

MANAGEMENT MEMO

SUBJECT: GUIDELINES REGARDING FOLLOW-ON CONTRACTS: POLICY AND REVIEW PROCESS	NUMBER: MM 04-09
REFERENCES: PCC §10365.5, PCC §10430 SUPERSEDES STATE ADMINISTRATIVE MANUAL (SAM) SECTION 5202 AND SUPERSEDES MM 03-19	DATE ISSUED: MARCH 30, 2004 <hr/> EXPIRES: MARCH 31, 2005 <hr/> ISSUING AGENCY: DEPARTMENT OF GENERAL SERVICES

The purpose of this Management Memo is to inform departments of the changes in state law regarding “*follow-on* contracting” as a result of SB 1467 (Bowen) and to establish policy and guidance for evaluating whether particular contracting engagements might conflict with Public Contract Code (PCC) section 10365.5. **

BACKGROUND

SB 1467 was chaptered into law in September 2002, and became operative July 1, 2003. SB 1467 amended section 10430 to extend the prohibitions already contained in section 10365.5 to Information Technology (IT) contracts.

Section 10365.5 generally prohibits a consultant from bidding on or being awarded a *follow-on* contract based on the product of a previous contract by that consultant. It applies to all bids submitted or contracts to be awarded after July 1, 2003, even if the earlier advice or recommendations were provided under a contract executed prior to that date. Section 10365.5 does not distinguish between intentional, negligent and/or inadvertent violations. A violation could result in disqualification from bidding, a void contract and/or the imposition of criminal penalties (PCC 10420).

Additionally, SB 1467 extended the prohibitions of sections 10410 and 10411 to IT contracts. These latter sections contain various prohibitions against state employees and former state employees contracting with the state. This Management Memo does not address those sections, or other conflict of interest statutes, but agencies must be aware of the prohibitions contained in those provisions.

**** Further statutory references will be to the Public Contract Code, unless otherwise indicated.**

APPLICABLE LAW

PCC section 10365.5 provides in part as follows:

“(a) No person, firm, or subsidiary thereof who has been awarded a consulting services contract may submit a bid for, nor be awarded a contract for, the provision of services, procurement of goods or supplies, or any other related action which is required, suggested, or otherwise deemed appropriate in the end product of the consulting services contract.”

PCC section 10430(b) (2) states that:

“.....Section 10365.5 shall not apply to incidental advice or suggestions made outside the scope of a consulting services contract.” (Note that this section only applies to IT contracts.)

EXCLUSIONS

A person, firm, or subsidiary awarded a sub-contract of an *original* consulting services contract amounting to no more than 10 percent of the consulting services contract is exempt from the prohibition of section 10365.5 as applied to the subsequent bidding or award of the *follow-on* contract. (Section 10365.5(b).)

PCC section 10365.5 does not apply to contracts awarded pursuant to Government Code 4525 et seq. (Section 10365.5(c).)

Consultants/employees of a firm which provides consulting advice under an *original* consulting services contract are not prohibited from providing services as employees of another firm on a *follow-on* contract, unless they are named contracting parties or named parties in a subcontract under the original contract. Section 10365.5 applies only to persons, firms, or subsidiaries who have been awarded an *original* consulting services contract. However, consultant-employees should be aware of other conflict of interest statutes, which may, in certain circumstance apply, e.g. Government Code section 87000, et seq.; PCC section 10410, 10411.

ANALYSIS

Analysis of potential *follow-on* issues should consider the following factors in evaluating the relationship of the information that is the product of the initial contract and the subsequent (potential *follow-on*) contract.

I. Initial Contract

Is the initial contract a consultant services contract? The key to evaluation of a *follow-on* situation is the determination whether the initial contract is a consulting services contract. If it is not, the prohibitions of section 10365.5 do not apply.

