

CITY OF GALVESTON
REPORT ON PORT OF GALVESTON PURCHASING CONTROLS AND
CONTRACT MANAGEMENT
PREPARED BY THE CITY OF GALVESTON CITY AUDITOR’S OFFICE

July 14, 2020

The Purpose for this Report.

The City Auditor’s Office is submitting this report to the Board of Trustees of the Galveston Wharves and the Galveston City Council to explain our significant mutual opportunities to increase collaboration, efficiency, and transparency in public purchasing and procurement. Moreover, these opportunities will also likely add value in driving a more competitive procurement process, reduce costs, and add dollars to the Port of Galveston’s bottom line, a primary goal expressed to us by Port Director/CEO, Rodger Rees, and his staff. The City Auditor’s Office wishes to communicate the opportunities available for collaboration, efficiency, and transparency through the creation and implementation of efforts to routinely justify and document procurement compliance by the Port of Galveston’s Procurement Compliance System (“PCS”) with Local Government Code, Chapter 252, which sets out applicable competitive bidding laws (hereafter, “Chapter 252”).

This report satisfies two audits required in the City Auditor’s audit plan for the fiscal year 2020. These reports are “Purchasing Controls for the Port of Galveston (AUDIT-PORT2020-2) and Contract Management for the Port of Galveston (AUDIT-PORT2020-3).” As a brief overview, the City Auditor’s Office will discuss the following to help readers understand its full vision:

- Section I.** Explain PCS and the benefits it can produce in governmental procurement.
- Section II.** Discuss portions of Chapter 252 in order to illustrate the interaction between PCS and applicable law.
- Section III.** Disclose the potential organizational risks, including litigation even with full compliance with Chapter 252 and the need to minimize potential misunderstandings, disputes, and questions related to the procurement process.
- Section IV.** Explicate the transactions with the Port of Galveston and a certain vendor.
- Section V.** Provide reference to opinion letters from the City of Galveston’s City Attorney (attached hereto as *Exhibit 1*) and the Port of Galveston’s General Counsel (attached hereto as *Exhibit 2*).
 - Please note that the State of Texas prohibits the unauthorized practice of law, and therefore, the City Auditor’s Office has not and shall not express a legal opinion or conclusion concerning the transactions of the Port of Galveston.
- Section VI.** Auditor’s Recommendation introducing the Contract Monitoring System (“CMS”) to the Board of Trustees of the Galveston Wharves, the Galveston City Council, the Park Board of Trustees, and the public, familiarizing readers with the members of CMS, their roles, as well as proposed methods to promote public transparency, more efficient operations, and resulting opportunities for cost savings in the area of governmental procurement.

CITY OF GALVESTON
REPORT ON PORT OF GALVESTON PURCHASING CONTROLS AND
CONTRACT MANAGEMENT
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- Section VII.** Auditor’s Recommendation detailing a standardized coding method already proposed by the CMS project team in meetings that transpired prior to the date of this report.
- Section VIII.** Auditor’s Recommendation itemizing a system of documentation of procurement files already proposed by the CMS project team in meetings that transpired prior to the date of this report.
- Section IX.** Conclusion.

The City Auditor’s Office is optimistic that the CMS project will improve public transparency with respect to procurement practices for the Port of Galveston, the Park Board, and the City of Galveston (collectively, the “CMS Participants”).

Section I. What is a Procurement Compliance System (PCS) and What Good Does it Do?

A PCS is a series of documents in the form of checklists, questionnaires, flowcharts, and guidelines used by governmental procurement employees to detect “and report” compliance at all stages of the organizations procurement cycle. These types of documents should adhere to the requirements of Chapter 252 and will ensure all competent vendors have an equal chance to participate in the competitive bidding processes and, at the same time, provide the best value to the CMS Participants.

However, the readers of this report should recognize that there is no special formula for determining the different types of compliance with Chapter 252. Therefore, a government agency’s objective is to design a PCS that minimizes litigation and/or financial risks and potential increased procurement costs associated with non-compliance.

The Port of Galveston conducts a large number of complex transactions with preparation performed by trained personnel at all stages of the procurement process. PCS will allow for a tracking of procurement decisions that, in these conditions, will demonstrate compliance best value by reinforcing existing written procedures at all stages of the procurement process.

In this process, litigation risk could originate from different sources such as a bidder or potential vendor not being awarded contract or, in some circumstances, public watchdogs. Responding to public information requests, possible discovery actions or potential legal action is an expensive task requiring staff time and, potentially, legal fees. A properly implemented PCS should help to reduce the time and cost to produce relevant records when requested, such as bids and evaluations, to the public. The written detail of the processes and criteria used for awarding contracts provides confirmation to all participating bidders that they were treated fairly and on equal terms. At the same time, it demonstrates a properly operating “level playing field” that will encourage more competition, which could lead to better value for the public procurement dollar spent.

Thus, providing clear documentation through PCS, minimizes risk. A well-documented PCS guarantees limited disputes and/or litigation, as it adds value by reducing procurement costs. Additionally, the cost of resolving questions raised by bidders and/or public watchdogs would

CITY OF GALVESTON
REPORT ON PORT OF GALVESTON PURCHASING CONTROLS AND
CONTRACT MANAGEMENT
PREPARED BY THE CITY OF GALVESTON CITY AUDITOR'S OFFICE

decline significantly by providing the required documentation of PCS. Furthermore, the PCS enables the Port of Galveston to grow business relationships, share greater insight on the decisions of contract awards, and implement shared best practices.

A trustworthy PCS should promote in writing three components that will benefit an organization: reduced risk, best value to the organization, and public transparency and fairness.

Section II. What is Local Government Code, Chapter 252?

Chapter 252 provides the purchasing and contracting authority of municipalities and details the provisions by which procurement and purchases must be made. Section 252.021(a) of the Local Government Code prescribes the competitive bidding requirements for purchases of more than \$50,000. Section 252.021(a) reads, in part:

- “(a) Before a municipality may enter into a contract that requires an expenditure of more than \$50,000 from one or more municipal funds, the municipality must:
- (1) comply with the procedure prescribed by this subchapter and Subchapter C for competitive sealed bidding or competitive sealed proposals;
 - (2) use the reverse auction procedure, as defined by Section 2155.062 (d), Government Code, for purchasing; or
 - (3) comply with a method described by Chapter 2269, Government Code.”

The Port of Galveston is required to use one of the three choices listed above for purchasing and contracting in excess of \$50,000, unless a particular purchase is covered by one of the exceptions contained in Section 252.022 of the Local Government Code.

