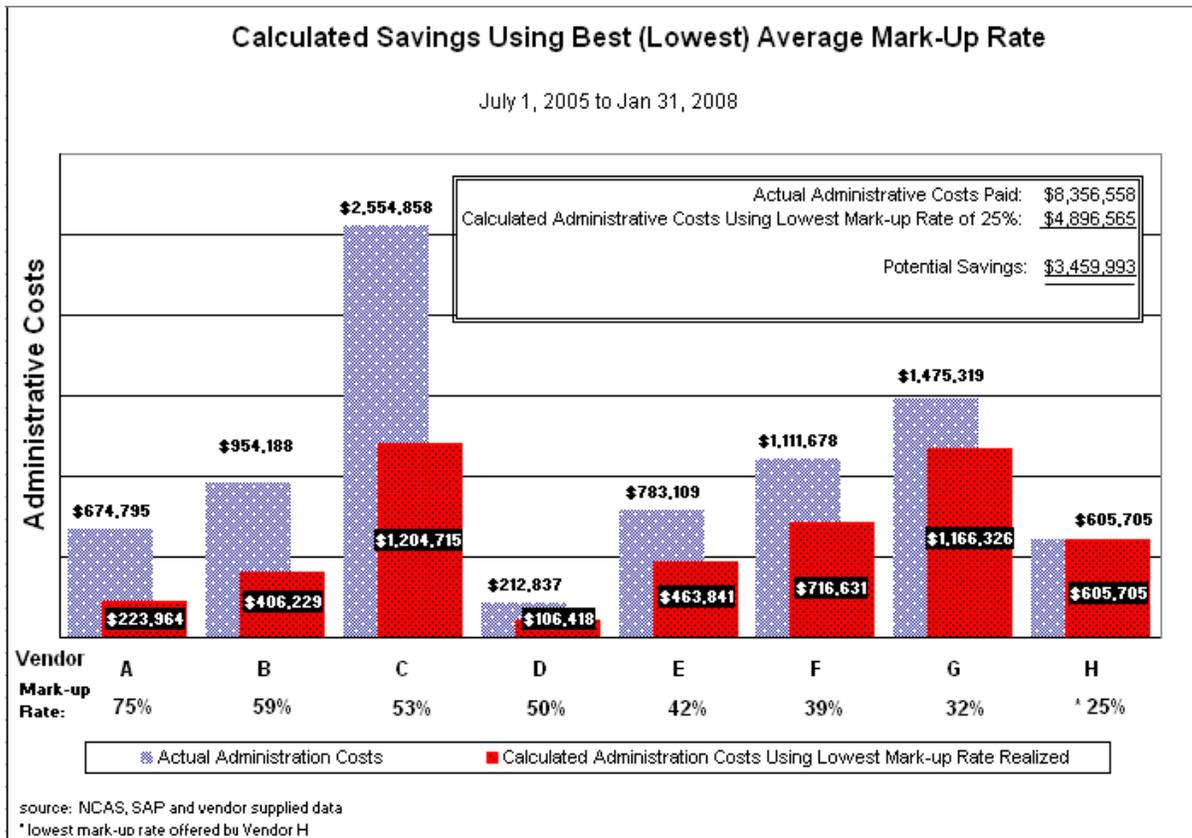
## FINDINGS AND RECOMMENDATIONS

direct and indirect costs (e.g. taxes, employee benefits, and overhead) as well as the vendor’s profit margin. The administrative mark-up rate often varies with each temporary staffing agency, class of worker, assignment, and individual. Though part of the total cost, the mark-up rate is not generally known by the state agency.

Based on details provided by the eight vendors, the average mark-up rate charged by each commercial vendor ranged from 25% to 75%. One temporary staffing vendor reported mark-up rates for individual workers as low as 7% and as high as 116% of the hourly wage amount. Different overhead rates, benefit packages, and profit margins may account for these large variances among vendors and individuals.

The five agencies paid almost \$8.4 million in administrative costs for these services. If the State had used its collective buying power and obtained the lowest average mark-up rate charged by a vendor (25%), almost \$3.5 million would have been saved at the five state agencies between July 1, 2005, and January 31, 2008 (see chart 2).

*Chart 2 compares the actual administrative costs and average mark-up rates by vendor to the calculated administrative costs using the lowest mark-up rate noted.*



It is reasonable to conclude that the potential savings is even higher than amounts noted above. This audit focused on billings for eight temporary staffing vendors providing services at five state agencies. While reviewing invoices at DHHS, auditors noticed invoices from 45 other vendors that appeared to be for temporary staffing type services.

## **FINDINGS AND RECOMMENDATIONS**

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### **Why State Agencies Do Not Seek Open and Competitive Bidding**

State agency managers stated that they do not routinely use open competition and competitive bidding for temporary staffing services because it is not clear that seeking competitive proposals is a requirement. Although implicit, neither the Administrative Code nor the Division of Purchase and Contracts (P&C) Purchasing Manual specifically addresses competitive bidding requirements or exceptions for services provided by temporary staffing vendors. Furthermore, the same regulations state that competitive bidding requirements do not apply to “employment contracts” and allow an exemption of competitive bidding requirements for “personal services.” Given the nature of the desired service – staff capable of performing certain skill sets – it is understandable that managers might confuse temporary staffing arrangements with employment contracts or personal services. Adding clarity to applicable regulations and providing guidance would reduce confusion. P&C developed draft wording meant to clarify this issue, but the draft wording has not been officially adopted or codified in the Administrative Code. P&C periodically conducts compliance reviews of agency purchasing practices, however, the fact that temporary staffing services were not awarded through a competitive bidding process was not identified as a compliance issue during the most recent review at any of the five agencies. This may reinforce the misconception that temporary staffing services are exempt from competitive bidding requirements.

