

## **NEW SUBCHAPTER C. THE INTEGRITY OF THE TEXAS WORKFORCE SYSTEM**

**ADOPTED RULES WITH PREAMBLE TO BE SUBMITTED TO THE *TEXAS REGISTER*. THIS DOCUMENT WILL NOT HAVE ANY SUBSTANTIVE CHANGES BUT IS SUBJECT TO FORMATTING CHANGES AS REQUIRED BY THE *TEXAS REGISTER*.**

The Texas Workforce Commission (Commission) adopts new Subchapter C. The Integrity of the Texas Workforce System and new §§801.51–801.56 regarding Local Workforce Development Boards with changes to the proposed text as published in the January 9, 2004, issue of the *Texas Register* (29 TexReg 344).

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## **PART I. PURPOSE, BACKGROUND, AND AUTHORITY**

**A. Purpose.** The purpose of Subchapter C is to set forth provisions and guidelines to ensure the integrity of the Texas workforce system. Subchapter C ensures that Local Workforce Development Boards (Boards):

- \*do not directly provide workforce services or determine eligibility for those services;
- \*do not award workforce service contracts to Board members and thereby create the perception that Board membership provides an advantage in competing for workforce service contracts;
- \*do not direct and control the daily activities and operations of their workforce service contractors in an attempt to circumvent the provisions prohibiting Boards from delivering workforce services;
- \*prevent potential conflicts of interest between themselves and workforce service contractors;
- \*apply the Board contracting guidelines when contracting for workforce services;
- \*develop fiscal integrity indicators with which to assess the financial integrity of their workforce service contractors;
- \*protect the overall financial security of the workforce service contractors' funds and operations; and
- \*abide by the post-employment provisions applicable to former Board employees seeking employment with a Board's workforce service contractor in order to avoid any conflict of interest or any appearance of a conflict of interest.

**B. Background and Authority.** The 74th Texas Legislature enacted House Bill 1863 (HB 1863), which is codified in part in Texas Labor Code, Chapter 302, and Texas Government

Code, Chapter 2308. HB 1863 provided local elected officials the opportunity to establish Boards that oversee the delivery of workforce services that meet the needs of local employers and workers. Rules relating to the Boards' roles and responsibilities are set forth in 40 T.A.C. Chapter 801.

Texas Government Code, Chapter 2308; Texas Labor Code, Title 4; and federal statutes and regulations have made Boards responsible for a number of duties related to the administration of Commission-funded workforce services, including:

- \*contracting with service providers;
- \*ensuring that workforce service contractors directly provide the workforce services and the eligibility determinations related to those services;
- \*maintaining adequate fiscal systems;
- \*complying with the uniform rules for administration of grants and agreements;
- \*meeting contracted performance targets; and
- \*complying with all applicable federal and state statutes and regulations.

Section 2308.264 of the Texas Government Code specifically prohibits Boards from directly providing workforce services. Furthermore, Senate Bill 280 (SB 280) amended §2308.264 to require that, in consultation with the Boards, the Commission by rule establish Board workforce service provider contracting guidelines that:

- (1) ensure that each independent contractor that contracts to provide one-stop workforce services has sufficient insurance bonding and liability coverage for the overall financial security of one-stop workforce services funds and operations;
- (2) prevent potential conflicts of interest between Boards and entities that contract with Boards; and
- (3) ensure that if a Board acts as a fiscal agent for an entity that contracts with the Boards to provide one-stop workforce services, the Board does not deliver the services or determine eligibility for the services.

The Legislature also amended §2308.267, Texas Government Code, to state that a Board's staff may not direct or control the workforce service contractor or its employees in providing workforce services as set out in 40 T.A.C. §801.28.

Additionally, the Commission, under 29 CFR Section 97.36(b)(3) that addresses conflict of interest provisions for grantees and subgrantees of federal funds, 29 CFR Section 95.42 that sets forth code of conduct requirements for entities receiving federal funds, Workforce Investment Act (WIA) Section 117(g) that addresses conflicts of interest, and its existing rule-making authority in §301.0015, Texas Labor Code, adopts provisions in Subchapter C to strengthen standards of conduct and integrity of the Texas workforce system in order to prevent the erosion of the public's confidence and trust in the system.

## **PART II. EXPLANATION OF INDIVIDUAL PROVISIONS**

Subchapter C. The Integrity of the Texas Workforce System is added as the location for the rules and provisions that ensure an ethical and accountable workforce system.

### Section 801.51. Purpose and General Provisions

Section 801.51 sets forth the purpose and intent of Subchapter C. The intent of the rules is to strengthen the public confidence in the integrity of the Texas workforce system. Section 801.51 also establishes the time frame for implementing certain provisions of the rules. The rules are effective 20 days following adoption. The Commission, however, does not want to impose an undue burden on the Boards or Board members and thereby provides that the Boards have until September 1, 2004, to develop the policies and procedures set forth in this subchapter. In order to prevent a Board from becoming noncompliant with Board membership requirements and avoid the disruption of the provision of workforce services, the Commission affords Board members, who have an existing workforce service contract, the earliest of the following to adhere to the provision prohibiting Board members from having contracts with the Board: (1) the expiration of the contract; (2) the renewal date of the contract; (3) the expiration of the Board member's term or Board member's resignation; or (4) September 1, 2005.

### Section 801.52. Definitions

Section 801.52 provides definitions relevant to the provisions in Subchapter C. The Commission defines a workforce service contractor as a person or an entity, other than a state agency or an institution of higher education as defined in §61.003 of the Texas Education Code, that contracts with the Board to provide workforce services listed in §801.28.

A conflict of interest exists if an individual has a direct or indirect interest—particularly a substantial financial interest—that influences the individual's ability to perform job duties and fulfill responsibilities. An appearance of a conflict of interest is a situation in which an individual's actions appear to be influenced by personal gain or gain to the organization in which the individual is employed. An appearance of a conflict of interest also exists if an individual's actions appear to be motivated by design to gain an improper influence over the Commission, the Agency, or the Board.

Individuals included in the conflict of interest provisions are Board decision-making employees as well as workforce service contractors and workforce service contractor employees in decision-making positions. The Commission defines a Board decision-making position as a position with a Board that has final decision-making authority or final recommendation authority on matters that directly affect workforce service contractors. A Board decision-making position is one, regardless of the official title, that functions as the executive director, deputy executive director, chief financial officer, lead contract manager, or lead contract monitor. The Commission defines a workforce service contractor employee in a decision-making position as a position with a workforce service contractor that includes the ability to commit or bind the contractor to a particular course of action with respect to carrying out the contractor's duties and activities under the contract.

By limiting the conflict of interest provisions to these decision-making employees, the Commission intends to provide guidelines and standards of conduct for those individuals who have the greatest ability to influence financial or policy decisions within the workforce system.

An individual has a substantial financial interest in an entity if the individual owns 10% or more of the entity; owns more than \$5,000 of the fair-market value of the entity; receives more than 10% of the person's annual income from the entity; is a paid board member of the entity; serves as an elected officer of the entity; or is related to a person who has a substantial financial interest in the entity. The Commission modeled the definition of "substantial financial interest" after the definitions of "substantial interest" in Texas Local Government Code Section 171.002 and Texas Government Code Section 527.005, and included provisions consistent with 40 T.A.C. Section 801.13.

Finally, §801.52 defines a "particular matter" as a specific investigation, application, request for a ruling or determination, rule-making proceeding, administrative proceeding, contract, claim, judicial proceeding or any other proceeding. The Commission intends that the particular matter provisions affect all Board members and Board employees. The Commission, however, reasons that the definition of a particular matter is so specific and narrow that for all intents and purposes, only Board members, and Board employees who are in decision-making positions will be affected. State statute imposes a lifetime ban from working on particular matters. The Commission believes that while Boards are quasi-governmental entities, the fact that Boards are stewards of the public's money is reason enough to apply the lifetime ban from working on particular matters to Board employees.

#### **Questions and Answers:**

**Q:** Does the lifetime ban from working on a particular matter mean that former employees who worked on a particular matter are not ever allowed to work for a workforce service contractor?

**A:** No. A workforce service contractor is not prohibited from hiring a former Board employee who worked on a particular matter—as long as the former Board employee does not work on that particular matter when working for the same Board's workforce service contractor.

The term "particular matter" is defined narrowly to mean something quite specific, such as an investigation, application, contract, rule-making, or other administrative proceeding.

This means a person subject to the particular matter restriction may work on matters similar to matters the individual worked on as a Board employee, but not work on exactly the same matter. For example, a former Board employee who worked on contract X at the Board could not leave the Board and work on the same contract X for the workforce service contractor. The former Board employee could, however, work on contract Z, even if contract Z involved similar issues as those raised in connection with contract X.

**Q:** Is an individual's brother, sister, brother-in-law, or sister-in-law included as a relative in determining if the individual has a "substantial financial interest" in the business entity?

**A:** No. The rules define substantial financial interest to include the "first degree of consanguinity or affinity," which means only the individual's parents and children, adopted children, or spouse.

#### **Section 801.53. Prohibition against Directly Delivering Services**

State law clearly prohibits Boards, Board members and Board staff from delivering workforce services. Section 2308.264(a) prohibits Boards from directly delivering services. During the 78<sup>th</sup> Texas Legislature, Regular Session, lawmakers expanded this prohibition in SB 280 (codified in §2308.267(b) of the Texas Government Code) by requiring that a Board's employees be separate from and independent of any organization providing workforce services in the Board's local workforce development area (workforce area). It also prohibits a Board's employees from directing or controlling the daily activities and operations of a workforce service contractor. SB 280 also required the Commission to develop rules to ensure that if a Board acts as a fiscal agent for a workforce service contractor, the Board does not deliver services or determine eligibility for those services. Not only did the Legislature clearly indicate that Boards and their employees shall not deliver services or control their workforce service contractors and their employees, but SB 280 also included an additional provision requiring the Commission to establish rules that prevent potential conflicts of interest between Boards and their workforce service contractors.

Subsection 801.53(a) is created in order to implement SB 280, which directed the Commission to develop rules that prevent potential conflicts of interest between Boards and entities that contract with Boards. This subsection stipulates that a Board member; a Board member's business, organization, or institution; a business, organization, or institution that a Board member represents; or a Board employee shall not receive a contract from the Board to deliver workforce services. Boards shall also ensure that a Board member; a Board member's business, organization, or institution; a business, organization, or institution that a Board member represents; or a Board employee do not directly deliver workforce services or determine eligibility for workforce services. With this subsection, the Commission intends to prevent potential conflicts of interest between Boards and workforce services contractors.