Local Government Code Section 252.062 lists the criminal penalties associated with knowingly violating the competitive bidding requirements of Section 252.021 of the Local Government Code in circumstances to which no statutory exception applies. These penalties include:

- “(a) A municipal officer or employee commits an offense if the officer or employee intentionally or knowingly makes or authorizes separate, sequential, or component purchases to avoid the competitive bidding requirements of Section 252.021. An offense under this subsection is a Class B misdemeanor.
- (b) A municipal officer or employee commits an offense if the officer or employee intentionally or knowingly violates Section 252.021, other than by conduct described by Subsection (a). An offense under this subsection is a Class B misdemeanor.
- (c) A municipal officer or employee commits an offense if the officer or employee intentionally or knowingly violates his chapter, other than by conduct described in Subsection (a) or (b). An offense under this subsection is a Class C misdemeanor.”

CITY OF GALVESTON
REPORT ON PORT OF GALVESTON PURCHASING CONTROLS AND
CONTRACT MANAGEMENT
PREPARED BY THE CITY OF GALVESTON CITY AUDITOR'S OFFICE

Section III. How can Local Government Code Section 252.021(a) be Bypassed?

Governmental purchasing and contracting may be manipulated in several different ways that will violate Local Government Code 252.021(a). These include:

- (1) "Component Purchases," meaning purchases of a component part of an item that, in normal purchasing practices, would be purchased in one purchase.
- (2) "Separate Purchases," meaning purchases, made separately, of items that in normal purchasing practices would be purchased in one purchase.
- (3) "Sequential Purchases," meaning purchases, made over a period, of items that, in normal purchasing practices, would be purchased in one purchase.

Section IV. Which Transactions Are Under Question For Compliance With Chapter 252?

The Port of Galveston entered into two written contracts with the same company, Octagon LLC ("Octagon"), in the month of September 2018. Both contracts were executed within ten days of each other. The first of these contracts was entered into on September 16, 2018 and has as its listed projects: "Job Audit" and "Market Survey and Org Chart Development," defined as:

A job audit is a formal procedure in which a compensation professional meets with the manager and employee to discuss and explore the position's current functions, tasks, and responsibilities. Within this analysis, a classification audit is a tool used by compensation professionals to gather information about a position to determine the proper pay range of the position by comparing actual responsibilities to criteria in published classification standards. The audit assists in determining where a position fits into the hierarchy of positions with regard to function and compensation. A job audit is a mutual, responsible part of the process of ensuring attention to an organization's compensation and classification system. Job audits are generally conducted with the following objectives:

- *To clarify and/or verify and measure the duties and reporting relationships of the employee;*
- *To see first-hand the employee work process and the department operation; and*
- *To allow the employee the opportunity to provide further explanation of the duties or examples of work product and responsibilities described in the position description.*

Performing a market survey or compensation analysis ensures an organization's pay decisions remain in line with both external factors, such as current market trends, as well as internal needs, including your company goals. The survey is a collection of wage figures and annual salary numbers for a given industry, in this case Ports, Transportation, and Government. In order to maintain preferred skills in staffing, the most basic functions of management is to establish a compensation scheme that is competitive and equitable and that promotes employee engagement and high performance. Competitive compensation practices are essential to employee recruitment and retention efforts.

CITY OF GALVESTON
REPORT ON PORT OF GALVESTON PURCHASING CONTROLS AND
CONTRACT MANAGEMENT
PREPARED BY THE CITY OF GALVESTON CITY AUDITOR'S OFFICE

Developing an organizational structure involves defining the framework around which your business operates. By defining how the organization works, the decision making hierarchy is defined. A clearly established structure helps employees resolve disputes and work together to achieve strategic goals.

The second of these contracts was entered into September 25, 2018 and had as its project an "Employee Handbook Review and Update," with the following expectations and objectives outlined, below:

An employee handbook can be a valuable communication resource for both the employer and the employee. It provides guidance and information related to the organization's policies, procedures, and benefits in a written format. The Port of Galveston's most recent guidance had been published in 2008. Over the course of 10 years, a number of organizational and legal changes were observed that needed to be documented in the employee handbook so as to: (1) establish expectations for employees; (2) codify, organize, and update company policies; (3) make training and enforcement easier for managers; (4) reduce the administrative burden on Human Resources; and, (5) protect the Port of Galveston from compliance violations and, therefore, legal action. The review process ensures that the information is accurate and easy to comprehend and should be conducted on a biannual basis.

The sum of these two contracts totaled \$49,800 (\$37,900 for the "Job Audit" and "Market Survey and Org Chart Development" and \$11,900 for the "Employee Handbook Review and Update"). The procurement file consisted of a company profile for Octagon, a copy of the two signed contracts, and the final work prepared by the vendor but prior negotiations or other actions by the Port of Galveston were not noted. Therefore, due to the amount of the combined total as well as the fact that these services are distinct and separate projects, these transactions are not under question in this audit.

Octagon was later hired for temporary staffing services that have been reviewed for compliance. The possible bundling of services remains uncertain because of the non-existence of written contracts. Prior engagement of temporary staffing firms had been on an "as needed basis." As such, per historical practices, Octagon's temporary staffing services for the Port of Galveston were not documented in writing by a contract or other written agreement.

The total amount paid to Octagon for the temporary services through December 1, 2019 was \$44,514.02, for standard, as-needed administrative support, and \$26,158.19 for the Port of Galveston's 2019 Internship Partnership. It appears that with regard due to the \$50,000.00 threshold there was no competitive sealed bidding as prescribed by Local Government Code Section 252.021(a) or board approval prior to contract award as warranted by Port of Galveston policy. For more information regarding these transactions, please see the attached opinion memorandum from the Port of Galveston's General Counsel (*Exhibit 2*).

CITY OF GALVESTON
REPORT ON PORT OF GALVESTON PURCHASING CONTROLS AND
CONTRACT MANAGEMENT
PREPARED BY THE CITY OF GALVESTON CITY AUDITOR'S OFFICE

If PCS had been implemented prior to these transactions, a thorough examination of the buying patterns of these types of services could have timely raised any relevant issues. We believe that an examination of the Port's past buying patterns for these two types of services should have been performed at the time of the purchase.

Section V. No Legal Opinion on Specific Transactions.

Please note that the State of Texas prohibits the unauthorized practice of law, and therefore, the City Auditor's Office has not and shall not express a legal opinion or legal conclusion concerning whether the transactions of the Port of Galveston comply with the requirement of Chapter 252. As such, please see the attached opinions from the City of Galveston's City Attorney (*Exhibit 1*) and the Port of Galveston's General Counsel (*Exhibit 2*).

Section VI. Auditor's Recommendation - What is the Contract Monitoring System and How Would Periodic Reviews Improve Governmental Procurement?