Another reason why state agency managers do not use open competition and competitive bidding for non-IT temporary services is because it would take too long. Managers faced with timelines and program mandates may need to make strategic adjustments to work force levels or replace unanticipated vacancies quickly to ensure that service levels are maintained. Developing a bid proposal for each temporary staffing need and going through an evaluation and award process takes time and is seen as an impediment when compared to the simple process of picking up the phone and getting someone in place within a few days.

While these reasons may explain why state agencies did not seek open competition and competitive bidding for non-IT temporary staffing needs, these reasons do not relieve management of their responsibility to economically manage public funds.

### **Other States Use Collective Buying Practices to Manage Costs**

Other states use their collective buying power to control temporary staffing costs and have implemented statewide processes and contracts to quickly facilitate the acquisition of temporary staffing services.

The Commonwealth of Virginia issued a statewide temporary staffing service request-for-proposal (non-medical and non-IT) and awarded contracts to two vendors. Using their state personnel professionals to assist in determining appropriate hourly wages, these contracts also limit the administrative mark-up rate to between 17% and 23%, depending on the job classification. Virginia procurement officials estimate that the average mark-up rate is around 20%, down from an estimated 30% before the current contracts were awarded. Virginia officials estimate that the Commonwealth saves approximately \$1.7 million a year in administrative costs.

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South Carolina and Oregon use a temporary staffing broker to quickly meet the competitive bidding requirements of their temporary staffing needs, while Maine uses a list of 12 approved temporary staffing vendors that can bid on temporary staffing requests. Texas and Illinois have statewide contracts in place that incorporated open competition and competitive bidding during the award process. Unlike Virginia, none of these temporary staffing procurement methods control the administrative mark-up rate, but they do use the states' collective buying power, open competition, and competitive bidding to control overall costs.

**Recommendation:** State agencies should use open competition and competitive pricing in order to control costs when seeking temporary staffing services. Procurement managers should coordinate with area managers to estimate temporary staffing usage and needs and should solicit bid proposals that include hourly wage ranges and administrative mark-up rates for needed positions.

Contracting, personnel, and employment law experts from the Division of Purchase and Contract, the Office of Information Technology Services, the Office of State Personnel, and the Attorney General's Office should collaborate with a group of managers from key state agencies to establish statewide convenience contracts or other statewide contracting methods for temporary staffing services. The outcome should be a system or program that enables state agency managers to use the State's collective buying power to keep temporary staffing wage and administrative costs in check while providing the speed and flexibility needed by agency managers to quickly fill unexpected and critical vacancies on a temporary basis. This work group should focus initial efforts on general temporary staffing categories and progress to more specialized categories as feasible or needed.

Though leaders of these central service agencies may act on this recommendation on their own, the General Assembly or Governor should assign responsibility for this project to the Division of Purchase and Contract and direct other agencies to contribute subject matter expertise to ensure that an effective statewide solution for general temporary staffing needs is developed in a timely manner.

### **2. BUSINESS AND LEGAL RISKS ARE NOT WELL MANAGED**

State agencies do not manage temporary staffing arrangements in ways that minimize the business and legal risks associated with those services. The lack of written contracts between state agencies and temporary staffing vendors and the nature of some working arrangements increase the risk of dispute, litigation, and liability to the State.

#### **Understanding and Managing Business and Legal Risks**

Managers are responsible for understanding and minimizing business and legal risks associated with administering their programs. Whether and how to contract for temporary staffing services is a management business decision, with unique legal implications and risks. A prudent manager should be aware of these business and legal risks and take measures to mitigate them.

## FINDINGS AND RECOMMENDATIONS

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Temporary staffing arrangements introduce a variety of unique business and legal risks to the state agency requesting services. Two examples of these risks include the risk that a vendor fails to withhold or pay employment taxes and the risk that temporary workers will sue for state benefits. If realized, these situations could create a significant financial liability for the State.

Temporary staffing services obtained from a category of vendors known as a Payroll Service Provider (PSP) or a Professional Employment Organization (PEO) introduce a unique business risk. These third party payer organizations manage the payroll function of the workers, including reporting wages and withholding employment taxes, while the client organization maintains management control over the work. If, however, the PSP or PEO fails to withhold and pay employment taxes, the client organization (i.e. state agency) may be held financially responsible. In 2004, the Internal Revenue Service issued a statement warning client organizations of their potential liability if a PSP or PEO fails to pay the required payroll taxes and cautioned client organizations to exercise due diligence in selecting and monitoring such staffing organizations.<sup>6</sup>

Another risk is that agencies may manage temporary staffing workers like they manage state employees. Agency involvement in items such as interviewing, skill training, and disciplinary action taken against temporary workers can blur the line between temporary staffing and regular employee status. These actions can increase the risk that temporary staffing workers will bring claims against the State for retroactive employment benefits.

The use of written contracts that are reviewed by attorneys experienced in employment law is a prudent first step in managing business and legal risks when contracting for all temporary staffing services. Among other things, written contracts can define the vendor's responsibilities to withhold and pay employment taxes and require the vendor to provide documentation to the client organization regarding the payment of those taxes.

### **Risks Are Not Managed**

State agency managers are not adequately managing business and legal risks associated with the use of temporary staffing workers. Agency managers are entering into PEO type staffing arrangements without taking steps to mitigate the business risks. In addition, some temporary workers are managed in a manner similar to regular state employees, increasing the risk of legal challenges from temporary staffing workers that assert they are entitled to State benefits.