Subsection 801.53(b) stipulates that the prohibitions in §801.53 do not apply to public education agencies, such as community colleges and independent school districts, that have Board members, former Board members, or former Board employees who fulfill the requirements set forth in Texas Government Code §2308.256(a)(3)(A) – education agency representatives.

Subsection 801.53(c) is created to allow a Board to grant a one-year exception to the prohibitions in §801.53(a) for a community-based organization that fulfills the requirements set forth in Texas Government Code §2308.256(a)(2). The exception can only be granted by a two-thirds vote of the Board in an open meeting. The exception may not be granted for a contract to operate a Texas Workforce Center. It is the intent of the Commission that this exception be provided for a special project that may require the specialized services of one community-based organization that also has a member on the Board. The exception may be provided for up to one year to allow for completion of the special project. It is not the Commission's intent that the same exception be applied across multiple years.

Subsection 801.53(d) is created in order to implement SB 280 (codified in §2308.267(b) of the Texas Government Code) that prohibits a Board and its employees from directing or controlling the employees of any entity providing contracted workforce services. Subsection 801.53(d) directs Boards to ensure that the Board, Board members, and Board employees do not directly control the daily activities and operations of its workforce service contractors. This subsection stipulates that the Commission may use the guidelines established in 40 T.A.C. §821.5, Employment Status: Employee or Independent Contractor, in order to test the employment status

of the workforce service contractor. These guidelines are commonly referred to as the "20-point test."

The 20-point test applies to all 400,000 Texas businesses; therefore, it should apply to Boards and Board contractors as well. The Commission does not intend to prohibit Boards from utilizing any specific management model when contracting for the delivery of workforce services. In fact, Texas Government Code Chapter 2308 prohibits the Commission from requiring Boards to use a specific management model for the provision of workforce services. However, Boards should avoid creating contract provisions that could be construed to effectively make the contractor or the contractor's staff employees of the Board. The Texas workforce system may be a unique service delivery model in which Boards contract with service providers to deliver specific workforce services based on state and federal regulations and guidelines. As a contractor of services, however, Boards should strive to meet the 20-point test in determining employment status of workforce service contractors and their employees.

The Commission emphasizes to the Boards that they examine the totality of the 20-point test to ensure they are not acting as employers of contract staff. They may not meet some of the points, but as 40 T.A.C. §821.5 states: "the importance assigned each factor may vary depending on the occupation or on the facts of that particular case." Furthermore, "if an employment relationship exists, it is of no consequence that the employee happens to be called something else, such as: partner, agent, co-adventurer, contractor laborer, subcontractor, or independent contractor." Most importantly, Boards, through their contract management and oversight, must ensure that contracts are not written to give Board staff the right to control or direct contractor staff. It is the totality of the 20-point test that must be considered in determining whether an employment relationship exists between a Board and its workforce service contractor or, for that matter, between the Commission and a Board. There are many factors involved in the relationship between a worker and the recipient of the worker's services. Some of those factors may suggest an independent contractual relationship while others may suggest an employer-employee relationship. All of the facts must be carefully considered when deciding whether the recipient of the services has the right to control or direct the worker's daily activities.

Subsection 801.53(e) is created to clarify that the provisions in this section do not restrict Board members or Board members' organizations from receiving services from the Texas workforce system and thereby being customers of a Board's workforce service contractors' services. In fact, the Commission trusts that Board members will champion the Texas workforce system by actively using the system to meet their employment and workforce needs.

### **Questions and Answers:**

**Q:** Does the §801.53 prohibition against directly delivering services prohibit a child care provider, or someone affiliated with a child care provider that is part of the child care management system, from sitting on a Board?

**A:** Not necessarily. If the child care representative does not contract directly with the Board as its child care contractor or for other workforce services, then the person may be a Board member. If the Board member is a child care provider that accepts Agency-subsidized children, then the child care provider may sit on the Board. The important distinction is in the contractual relationship. If the Board member is a direct contractor of the Board, then the individual shall

not sit on the Board. If the Board member is a contractor of the Board's workforce service contractor, then the individual may sit on the Board.

**Q:** In rural communities, a Board member may own the only retail store in town that processes gas and work-related expense vouchers for Choices clients. Are these activities affected by the prohibition against a Board contracting with Board members' businesses for workforce services?

**A:** No. Processing a voucher is not a contractual relationship between a Board member and a contractor. This example would not fall under the prohibition to deliver services, because in this case the Board member is not determining eligibility or delivering services. The contractor issuing the voucher is determining eligibility and providing the service. If the client takes the voucher and processes it at a Board member's business, that would not be prohibited under the rules because processing the voucher is not a contractual activity with the Board. If, however, the Board contracts with the Board member's business to process vouchers, that activity would be prohibited by the rules. In most workforce areas, a Board's workforce service contractor contracts with an entity to provide services. Because the service provider is not directly contracting with the Board, the service provider could serve as a Board member, which would be allowed under the rules.

**Q:** Would a private sector Board member whose business is part of a consortium that receives customized or other training—whether from WIA Statewide Activity Funds, Skills Development or Self-Sufficiency Funds, or H1B Skills grants—need to resign from the Board?

**A:** If the contract is with the state and not the Board, the Board member would not have to resign as it would not violate the prohibition against a Board contracting with a Board member or a Board member's business.

In cases in which the Board contracts directly with the consortium to provide services, the Board member's company that is participating in the consortium must not have signature authority for the consortium. Section §801.53(e) emphasizes that the rules do not restrict a Board member or a Board member's business from receiving workforce services and being a customer of a Board's workforce service contractors' services. Even though Boards are not allowed to contract directly with a Board member or a Board member's business, in most cases, members of a consortium receive workforce services from a provider under contract with the Board's workforce service contractor. Typically, Boards do not contract directly with the businesses in the consortium.

**Q:** Can a Board member's company receive on-the-job (OJT) training funds from the Board?

**A:** A Board cannot contract with a Board member or a Board member's company to provide workforce services. The Commission strongly encourages private sector Board members to use workforce services. OJT is a special case in which the company is both the provider and user of workforce services. Again, the answer depends on the Board's contractual relationship with the Board member's company. If the Board awards OJT funds directly to a company, then a Board member's company is not allowed to receive the OJT funds unless the Board member resigns. If the workforce service contractor contracts with the company for OJT funds, then the Board member's company is allowed to receive OJT funds.

**Q:** Is a Board allowed to provide apprenticeship training funds to a labor union if a Board member represents that union on the Board?

**A:** The union is allowed to receive the funds if the apprenticeship funds are provided to the labor union under contract with the workforce service contractor.

**Q:** Does a Board labor representative who also sits on an apprenticeship advisory committee have to resign from the Board in order for the committee to receive apprenticeship training funds from the Board?

**A:** No. The apprenticeship advisory committee can receive the funds and the Board member does not have to resign as long as the Board member does not represent the advisory committee on the Board.

**Q:** If a Board receives other workforce funding from its local community, is the prohibition against directly delivering services still in place?

**A:** Yes. Boards have always been prohibited by law from delivering workforce services, regardless of the funding source.

**Q:** Why do the rules reference the 20-point test as a tool the Agency may use to determine if a Board directly controls the daily activities of its workforce service contractors?

**A:** The use of the 20-point test is a standard, common-law test that has been used for more than 30 years by the Internal Revenue Service, courts of law, and the Agency to determine if an employer-employee relationship exists. Even if the rules did not specifically reference the 20-point test, the test would still be used by courts to determine whether an employer-employee relationship exists. This test is applied to all Texas businesses and may be applied to Boards as well. The 20-point test is referenced in the rules as a permissible—not mandatory—model that the Commission could use to determine an employer-employee relationship between a Board and its contractor.

**Q:** How can the 20-point test be used as a tool to ensure that Boards do not directly deliver services?

**A:** The 20-point test is a standard tool that may be used to determine if the Board-contractor relationship is an employer-employee relationship or an independent contractor relationship. Boards should review each point in the test and determine how they can maintain an arm's-length relationship with the contractor. Boards need to examine the totality of the test and develop operational procedures that will not directly control the day-to-day activities and operations of the contractor.

**Q:** Will the 20-point test effectively prohibit the use of a PEO model?

**A:** No. The proposed rules are meant to fulfill the intent of SB 280, which states that Boards may not direct or control the staffing of any entity that provides one-stop workforce services. Furthermore, Texas Government Code §2308.267(b) stipulates that a Board's staff shall be separate and independent of any organization providing workforce services. The rules do not

prohibit Boards from using a particular management model—unless that management model allows Board staff to direct or control the staffing of the workforce service provider or infringe upon the separation and independence of the workforce service contractor.

**Q:** One element of the 20-point test states that independent contractors normally pay all of their own business and travel expenses without reimbursement. If a Board reimburses a contractor for travel expenses, can this be construed as an employer-employee relationship?

**A:** Boards are encouraged to examine all of their contracting policies, procedures, and guidelines in light of the 20-point test. In this situation, because it is not a federal or state requirement that Boards directly reimburse a contractor for travel expenses, Boards should refrain from doing so. Boards shall require that travel expenses meet the state guidelines in accordance with the TWC Financial Manual for Grants and Contracts, but they should refrain from directly reimbursing a contractor for travel expenses.

#### Section 801.54. Board Contracting Guidelines

Section 801.54 is created in order to implement provisions in SB 280 (codified in §2308.264(e)(1)) requiring the Commission to develop rules to ensure that each workforce service contractor "has sufficient insurance, bonding, and liability coverage for the overall financial security of one-stop workforce services funds and operations." In implementing this provision, the Commission establishes guidelines that the Boards shall follow to routinely assess the fiscal integrity of their workforce service contractors. The Commission also establishes minimum bonding amounts and other methods Boards may use to secure funds to cover losses.

Subsection 801.54(a) requires Boards to develop a fiscal integrity evaluation designed to assess the fiscal integrity and stability of their workforce service contractors. The fiscal integrity evaluation shall include provisions to ensure that workforce contractors are meeting performance measures in compliance with federal and state statutes, regulations and directives; Office of Management and Budget (OMB) circulars; and other safeguards a Board has identified to ensure the proper and effective use of funds. The fiscal integrity evaluation shall also include a review of the contractor's most recent three-year financial history as well as a review of any adverse judgments or findings.