Beginning on or about January 30, 2020, Port staff met with Glenn Bulgherini and Carrie Sumrall, the City of Galveston's Auditor Office, to discuss the Port of Galveston's participation in the Contract Monitoring System ("CMS"), a collaborative coalition of procurement, administrative, and financial professionals from the City, the Port, and the Park Board in efforts to create and implement consistent, efficient, and sensible best practices allowing for a more manageable approach to contract management, consistent and streamlined procurement practices, and implementation of internal and external process controls.

The City Auditor's Office has identified CMS as the key to successful contract monitoring for all three governmental organizations working for the betterment of our city. This collaborative effort is designed to establish a third-party, non-punitive checkpoint that will serve to document and, thus, "audit proof" future procurement issues in a collaborative, stress free environment. The CMS group has been assembling in both formal and non-formal meetings for approximately six months prior to the date of this report.

Through these gatherings and discussions, the City Auditor's Office has been able to identify the key stages of a governmental procurement cycle: (1) Ascertaining the Necessity for a Purchase; (2) Identifying and Terming the Contract Stipulations; (3) Suggesting Processes; (4) Contract Award; and, (5) Managing and Supervising Contract Execution.

The identification of these key stages has allowed the CMS group to begin to map various indicators to each entity's respective procurement legal and procedural requirements and provide a series of warning indicators for the detection of possible errors. These warning indicators will be under constant revision by the CMS group in order to allow each organization to operate their procurement cycles as efficiently and effectively as possible under their respective procurement regulations. Therefore, these warning indicators include, but are not limited to, the following:

CITY OF GALVESTON
REPORT ON PORT OF GALVESTON PURCHASING CONTROLS AND
CONTRACT MANAGEMENT
PREPARED BY THE CITY OF GALVESTON CITY AUDITOR'S OFFICE

1. Multiple contracts awarded to the same vendor each below the \$50,000 level.
2. Alterations to contract specifications and award amounts after the original signing of the contract.
3. Complaints from bidders and other parties.
4. Fictitious companies that do not have the appearance of any competition.
5. Unusual bid patterns that allow the rotation of winning bidders.
6. Inadequate quality or undelivered goods or services.

Additionally, the CMS group is working on solutions to centralize the location of all organizational contracts for ease in the retrieval process to perform work and fulfill open records requests and to create checklists that will ensure and confirm compliance.

To date, CMS Participants have worked together to discuss and develop preliminary best practices for future application, including but not limited to an Acquisition Plan, File Creation Standard Operating Procedure & Checklist, Contract Management File Checklist, and Contract Review Checklist. CMS Participants have also begun reviewing the sample audit proofing tools created for a sample contract, with the understanding that these tools would be modified where necessary on case-by-case basis for future contracts, as well as contract management software applications that would work best within their respective organizational needs. CMS Participants have also discussed their collective desire to meet on a bi-monthly basis in order to begin reviewing sample contractual terms and conditions in order to develop best practices generally and specifically including refined audit proofing controls to be applied in preparing future contracts. Moving forward, while the controls applicable to Chapter 252 would largely remain the same, additional monitoring tools, as applicable on a contract-by-contract basis, would be developed. This will drive a “best practices” culture in each participant’s procurement function and help add dollars to each participant’s bottom line.

The Purchasing Policy of the Board of Trustees of the Galveston Wharves, and its incorporated procedure calls for a centralized procurement system. Therefore, the Port of Galveston has begun to work with internal users to better manage the departmental procurement process and respective obligations throughout the pre-solicitation and post-contracting processes. These controls, developed through the supporting collaborative efforts of CMS facilitate greater guidance through the pre-solicitation and post-contracting processes, thereby assigning ownership and empowering individual contract managers on a project-by-project basis.

Uniquely standardizing and utilizing the audit proofing controls to perform periodic review would allow for greater oversight by the procurement function as well as provide a basis for improved procurement decisions going forward. Additionally, inspired by the efforts of the CMS

CITY OF GALVESTON
REPORT ON PORT OF GALVESTON PURCHASING CONTROLS AND
CONTRACT MANAGEMENT
PREPARED BY THE CITY OF GALVESTON CITY AUDITOR’S OFFICE

Participants, the Port of Galveston has begun to develop more robust contract-specific plans to implement periodic internal reviews of specific contracts in order to ensure contractual compliance and vendor performance.

Section VII. Auditor’s Recommendation – How Will the Standardized Coding Method Add Value to the Governmental Procurement Process?

A Standardized Coding Method is a structured approach to evaluate the procurement process for “*best values*” to the governmental organization. It is the written guiding principles to help a governmental organization safeguard its procurement process within the confines of Chapter 252. Many governmental organizations have a standardized coding method that begins by defining each purchase as a Project. The Project Method guarantees thorough compliance of the whole purchase process with Chapter 252. The Project Method is recommended to be arranged as a participatory group development process composed of individuals who have the technical skills and expertise to review the procurement process design and reports throughout the project cycle.

The City Auditor’s Office recommends that the Port of Galveston follow up after analyzing the Project Method with reviewing the possibility of an analysis that can be termed the Commodity Method. This method would consider all of the parallels and likenesses of each good and service acquired in connection with each project that does not exceed the \$50,000.00 threshold. These identified goods and services would then be combined whenever possible to be competitively bid to the public so as to receive the best value for the Port of Galveston in addition to potential economies of scale. This implies that adequate human resources allocated to the commodity analysis portion of the procurement project would lead to an even more transparent procurement process that will lead to even greater cost savings.

A hypothetical example applying these methods would be a situation where the Port of Galveston has identified two, completely separate small projects to perform with a cost to Projects A and B of \$30,000 and \$35,000, respectively. These are two completely separate projects that would not be combined in the normal course of business. However, both projects require the purchase of laptop computers. The Port of Galveston could possibly publish a competitive bid request to the public, or – alternatively – use the authorized Buy Boards, for the purchase of laptop computers needed for both Project A and Project B even though the \$50,000.00 level has not been met. This intra-project approach could also be incorporated, through negotiations, with projects that exceed the \$50,000.00 mark.

Port of Galveston staff will continue to review both the Project Method and the Commodity Method for opportunities of application.

Section VIII. Auditor’s Recommendation – What is the Importance of a System of Documentation of Procurement Files?