In some instances, state agency managers know or identify the individual they want to fill a particular temporary staffing need and direct the person to a predetermined temporary staffing vendor so that the person can be assigned back to the state agency. Of the 525 individuals provided by two of the vendors,<sup>7</sup> 144 (27%) were assigned in this manner. According to the PEO Administrator at the Department of Insurance,<sup>8</sup> the nature of the temporary staffing arrangements mentioned above are PEO staffing arrangements and introduce the risk that the state agency will be liable for the vendors' failure to

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<sup>6</sup> IRS Information Release 2004-47 (April 5, 2004)

<sup>7</sup> The other six vendors did not supply this level of detail about the workers' classification.

<sup>8</sup> In North Carolina, the Department of Insurance regulates the PEO industry.

## FINDINGS AND RECOMMENDATIONS

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withhold and pay employment taxes. State agencies, however, are not managing this risk. More than \$18 million (65%) of the approximately \$28 million expended between July 1, 2005, and January 31, 2008, lacked contracts specifically written for temporary staffing services. In these cases, vendor responsibilities like withholding and paying employment taxes, were left to verbal agreements, if discussed at all.

In other situations, the working relationship between the state agency and the temporary worker resembles more of a traditional employer and employee relationship than a temporary staffing assignment and could lead to legal challenges if the workers believe they are entitled to State benefits. At least one vendor requires individuals who were identified and referred by the state agency to sign an agreement stating that they have been selected by the client (i.e. state agency). The agreement goes on to say that since they were not recruited by the vendor, the worker will not be supervised or managed by the vendor, nor will the worker be reassigned to another client unless they apply and are accepted for employment by the vendor.

Some temporary staffing workers have been in place at a single state agency for multiple years – some as long as five years – and fundamentally perform the same job and receive the same oversight as the state employees they work beside. In these instances, agency managers appear to use temporary staffing workers as a method to work around restrictions on the number of authorized positions or the eleven month time restriction that comes with state-employed full time temporary workers. Managers at two agencies stated that they requested permanent positions to meet their existing workload but that their request for positions was denied.

Though difficult to quantify, the potential liability associated with legal challenges that could arise from these non-managed risks is significant.

**Recommendation:** State agencies should use written contracts to clarify terms, conditions, and responsibilities when procuring temporary staffing services. These contracts should be reviewed by legal counsel experienced in employment law in order to minimize the business and legal risks associated with temporary staffing services.

Upper level managers should determine and evaluate their agency's use of temporary staffing workers and develop appropriate guidance, training, and policy in order to minimize the risk of legal challenges.

To facilitate this process for all state agencies, the Office of State Personnel, the Division of Purchase and Contract, the Office of Information Technology Services and Contract and the Attorney General's Office should work with key state agencies to formulate a contract template that can be used by individual state agencies. The Office of State Personnel and the Attorney General's Office should collaborate to educate state agency managers about areas of risk and appropriate methods to manage temporary staffing workers.

Though leaders of these central service agencies may act on this recommendation on their own, the General Assembly or Governor should assign responsibility of this project to the

## FINDINGS AND RECOMMENDATIONS

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Division of Purchase and Contract and direct other agencies to contribute subject matter expertise.

### 3. RETIREES DO NOT COMPLY WITH RETURN-TO-WORK LAWS

This audit identified retirees returning to work for the State through temporary staffing vendors that are out of compliance with the State's return-to-work laws. Unknowingly, the Retirement Systems Division paid approximately \$633,000 in retirement payments to 27 retirees who were out of compliance with the State's return-to-work laws.

#### Return-to-Work Laws

State laws put certain limits on state retirees returning to work for the State. The intent of the limits is to keep the State's pension funds in compliance with Internal Revenue Service (IRS) regulations and to help protect the funds' financial stability.

*General Statute 135-3(8)c.* applies to the Teachers and State Employees Retirement System (TSERS) and states that retirees who are, "reemployed by, or otherwise engaged to perform services for, an employer participating in the Retirement System on a part-time, interim, temporary, or fee-for-service basis, whether contractual or otherwise ..."

- Must not exceed their annual earnings limit, which is the greater of 50% of pre-retirement earnings, indexed, or a statutory minimum, indexed annually. The earnings restriction applies for the first 12 months immediately following retirement and for each calendar year following the year of retirement;<sup>9</sup>
- Must have a six-month separation from the date of retirement;
- Must have no intent or agreement, express or implied, to return to service.

The law specifies that state retirees violating these regulations are not eligible for retirement benefits and must repay any ineligible retirement benefits received.

Return-to-work laws apply to retirees who work directly for the State as well as those who return through a temporary staffing agency. The 2007 and 2008 editions of the *TSERS Your Retirement Benefits* handbook states that retirees are subject to reemployment provisions based on the nature of the particular work they perform for a state agency that participates in TSERS, "regardless of their technical employment status (which may include being assigned to work for a covered employer by a private company such as a temporary agency)."

Retirement Systems Division officials confirmed that state retirees, working through a temporary staffing vendor and assigned to a state agency that participates in TSERS, meet the technical definition of returning to work for the State and are subject to those return-to-work limitations. The same officials also confirmed that retirees who comply with all return-to-work laws are fully eligible to return-to-work with no consequences to their retirement benefits.

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<sup>9</sup> An annual earnings cap exemption exists for K-12 classroom teachers.

## FINDINGS AND RECOMMENDATIONS

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### **Retirees Out of Compliance**

State agencies do not manage temporary staffing arrangements to mitigate the risk that retirees returning to work for the State violate return-to-work laws. As a result, the Retirement Systems Division is unknowingly making benefit payments to ineligible members.