Boards shall use the fiscal integrity evaluation in order to verify fiscal indicators prior to the award of the contract and at each renewal of the contract. For contracts between \$100,000 and \$500,000, the review must be prior to the award and at each contract renewal, and not less than biennially. For contracts over \$500,000, the review must be prior to the award and at each contract renewal, and not less than annually. Boards are also required to use this schedule to ensure that workforce service contractors have proper and valid bonding and protections for funds.

The Commission establishes §801.54(b) to implement the requirement of §2308.264(e)(1) that contractors have sufficient protection for the "overall financial security" of workforce funds and operations. Subsection 801.54(b) establishes bonding, insurance and other methods of securing funds to cover losses. The Commission requires Boards to ensure that at least 10% of the funds subject to the control of the Boards' workforce service contractors be protected through bonds, insurance, escrow accounts, cash on deposit, or other methods. The subsection allows Boards to

pay for the protection directly or to require their contractors to pay for the protection, to the extent allowable under state and federal law.

For Fiscal Year 2004 adhering to existing bonding requirements, the Boards secured, on average, 7.6% of their total allocated funds. Six of the 28 Boards secured over 10%, six secured less than 5%, and 16 secured between 5% and 10% of their total funds. Overall, 6.6% of the 28 Boards' total allocated funds are bonded or otherwise protected by the Boards. Assuming that 80% of the total allocated funds are under the control of workforce service contractors, the Boards' current bonded amounts represent 8% of the total funds under the control of workforce service contractors. Therefore, the 10% minimum set forth in §801.54(b) will not create an undue burden on the Boards because it does not require that 10% of the entire allocation be secured, but only 10% of the amount under the control of the workforce service contractors. In addition, the Commission has confirmed that the Boards' existing crime and theft bonds may be amended to include errors and omissions.

Subsection 801.54(c) establishes standards of conduct for workforce service contractors in order to further implement the intent of SB 280 as codified in Texas Government Code §2308.264(e)(2) that requires the Commission to establish rules to prevent potential conflicts of interest between a Board and its workforce service contractor.

Boards shall ensure that their contractors comply with federal and state statutes regarding standards of conduct. Boards must also ensure that contractors avoid any conflict of interest or the appearance of a conflict interest as well as refrain from using non-public information gained through a relationship with the Commission, an Agency employee, a Board, or a Board employee to seek financial gain that would be a conflict of interest or an appearance of a conflict of interest.

Subsection 801.54(d) requires a Board's contractor to disclose any conflict of interest and any appearance of a conflict of interest or the absence of any conflict and any appearance of a conflict interest. Workforce service contractors must disclose annually any substantial financial interest that the contractor or its employees in decision-making positions have in any business transaction with a Board member or Board decision-making employee. Contractors must disclose gifts greater than \$50 in value provided to a Board member or Board decision-making employee by the workforce service contractor or a contractor decision-making employee. The gifts must be disclosed within 10 days. The disclosures must describe the conflict of interest or the appearance of a conflict of interest as well as actions the contractor and its employees will take to avoid any conflict of interest.

### **Questions and Answers:**

**Q:** How far up the corporate chain is a Board required to review for the three-year financial history of adverse judgments and findings of a contractor?

**A:** It depends on what entity signed the contract. If the contract is in the name of the larger corporate entity only and the Board typically deals with one division instead of the entire corporation, then the review must be of the entire corporation's history of adverse judgments or findings. The thoroughness of the review may be more in depth for the division that is more closely related to the type of services that are contracted and less in depth for the unrelated

divisions of the corporation. While adverse judgments or findings of a specific division may have a higher relevance to the ability of the contractor to perform under the Board's contract, the stability of the larger corporation is important. The key language is "review and consider." The amount of time spent reviewing and considering is up to the Board and may vary depending on the Board's assessment of the relevance of the adverse judgments or findings.

**Q:** May a Board withhold a portion of a payment to a workforce service contractor and place this amount in escrow until a future period? The amount will be reported as contractor payments on IRS Form 1099 when initially paid to the contractor—not when released from escrow. Will this be viewed as establishing a contingency fund, which is not allowed under OMB Circular A-122?

**A:** OMB Circular A-122, Attachment B, Item 8, does not prohibit a reserve of funds as described above. The term "contingency reserve," as used in OMB Circular A-122, refers to a reserve of funds that is drawn down, set aside, and not expended unless the contingency for which the reserve was established occurs. In contrast, this scenario is more akin to the concept of retainage, in that the funds the Board would be withholding from its contractor would be a portion of the contractor's reimbursement for allowable expenditures that it incurred. The contractor would only receive the withheld funds, if at the end of the contract the contractor met specific provisions outlined in the contract—i.e., no losses occurred.

**Q:** Many rural Board members in the private sector are also that community's banker who makes loans to our contractor, contractor's staff, and the community at large. Will these rules prohibit a Board member from providing loans to a contractor or contractor's staff?

**A:** Nothing in the rules prevents Board members or workforce service contractors from conducting normal business activities within the community. In fact, §801.54(d)(1)(E) specifically states that the disclosure provision does not apply to a transaction or benefit provided to a Board member or a Board employee under the same terms and conditions provided to members of the general public.

**Q:** If a workforce service contractor employee in a decision-making position sells his car to a Board member, is the workforce service contractor required to report this transaction?

**A:** If the transaction is offered to a Board member or a Board employee under the same terms and conditions provided to members of the general public, then the contractor does not have to disclose the transaction. Normal business transactions should include a good faith offer to the general public and not be offered exclusively to Board employees or Board members, and the sale should be genuinely open to the public. The sale of the car should not appear to be a preferential arrangement provided to a Board member or employee on the basis of the Board member's or Board employee's position. These normal business transactions do not have to be reported by the workforce service contractor. The Commission recognizes that there are situations in which individuals sell personal items exclusively to friends and acquaintances and do not make the sale open to the public. If a workforce contractor conducts such a business transaction with a Board member, then that transaction must be reported. The intent of the rule is not to prohibit such transactions, but to make the transactions transparent to the public in order to show that contracts are awarded on the basis of cost and quality, not on personal relationships and favors provided to Board members.

**Q:** Would a workforce service contractor or its employee in a decision-making position have to report a contract with a Board member to paint the Board member's house?

**A:** Again, nothing in the rules prevents Board members or workforce service contractors from conducting normal business activities within the community. The workforce service employee would not be required to report this transaction as long as the business (painting the house) is available to the general public. The Commission recognizes that there are personal relationships and long-standing friendships between Board employees and workforce service contractor staff. In many of these friendships, services of value may be performed exclusively for friends and at a much reduced price. If a workforce service contractor conducts such a business transaction with a Board member, then that transaction must be reported. The intent of the rule is not to prohibit such transactions, but to make the transactions transparent to the public in order to show that contracts are awarded on the basis of cost and quality, not on personal relationships and favors provided to Board members.

**Q:** Would a gift of a briefcase or portfolio from a workforce service contractor to a Board member or Board employee need to be reported by a contractor or contractor's employee under the disclosure rules?

**A:** No—if the value of the portfolio is \$50 or less. Yes—if the value is over \$50.

**Q:** Would a Board member have to resign from the Board if the member's son or daughter worked for a Board contractor?

**A:** No. Under §801.13, the Board member must disclose such a relationship. There is no provision in either §801.13 or §801.54 that would disallow a Board member from sitting on the Board or a contractor from receiving a contract if the Board member's son or daughter worked for the contractor.

*Section 801.55. Employment of Former Board Employees by Workforce Service Contractors*

The Commission creates §801.55 in order to establish guidelines for the Boards and workforce service contractors to follow when the contractors hire former Board employees. The intent of this section is to implement provisions in SB 280 requiring the Commission to establish rules to "prevent potential conflicts of interest between boards and entities that contract with boards...." The Commission establishes the provisions in §801.55 in order to establish high ethical standards of conduct and assure the public that hiring standards and practices are fair, aboveboard, open, and free of the appearance of favoritism. Additionally, 29 CFR Section 97.36(b)(3) applies to the Agency as the "grantee" and the Boards and their contractors as "subgrantees" and sets forth the following: "Grantees and subgrantees will maintain a written code of standards of conduct governing the performance of their employees engaged in the award and administration of contracts. No employee, officer or agent of the grantee or subgrantee shall participate in the selection, or in the award or administration of a contract supported by Federal funds if a conflict of interest, real or apparent, would be involved." 29 CFR Section 97.36(b)(3) continues to provide that "such a conflict would arise when (i) the employee, officer, or agent; (ii) any member of his immediate family; (iii) his or her partner; or (iv) an organization which employs, or is about to employ, any of the above, has a financial or

other interest in the firm selected for award. The grantee's or subgrantee's officers, employees, or agents will neither solicit nor accept gratuities, favors, or anything of monetary value from contractors, potential contractors, or parties to subagreements."

Subsection 801.55(a) establishes a post-employment restriction on workforce service contractors employing or compensating a former Board employee who was in a decision-making position with the Board during the 12 months prior to the date of employment with or compensation by the workforce service contractor. The restriction only applies to intra-Board area employment, not inter-Board area employment. It is not the intent of the Commission to restrict a former decision-making Board employee from working for a workforce service contractor in another Board's workforce area.

Subsection 801.55(b) sets forth the process the Board shall use in granting exceptions to the post-employment restriction when no conflict of interest exists. A Board in an open meeting may provide for an exception to the post-employment restriction by a two-thirds vote of the membership present. In providing an exception, the Board shall assess all relevant factors, including but not limited to, whether there is a critical need for the skills involved, the relative cost and availability of alternatives, and the need to protect the integrity and stability of the Texas workforce system. In such an instance, the Board shall impose whatever terms and conditions it deems necessary to mitigate the appearance of a conflict of interest. The Commission establishes the exception procedures in order to provide flexibility for former Board employees and workforce service contractors, while also creating an open process to prevent potential conflicts of interest.

Subsection 801.55(c) stipulates that Boards, in their contracts with workforce service contractors, require the contractors to comply with the post-employment restriction. Contracts shall also contain effective enforcement mechanisms that allow corrective actions, up to and including contract termination, for violating this section.

Subsection 801.56(d) establishes restrictions and guidelines for workforce service contractors to follow in hiring former Board employees who worked on a "particular matter" when employed with the Board. The Commission intends that the particular matter provisions affect all Board employees. The Commission believes that while Boards are quasi-governmental entities, the fact that Boards are stewards of the public's money is reason enough to apply the lifetime ban from working on particular matters to former Board employees. The Commission, however, reasons that the definition of a particular matter is so specific and narrow that for all intents and purposes, only Board employees who are in decision-making positions will be affected. It is important to note, however, that a workforce service contractor is not prohibited from hiring a former Board employee as long as the former Board employee does not work on that particular matter when working for the Board's workforce service contractor.