One of the more important aspects of documenting a procurement file is to eliminate the possibility of noncompliance, through written documentation and justification for any apparent deviation from standard practice, which – in turn – eliminates misunderstanding to management and the

CITY OF GALVESTON
REPORT ON PORT OF GALVESTON PURCHASING CONTROLS AND
CONTRACT MANAGEMENT
PREPARED BY THE CITY OF GALVESTON CITY AUDITOR'S OFFICE

public. Documentation in the procurement file should anticipate any and all questions that pertain to an organization's procurement of goods and/or services and explain that reasoning in such a way that it makes sense to a reasonable, independent third party. The CMS group has divided the documentation process into seven best practices shown with objectives below:

1. Acquisition Plan
 - a. *Key Objective.* A checklist completed throughout the procurement process designed to ensure contract requirements are timely fulfilled.
2. File Creation Standard Operating Procedures
 - a. *Key Objective.* A centralized location whereby all contracts may easily be assessed by staff.
3. Contract Management File Checklist
 - a. *Key Objective.* A tool used to review contract files to conclude that all phases of the procurement steps have been documented in the contract files.
4. Contract Review Checklist
 - a. *Key Objective.* An expansion of review procedures to allow for the identification and reporting of any two contracts or more with substantially equivalent specifications, characteristics, and timing.
5. General Clarification
 - a. *Key Objective.* An increase in audit-proofing procedures that create a worksheet certifying the use of contracted services as "professional services."
6. Technical Clarification
 - a. *Key Objective.* A system within the procurement process that will identify exceptions to Port of Galveston policies to the Board of Trustees of the Galveston Wharves.
7. Checkpoint into Software
 - a. *Key Objective.* A repetitive routine procedure that will verify each Port of Galveston contract has been approved by qualified procurement staff.

Practices identified above help to understand each agency's buying pattern for a particular good or service. In other words, a review and documentation of the buying history will authenticate the organization's "normal course of business", referred to in Chapter 252, and validate procurement decisions made in connection with the purchase.

Another important result of this process will be to discern the similarities or differences in goods and services submitted by different bidders/vendors. For example, perhaps there is an expected change in a product line or ever-advancing technology, and the agency does not want to commit to purchasing any more products or services than necessary before newer versions become available. It is imperative that all communications and decisions are documented in the procurement file in these situations. In the same way, sometimes there are limitations on the availability of storage space at the organization's facility, reducing the size of a particular purchase. Documenting this decision in the procurement file to prevent future questions or claims that bid splitting occurred.

CITY OF GALVESTON
REPORT ON PORT OF GALVESTON PURCHASING CONTROLS AND
CONTRACT MANAGEMENT
PREPARED BY THE CITY OF GALVESTON CITY AUDITOR'S OFFICE

Following this process of internal periodic review and update to the procurement files also provides a method to assist the organization in avoiding criticism of its buying patterns. This internal periodic review would identify repetitive purchases, which could assist in determining whether consolidation and larger procurements would be warranted.

These topics focus on the identification of process changes requiring additional steps at the time of bidding, evaluation, and issuance of the initial contract. The additional data will assist in ensuring the entity receives the best value for the dollars spent.

Section IX. Conclusion

A comprehensive PCS promotes three components, designed to aid an organization, which include a risk reduction, achieving best value to an organization, and public transparency and fairness. Through this review, the City Auditor's Office has developed, with the assistance of the Port of Galveston and Park Board, a wide-ranging CMS program, that will include a comprehensive PCS system, resulting in clear and ongoing organizational benefits: efficiency, transparency, compliance, and best practices. While working together, the City Auditor's Office, the Port of Galveston, and the Park Board developed a collaborative means through which additional opportunities for collaboration, transparency, and best practice sharing becomes increasingly possible, while removing the practice of punitive scrutiny. The CMS Participants should strive to achieve these improvements – together – and provide relevant tools and guidance for public employees and management. The City Auditor's Office hopes to create a systematic practice of two CMS meetings per month comprised of individuals from the Port of Galveston, Park Board, and City of Galveston. A CMS group composed of all agencies will help to *audit proof* procurement since significant purchases can be discussed within the group and best practices implemented as agreed. These two monthly meetings could produce a quarterly CMS report presented to City Council and the Board of Trustees of the Galveston Wharves on the accomplishments achieved. When properly employed, along with the necessary expert advice of individuals invited to these meetings, the CMS should both help each entity maximize the value obtained for each procurement dollar spent, for the benefit of all.

Exhibit 1
City of Galveston's City Attorney

Issue: Did the Port violate State law or its purchasing policy when entering into contracts or otherwise paying for services with the Octagon?

Rule: State Law – Local Government Code 252.001

(2) “Component purchases” means purchases of the component parts of an item that in normal purchasing practices would be purchased in one purchase.

(6) “Separate purchases” means purchases, made separately, of items that in normal purchasing practices would be purchased in one purchase.

(7) “Sequential purchases” means purchases, made over a period, of items that in normal purchasing practices would be purchased in one purchase.

Local Government Code 252.021

(a) Before a municipality may enter into a contract that requires an expenditure of more than \$50,000 from one or more municipal funds, the municipality must:

- (1) comply with the procedure prescribed by this subchapter and Subchapter C for competitive sealed bidding or competitive sealed proposals;
- (2) use the reverse auction procedure, as defined by Section 2155.062(d), Government Code, for purchasing; or
- (3) comply with a method described by Chapter 2269, Government Code.

(b) A municipality may use the competitive sealed proposal procedure for the purchase of goods or services, including high technology items and insurance.

(c) The governing body of a municipality that is considering using a method other than competitive sealed bidding must determine before notice is given the method of purchase that provides the best value for the municipality. The governing body may delegate, as appropriate, its authority under this subsection to a designated representative. If the competitive sealed proposals requirement applies to the contract, the municipality shall consider the criteria described by Section 252.043(b) and the discussions conducted under Section 252.042 to determine the best value for the municipality.

(d) This chapter does not apply to the expenditure of municipal funds that are derived from an appropriation, loan, or grant received by a municipality from the federal or state government for conducting a community development program established under Chapter 373 if under the program items are purchased under the request-for-proposal process described by Section 252.042. A municipality using a request-for-proposal process under this subsection shall also comply with the requirements of Section 252.0215.

Exhibit 1
City of Galveston's City Attorney

See also Texas Attorney General Opinion No. MW-344 – “The Board of Trustees of Galveston Wharves was required to receive competitive bids pursuant to Vernon's Ann.Civ.St. art. 2368a (see, now, this section), in order to award a contract for the services of a container terminal operator.”

Local Government Code 252.062

- (a) A municipal officer or employee commits an offense if the officer or employee intentionally or knowingly makes or authorizes separate, sequential, or component purchases to avoid the competitive bidding requirements of Section 252.021. An offense under this subsection is a Class B misdemeanor.

Port Purchasing Policy

Section 2.01 Obtaining Prices – The Purchasing Agent or designee will obtain prices for purchasing goods or services (except professional services, as defined below) according to the following guidelines.