In total, 27 (38%) of the 72 retirees<sup>10</sup> that returned to work for the State through one of the eight temporary staffing vendors were out of compliance with return-to-work laws and received approximately \$633,000 in ineligible retirement benefits. Twenty-three of the 72 (32%) retirees exceeded their earnings limitations in 2006 or 2007, while five (7%) returned to work within six months of their official retirement date.<sup>11</sup> Individual earnings exceeded limits by as little as 9% and as much as 194%.

Agency managers likely knew that some of the temporary staffing workers were state retirees. Forty two (58%) of the 72 retirees were identified and referred to the temporary staffing vendor by the state agency for a specific staffing need. Twenty-five of these individuals (65%) worked as a temporary staffing worker at the same state agency and division from which they retired.

### **Potential Impact**

Based on the 2005 Retirement Systems Division report<sup>12</sup> to the General Assembly, retirees returning to work and exceeding their earnings limits, without a sufficient break in service after retirement, or via a pre-arranged reemployment arrangement, jeopardize the tax-exempt status of the State's retirement plan. The report recommended that all return-to-work policies and laws be in compliance with IRS regulations. The report noted that losing the tax-exempt status would subject all of the pension fund's income sources (employer contributions, member contributions, and investment earnings) to federal taxes. Such an outcome would be financially devastating to state employees, the pension fund, and state government.

The report also identified a risk that the state pension fund could experience increased financial pressure if employees were incented to retire earlier than projected in anticipation of receiving retirement benefits and state wages in excess of their earnings limits. The report noted a similar change in behavior starting in 1999 when the earnings limitation was removed for teachers returning to work in K-12 classrooms.

These risks may be realized if state workers and agency managers believe that returning to work for the State through a temporary staffing vendor is an undetectable or even legitimate method to double dip (receive retirement benefits from the same entity where they work). State workers may be incented to retire earlier than they would otherwise, creating unanticipated and unfunded financial pressure on the State's pension funds. If

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<sup>10</sup> In total, the eight vendors provided 968 temporary workers to the five state agencies from July 2005 through January 2008, however, only 72 of these individuals were retired state employees.

<sup>11</sup> The six month separation requirement went into effect on October 31, 2005.

<sup>12</sup> North Carolina Department of State Treasurer Retirement Systems Division Report to the General Assembly – [Evaluation of North Carolina's Policy Governing State Retirees Returning to Service](#) – February 2005.

## FINDINGS AND RECOMMENDATIONS

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this practice was to become prevalent, the financial pressure on pension funds and risk of IRS scrutiny would increase significantly.

Noncompliance with return-to-work laws places individuals and state agencies at risk. If the Retirement Systems Division (RSD) determines that these 27 individuals violated the State's return-to-work laws and were not eligible to receive the \$633,000 in retirement benefits, the RSD may attempt to recover ineligible benefits directly from the individuals. If the retirees believe that state agency managers encouraged them to return-to-work or were advised that the return-to-work rules do not apply, it is possible that the retirees may contest their liability and initiate legal action against the state agency.

It is reasonable to think that the total impact of ineligible retirement benefits is greater than the amount noted. We reviewed activity for eight temporary staffing vendors at five state agencies. While reviewing invoices at the Department of Health and Human Services, we noticed invoices from 45 other vendors that appeared to be for temporary staffing services. Furthermore, we reviewed return-to-work limits only for calendar years 2006 and 2007. Temporary staffing vendors reported that 39 (54%) of the 72 retirees that returned to work for the State did so prior to calendar year 2006.

### **Potential Reasons for Non-Compliance**

Most likely, retirees and state agency managers may not understand that returning to work through a temporary staffing vendor constitutes a true return-to-work condition that invokes certain limitations. Before 2007, this area was not as clearly defined in reference materials commonly available to state workers and retirees. Therefore, retirees and agency managers may have incorrectly believed that returning to work through temporary staffing vendors was an acceptable 'work around' of return-to-work laws. This misconception may have led to a culture that fosters both retirees and agency management to disregard the return-to-work laws, and unknowingly put the State at financial risk.

However, due to minimal risk of detection, some retirees may knowingly violate return-to-work rules in order to improve their own economic situation. The risk of detection is minimal because RSD has no data on retirees who return to work at state agencies through arrangements with temporary staffing vendors. Consequently, the RSD relies on retirees who return to work for the State in that fashion to self-monitor compliance with return-to-work laws.

**Recommendation:** State agencies need to develop and structure temporary staffing arrangements so that the risks associated with violations of return-to-work laws are minimized. Contracts with the temporary staffing vendors should have terms and conditions that require temporary staffing vendors to screen for state retirees and report assignments to state agencies.

The Retirement Systems Division needs to strengthen efforts to alert state agency managers and state retirees that return-to-work laws and limits apply to retirees rehired through temporary staffing vendors. This communication effort should highlight the risks to the pension plan and the consequences of noncompliance for both retirees and the

## FINDINGS AND RECOMMENDATIONS

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State. The RSD should also identify and allocate sufficient resources to its enforcement function and determine if ineligible retirement benefits were paid that should be recovered.

Due to the potential impact to the pension funds, it is imperative that the Retirement Systems Division participate in the planning and implementation of the previously recommended statewide temporary staffing procurement program.