### **Questions and Answers:**

**Q:** Do the rules regarding employment of former Board employees apply if a Board wants to hire a former workforce service contractor staff member?

**A:** No. The post-employment restriction only applies to movement from a Board to a workforce service contractor. The post-employment restriction follows the contract relationship.

Section 801.56. Enforcement

Section 801.56 provides that the Commission may impose corrective actions, including sanctions, if the Board fails to adhere to the provisions in this subchapter.

**PART III. COORDINATION ACTIVITIES**

The Commission engaged interested entities as follows:

\*On September 30, 2003, the Commission considered the methods of developing the rules, including negotiated rule making. The Commission selected a method that would afford the greatest amount of flexibility for interchange and dialogue. The Commission directed staff to convene a work group composed of Boards, Boards' workforce service contractors, and any interested persons to develop draft rules for consideration by the Commission.

\*On October 8, 2003, the Commission published notice of the work session of October 16, 2003, on the Texas Register Web site. In addition, individual invitations were mailed to all Board chairs and executive directors, which included members of the Texas Association of Workforce Boards' Policy Committee and the members of the Local Workforce Development Board Advisory Committee. Invitations were also sent to Board contractors that, at the time, used the managing director model. The notice was also sent to other interested contractors.

\*On October 13, 2003, instructions were sent to all Boards to encourage participation by Internet and teleconference in the October 16, 2003, work session.

\*On October 15, 2003, the Commission commenced the use of the Internet Web page for rule development documents, information, timelines, resource materials, and as a forum for posting suggestions and feedback from workgroup members.

\*On October 16, 2003, the Commission held the first posted work session at which interested individuals participated in person, by telephone, and over the Internet through the use of Live Meeting software that was made available through remote sites at Board locations around the state. At the work session the participants discussed concepts and basic principles to be included in the rule language. Those present in person included Board chairs, members and executive directors, Board contractors, and legislative staff. In addition, chief elected officials, Board chairs, members and executive directors, as well as Board staff, participated by Internet and teleconference.

\*On November 13, 2003, draft language was circulated to interested participants with a reminder of the next day's work session.

\*On November 14, 2003, the Commission held the second work session using the same multimedia approach to maximize participation. The work group participants discussed in detail the language of the draft rules and were requested to submit any further suggestions in writing over the next three weeks.

\*On December 14, 2003, a revised draft was circulated to the work group and interested parties that reflected materials to be presented to the Commission for possible proposal on December 23, 2003. Work group participants were requested to provide feedback.

\*On December 18, 2003, the final draft of the rules resulting from the feedback was circulated to the Commission for consideration on December 23, 2003.

\*On December 23, 2003, the Commission voted to propose the rules with some amendments from staff resulting from continued feedback from work group members and specific decision points by the Commission.

<p>\*On January 9, 2004, the rules were published for public comment in the *Texas Register*.

\*On February 9, 2004, the public comment period ended.

\*On February 17, 2004, the Commission met with the Local Workforce Development Board Advisory Committee. At the work session, Donna Davidson, ethics advisor, presented information regarding public perceptions of public servants when a conflict of interest or the appearance of a conflict of interest exists. The Commission and the Advisory Committee reviewed the proposed rules and Advisory Committee members discussed the content of the proposed rules with the Commission. Agency staff, Board members, and Board staff attended the work session as did an Assistant District Attorney for Travis County. The work session was broadcast over the Internet so Board members and staff and other interested individuals, who were unable to attend in person, could benefit and learn from the presentation and discussion.

\*On March 16, 2004, the Commission approved language revisions and circulated the revised rules to the Boards to review and comment by March 24, 2004.

The work group sessions were attended by a number of representatives from both public and private entities, including nonprofit and for-profit contractors. Sessions were also attended by entities that represent various Board contracting structures. The participants provided written and verbal feedback in person and via teleconferences throughout the development of the rules. The public was also able to monitor the rule development as rule development materials were posted on the Commission's Web page. The Web page served as a clearinghouse for information on the rules' development. The work sessions involved discussions of each of the individual provisions of the proposed rules.

#### **PART IV. PUBLIC COMMENTS AND RESPONSES**

Public comments were received from the following:

State Elected Officials: Senator Ken Armbrister; Representative Jim McReynolds, Representative Elliott Naishtat, Representative Larry Phillips, and Representative Gene Seaman.

Chief Elected Officials: Gary B. Streit, Wilbarger County Judge; John D. Shavor, Cottle County Judge; Charlie Bell, Foard County Judge; Stanley H. Peavy, III, Young County Judge; Kenneth Liggett, Clay County Judge; John Hull, Coryell County Judge; and James O. Kittrell, Montague County Judge.

The Local Workforce Development Board Advisory Committee.

Local Workforce Development Boards: Alamo Workforce Development Board; Brazos Valley Workforce Development Board; Capital Area Workforce Development Board; Central Texas Workforce Development Board; Coastal Bend Workforce Development Board; Dallas Workforce Development Board; Deep East Texas Workforce Development Board; East Texas Workforce Development Board; Golden Crescent Workforce Development Board; Lower Rio

Grande Valley Workforce Development Board; Middle Rio Grande Workforce Development Board; North East Texas Workforce Development Board; North Central Texas Workforce Development Board; North Texas Workforce Development Board; Permian Basin Workforce Development Board; South Plains Workforce Development Board; Tarrant County Workforce Development Board; Texoma Workforce Development Board; West Central Texas Workforce Development Board.

Board Members: Ken Tritton, North Texas Workforce Development Board; and Sam Vale, Lower Rio Grande Valley Workforce Development Board.

Texas Association of Workforce Boards' Policy Committee.

Mike Allen, President and CEO of the McAllen Economic Development Corp; Sylvia R. Hatton, Region One Education Service Center; Mike Gross, Texas State Employees Union/CWA 6186.

Some commenters supported the rules, some disagreed with the rules, and some made recommendations for changes to the proposed language. The following comment summaries reference the proposed rule sections; the Commission responses reference the adopted rule sections. The comment summaries and responses are as follows:

*Proposed Rule Preamble, Part III. Impact Statements*

**Comment:** The commenter stated that the impact statements appear to be inaccurate and ignore the additional costs associated with enforcing and administering the new rules as proposed.

**Response:** The Commission has reviewed the impact statements and believes that the statements are accurate and that there are no additional estimated costs as a result of enforcing and administering this rule.

*Subchapter C. Proposed Board Contracting Guidelines*

**Comment:** Six commenters agreed with the proposed rules entirely and their intent to prevent any potential conflict of interest between Boards and entities that contract with Boards. One of the commenters stated that the rules show a commitment to making strides in restoring and establishing corporate integrity and credibility. One commenter strongly supported the Commission's efforts to develop rules in accordance with SB 280, even if the rules require Board members either to resign from the Board or terminate existing contracts with the Board. The commenter encouraged the Commission to ensure that the final rules include sufficient guidance and minimum requirements to protect workforce areas from any real or perceived conflict of interest. Another commenter commended the Commission for taking seriously the Legislature's charge of developing contracting guidelines that include strong ethics provisions that limit any conflict of interest. The commenter stated that it is important for those responsible for spending taxpayer dollars to ensure that those dollars are spent wisely and that there is no appearance of impropriety or self-dealing.

**Response:** The Commission agrees and appreciates the comments.

**Comment:** One commenter expressed appreciation for the Commission's acknowledgment in the preamble of the Boards' successes in managing programs and thereby virtually eliminating disallowed costs, and the Boards' good local business practices.

**Response:** The Commission agrees and recognizes the accomplishments of the Boards. It is important to note, however, that these rules were not developed because of any inability or failure of the Boards in managing the delivery of workforce services. The rules were developed to ensure the continued integrity of the Texas workforce system by removing the potential for any conflict of interest or any appearance of a conflict of interest between Boards and their workforce service contractors.

**Comment:** Two commenters appreciated the opportunity to comment and the Commission's involvement of Boards in the development process of the proposed guidelines. The Commission's open process to develop the rules was applauded, and the commenters encouraged the Commission to continue this process in future rule making.

**Response:** The Commission is encouraged by the level of participation in the development of these rules.

**Comment:** One commenter requested that the Commission develop and institute new rules and policies to disallow people with apparent conflicts of interest from becoming Board members.

**Response:** The Commission appreciates the comment and believes that the adopted rules remove the potential for any conflict of interest among Board members by prohibiting them from contracting with the Board on which they serve.

#### §801.51. Purpose and General Provisions

**Comment:** One commenter stated that proposed §801.51(b) appears to apply only to the "workforce service providers that deliver one-stop services." Yet, proposed §801.51(a) appears to apply to workforce service providers, which include contractors for child care services or individual programs such as WIA Youth services, because they provide services to enhance one-stop services. It is difficult to have different contracting rules for each type of service provider for the programs that are implemented by the Boards. The commenter requested that a definition be developed to better clarify that these rules apply to all workforce contractors.

**Response:** While the definition of "workforce service providers that deliver one-stop services" includes contractors for child care services as well as WIA Youth services, the Commission agrees that the reference to one-stops in the rule language is unclear and could be misinterpreted. Therefore, the references to one-stop services have been deleted and replaced with a Board's workforce service contractors, and the definition references §801.28, which lists all workforce services.

#### §801.53 Prohibition against Directly Delivering Services

**Comment:** One commenter stated that as a Board member and a contractor, the commenter always felt it was a conflict of interest to sit on the Board and receive vendor contracts, and thus

resigned from the Board. The commenter expressed a strong belief that Board members should not be involved in matters that can be misconstrued as a conflict of interest.

**Response:** The Commission agrees and appreciates the comment.

**Comment:** Two commenters questioned whether the proposed §801.53 will apply retroactively and, if so, whether Boards and contractors will be required to cancel current contracts or will the Board member be required to resign immediately. The commenter also asked if Boards will have the option to renew current contracts and maintain the Board member or will the Board member be forced to resign prior to renewal. The commenter also questioned if Boards will be required to terminate the contract if the Board member does not resign.

**Response:** The Commission does not apply rules retroactively. The Commission does not intend to cause a Board to become noncompliant with Board membership requirements; therefore, the Commission has determined that Boards shall comply with Subchapter C no later than the earliest of the following:

1. the expiration of the contract;
2. the renewal of the contract;
3. the expiration of the Board member's term or the Board member's resignation; or
4. September 1, 2005.