Pursuant to section 10335.5(a), a consultant services contract is a formal agreement which delivers services which have all of the following characteristics:

- (1) *Are of an advisory nature.*
- (2) *Provide a recommended course of action or personal expertise.*
- (3) *Have an end product that is basically a transmittal of information, either written or verbal and that is related to the governmental functions of state agency administration and management and program management or innovation.*
- (4) *Are obtained by awarding a contract, a grant, or any other payment of funds for services of the above type.*

The product may include anything from answers to specific questions to design of a system or plan, and includes workshops, seminars, retreats, and conferences for which paid expertise is retained by contract.

Contract Type

While there are no hard and fast rules, an evaluation of type of the initial contract is a useful first step.

In the life cycle of a typical information technology project, contracts are typically let for the following activities: Feasibility Study Report, Acquisition Specialist, Design Development and Implementation, Project Management, Independent Validation and Verification, Independent Project Oversight Consultant, and Maintenance and Operations. Of these, Design Development and Implementation, Project Management, Independent Validation and Verification, Independent Project Oversight Consultant, and Maintenance and Operations are typically not considered consulting services contracts because their primary purpose is not the delivery of services having the characteristics outlined in section 10335.5 (a). A Feasibility Study Report contract is typically considered a consulting services contract. An Acquisition Specialist contract is one which cannot typically be determined to be a consulting services contract without an analysis of the specific details of the contract. On the other hand, Strategic Planning contracts and business process reengineering/improvement contracts while not included in the lifecycle of a typical information technology project, typically would be characterized as consulting services contracts.

While the foregoing examples are typically characterized as noted, characterization based on contract type will not preclude a factual demonstration that a different characterization is appropriate. The ultimate analysis of contracts for purposes of the *follow-on* statute must be made on a case-by-case basis. The essential issue is what the contract delivers, not how it is labeled.

Evaluation of Work and Deliverables

In evaluating contracts on a case-by-case basis, the following inquiry may prove helpful.

First, are consulting services present? Does the contract call for services that are advisory in nature, providing a recommended course of action or personal expertise and having an end product that transmits information or analysis related to the governmental functions of a state agency? An analysis of the scope of work with these criteria in mind should suggest an answer.

Second, are the actions “required, suggested, or otherwise deemed appropriate,” found in an “end product,” or deliverable of the contract (Section 10365.5(a).) If there is no “end product” or deliverable which embodies the characteristics of a consultant services contract, a *follow-on* situation will not exist.

Multipurpose Contract

The above inquiry does not deal with the situation in which the initial contract is not “primarily” a consultant services contract, but nevertheless includes, in the contract’s deliverables, work that is “consulting services” in nature. Neither the statute nor the legislative history provides explicit guidance. The statute is silent with regard to contracts which do not provide consulting services as their primary deliverable, but include them as a relatively minor part of the contract. No definitions are provided, nor is there any other specific guidance. However, there are potentially enormous business implications to an approach which deems as a consulting services contract any engagement which contains any consulting service deliverable, however small in comparison with the overall purpose of the contract. Taking such an approach may often be not in the state’s best interest.

In the absence of specific statutory guidance, we look to determine the primary or predominant purpose of the initial contract. Again, section 10335.5 provides some guidance. Is the primary or predominant purpose of the contract “advisory in nature;” does it “recommend a course of action or personal expertise”? Is the end product of the contract “basically a transmittal of information... related to the governmental functions of a state agency?”

For example, in a large system implementation contract, the vendor’s principal work is to design a new data processing system. This contract would not reasonably be considered a consulting services contract even if, in the course of contract performance, the vendor makes recommendations regarding the new system which it is implementing.

Therefore, if the primary or predominant purpose of the initial contract is not that of a consultant services contract, a *follow-on* situation will not exist.

Although not based explicitly in statutory language, this approach can be viewed as a reasonable attempt to harmonize the Legislature’s clear purpose to effectuate the state’s best interest in IT contracting, while guarding against the potential dangers inherent in the *follow-on* contracting situation. Please be advised, however, that this is an administrative interpretation which has not been tested in the courts. Both contracting agencies and vendors are urged to exercise caution in this area.