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## APPENDIX

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### North Carolina Department of Health and Human Services

2001 Mail Service Center • Raleigh, North Carolina 27699-2001  
Tel 919-733-4534 • Fax 919-715-4645

Michael F. Easley, Governor

Dempsey Benton, Secretary

December 22, 2008

Honorable Leslie Merritt, Jr., CPA, CFE  
Office of the State Auditor  
2 S. Salisbury Street  
20601 Mail Service Center  
Raleigh, NC 27699-0601

Dear Mr. Merritt:

Thank you for the opportunity to respond to the draft performance audit report on select State Agency Use of Temporary Staffing Vendors. Temporary staffing plays an important role in department operations. Temps are used for a variety of reasons such as employee vacancies due to sick leave, maternity leave, disability, subject matter experts and special projects that can not be covered with existing personnel resources. In DHHS, temporary staffing represents approximately 1% of personnel expenditures.

The DHHS response follows each of the audit findings in the narrative below.

#### AUDIT SUMMARY RECOMMENDATION

State agencies should use open competition and competitive pricing in order to control costs when seeking temporary staffing services. Procurement managers should coordinate with area managers to estimate temporary staffing usage and needs and solicit bid proposals that include hourly wage ranges and administrative mark-up rates.

State agencies should use written contracts to clarify terms, conditions, and responsibilities when procuring temporary staffing services. These contracts should be reviewed by legal counsel experienced in employment law in order to minimize the unique business and legal risks associated with temporary staffing services. Upper level managers should evaluate their agencies use of temporary staffing workers and develop appropriate guidance, training, and policy in order to minimize the risk of legal challenges.

State agencies need to develop and structure temporary staffing arrangements so that the risks associated with violations of return-to-work laws are minimized. Contracts with the temporary staffing vendors should have terms and conditions that require temporary staffing vendors to screen for state retirees and report assignments to state agencies. The



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Retirement Systems Division should determine if ineligible retirement benefits were paid that should be recovered.

The Office of State Personnel and the Attorney General's Office should collaborate to educate state agency managers about areas of risk and appropriate methods to manage temporary staffing workers.

To increase efficiency for all state agencies, subject matter experts from the Division of Purchase and Contract, the Office of Information Technology Services, the Office of State Personnel, the Retirement Systems Division, and the Attorney General's Office should collaborate with a group of managers from key state agencies to establish statewide convenience contracts or other statewide contracting methods for temporary staffing services. The outcome of the work group should be a system or program that enables state agency managers to use the State's collective buying power to keep temporary staffing wage and administrative costs competitive while providing the speed and flexibility needed by agency managers to quickly fill unexpected and critical vacancies on a temporary basis. This work group should focus initial efforts on general temporary staffing categories and progress to more specialized categories as feasible or needed.

Though leaders of these central service agencies may act on this recommendation on their own, the General Assembly or Governor should assign responsibility for this project to the Division of Purchase and Contract and direct other agencies to contribute subject matter expertise to ensure that an effective statewide solution for general temporary staffing needs is developed in a timely manner.

**DHHS Response:** *We concur with the summary recommendation.*

### **Finding 1. State Agencies Pay Too Much For Temporary Staffing Services**

**Audit Recommendation:** State agencies should use written contracts to clarify terms, conditions, and responsibilities when procuring temporary staffing services. These contracts should be reviewed by legal counsel experienced in employment law in order to minimize the business and legal risks associated with temporary staffing services.

Upper level managers should determine and evaluate their agency's use of temporary staffing workers and develop appropriate guidance, training, and policy in order to minimize the risk of legal challenges.

To facilitate this process for all state agencies, the Office of State Personnel, the Division of Purchase and Contract, the Office of Information Technology Services and Contract and the Attorney General's Office should work with key state agencies to formulate a

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Honorable Leslie Merritt, Jr., CPA, CFE  
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contract template that can be used by individual state agencies. The Office of State Personnel and the Attorney General's Office should collaborate to educate state agency managers about areas of risk and appropriate methods to manage temporary staffing workers.

Though leaders of these central service agencies may act on this recommendation on their own, the General Assembly or Governor should assign responsibility of this project to the Division of Purchase and Contract and direct other agencies to contribute subject matter expertise.

***DHHS Response:*** *While we agree that there should be significant savings, the method of calculation in the audit report may have been overstated somewhat. As stated in the audit report, administrative charges vary based on the fringe benefit package offered to temporary staff by the temporary employment agency. Virginia's state-wide administrative mark-up rates (17% to 23%) support the fact that administrative rates need to vary based on job classification. Thus, to employ the lowest administrative rate in the savings calculation may be on the optimistic side. Nonetheless, we do believe and agree that savings should accrue from a statewide contract(s).*

### **Finding 2. Business and Legal Risks are not well managed**

**Audit Recommendation:** State agencies need to develop and structure temporary staffing arrangements so that the risks associated with violations of return-to-work laws are minimized. Contracts with the temporary staffing vendors should have terms and conditions that require temporary staffing vendors to screen for state retirees and report assignments to state agencies.

The Retirement Systems Division needs to strengthen efforts to alert state agency managers and state retirees that return-to-work laws and limits apply to retirees rehired through temporary staffing vendors. This communication effort should highlight the risks to the pension plan and the consequences of noncompliance for both retirees and the State. The RSD should also identify and allocate sufficient resources to its enforcement function and determine if ineligible retirement benefits were paid that should be recovered.

Due to the potential impact to the pension funds, it is imperative that the Retirement Systems Division participate in the planning and implementation of the previously recommended statewide temporary staffing procurement program.

***DHHS Response:*** *We concur with the recommendation.*

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### **Finding 3. Retirees do not comply with return-to-work laws**

**Audit Recommendation:** State agencies need to develop and structure temporary staffing arrangements so that the risks associated with violations of return-to-work laws are minimized. Contracts with the temporary staffing vendors should have terms and conditions that require temporary staffing vendors to screen for state retirees and report assignments to state agencies.