**Comment:** One commenter stated that proposed §801.53 could reduce the availability of qualified candidates, thus reducing the pool of eligible appointees, and many Board members may resign. This could result in Boards being noncompliant with membership requirements while vacancies are filled.

**Response:** The Commission disagrees that the provisions in Subchapter C will reduce the number of qualified candidates for Board membership. In fact, the Commission contends that, as provided in Subchapter C, if the perception of any conflict of interest is removed, the Texas workforce system will gain and maintain the public's trust, and the pool of eligible Board member appointees and potential workforce service contractors will increase.

**Comment:** Two commenters objected to the proposed rules prohibiting service delivery by Boards because they make no express provision for a waiver as authorized in Texas Government Code §2308.264. The commenters contended that although the SB 280 amendments continue to recognize the appropriateness of waivers, the Commission has not made any effort to reevaluate its waiver rules in conjunction with the development of Subchapter C.

**Response:** The Commission believes that the adopted Subchapter C allows for exceptions, as well as the development of individual Board policies, procedures, and financial integrity indicators. Due to the time line specified in SB 280, the Commission believes it prudent to first address the provisions in §2308.264(e). The Commission plans to address the waivers referenced in §2308.264(b) and (c), Texas Government Code, as amended, when it amends 40 T.A.C. Chapter 801 during the 2004–2005 biennium.

**Comment:** One commenter stated that existing Texas Government Code §2308.257 calls for recusal of any Board member from voting or participation in a decision to avoid the appearance of a conflict of interest.

**Response:** The Commission does not agree that a Board member's recusal from voting or participating in a decision regarding the award of a workforce service contract prevents the perception that the Board member has an advantage in the contracting process simply because of Board membership. The perception may still exist that other Board members will award the contract in return for an affirmative consideration on a contract in which they have an interest. It is important to note that the Commission does not, in any way, imply that this practice is occurring. By adopting this rule, however, the Commission and the Boards will assure the public that all potential workforce service contractors have a fair opportunity to compete for contracts.

**Comment:** One commenter stated that the rule limits local Board control and potentially inhibits the competitive bidding process.

**Response:** The Commission disagrees that the rule potentially inhibits the competitive bidding process. In fact, the Commission expects the rule to strengthen the competitive bidding process because the perception that Board members and Board members' organizations have a competitive advantage in the bidding process is now without reason.

**Comment:** One commenter questioned whether the rules prohibit Boards from making payments for supportive services, needs-related payments, and child care.

**Response:** Subchapter C prohibits a Board from directly providing workforce services, which include support services such as child care and transportation. However, a Board may make payments to its workforce service contractors if the Board is acting as its own fiscal agent.

**Comment:** One commenter stated that the term "one-stop workforce services" as defined in the proposed rules includes training and other services, as well as core and intensive services. Given this definition and depending on what is meant by "persons do not directly deliver," there is potential to wipe out the Board members.

**Response:** The Commission is deeply concerned about the statement that Board members will be wiped out if this provision is implemented, as it implies that the majority of the Board's members presently have workforce service contracts with the Board. This is precisely the reason Texas Government Code §2308.264(e)(2) was developed—to avoid the perception that only Board members receive workforce service contracts. The section states that the Commission's contracting guidelines should "prevent potential conflicts of interest between boards and entities that contract with boards." By implementing Subchapter C, the public can be assured that taxpayer money is awarded to entities based solely on the quality and the cost of the services—not Board membership.

**Comment:** Two commenters stated that the community college has a representative on the Board and is also a provider of services, and several community-based organizations on the Board also have small contracts for specialized services. The proposed rule language would restrict the ability of Boards to fill required Board membership from educational agencies.

**Response:** The Commission understands the commenters' concern regarding community colleges. To ensure that Boards are able to comply with membership requirements, the Commission has modified the rule as follows: public education agencies, such as community colleges and independent school districts, that have Board members, former Board members, or former Board employees who are serving as the required educational agency representative on the Board, may bid and be awarded workforce service contracts. The Commission has also modified the proposed rule to allow Boards to grant a one-year exception in order for a community-based organization represented on the Board to receive a contract for special projects.

**Comment:** One commenter stated that the language "all programs and activities administered by Texas Workforce Center Partners" would prohibit required Board members from serving on the Board. In addition, no private sector Board member could be actively involved in the Board's workforce programs in these areas.

**Response:** The Commission disagrees. Subchapter C does not prohibit Board members from using workforce services. In fact, the Commission trusts that Board members will champion the Texas workforce system throughout the state by actively using the system to meet their employment and workforce needs. The Commission has established §801.53(e) to clarify that the provisions in this section do not restrict Board members, or Board members' organizations, from using the Texas workforce system, and thereby being a customer of a Board's workforce service contractors' services.

**Comment:** One commenter stated that the proposed §801.56 references §821.5, which states that the Commission may use the 20-point test for independent contractors. The commenter stated that as applied to Board contractors, it is doubtful any Board contractor would pass this test. Boards contract with the Commission to manage funds and meet performance measures while overseeing local service delivery. The Commission holds the Boards accountable, not the contractors. The commenter believes that the reference to §821.5 is not appropriate.

**Response:** The Commission disagrees. The guidelines established in §821.5, Employment Status: Employee or Independent Contractor, are the official guidelines the Commission uses to determine if an employer-employee relationship exists when hearing Unemployment Insurance appeals. The 20-point test applies to all 400,000 Texas businesses; therefore, the content also applies to the Boards. Furthermore, a court of law will likely use the 20-point test to determine if a Board has violated the provision in the proposed §801.56 (adopted §801.53) that prohibits Boards from delivering workforce services and determining eligibility for those services. The Commission emphasizes that Boards examine the totality of the 20-point test to ensure they are not acting as the employers of their workforce service contractors or their contractors' staff. Boards may not meet some of the points, but, as §821.5 states: "the importance assigned each factor may vary depending on the occupation or on the facts of that particular case."

**Comment:** One commenter recommended eliminating the third and fourth sentences of proposed §801.56(a) to reflect only the legal prohibitions of a Board directly providing services.

**Response:** The Commission agrees with this suggestion and has deleted the referenced sentences as the information is already addressed in §821.5.

**Comment:** One commenter objected to referencing or imposing the factors for testing employment status set out in 40 T.A.C §821.5, as referenced in proposed §801.56. The factor analysis is flawed considering that many circumstances upon which to apply the factors are predetermined and outside the control of the contracting parties. For example, factors such as "what are the hours of operation" or "whether it is a long term or short term contract" would always be determined to be in favor of an "employee" because these factors are dictated by law and necessity without considering the degree of control exercised by either party to the contract. Thus, to have a multiple-factor test wherein fair application of the totality of the factors cannot be accomplished is arbitrary and misguided. Rule 821.5 was not designed for the concerns outlined in SB 280 and continued reference to this factor test should be abandoned.

**Response:** The Commission disagrees and emphasizes that it is the totality of the 20-point test that must be considered in determining whether a Board or its employees are controlling and directing the day-to-day activities and operations of the workforce service contractor or the contractor's employees. Furthermore, it is the 20-point test that will likely be used in a court of law to determine whether a Board has violated the provision in proposed §801.56 (adopted §801.53) that prohibits Boards from delivering workforce services and determining eligibility for those services. However, any one individual factor, such as a factor over which the Boards have no control, may be treated as neutral or nondispositive. The courts will likely look at the totality of the facts.

**Comment:** One commenter stated that the use of the 20-point test is inappropriate given that federal and state rules dictate the structure within which Texas Workforce Centers and Boards operate. If the 20-point test is adopted, then all Board staff are state employees.

**Response:** While the Texas workforce system is unique in that the Commission contracts with Boards to manage and oversee the provision of workforce services, and Boards then contract for the delivery of those workforce services, the Commission believes that the 20-point test still applies to the Boards. The Commission disagrees that the application of the 20-point test will result in the determination that an employer-employee relationship exists between the Commission and Board employees. Again, the Commission emphasizes that it is the totality of the 20-point test that must be considered in determining whether an employment relationship exists between a Board and its workforce service contractor or, for that matter, between the Commission and a Board. The Commission stresses that Boards should reflect on the guidance provided in §821.5 that states it is the importance assigned to each factor that may vary depending on the occupation or the facts of a particular case.

**Comment:** One commenter questioned if the proposed §801.56(a) prohibits the Board from directing the contractor to use a particular service model or to better use or allocate human resources in order to accomplish program goals.

**Response:** The rule does not preclude the use of the managing director model or any other model. In fact, Texas Government Code, Chapter 2308 prohibits the Commission from requiring Boards to use a specific management model for the provision of workforce services. However, the rule does prohibit the Board and Board employees from directly controlling the day-to-day operations of the managing director. The Commission has modified the proposed §801.56(a) (adopted §801.53) to clarify its intent.

**Comment:** Two commenters contended the rules would prohibit the PEO model. The elimination of the model would limit local control by restricting the Board from selecting a contracting model most appropriate for its workforce area. The elimination of the PEO model would provide Boards in less populated areas fewer choices in selecting workforce service providers and will increase the bargaining leverage of a single bidder for workforce services. Prohibiting the PEO model would violate the letter and spirit of the Agency's Sunset legislation by limiting local control.

**Response:** The Commission disagrees. The rules do not prohibit the PEO model or any other workforce service delivery model.

**Comment:** Three commenters stated that proposed §801.56(b) was unnecessary, too broad and meaningless, and questioned if it would complicate Boards' ability to monitor the contractor regarding staff allocation.

**Response:** The Commission agrees and deletes proposed §801.56(b).

**Comment:** One commenter recommended deletion of the test for employment status as set out in §821.5. This test has been used in determining independent contractor status for Unemployment Insurance appeals. The current test is out of date and is being applied to a situation for which it was not intended. Using this test for Boards would show that Boards are not independent contractors to the Commission, which is in conflict with state statute.

**Response:** The Commission disagrees with the recommendation to delete the use of the employment status test set forth in §821.5. While this test is used in determining employment status for the purposes of ruling on unemployment insurance cases, the Commission disagrees that the test is "out of date" and does not apply to the Boards. The Commission emphasizes that it is the totality of the 20-point test that must be considered in determining whether an employment relationship exists between a Board and its workforce service contractors or, for that matter, between the Commission and a Board. There are many factors involved in the relationship between a worker and the recipient of the worker's services. Some of those factors may suggest an independent contractual relationship while others may suggest an employer-employee relationship. All of the facts must be carefully considered when deciding whether the recipient of the services has the right to control or direct the worker's daily activities. The Commission disagrees that the application of the 20-point test will result in the determination that an employer-employee relationship exists between the Commission and Board employees.