- (b) Purchases of \$3,000 but no more than the Bidding Threshold. The purchasing agent must obtain informal written quotations from at least three vendors. These purchases will be accomplished through the use of completed Request Forms submitted and issuance of purchase orders, subject to the provisions of Section 3.02 below. In addition, the Purchasing Agent must contact at least two historically underutilized businesses in Galveston County on a rotating basis, based on the information provided by the General Services Commission pursuant to Chapter 2161 of the Texas Government Code. If no historically underutilized business provides the desired goods or services in Galveston County, the port is exempt from this requirement.
- (c) Purchases in excess of the bidding threshold. Unless the expenditure is exempt by applicable law, the purchasing agent must make any expenditure for goods or services in excess of the bidding threshold in accordance with, and may utilize any purchasing procedure permitted by, Applicable law. From time to time the Port's general counsel will provide the purchasing agent with guidelines that must be followed in order to comply with applicable law, and those guidelines must be adhered to by the purchasing agent.

Application: The Port entered into two contracts with the same company, Octagon (both contracts executed within ten days of each other). One of these contracts was entered into September 16, 2018, and had as its Projects “Job Audit” and “Market Survey and Org Chart Development”. The second of these contracts was entered into September 25, 2018 and had as its Project “Employee Handbook Review and Update”.

It should be noted that except for Numbers 2 and 7 of each Statement of Work prepared by Octagon for these two contracts (those numbers list Scope of Work and Deliverables,

Exhibit 1
City of Galveston's City Attorney

respectively) the Statements of Work are identical. It also appears to an outside observer that the deliverables are linked in both nature and type, in that both deliverables are focused on staffing needs of the Port.

It also appears the Port paid for additional services from Octagon, contract services and temp services. It is unknown at this time whether contracts exist for these services, or the specific natures of the services being performed by Octagon.

In total, the Port has spent over \$120,000.00 with Octagon on services related to the Port's employees. \$120,000.00 is \$70,000.00 more than the bidding threshold as defined by Texas Local Government Code, and \$117,000.00 more than the \$3,000.00 threshold as set out in the Port's purchasing policy.

Conclusion: At this time, it is unknown whether the Port of Galveston violated Texas state law or the Port's purchasing policy. More information is necessary to determine whether the payments made to Octagon were part of a scheme to intentionally or knowingly make or authorize separate, sequential, or component purchases to avoid competitive bidding requirements.

It is also unknown whether the Port abided by its own purchasing policy by not obtaining informal quotes for any contracted amounts that were more than \$3,000.00 but less than the bidding threshold.

It is imperative the Port provide all existing documents relating to procurement and/or payments of Octagon and any services they have performed for the Port, in order to determine the legality of the Port's actions.

Addenda re: personal services

The Local Government Code contains provisions exempting political subdivisions from the procurement requirements laid out in other sections of the Code. One of those exemptions is for personal, professional, or planning services.¹ To date, there has been no definitive ruling on the definition of the terms personal, professional, or planning services by the courts of this State. Nor is there a definition for personal or professional services. Rather, our courts and our Attorneys General have instead ruled narrowly on the basis of the circumstances before them, stating specific exceptions rather than giving a broad ruling on a type of services being performed.

While it's possible to win in a court of law on that basis, it is likely best practice to attempt to avoid getting into a situation of having to explain why a particular procurement falls under a personal services exception.

¹ 252.022a(4)

June 18, 2020

RE: Pending Audit by City Auditor Glenn Bulgherini – Contracts With and Services Provided by Octagon Consulting, LLC – City Auditor’s Request for Response from Port Legal Counsel

Background Information

City Auditor Glenn Bulgherini has approached our office with regard to his ongoing audit of the Wharves and has specifically inquired as to matters involving two contracts the Wharves entered with Octagon Consulting, LLC (“Octagon”) in September 2018, as well as the Wharves’ prior use of Octagon to provide temporary workers as needed by the Wharves. Mr. Bulgherini has asked for the Wharves to have its legal counsel provide opinions regarding the above referenced contracts as follows:

- (1) He has asked us to address matters he has attributed to “Port Attorney’s Office” in work papers he provided to us, to either confirm their accuracy or clarify as necessary, to ensure that he has not misinterpreted what he has heard in prior conversations; and
- (2) He has also asked us to address matters he has attributed to the “City Attorney’s Office” in his work papers, and in a memorandum generated by that office on this topic.

Mr. Bulgherini provided an unsigned memorandum from the City Attorney’s office¹ raising questions about these contracts and the additional use of Octagon for providing temporary workers, and issues concerning compliance with bidding statutes found in Chapter 252 of the Texas Local Government Code (hereafter, “Chapter 252”) and the Port’s Purchasing Policy.

As authorized by the Board Chairman and the Port Director/CEO, I have prepared this Memorandum in response and plan to forward same to Mr. Bulgherini following review by the client.

Applicable Law and Policy

Local Government Code

Chapter 252 generally requires a competitive bidding process for purchases of goods and/or services involving a threshold of \$50,000 or more.² The Act also contains a provision creating a

¹ There is no specific author identified in this memorandum. However, “metadata” properties for the document identify the author to be Mehran Jadidi, who we understand is an Assistant City Attorney for the City of Galveston.

² Tex. Loc. Govt. Code Sec. 252.021

COMPETITIVE REQUIREMENTS FOR PURCHASES. (a) Before a municipality may enter into a contract that requires an expenditure of more than \$50,000 from one or more municipal funds, the municipality must:

- (1) comply with the procedure prescribed by this subchapter and Subchapter C for competitive sealed bidding

Opinion Memorandum Regarding Octagon Consulting Contracts

June 18, 2020

Page 2

preference for historically underutilized businesses.³ It also prohibits public officials or employees from taking steps to circumvent this requirement such as allowing “separate⁴, sequential⁵ or component⁶ purchases.”⁷ In responding to requests for opinions as to whether discrete facts constitute violations of this provision the Attorney General has repeatedly refused to provide such opinions.⁸

or competitive sealed proposals;

³ Id. At Sec. 252.0215.

COMPETITIVE BIDDING IN RELATION TO HISTORICALLY UNDERUTILIZED BUSINESS. A municipality, in making an expenditure of more than \$3,000 but less than \$50,000, shall contact at least two historically underutilized businesses on a rotating basis, based on information provided by the comptroller pursuant to Chapter 2161, Government Code. If the list fails to identify a historically underutilized business in the county in which the municipality is situated, the municipality is exempt from this section.

⁴Under Section 252.001 (a)(6) "separate purchases" means purchases, made separately, of items that in normal purchasing practices would be purchased in one purchase.

⁵Under Section 252.001 (a) (7) a “sequential purchase” means purchases, made over a period, of items that in normal purchasing practices would be purchased in one purchase.

⁶Under Section 252.001 (a) (2) "component purchases" means purchases of the component parts of an item that in normal purchasing practices would be purchased in one purchase.