The Retirement Systems Division needs to strengthen efforts to alert state agency managers and state retirees that return-to-work laws and limits apply to retirees rehired through temporary staffing vendors. This communication effort should highlight the risks to the pension plan and the consequences of noncompliance for both retirees and the State. The RSD should also identify and allocate sufficient resources to its enforcement function and determine if ineligible retirement benefits were paid that should be recovered.

Due to the potential impact to the pension funds, it is imperative that the Retirement Systems Division participate in the planning and implementation of the previously recommended statewide temporary staffing procurement program.

***DHHS Response:*** *Until recently, the Teachers' & State Employees' Retirement System (TSERS) has advised that retired state employees could exceed their earnings cap per calendar year of approximately 50% of their previous salary, if they worked for a temporary staffing agency other than Temporary Solutions which is operated by the Office of State Personnel, a state agency. DHHS understood this was based on the fact that the primary employer/employee relationship was between the temporary staffing agency and the retired employee.*

*We believe that the evolving return to work policy and the proper communication of that policy should be considered before determining employees to be out of compliance. The evolving nature of the policy can be seen over the years. For example, recent changes in the law and handbooks indicate that there has been confusion over return to work policies. For example, Session Law 2007-431 (HB 777) to make "Technical Corrections..." enacted in July, 2007, changed two prepositions in Section 9. GS 135-3(8) c as follows:*

*"c. Should a beneficiary who retired on an early or service retirement allowance under this Chapter be ~~reemployed~~, reemployed by, or otherwise engaged to perform ~~services~~, by services for, an employer participating in the Retirement Systems on a part-time, temporary, interim, or on a fee-for-service basis, whether contractual or otherwise, and if such beneficiary earns an amount during the 12-month period immediately following the effective date of retirement or in any*

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*calendar year which exceeds fifty percent (50%) of the reported compensation, excluding terminal payments, during the 12 months of service preceding the effective of retirement, or twenty thousand dollars (\$20,000), whichever is greater, as hereinafter indexed, then the retirement allowance shall be suspended as of the first day of the month following the month in which the reemployment earnings exceed the amount above, ....”*

*These minor wording changes may be the basis for the new wording in the 2007 and 2008 TSERS Handbooks (“Your Retirement Benefits”). The 2008 handbook is dated January 1, 2008, but was not made available on the Website until May, 2008. We cannot verify the date the 2007 handbook was made available via the Website (dated January 1, 2007). However, one explanation is that the addition of the following sentence added to the 2007 handbook was validated by the technical correction passed in July 2007:*

*“You will be subject to reemployment provisions based on the nature of the particular work you perform for a covered employer, regardless of your job classification or your technical employment status (which may include being assigned to work for a covered employer by a private company such as a temporary agency.)”*

*On September 29, 2008, (after this audit), the “Recruitment Monitor” sent by email to employers included an attachment, “Understanding the Return-to-Work Laws for Teachers’ and State Employees’ Retirement System.” This represents the most complete explanation of this issue, including the following:*

*“In addition, a retiree who goes back to work for a private entity which then assigned or ‘leases’ that person back to a TSERS employer will be subject to the same return-to-work provisions where such an arrangement is merely a pass-through arrangement or is seen as an attempt to circumvent the applicable return-to-work laws.”*

*Finally, TSERS has not communicated this change to its members or the HR Offices, Business Offices and management who make decisions about hiring retired state employees through private temporary staffing agencies. Retirement counselors who answer the telephones at TSERS are dispensing conflicting advice. Two phone calls made less than 30 minutes apart on Sept. 4, 2008, yielded two different answers: (a) that there is no restriction on the earnings of a retired state employee if they were working for a temporary staffing agency, such as Manpower, and (b) that there is such a restriction. Another caller was told that “as long as the check you received was not a State check, there was no restriction on your earnings.”*

*Thus, it is clear that the policy interpretations have been evolving and that there has been much confusion over the interpretation provided to retirees by the TSERS office. We*

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*believe it is the responsibility of TSERS to communicate clearly to all members a change as major as this with potentially serious implications for many of its retired members and that no recoupments from retirees should be effective until employees are properly and uniformly notified of the current policy.*

DHHS believes that there are opportunities for significant savings in the area of state-wide contracts and looks forward to participating with the Department of Administration and other agencies in formulating a standard request for proposal that will become the basis for state-wide temporary staffing contracts. We will strongly support this initiative to be more efficient in the use of State resources and appreciate your leadership in this area. We are also appreciative of the professional manner in which your staff conducted this performance audit.

Sincerely,



Dempsey Benton

Cc: Dan Stewart  
Kathy Gruer  
Jim Slate

## APPENDIX

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**RICHARD H. MOORE**  
*Treasurer*  
*State of North Carolina*

December 19, 2008

The Honorable Leslie W. Merritt, Jr.  
State Auditor of North Carolina  
20601 Mail Service Center  
Raleigh, NC 27699-0601

Dear Mr. Merritt:

I have received your draft audit report related to State Agency Use of Temporary Staffing Vendors. I appreciate the opportunity to respond to your findings on the use of temporary staffers and the challenges presented in enforcing the State's Return to Work laws.

The Department of State Treasurer utilizes temporary employees to accommodate temporary spikes in workflow, to accommodate long-term needs for which permanent positions have not yet been approved and to fulfill personal services contracts. Our department and all of state government would benefit from a competitive purchasing process to procure the services of a temporary staffing vendor. We would support the use of a statewide contract to create a pool of vendors from which to select for our temporary staffing needs. This process would also assist with the establishment of written contracts to clarify terms, conditions, and responsibilities of the vendor as it relates to the procurement of temporary staffing services.