**Comment:** Seven commenters opposed the language of proposed §801.53(b)(2)(c)(iii) that prohibits Boards from contracting with their fiscal agents for delivery of one-stop workforce services. One commenter stated it was allowable as long as the procurement of the contracted operator was an open and competitive process. Two of the commenters stated that the rule would be a financial hardship for rural areas. The current arrangement allows Boards in rural areas to stretch their small budgets and provide services to more people. The commenters stated that the present system is the most efficient method of service delivery and allows better control and accountability. The commenters questioned the need for this provision because they believe the present system works well.

**Response:** The Commission agrees with the comments and has removed this prohibition from the rules. Section 2308.24(e)(3), Texas Government Code, as amended, requires that the Board contracting guidelines ensure that if a Board—not a workforce service contractor—acts as the fiscal agent for a workforce service contractor, the Board does not deliver workforce services or determine eligibility for those services. The Commission has addressed this requirement in the adopted §801.53. Furthermore, the Agency's subrecipient monitors routinely verify that Boards are not delivering workforce services or determining eligibility for those services.

**Comment:** One commenter supported the language prohibiting the fiscal agent from providing one-stop workforce services. The commenter believed it was a conflict of interest. The commenter also stated that Chief Elected Officers (CEOs) for the workforce area also are CEOs for the one-stop workforce service providers, and that too may be a conflict of interest.

**Response:** The Commission agrees that there remains an appearance of a possible conflict of interest and strongly encourages Boards to weigh the advantages of having their workforce service contractors act as their fiscal agents. However, the Commission recognizes that some economies of scale have been achieved with this structure, that some workforce areas have a limited number of entities to serve as fiscal agents, and that the CEOs are ultimately responsible for the expenditure of funds.

#### §801.54 Board Contracting Guidelines

**Comment:** One commenter stated that because the Office and Management and Budget (OMB) circulars and *Uniform Grant Management Standards* (UGMS), cited in proposed §801.53(b)(1)(B) and §801.54(c)(2), are for nonprofit, governmental, and educational entities, Boards are confused about how to apply them to for-profit entities. The commenter stated that the OMB circulars and UGMS should apply to for-profit entities, but separate policy guidance is needed.

**Response:** The Commission disagrees. OMB circular and UGMS requirements apply to nonprofit, governmental, educational, and for-profit entities. Specifically, the following requirements are generally applicable to for-profit entities: cost principles at 48 CFR part 31; administrative requirements at OMB Circular A-110; and audit requirements as specified by the WIA Final Rule at 20 CFR 667.200(a)(2) and OMB Circular A-133. In addition, all entities that receive federal block grant funds are subject to the requirements in OMB circulars and UGMS.

**Comment:** One commenter also objected to proposed §801.53(c) as being vague and burdensome. The rule uses indeterminate terms like "reasonable person" and "\$50 in value." The commenter requested that the Commission outline simple standards to which the applicable parties must adhere.

**Response:** The Commission has deleted the term "reasonable person" and replaced it with clear and concise language. The Commission has also modified the rule language that references "\$50 in value" based upon similar provisions in Texas Penal Code Section 36.08 relating to gifts to public servants.

**Comment:** One commenter commended the Commission for allowing Boards to design their own fiscal indicators.

**Response:** The Commission appreciates the comment and believes that this provision is consistent with the tenets of Chapter 2308, Texas Government Code and the current practice of Boards' developing their own monitoring practices.

**Comment:** One commenter questioned how the monitors would define the time period "prior to" (the award of the contract). If the Board performed a fiscal monitoring of the workforce service provider 12 months prior to contract renewal, would that be considered verification of the fiscal indicators?

**Response:** Section 801.54(b) sets forth the baseline schedule for evaluating the fiscal integrity of workforce service contractors. Boards are required to evaluate their workforce service contractors before awarding a contract. Based on the amount of the contract, Boards are also required to verify that workforce service contractors meet the financial indicators—consistent with the provisions set forth in §801.54—as follows:

- \*at each renewal of a contract;
- \*at each renewal of the contract, and not less than every two years; or
- \*at each renewal of the contract, and not less than once a year.

If the Board monitored the fiscal integrity of its current workforce service contractors 12 months prior to the renewal of their contracts, the Board still would be required to conduct another review upon the renewal of those contracts.

**Comment:** One commenter objected to proposed §801.54(c) and (d) because the rules refer to standards that are not adopted pursuant to the rule-making requirements of Chapter 2001, Texas Government Code. The commenter states that the Commission seeks to impose rule status to its circulars, manuals, and guidelines. The commenter pointed out that a rule may not be invoked by an agency against a party unless it complies with the Texas Administrative Procedure Act.

**Response:** Section 801.54(c) requires no more than what the Commission currently requires in its rules and contracts with the Boards. Presently, Boards are required to comply with federal and state statutes and regulations as well as Commission rules. Boards are also required to comply with Commission directives, OMB circulars, and UGMS to the extent that they are written in accordance with compliance requirements in statutes, regulations, and rules. The Commission finds that referencing these requirements is consistent and in compliance with existing laws and regulations including, but not limited to, the Texas Administrative Procedure Act codified in Texas Government Code Chapter 2001 et seq. In addition, any costs for compliance activities are allowable expenditures pursuant to contracted funds. Furthermore, §801.54(a)(5) (proposed §801.54(d)) is a permissive provision—not a requirement.

**Comment:** One commenter recommended eliminating this section or revising the language to allow the Board to determine the time period for review and the items to be reviewed. The commenter also stated that, if the Commission intends to ensure that the system addresses prior performance, an additional requirement to "avoid adverse judgments or findings in the current and past years" is recommended.

**Response:** The Commission recognizes the importance of Board decision making and, consequently, the provisions in the adopted §801.54 allow Boards to design their own fiscal integrity evaluations and indicators and set forth only four Board requirements. The first two are existing requirements in Commission rules and contracts; the third requirement allows Board discretion in developing and applying any other safeguards; and the fourth requires the review and consideration of a prospective workforce service contractor's fiscal performance (a standard practice among public and private entities). The items listed in the adopted §801.54(a)(5) are permissive provisions—not requirements. While the Commission has allowed for local decision making in developing the fiscal integrity evaluation, the Commission disagrees that Boards should have discretion in setting the baseline schedule for evaluating the fiscal integrity of workforce service contractors. The schedule in this provision adheres to standard procurement schedules and requirements set forth in the Single Audit Act, and represents the Commission's minimum requirements. Boards do have the discretion to establish a more frequent schedule for fiscal contract reviews.

The Commission disagrees with the suggested modification regarding the review of a workforce service contractor's history. However, the Commission has reduced the review of a workforce service contractor's prior four-year financial history to a review of a prior three-year financial history. By reviewing the prior three-year financial history of a workforce service contractor, a Board will have a sufficient amount of information regarding the contractor's fiscal abilities, as at least two years of complete financial information will be available. Again, Boards have the discretion to expand the historical period of review, but as a minimum standard, the Commission has determined that a review of a contractor's prior three-year financial history is a sound business practice.

**Comment:** One commenter stated that the requirement in proposed §801.55(b) to bond 10% of the Board's full allocation will reduce funds for services to customers. The commenter also believed that under proposed §801.55(d) smaller contractors and HUBS may be at a disadvantage because they do not have resources to provide a large escrow to offset some of the bonding requirements.

**Response:** The Commission clarifies that the adopted §801.54(b) (proposed §801.55(b)) requires that 10% of the amount under the control of the workforce service contractor is subject to security—not 10% of the Board's full allocation. In addition, not only bonding, but a combination of methods for securing funds may be employed, and Boards may choose to pay for the securing of funds rather than passing that responsibility to their workforce service contractors. Adopted §801.54(b)(3) regarding the escrow of funds is a permissive provision, not a requirement. In addition, Texas Government Code §2308.264(e)(1) requires that contractors have sufficient coverage for the "overall financial security" of workforce funds and operations. The Commission believes that the protections afforded the Texas workforce system are balanced with the costs of securing funds, and decides that 10% of the amount under the control of the workforce service contractor is a reasonable amount to secure in order to implement the provisions of SB 280.

**Comment:** One commenter questioned whether the 10% bonding requirement applies to each of the Board's grants or if the Board passes the requirement on to the subcontractor, whether it applies to 10% for each subcontract or 10% for each subcontractor.

**Response:** The Commission clarifies that the 10% bonding requirement applies only to funds under the authority of the Board's workforce service contractors—not the Board's total allocation. If a workforce service contractor has multiple contracts with the Board, combining the total funds and securing one bond may be more efficient.

§801.55. *Employment of Former Board Employees by Workforce Service Contractors*

**Comment:** One commenter stated that the integrity of the competitive bid system could be compromised if the successful contractor hired a former employee of the Board. One commenter expressed support for regulations that prevent Board members from going to work for the Board or contracted workforce service provider staff and vice versa for a period of one year. Vendors that annually secure significant funds from Boards should not be allowed to serve on Boards.

**Response:** The Commission agrees and appreciates the comment.

**Comment:** Three commenters supported the proposed rules regarding the hiring of former employees. One of the commenters stated that the proposed rules would remove public suspicion.

**Response:** The Commission agrees and appreciates the comment.

**Comment:** Twenty commenters stated that proposed §801.53 sufficiently addresses conflicts of interest and recommended eliminating the proposed §§801.57-801.59 as these sections are outside the authority of the enabling statute. The commenters stated that the proposed rules are overreaching and unnecessarily restrictive in their efforts to prevent potential conflicts of interest. Several commenters stated that it is the Boards' obligation to develop and monitor conflicts of interest with contractors in their workforce areas. The Commission should monitor the Boards to verify they have effective conflict of interest policies that are being followed and enforced. In the absence of conflict of interest, the Board should have the autonomy and opportunity to hire the most qualified candidate for a position without seeking permission from the Commission. Several of the commenters also stated that the proposed rule removes all local control in determining appropriate employment and contracting.

**Response:** The Commission agrees that aspects of the proposed rules may be unnecessarily restrictive in preventing any conflict of interest or any appearance of a conflict of interest. Therefore, the Commission modifies the provision regarding the 12-month post-employment restriction to apply to Board employees in decision-making positions. In addition, the Commission includes a provision for exceptions and the process a Board shall follow in granting an exception. The Commission disagrees with eliminating all of the provisions in the proposed §§801.57–801.59 (adopted §801.55). The Commission agrees, however, with removing the post-employment restriction for current or former Agency employees and decides that the requirements of Chapter 572, Texas Government Code, regarding post-employment restrictions are sufficient for current or former Agency employees.