II. Subsequent Contract

If the initial contract is determined to be a consulting services contract, the analysis must turn to the causal link, if any, between the initial contract and the potential *follow-on* contract. The purpose of the causal inquiry is to determine whether there is a sufficient nexus between the end product(s) of the first contract and the deliverable(s) to be procured by the second contract to warrant preclusion of the vendor that performed the first contract.

Does the new contract or the solicitation for the new contract call for goods, services, or supplies that were “required, suggested or otherwise deemed appropriate” in the end product of the initial consulting services contract?

If the solicitation for the new contract or the new contract itself does not reflect the advice of the initial contract, the causal relationship clearly required in section 10365.5 does not exist. However, if the causal relationship does exist, the initial contract vendor is prohibited from participating in the subsequent contract as either a prime contractor or a subcontractor to either the prime contractor or any subcontractor to the prime contractor.

In order to assist departments and vendors in determining whether there may be potential *follow-on* issues, the Department of General Services (DGS) recommends that in all procurements, bidders should be required to disclose the following information:

Whether they, or any subcontractor they intend to use, are currently providing consulting services to the state under a state contract (or as a sub-contractor providing more than 10 percent of the dollar value of a consulting services contract with the state) or have provided such services within five (5) years prior to the release of the solicitation document (RFI, RFP) which are related in any manner to the goods, services, or supplies to be acquired pursuant to the solicitation document.

Note: The fact that services were provided more than five years prior to the release of the solicitation document does not create a blanket exception. The *follow-on* analysis outlined above must still be performed.

PRACTICAL RECOMMENDATIONS

Since the determination of *follow-on* issues is dependent on the services rendered pursuant to the scope of the initial contract, care must be exercised in the drafting of the scope of services anticipated by these engagements. The awarding department and potential bidders should give serious consideration at the time that an initial contract is being developed to whether there may be potential future contracting opportunities that could fall within *follow-on* prohibitions. Solicitations for all consulting services contracts should advise of the application of section 10365.5.

ADVICE PROCESS

Before determining to either reject a potential bidder or withhold an award of a contract, a department or agency should analyze the issues considering the information provided in this Management Memo and applicable statutes. Consultation with departmental counsel is strongly recommended. Further advice may be sought when a bidder is participating in a solicitation to provide services or goods under circumstances which might constitute a *follow-on* (subsequent) contract. The purpose of this advice is to facilitate an early determination to allow vendors and departments to ascertain eligibility for proposed/pending procurements.

For contracts awarded by the DGS, or pursuant to purchase authority delegated by the DGS, or which are subject to the approval of the DGS, the Procurement and Contracting Officer (PCO) of the contracting department or a potentially disqualified bidder may seek advice from the Deputy Director, Procurement Division within 10 days after a contracting opportunity is advertised or announced to bidders, typically through the issuance of an RFI or RFP, whichever occurs first. (If

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the tenth day falls on a non-state business day, the request is due on the next state business day). The DGS may, in its discretion, consider requests made after the expiration of the time period. For its part, the DGS will make every effort to provide an expeditious response. If the inquiry is from the contracting department, that department shall reimburse the DGS for any costs associated with such review.

The request for advice should be submitted to:

Deputy Director, Procurement
Department of General Services
707 Third Street, 2nd Floor
West Sacramento, CA 95605

Fax: (916) 375-4505

Any documents submitted for review, and any written advice of the DGS shall be subject to the Public Records Act (Government Code 6250, et seq.) and applicable exemptions thereto.

The advice provided will be considered informal and not an official determination by the DGS. The provision of this informal advice shall not constrain any subsequent determination under law, nor will the DGS be restricted from the full exercise of its contract review responsibilities, including further review of issues related to section 10365.5 based on factors discovered by the DGS subsequent to the initial determination.

For questions regarding this Management Memo, please contact the DGS Procurement Division and speak to Senior EDP Acquisition Specialists Pam Mizukami at (916) 375-4430 or Scott Norton at (916) 375-4503.

Original signed by Ron Joseph, Interim Director

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Department of General Services