Your audit also addressed the difficulties associated with retirees returning to work as temporary employees. Please know that the department has increased its efforts to communicate with active and retired employees about the Return to Work statutes and to educate employers about these statutes.

In addition, we will continue to pursue violations of the state statutes when they are reported to us or we discover them in the course of our daily business. Working with the Attorney General's Office, we are carefully reviewing these cases and pursuing reimbursement for the appropriate retirement system. However, implementation of an expanded enforcement program could require additional resources due to the minimal amount of existing staff in the division.

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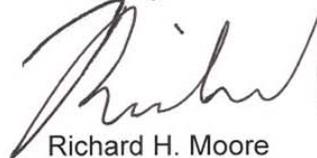
At the department, we will also continue to explore additional options for enforcement and prevention of these violations. At the present time, all penalties for violating state Return to Work statutes fall upon the retiree/employee. The General Assembly may wish to impose penalties on employers who rehire the retirees.

I would like to point out that if a statewide contract list is put in place, those contracts can incorporate some language to assist with the monitoring of return to work rules, for example, requiring the vendor to supply social security numbers to our office. My office is happy to serve on a statewide committee to put this process in place.

Finally, the Retirement Services Division is investigating the names of retired state employees who have returned to work at state agencies and who were forwarded to us by the State Auditor's Office to see if they have done so in violation of current Return to Work statutes. Appropriate action will be taken in each case upon completion of these investigations.

Thank you for the opportunity to respond to this situation, and I do commend your staff for the professional manner in which this audit was conducted.

Sincerely,



Richard H. Moore

RHM/sls

## APPENDIX

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### ☒ North Carolina Wildlife Resources Commission ☒

Gordon S. Myers, Executive Director

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December 11, 2008

The Honorable Leslie W. Merritt, Jr., State Auditor  
Office of the State Auditor  
2 South Salisbury Street  
20601 Mail Service Center  
Raleigh, North Carolina 27699-0601

Dear Mr. Merritt:

Thank you for the opportunity to respond to the findings associated with your draft audit report of the use of commercial temporary staffing services as of November 11, 2008 and for the period July 1, 2005, through January 31, 2008. On behalf of the Wildlife Resources Commission, I want to express our appreciation to you and your staff on this project for the professionalism demonstrated in the conduct of this assessment.

We have reviewed your office's findings and recommendations. Overall, we agree with the findings and conclusions described in the draft audit report. We are pleased with the conclusion stated in your draft audit report that subject matter experts from the Division of Purchase and Contract, the Office of Information Technology Services, the Office of State Personnel, the Retirement Systems Division, and the Attorney General's Office should collaborate with a group of managers from key state agencies to establish statewide convenience contracts or other statewide contracting methods for temporary staffing services.

Should you or your staff require further information, please feel free to contact me or my staff.

Sincerely,

A handwritten signature in black ink, appearing to read "Gordon Myers".

Gordon Myers, Executive Director  
North Carolina Wildlife Resources Commission

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**Mailing Address:** Director's Office • 1701 Mail Service Center • Raleigh, NC 27699-1702  
**Telephone:** (919) 707-0010 • **Fax:** (919) 707-0020

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## APPENDIX

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STATE OF NORTH CAROLINA  
DEPARTMENT OF TRANSPORTATION

MICHAEL F. EASLEY  
GOVERNOR

1501 MAIL SERVICE CENTER, RALEIGH, N.C. 27699-1501

LYNDO TIPPETT  
SECRETARY

December 17, 2008

The Honorable Leslie W. Merritt, Jr.  
State Auditor  
Office of State Auditor  
20601 Mail Service Center  
Raleigh, North Carolina 27699-0601

Dear Auditor Merritt:

Thank you for the opportunity to respond to the Performance Audit of State Agency Use of Temporary Staffing Vendors. I have reviewed the report and offer the following comments:

1. State Agencies Pay Too Much For Temporary Staffing Services

**Recommendation:** *State agencies should use open competition and competitive pricing in order to control costs when seeking temporary staffing services. Procurement managers should coordinate with area managers to estimate temporary staffing usage and needs and should solicit bid proposals that include hourly wage ranges and administrative mark-up rates for needed positions.*

*Contracting, personnel, and employment law experts from the Division of Purchase and Contract, the Office of Information Technology Services, the Office of State Personnel, and the Attorney General's Office should collaborate with a group of managers from key state agencies to establish statewide convenience contracts or other statewide contracting methods for temporary staffing services.*

**Response:** The Department uses low bids to procure services for temporary staffing, but was not aware of the amount of administrative mark-up that the vendors were including in the low bid prices. The Department looks forward to collaborating with other agencies to stipulate in the contracts the maximum amount of administrative mark-up. The cost savings realized from this procedure will be beneficial.

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### 2. Business and Legal Risks are Not Well Managed

**Recommendation:** *State agencies should use written contracts to clarify terms, conditions, and responsibilities when procuring temporary staffing services. These contracts should be reviewed by legal counsel experienced in employment law in order to minimize the business and legal risks associated with temporary staffing services.*

*To facilitate this process for all state agencies, the Office of State Personnel, the Division of Purchase and Contract, the Office of Information Technology Services and Contract and the Attorney General's Office should work with key state agencies to formulate a contract template that can be used by individual state agencies. The Office of State Personnel and the Attorney General's Office should collaborate to educate state agency managers about areas of risk and appropriate methods to manage temporary staffing workers.*

**Response:** The Department concurs with the need for contracts that are written to address the variety of business and legal issues regarding temporary staffing, and therefore, looks forward to utilizing a contract template developed by key agencies with expertise in this area.