The Commission also disagrees that Boards should be allowed to set the baseline for conflict of interest provisions. For the Texas workforce system to maintain its integrity, the Commission believes that it must establish the minimum requirements or a threshold for conflict of interest policies. Boards have the flexibility to establish more restrictive conflict of interest policies.

The Commission believes that ensuring the public's trust demands that it provide the foundation for the system's standards of conduct—the adopted rules accomplish this goal. The Commission disagrees with the statements that the rules remove local control. Boards are allowed to make hiring and contracting decisions, and may contract with entities that hire former Board employees. The Commission believes the rules provide safeguards to ensure that hiring and contracting practices are fair and open and devoid of any conflict of interest and any appearance of a conflict of interest that could erode the public's trust in the Texas workforce system. Furthermore, it is the intent of the rules that hiring decisions and the awarding of contracts are based solely on the quality of the candidates and contractors. There should be no perception that other pecuniary or self-interest actions are factors in the awarding of contracts and hiring of staff.

**Comment:** Two commenters were concerned that the language and intent of the rules are unclear. The commenters questioned whether the intent was to prohibit employment of a former employee from another Board region.

**Response:** The Commission agrees and has modified the language to limit the applicability of the post-employment restriction to one workforce area, as it relates to former Board employees and current and former workforce service contractor employees from one workforce area being allowed to work in a different workforce area without having to wait 12 months. The post-employment restriction applies to intra-workforce area employment, not inter-workforce area employment.

**Comment:** Two commenters supported the proposed guidelines. The commenters' only change was to the waiver for the "revolving-door" conflict of interest. The commenters suggested a flexible process to allow CEOs and Boards to determine whether a conflict exists. If no conflict exists for a former Agency employee to work for a Board or contractor, a waiver or exception should be available at the local level.

**Response:** The Commission has modified the provision to apply to Board employees in decision-making positions and includes a provision for the Board to grant an exception to the 12-month post-employment restriction for a former Board employee to work for the Board's workforce service contractor.

**Comment:** Two commenters expressed concern that proposed §801.58 would prohibit Agency employees who were separated from employment with the Agency when Agency programs and positions were transferred to the Boards from continuing in those programs and positions at the Board level. In many cases, there would be no realistic risk of conflict of interest or other liability to the Board. The prohibition *against* Boards' employing former Agency employees merely would deprive the former employees of opportunities for continued employment in fields in which they have experience and deprive Boards of access to experienced and qualified employees.

**Response:** The Commission agrees and removes the post-employment restriction for current or former Agency employees as the requirements of Chapter 572, Texas Government Code, regarding post-employment restrictions are sufficient for current or former Agency employees.

**Comment:** One commenter stated that proposed §801.58 prevents Boards from hiring persons with recent workforce experience. Boards should not have to petition the state for permission to hire people who do not have the approval and review authority stated in proposed §801.57. The

commenter recommended that the duties in proposed §801.57 be applied to the definition of an employee who is restricted from employment, rather than the definition used in proposed §801.58.

**Response:** The Commission agrees and has modified the proposed §801.58 (adopted §801.55). The conflict of interest provisions do not prevent a Board from hiring persons with recent workforce experience, as a Board is not prohibited from hiring former workforce service contractor employees or former Board employees from another workforce area.

The Agency's Executive Director cannot grant an exception to the particular matter provision as state statute imposes a lifetime ban on working on particular matters. A Board, however, is not prohibited from hiring a former Agency employee who worked on a particular matter, as defined in §801.52, as long as the former Agency employee does not work on that particular matter when working for the Board.

**Comment:** One commenter stated that proposed §801.58 is unduly burdensome and restricts the opportunities for future employment and advancement of individuals within the workforce system. In the absence of a conflict of interest, the Board should have the autonomy and opportunity to hire the most qualified candidate for a position without seeking permission from the Commission.

**Response:** The Commission has modified the 12-month post-employment restriction in proposed §801.58 (adopted §801.55) to apply only to current or former Board employees in decision-making positions. Furthermore, the Commission allows for exceptions and sets forth provisions in which a current or former Board employee may request a review and consideration from the Board.

**Comment:** Two commenters objected to proposed §801.58 pertaining to employment restrictions on former Board employees, Board members, and contracted workforce service providers. As written, the rules apply standards that are reserved for state employees and members of state boards and commissions (usually applied to executive-level staff). The "revolving-door" statute does not apply to Boards or is limited in its application. The proposed rules are stated to mirror the revolving-door policies that apply to many state employees—when in fact, they do not. No distinction is made for the application of the rules to upper-level employees, but it gives a blanket prohibition against employment of any individual previously employed by the Agency, a Board, or a service provider. The new sections place an unfair and legally questionable restriction on free trade and the individual's right to seek and accept employment.

**Response:** The Commission has modified the rule language to make the distinction that the 12-month post-employment restriction applies only to Board employees in decision-making positions as defined in §801.52. The proposed rules do not prohibit a Board's workforce service contractor from ever hiring a former Board employee—the workforce service contractor must simply wait 12 months.

**Comment:** One commenter stated that the proposed rules are the equivalent of a covenant not to compete without an underlying agreement and without underlying justification. Covenants not to compete are common in industries with trade secrets or confidential and proprietary

information. Proposed §§801.57–801.58 imply that the Texas workforce system is not working together—but is competing—because the rules do not simply prevent conflicts of interest, they restrict contracting and employment as in a covenant not to compete.

**Response:** The Commission disagrees with equating public sector revolving-door policies with the private sector covenant not to compete. The issue is not trade secrets; rather, the issue is maintaining high ethical standards and assuring the public that hiring standards and practices are fair, aboveboard, open, and free of the appearance of "back-room deals" or favoritism. The Commission distinguishes between post-employment policies that apply to public employees and covenants not to compete that apply to private-sector employees. Compare Texas Government Code Section 572.001 and Texas Business and Commerce Code Section 15.50. The post-employment restrictions applying to public employees set standards of conduct for persons owing a responsibility to the people and government of this state in the performance of their official duties. Covenants not to compete, however, protect the goodwill or other business interests of the employer. The Commission believes the provisions in the rules strengthen the faith and confidence of the public in state government.

**Comment:** Two commenters stated that the requirement to seek a waiver is unreasonable because it places an additional burden on a Board to seek a waiver every time it wants to hire a worker or a contractor, and is unreasonable in light of the provision in proposed §801.53.

**Response:** The Commission agrees that aspects of the proposed rules may be unnecessarily restrictive in preventing any conflict of interest or any appearance of a conflict of interest. Therefore, the Commission modifies the provision regarding the 12-month post-employment restriction to apply to Board employees in decision-making positions. In addition, the Commission includes a provision for exceptions and the process a Board shall follow in granting an exception. The Commission agrees with removing the post-employment restriction for current or former Agency employees and decides that the requirements of Chapter 572, Texas Government Code, regarding post-employment restrictions are sufficient for current or former Agency employees.

**Comment:** Two commenters believed these provisions could negatively affect Agency employees serving on Boards as public employment representatives.

**Response:** The Commission agrees and removes the post-employment restriction on Agency employees.

**Comment:** Two commenters stated that the proposed restrictions will stifle the continuous improvement of the workforce system by limiting the ability of professional and skilled people to move within the system.

**Response:** The Commission does not intend to restrict movement within the system and has modified the language to apply only to Board employees in decision-making positions.

**Comment:** Two commenters suggested that limiting a workforce area's ability to hire qualified individuals conflicts with SB 280, which requires that Boards hire, train, and develop qualified employees. The restriction on hiring could have a negative impact on the Texas workforce system.

**Response:** The Commission disagrees with the comment that the proposed rules conflict with SB 280. The rules do not prevent Boards from hiring, training, and developing qualified employees.

**Comment:** One commenter stated that the employment restrictions are overbroad and seriously doubts the Texas Attorney General or a court of competent jurisdiction would enforce the restrictions. The exceptions and waivers do not cure the problems with proposed §801.57 and §801.58. Workforce system participants should not need to take an extra step to request permission to hire an employee. People experienced in operating the workforce system are the people needed to continue assisting in its operation. These employees and employers should not be subject to the discretion of the Commission regarding obtaining new employment or employees, especially because the rules do not establish standards for determining whether an actual or potential conflict of interest or emergency situation may exist. The commenter further stated that the proposed exception rule opens the Commission to claims of discriminatory treatment.

**Response:** The Commission agrees that aspects of the proposed rules may be unnecessarily restrictive in preventing any conflict of interest or any appearance of a conflict of interest. Therefore, the Commission modifies the provision regarding the 12-month post-employment restriction to apply to Board employees in decision-making positions. In addition, the Commission includes a provision for exceptions and the process a Board shall follow in granting an exception. The Commission disagrees with eliminating all of the provisions in the proposed §§801.57–801.59 (adopted §801.55). The Commission agrees, however, with removing the post-employment restriction for current or former Agency employees and decides the requirements of Chapter 572, Texas Government Code, regarding post-employment restrictions are sufficient for current or former Agency employees.

The Commission disagrees that the 12-month post-employment restriction and the prohibition from working on particular matters are "overbroad" and not defensible in a court of law. Post-employment restrictions are common in state and federal government. In fact, 30 states have some type of post-employment restrictions for former government employees. Additionally, federal statute (41 U.S.C. 423(d)) prohibits federal employees who were involved in a contract over \$10 million from working for the contractor for one year. In establishing post-employment restrictions on state employees, the legislative intent expressed in Texas Government Code §572.001 is to strengthen the faith and confidence of the public in Texas government.

Because the Boards are quasi-governmental entities, the Commission, in addition to applying Texas Government Code Chapter 572, researched the private sector provisions for covenants not to compete as codified in Texas Business and Commerce Code §15.50. The Commission found that the private sector has post-employment restrictions that balance the restrictions on the former employee's time, geographic area and scope of activity with only what is necessary to protect the business interests of the employer. The Commission rules satisfy both the public and private sector tests for the reasonableness of post-employment restrictions. Furthermore, governmental entities, quasi-governmental entities, and private entities that receive and operate with taxpayers' money should expect to be held to a higher standard than private sector entities to protect the public trust.