⁷ Id. at Sec. 252.062. This provision provides for Class B and C misdemeanor penalties for any municipal officer or employee who “intentionally or knowingly” violates the bidding requirements or who “intentionally or knowingly” uses separate, sequential, or component purchases to avoid the competitive bidding requirements. To date our office has yet to locate a single court opinion in Texas involving criminal charges being asserted under this particular statute. There have been a number of civil proceedings typically brought by a citizen or a competitor of the company awarded a contract, claiming the statute was violated. Local prosecutions may have occurred somewhere in Texas, but that information is not readily available.

⁸ See for example Attorney General Opinion No. GA-0604 (February 28, 2008) at page 5:

Having set out the relevant law, we conclude we cannot answer your second question because it would require us to resolve fact questions. For instance, it may have been more appropriate to undertake this purchase in compliance with the Act because certain facts you relay, such as (1) the invoices came from the same contractor and were delivered to the same commissioner, and (2) the invoices resulted from what is characterized as Phase I and Phase II of a single project, raise questions as to whether this purchase violates the Act. These facts are not, however, dispositive. Section 262.023(c) applies when "separate, sequential, or component purchases" are undertaken "with the intent of avoiding the requirements" of the Act. Id. § 262.023(c) (Vernon Supp. 2007) (emphasis added); see also *ide* § 262.034(a) (Vernon 2005) ("A county officer or employee commits an offense if the officer or employee intentionally or knowingly makes or authorizes separate, sequential, or component purchases to avoid the competitive bidding requirements of Section 262.023."). Moreover, in determining whether a separate, sequential, or component purchase has taken place, one must determine if the purchase would "in normal purchasing practices" be made as a single purchase. Id. § 262.022(2), (7)-(8) (emphasis added). *Determining whether the requisite intent is present and what constitutes a normal purchasing practice with respect to a particular item requires the taking of evidence and finding of facts that cannot be performed in the opinion process.* Tex. Att'y Gen. LO-94-087 (1994) at 2 (concluding that a determination of whether purchases by Smith County of culverts and road sign components would fall within the prohibitions of the Act involves questions of fact that cannot be resolved in an opinion)(emphasis added).

Opinion Memorandum Regarding Octagon Consulting Contracts**June 18, 2020****Page 3**

Included in the exceptions to this act are contracts for “a procurement for personal, professional, or planning services.”⁹ Again, differing fact patterns can make interpreting Attorney General Opinions on this exception problematic. For example, as the City Attorney’s memorandum notes Opinion No. MW-344, which stated that the Port of Galveston had to seek competitive bids on a contract to hire a terminal operator. However, the Attorney General has also said that a contract to hire a construction manager was not required to be let for bid, under this same exception. See Opinion No. MW-530. The Attorney General has also opined that a school district was allowed to act as its own construction manager for a project that exceeded the statutory threshold by subcontracting smaller contracts. *See* Opinion No. DM-242.¹⁰

Port Purchasing Policy

The Wharves Purchasing Policy in effect during the events involved in this memorandum was adopted in 2012. The policy applies to “goods and services.”¹¹ The policy also encouraged the use of “historically underutilized” and “local” businesses. Further, the policy states that to “the extent of any inconsistency between this Purchasing Policy and the provisions of any Applicable Law, Applicable Law will control.” The preamble of the Policy also states that “As used in this Purchasing Policy, the term “Bidding Threshold” means the stated dollar amount applicable to an expenditure of funds by a municipality under Section 252.021(a), Texas Local Government Code, for which competitive bids or proposals are required.” Under Section 2.01(b) of the Policy purchases in an amount between \$3,000 and the Bidding Threshold should utilize informal quotes. The policy did not state the format of such quotes¹² nor provide for a protocol for preserving them.

This policy is not law. Rather, it is an internal operating procedure guiding the staff. If a purchase that violated the policy were made but which did not violate Chapter 252 of the Local Government Code, the employees involved may face discipline but would not face criminal liability. An entity performing services under such a situation could well prevail in a claim for its services if the law were not violated.

Background Facts and Assumptions

At the outset, the matters attributed to the “City Attorney’s Office” and the “Port Attorney’s Office” in the City Auditor’s internal work papers is somewhat ambiguous, due to the fact that we

⁹ Tex. Loc. Govt. Code Sec. 252.022 (a)(4).

¹⁰ There are a number of other exceptions as well. For example, in another opinion a County was allowed to avoid the statute for a twenty year contract far exceeding the statutory threshold for waste disposal services due to the public health exception under the act. Texas Attorney General Opinion No. 908.

¹¹ Tex. Loc. Gov’t Code 252 .021 refers to “contract.” The Port policy does not expressly define the term services. Various provisions reference construction services, telecommunication services and professional services.

¹² For example, soliciting three bids by phone and putting those bids in writing in the file might potentially be in compliance. Email bids might as well.

*Opinion Memorandum Regarding Octagon Consulting Contracts**June 18, 2020**Page 4*

understand he has spoken to various individuals in the City Attorney's office. Further, he also conferred with several members of the Wharves Board of Trustees, as well as their legal counsel. That said, the following sets out our understanding, of the facts most relevant to this inquiry:

1. Octagon appears to be a small, closely held Texas LLC. Its mailing address is 6341 Stewart Rd Suite #342 Galveston, TX 77551. The registered office for the company is 310 Magnolia Estates Drive, League City, TX 77573. Octagon recently also established an office in Downtown Houston as well according the owner's Twitter account.
2. Octagon was incorporated as a Texas limited liability company in June 2018. Andy Soles of League City, Texas is listed as the sole member on the company's certificate of formation. The 2019 Public Information Report also listed a Ms. Stephanie Sawyer as a member, along with Mr. Soles. ("Members" of a Texas limited liability company are the owners of the company's shares. They are analogous to shareholders of a corporation.)
3. Octagon appears to be a locally owned minority business. Mr. Soles is African American and Ms. Sawyer is female.
4. Octagon stated on its website and in promotional materials that it had an attorney on staff, Ms. Teresa Hudson. A review of her State Bar profile, LinkedIn profile and other available online references show that Ms. Hudson is licensed to practice law in the state of Texas. She also apparently served as a Vice President for Human Resources for Plastic Express and has her own law practice in League City, Texas.
5. We understand generally that Ms. Annette Goldberg, a former Wharves employee serving in the Human Resources Department, initiated discussions with Octagon based on her prior work experience with Mr. Soles when she worked for the City of Houston and he worked for another company providing HR contract services.
6. It is not known whether Ms. Goldberg solicited informal bids or quotes for the services at issue, as Ms. Goldberg is no longer employed by the Wharves.
7. Ms. Goldberg was hired by the Wharves in September 2018 and resigned her position earlier this year, on March 6, 2020.
8. We understand generally that the Port Director/CEO relied on HR and purchasing staff to ensure that State law and Wharves Policies were followed in the Wharves' dealings with Octagon.
9. In September 2018, the Wharves signed two contracts with Octagon:
 - a. A contract dated September 16, 2018. Hereafter, this contract is referred to as the "Job Analysis Contract." The total cost for services under this contract was \$37,900. The services to be provided under this contract contained two components:

*Opinion Memorandum Regarding Octagon Consulting Contracts**June 18, 2020**Page 5*

- i. A job audit, to properly defined duties and responsibilities of specific positions. This task was a necessary step in order to perform a market survey, to determine market salaries for similar positions. The total cost for this component was \$18,450.00.
 - ii. The market survey itself, with a total cost of \$19,450.
 - b. A contract dated September 25, 2018, under which Octagon was to revise and update the current Wharves Human Resources Policy into a new Employee Handbook. Hereafter, this contract is referred to as the "Handbook Contract." The total cost for this service was \$11,900.
10. Under the Handbook Contract Octagon reviewed and submitted a redrafted Employee Handbook which was approved by the Wharves Board of Trustees in December of 2018.
 11. The job audits and market surveys were performed as contracted under the Job Analysis Contract.
 12. This office has not been advised of any deficiencies with the performance of those services under.
 13. If taken separately the two contracts are both below the thresholds for bidding set forth by Tex. Loc. Govt. Code Chap. 252. The combined amount of both contracts (\$49,800) was also slightly below this bidding threshold.
 14. Apparently Ms. Goldberg also engaged Octagon for two additional, distinct services. We are not aware of any written contracts for these services. One was for the hiring of temporary employees, such as clerks who would be brought in for a short period of time. The decision as to whom to send to the Wharves was with Octagon. The persons assigned could change periodically.
 15. The other service was to recruit and then provide placement services for prospective hires, placing them with the Wharves on a temporary basis to allow the Wharves to determine if the individual was a suitable hire for the particular department. In this instance, we understand that a particular person was engaged to be placed to the Wharves (as opposed to a "fungible" temporary worker who might be a different person day to day) for this purpose. This service avoided the need for formal "probationary" periods for new hires.
 16. The Wharves had previously issued one or more requests for proposals with regard to the engagement of temporary service companies but that process was not finalized. The specific results of the prior RFP process are unclear.
 17. The Wharves, as allowed by law, has interlocal agreements with other public entities referred to as "Buy Boards" as authorized under Chapter 791 of the Texas Government Code. Purchases through these services are deemed to satisfy bidding requirements. *Id.* at

*Opinion Memorandum Regarding Octagon Consulting Contracts**June 18, 2020**Page 6*

Sec. 791.025. We do not have information as to whether Ms. Goldberg understood the mechanisms of and the distinctions between using Buy Boards, which do not require bidding, and other purchases which did require bidding. We are also not aware of the extent of her actual knowledge as to bidding requirements generally. At the same time, we have no information indicating that Ms. Goldberg ever acted with an intent to avoid or evade competitive bidding requirements under State law or Wharves policies.

18. As noted above, Ms. Goldberg voluntarily resigned from her position with the Port earlier this year. We are not aware of any surviving notes, memoranda or other documents Ms. Goldberg may have created or possessed, documenting the process for the two contracts or the temporary services work performed by Octagon.

A. Were the two written contracts “linked in both nature and type” requiring consolidation for bidding purposes?

The City Attorney’s unsigned memo makes the following assertion:

It should be noted that except for Numbers 2 and 7 of each Statement of Work [each contract] prepared by Octagon for these two contracts (those numbers list Scope of Work and Deliverables, respectively) the Statements of Work are identical. It also appears to an outside observer that the deliverables are linked in both nature and type, in that both deliverables are focused on staffing needs of the Port.

This appears to be an arbitrary assumption. First, Sections 2 and 7 of each contract are “Scope of Work” and “Project Fees and Expenses.” These sections were obviously key elements to each contract, and are very different.¹³ While Octagon apparently has a standard form it used and created for its contracts, these two contracts are by no means identical.

Further, Chapter 252 does not contain an “outside observer” legal standard of review. Regardless, an “outside observer” could just reasonably interpret these contracts as providing two entirely different types of services being performed. While the two contracts might be generally characterized as involving human resources, revising and updating an Employee Handbook is separate and distinct from conducting a market salary survey, and taking steps necessary to perform that survey. Neither is a necessary condition precedent to the other. We are not aware of any recognized authorities in the human resources field stating that these activities are so interrelated that they would normally be part of a common process. The City Attorney’s memorandum does not identify any such authorities.

Under the Handbook Contract, Octagon was to provide the Wharves with proposed policy updates, which would become part of a new Employee Handbook. Part of this work involved providing recommendations concerning current employment laws, presumably with assistance from

¹³ Section 6 in each contract, under the heading “Deliverables,” were unique to each contract as well. The City Attorney’s memorandum does not discuss this Section.

Opinion Memorandum Regarding Octagon Consulting Contracts

June 18, 2020

Page 7

Octagon's staff counsel, Ms. Hudson. Had our firm been engaged to undertake this task, the work would clearly be classified as "professional services." As the work included legal analysis and opinions, at least some of these services may have constituted "professional services" which are not subject to competitive bidding. In contrast, the Job Analysis contract did not appear to involve such legal analysis, reinforcing the fact that the tasks involved in the two contracts were separate and distinct.¹⁴

Based on the foregoing, it appears to us that the subject matters of the two contracts were separate and distinct. They do not appear to be components necessary to accomplish the other. Neither appears to be a necessary condition precedent to the other, and they are not, to our knowledge, normally undertaken as a single effort. Rather, both are unique tasks typically performed in isolated instances. Therefore, in our opinion, these contracts do not represent "component," "separate" or "sequential" purchase as defined and proscribed by Chapter 252.

To the extent our office disagrees with the opinions of the City Attorney's office, this disagreement simply illustrates that there is not a clear consensus on this issue.

B. Did the Engagement of Octagon's Temporary and Placement Services Violate the Law or Port Policy?

As noted above, Texas Local Government Code Sec. 252.021(a) requires that before a municipality may enter into a contract that requires an expenditure of more than \$50,000 from one or more municipal funds the municipality must comply with competitive bidding procedures. Thereafter, Sec. 252.022 provides a number of exceptions to this requirement. Included in the exceptions are contracts for "*personal, professional, or planning services.*" Loc. Govt. Code Sec. 252.022(a)(4). There are no Texas cases or Attorney General Opinions directly interpreting this provision. However, the Attorney General has offered opinions on what "personal services" means in connection with other statutes, as discussed hereafter, which do provide some guidance on this issue.