### 3. Retirees Do Not Comply with Return-To-Work Laws

**Recommendation:** *State agencies need to develop and structure temporary staffing arrangements so that the risks associated with violations of return-to-work laws are minimized. Contracts with the temporary staffing vendors should have terms and conditions that require temporary staffing vendors to screen for state retirees and report assignments to state agencies.*

**Response:** The Department will review future temporary staffing vendor contracts to ensure language is included requiring the vendor to screen for state retirees and report assignments to the Department.

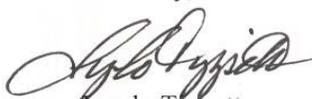
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Thank you again for the opportunity to respond to the recommendations in the report and for the expertise and professionalism demonstrated by your staff in conducting this performance audit. I appreciate the work of the Office of the State Auditor to help the Department achieve its goals and become aware of additional opportunities to improve its operation and reduce expenditures.

Sincerely,



Lyndo Tippet

LT/jbd

cc: Dan DeVane, Chief Deputy Secretary  
Angela Faulk, Human Resources Director  
Mark Foster, Chief Financial Officer  
Stephanie King, Accounting Operations Director  
Donnie Thorn, Purchasing Director  
Bruce Dillard, Inspector General

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**State of North Carolina  
Office of Information Technology Services**

**Michael F. Easley, Governor**

**George Bakolia, State Chief Information Officer**

December 18, 2008

The Honorable Leslie W. Merritt, Jr.  
N.C. Office of the State Auditor  
2 South Salisbury Street  
20601 Mail Service Center  
Raleigh NC 27699-0601

Dear Mr. Merritt:

Thank you for the opportunity to review the audit of state agency's use of temporary staffing vendors. Information Technology Services' (ITS) was one of the five (5) agencies involved in this audit. As the findings are addressed to all the state agencies with recommendations to be implemented by the General Assembly or Governor, it is challenging to respond to these findings. However, this letter serves as ITS' response to the findings in the audit. ITS has responsibilities both as an agency and also statewide for IT procurement; therefore, our responses are noted accordingly.

1. State Agencies Pay Too Much For Temporary Staffing Services

**Statewide**

- For temporary staffing requirements for IT resources, the Statewide IT Procurement Office has pre-qualified vendors through the competitive bid process to provided services to state agencies on an as needed basis.
- The Short-Term IT Staffing Contract provides rate ranges bid by vendors by category. As Task Orders are released to vendors for bid they must respond with competitive rates within the established range.
- The Statewide IT Procurement Office is preparing a Request for Proposal to award a contract for a Vendor Managed Service and Managed Service Provider to meet the IT resource needs of state agencies. The awarded contract will streamline the processes involved in the procurement and management of contingent labor. Use of such a system will further increase competition which can generate significant cost savings and gains in efficiencies.

**ITS (agency)**

- ITS solicits bids from qualified vendors for each posting under the contract.
- ITS negotiates the best rate for the skill sets required within the established rate range.

## 2. Business and Legal Risks are Not Well Managed

**Statewide**

- Legal risks associated with using temporary staffing for IT requirements are minimized since all vendors must agree to the North Carolina IT Procurement Office General Terms and Conditions for Goods and Services in order to qualify to bid on agency specific Task Orders.
- NC General Statute §147-33.72F provides that the Office of Information Technology Services shall establish procedures for the procurement of information technology. The procedures may include...restrictions on supplemental staffing. In order to manage the risk of having contractors in place in a single state agency for multiple years, the Short Term Staffing Contract has a restriction of six months. Procedures are in place to ensure contractors are not retained longer than necessary. All requests for contractors and contractor extensions must be approved in advance by the Statewide IT Procurement Office.
- The Statewide IT Procurement Office has collaborated with the Office of State Budget and Management and state agencies to convert contractor positions to permanent positions in an effort to manage risk and reduce costs. The Office of State Budget and Management has established a process for creating new information technology positions.

**ITS (agency)**

- ITS issues Task Orders subject to the terms and conditions of the master contract which is reviewed by legal counsel.
- ITS requires every contractor to successfully pass a criminal background check and sign a non-disclosure agreement prior to performing IT services.

## 3. Retirees Do Not Comply with Return-To-Work Laws

**Statewide**

- The Statewide IT Procurement Office will consult with the Office of State Personnel and the Attorney General's Office regarding the applicability of terms and conditions to address the hiring of retirees under the Short-Term Staffing Contract.

**ITS (agency)**

- There were no findings for ITS in this area.

As the contracts for staff augmentation for IT have evolved, the Statewide IT Procurement Office has applied lessons learned from previous contracts and implemented best practices for obtaining resources in an efficient and cost effective manner. The Statewide IT Procurement Office will consult with other agencies by providing these lessons learned and best practices with regard to implementing contracts similar to the Short Term Staffing Contract for non-IT resources. Additionally, the Statewide IT Procurement Office will collaborate and participate in

a workgroup as recommended to establish statewide convenience contracts or other statewide contracting methods for temporary staffing services.

I would like to take this opportunity to thank you for the professionalism demonstrated by your staff on this project.

Sincerely,



George Bakolia  
State Chief Information Officer

cc: Ann Garrett, State Chief Information Security Officer and ITS Internal Audit Director  
Patti Bowers, Chief IT Procurement Officer  
Nancy Burgart, ITS Internal Auditor

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