The Texas Attorney General's interpretation¹⁵ of the term "personal services" is essentially as follows:

¹⁴ The lines of whether the services were personal or professional under the Port's policies are not clear as well. The Port's policy does not define the term "services" but also later refers to several specialized types of services such as construction and telecommunication. An outside observer could find an ambiguity as to whether the types of services being provided by Octagon were of the type normally used by the Port. This may be a weakness in port internal controls that needs to be corrected but it is not a violation of statute.

¹⁵ A number of opinions of the Attorney General on the term "personal services" are related to the County competitive bidding statute in Loc. Govt. Code Chap. 262. These opinions can reasonably be used as a guide for how the Attorney General might construe the similar wording in Sec. 252.022.

*Opinion Memorandum Regarding Octagon Consulting Contracts**June 18, 2020**Page 8*

A personal services contract is a contract for the services of a particular individual. Unless the service to be provided is to be done by a unique, particular, named individual, rather than by anonymous and fungible workers, the contract is not for personal services.

Tex. Atty Gen. LO-98-023, at 2. For example, the Attorney General has found the following services **not** to be “personal services”

1. A contract requiring a service to generally provide persons for janitorial services. Attorney General Opinion No. JM-0486;
2. A contract for services to microfilm the entity’s records; Atty. Gen. Opinion JM-0890.

In each case the service was for “fungible employees,” that is employees who might change from week to week or even day to day. The goal of the contracts was not for the services of a particular person but rather for a service performed by persons that may never be known to the governmental entity in advance.

The Attorney General has also opined that the following, depending on the facts, may fall within the “personal services” exemption:

1. an airport operations contract could be eligible for exemption if the contract requires a particular, named individual to perform the services. Atty. Gen. Opinion KP-0246;
2. A contract for the services of a construction manager. Atty. Gen. Opinion MW-530.

These opinions involved the engagement of a particular person to perform a particular job. Other services such as those involving public health or emergency services may also be exempt, depending on how the services are placed.¹⁶

The key to determine whether a contract for staffing requires a bidding procedure is to determine whether the services to be provided by the staffing agency is to be done by a unique, particular, named individual. In the context of past uses of these agencies the following may be illustrative:

1. If the temporary staffing agreement is to provide clerical or administrative individuals chosen by the agency to work for Port based on agreed upon qualifications this is not likely

¹⁶ Chapter 252 also provides other exceptions which could apply in some cases. For example, the hiring of day workers to perform sanitation services or the employment of ambulance services could be excepted, as it was under Section 262.024(a)(2) as “necessary to preserve or protect the public health or safety of the residents of the county.” Tex. Atty Gen. Op. Nos. JC-0136 and JC-0281.

Opinion Memorandum Regarding Octagon Consulting Contracts**June 18, 2020****Page 9**

a contract for “personal services.” In this case the Port does not pick the persons in advance but rather sets the criteria for the agency to choose. The individuals would be “fungible” that is where they could be switched from time to time by the agency. A contract of this nature will require bidding if they exceed the bidding thresholds.

2. If the agency were engaged to recruit potential employees and then place those recruits, upon approval by the Port, at jobs for a probationary period to be hired as regular employees after the probation this may qualify as a “personal services” contract. The services are being performed by a unique particular, named individual. The service is not to have the agency provide temporary help but rather to have a specific individual act in a specific position for the Port to be hired permanently if approved by the Port.

These lines are not easily determined by a staff member seeking to apply them on a real-time basis. While the Wharves’ Purchasing Policy was intended to avoid such problems, more internal controls may have been helpful to assist employees in proper compliance. Ms. Goldberg’s work covered a relatively short period of time, which was also a period of significant transition. Following the Board’s hiring of Mr. Rees, there was a focused effort by Mr. Rees and senior management to both update and upgrade the Port’s policies and procedures.¹⁷

At this point we have not been able to specifically identify any attempts to “intentionally and knowingly” violate the bidding statutes.¹⁸ In some instances, the services provided appear to be a hybrid combination of personal, professional and other services. We have not located any Texas court cases directly on point interpreting these issues. It is therefore possible that a Court hearing this case could find that the Wharves use of Octagon for temporary staffing solutions was not proscribed by Chapter 252. That said, in our opinion the better practice would be to use competitive bidding (including the use of authorized Buy Boards) to procure temporary staffing services. As described below, Wharves staff has done so following these events, having entered into lawful, written contracts for several different temporary staffing needs.

Changes Going Forward

Going forward, and in order to avoid future confusion and procurement issues, the Wharves has entered lawful written contracts for with several different temporary staffing and placement

¹⁷ The Board of Trustees has pursued a similar path in seeking to update and upgrade its own governing documents. In the last two years there have been a number of revisions and modifications to documents such as the Trustees’ Bylaws and the “Policies Regulating Performance of Duties – Board of Trustees and Port Director of the Galveston Wharves,” also known as the “Board Management Policy.”

¹⁸ It does appear that Ms. Goldberg sought to engage a “local, historically underutilized business” as encouraged by State law and Wharves Policy.

*Opinion Memorandum Regarding Octagon Consulting Contracts**June 18, 2020**Page 10*

services.¹⁹ Using statutory procedures (i.e. conventional bidding or using authorized Buy Boards), the Wharves has now entered agreement with different temporary staffing providers for three separate categories of services – construction trades, finance and general administrative/clerical positions. These contracts all provide the Wharves with the ability to engage specific personnel resources when needed.

Additionally we have had informal conversations with the City Auditor and Wharves staff concerning additional processes to ensure compliance with State laws and Wharves policies. These include:

1. Adoption of a Contract Monitoring System (CMS).
2. Conducting an Annual Chapter 252 Review to be held in conjunction of the CMS.
3. Development of a standardized coding method to further avoid “separate,” “component” and “sequential” purchases proscribed by Chapter 252.
4. Developing standards and rules for documentation, and preservation of that documentation, in the Procurement File to ensure that there is an “audit trail” on specific procurement decisions.

I understand that as proposed by the City Auditor, these processes would be developed jointly by a working group including staff from the City, the Park Board of Trustees. Thereafter, these representatives (and their successors over time) would continue to act as a working group to conduct the Annual Review discussed above, and also to share best practices, lessons learned, and related matters on an ongoing basis. These could all help to ensure standardized compliance with both the letter and the spirit of State laws and Wharves Policies. We believe this effort would be beneficial to all three entities.

Anthony P. Brown

APB/ger

¹⁹ In addition to the temporary staffing services provided by Octagon, the Wharves has historically used other companies to provide such services, in areas such as construction trades and finance department functions. While at least some of those had gone through bidding in the past, it appears that a process of going out for bid drifted as these contracts ended, under prior management.