**Comment:** One commenter supported any provisions that allow for exceptions to "particular matters." Rural Boards are at a disadvantage when staffing positions that require specific experience, and many times existing contractor or state agency personnel will be the best candidates for key positions. The commenter stated that the rule potentially disqualifies exiting key staff from working for the Board when a new one-stop operator is procured or hired. The Board does not want to be restricted from excellent performance because it cannot hire the right person. The commenter requested modifications to the rule that allow for waivers in these instances and suggested that the staffing requirement exempt positions that do not have broad authority or fall into a particular classification.

**Response:** The Commission has modified the rule language to make a distinction that the 12-month post-employment restriction applies only to employees in decision-making positions as defined in §801.52. The proposed rules do not prohibit a Board's workforce service contractor from ever hiring a former Board employee. Again, the Commission emphasizes that a workforce service contractor is not prohibited from hiring a former Board employee who was in a decision-making position as defined in §801.52—the workforce service contractor simply must wait 12 months.

The Commission disagrees that an exception to the particular matter provision should be allowed for former Board employees. Particular matter has a narrow application, yet still does not prohibit a Board's workforce service contractor from hiring a former Board employee—it only prohibits that former Board employee from working on the particular matter when working for the Board's workforce service contractor. Finally, the Commission agrees that former employees may possess a certain depth of knowledge and are valuable to the system's stability. However, the Commission also believes that the system needs to look beyond internal staffing. The State of Texas has a wealth of potential employees—in the public and private sectors—who can bring new and innovative ideas and practices to the Texas workforce system.

**Comment:** One commenter proposed the following changes: a permanent ban of 24 months; all individuals agree to avoid any actual or apparent conflict of interest in performance of duties on behalf of the Board; and the imposition of a voluntary termination of 180 days and involuntary termination of 90 days, unless the Board expressly consents in writing to a waiver, and such consent shall not be unreasonably withheld.

**Response:** The Commission appreciates the comment. However, the Commission believes that a 24-month ban is more restrictive than necessary to protect the system's integrity. In addition, the Commission believes that the modifications it has made to the rules appropriately address the commenter's other suggestions.

**Comment:** One commenter stated that the rules do not reasonably fulfill the legislative intent, which charges that the Commission establish contracting guidelines to "prevent potential conflicts of interest between Boards and entities that contract with Boards." That does not require the Commission to adopt the rigorous policies in the proposed rules. The legislation clearly intends that the Commission adopt general guidelines to prevent potential conflicts of interest in a narrow set of circumstances, and does not contemplate that any rules would address the employer-employee relationship of Board employees. The legislation does not preclude the idea that the Commission enact guidelines requiring Boards to enact their own conflict of interest

policies, with the Commission's role being to verify Board implementation of local policies and ultimate compliance with the same.

**Response:** The Commission disagrees that the rules do not conform to the legislative intent of SB 280. The Commission is confident the conflict of interest and post-employment provisions set forth in these rules pass the tenets of reasonableness tests as well as adhere to legislative intent. The Commission also believes that the need to maintain the public's trust is all the justification needed for these provisions. Furthermore, governmental entities, quasi-governmental entities, and private entities that receive and operate with taxpayers' money should expect to be held to a higher standard than private sector entities. Finally, the Commission also disagrees that Boards should be allowed to develop their own conflict of interest policies. For the Texas workforce system to maintain its integrity, the Commission believes that it must establish the minimum requirements or threshold for conflict of interest policies. Boards have the flexibility to establish more restrictive conflict of interest policies. The Commission believes that ensuring the public's trust demands that it provide the foundation for the system's standards of conduct and the adopted rules accomplish this goal.

**Comment:** One commenter stated that the rules contain a significant number of procedural deficiencies, and the procedures the rules seek to enact are unquestionably vague and potentially unworkable—particularly proposed §801.57 and §801.58, which mandate broad prohibitions on employment for new Boards if an employee has formerly worked for a contractor. The rules place the burden on a Board to ensure that its former employees do not gain employment with contractors around the state. That is virtually impossible in Texas, a state with an "at-will" employment legal regimen. In a majority of cases, a Board or its contractors will not have contracts with their employees.

Therefore, regardless of the time limitations set forth in the rules, a Board has no post-termination mechanism to enforce the requirement that a former employee not take employment with a prohibited group. At a minimum, the potential sanctions for violations of these sections should only be imposed upon the hiring Board, rather than the former Board, and the burden should be on the hiring Board to perform background checks and obtain the necessary information from individuals seeking employment.

**Response:** The Commission has modified the language in proposed §801.57 and §801.58 (adopted §801.55) to clarify its intent. The modified provision applies only to former Board employees in decision-making positions as defined in §801.52. The revised rules allow for exceptions to the post-employment restriction for former Board employees to work for the Board's workforce service contractors in those situations that warrant an exception. Furthermore, the 12-month post-employment restriction does not apply to a Board that wants to hire former Board employees from other workforce areas or to a former Board employee who wants to work for a workforce service contractor in other workforce areas. Again, the Commission emphasizes that a workforce service contractor is not prohibited from hiring a former Board employee who was in a decision-making position as defined in §801.52—the workforce service contractor simply must wait 12 months. The Commission, however, provides for the Board to grant exceptions.

**Comment:** One commenter stated that the permanent prohibition in proposed §801.58(b) contains no time limitation and is vague as to the subject matters. Taken literally, this rule could

prevent the employment of an office clerk should that office clerk have had "personal involvement" with a case or proceeding on behalf of a Board or the Agency. Clearly, the intent of the enacting legislation coupled with the vagueness of the actual language of proposed §801.58(b) argues very strongly for the complete deletion of this overly broad rule.

**Response:** The Commission has modified the rule language to make a distinction that provision applies only to employees in decision-making positions as defined in proposed §801.52. The Commission disagrees that an exception to the particular matter provision should be allowed for former Board employees. Particular matter has a narrow application, yet does not prohibit a Board's workforce service contractor from hiring a former Board employee—it only prohibits that former Board employee from working on the particular matter when working for the Board's workforce service contractor.

**Comment:** One commenter stated that the process to request and receive a waiver is undefined or is unclear and requires substantial clarification. Proposed §801.59 simply states, "the Commission may waive one or more of the provisions of this subchapter if the Commission determines that no conflict of interest exists." Where does an individual or a Board go to request a waiver? The rules do not provide waiver request contact information or contain any indication as to a reasonable amount of time the Commission has to respond to a waiver request. How long does the Commission have to consider a waiver request? Can the Commission grant temporary waivers under the language of the rules? Finally, what is the appeal process if the Commission denies a request for a waiver?

**Response:** The Commission agrees and has removed proposed §801.59 from the adopted rules.

**Comment:** Further study should be conducted by the Commission before adopting the 12-month prohibition. Sufficient protections exist within individual Board conflict of interest policies. The major factor in drafting guidelines should be flexibility.

**Response:** The Commission appreciates the comment and additional research has been conducted regarding post-employment provisions. Post-employment restrictions are common in state and federal government. Thirty states have some type of post-employment restrictions for former government employees. Additionally, federal statute (41 U.S.C. 423(d)) prohibits federal employees who were involved in a contract over \$10 million from working for the contractor for one year. In establishing post-employment restrictions on state employees, the legislative intent expressed in Texas Government Code Section §572.001 is to strengthen the faith and confidence of the public in Texas government.

Because the Boards are quasi-governmental entities, the Commission, in addition to applying Texas Government Code Chapter 572, researched the private sector provisions for covenants not to compete as codified in Texas Business and Commerce Code 15.50. The Commission found that the private sector has post-employment restrictions that balance the restrictions on the former employee's time, geographic area and scope of activity with only what is necessary to protect the business interests of the employer. The Commission rules satisfy both the public and private sector tests for the reasonableness of post-employment restrictions. Furthermore, governmental entities, quasi-governmental entities, and private entities that receive and operate with taxpayers' money should expect to be held to a higher standard than private sector entities to protect the public trust.

The Commission also disagrees that Boards should be allowed to set the baseline for conflict of interest provisions. For the Texas workforce system to maintain its integrity, the Commission believes that it must establish the minimum requirements or threshold for conflict of interest policies. Boards have the flexibility to establish more restrictive conflict of interest policies. The Commission believes that ensuring the public's trust demands that it provide the foundation for the system's standards of conduct and the adopted rules accomplish this goal.

**Comment:** The commenter felt strongly about the revolving door between our Board management staff members and our service contractors and will be willing to elaborate on this if requested.

**Response:** The Commission appreciates the comment and the commenter's willingness to provide additional information and assistance.

**Comment:** One commenter agrees with the spirit of the proposed rules on Board contracting. However, the commenter stated that restrictions on the Boards' employing or contracting with former Agency or workforce service provider employees, or workforce service providers' employing or contracting with former Agency or Board employees for 12 months, severely limits small Boards and small workforce service providers' pool of experienced job applicants. The rules may give an unfair advantage to large service providers over small local contractors. Rural areas have a much smaller labor pool and limited budgets to attract workforce solutions employees. Had the rules been in force in the past, the commenter stated that the Board's Executive Director and several other key personnel would have been ineligible for employment by the Board.

The commenter stated that the current conflict of interest guidelines from the state provide sufficient boundaries for Boards to develop local policy, based on local need. The commenter stated that there should be local-level, employer-driven discretion regarding the length of time seasoned workforce professionals should remain outside the loop before they can reenter the delivery system. In lieu of new rules, monitoring of current rule compliance and appropriately applied technical assistance would go a long way in preventing the perception of a conflict of interest, real or apparent.

**Response:** The Commission appreciates the comment and has modified the language to apply only to former Board employees in decision-making positions as defined in §801.52. The revised rules allow for exceptions to the post-employment restriction to be made by the Board. Furthermore, the 12-month post-employment restriction does not apply to Boards that want to hire former Board employees from other workforce areas or to former Board employees who want to work for workforce service contractors in other workforce areas.

The Commission agrees that former employees may possess a certain depth of knowledge and are valuable to the system's stability. However, the Commission also believes that the system needs to look beyond internal staffing. The State of Texas has a wealth of potential employees—in the public and private sectors—who can bring new and innovative ideas and practices to the Texas workforce system.

Finally, the Commission disagrees that Boards should be allowed to develop their own conflict of interest policies. For the Texas workforce system to maintain its integrity, the Commission believes that it must establish the minimum requirements or threshold for conflict of interest policies. Boards have the flexibility to establish more restrictive conflict of interest policies. The Commission believes that ensuring the public's trust demands that it provide the foundation for the system's standards of conduct, and the adopted rules accomplish this goal.

**Comment:** One commenter states that the exception to the prohibition in this rule would require Boards to request permission from the Commission before making certain hiring decisions. This is counter to the spirit of the Sunset legislation. SB 280 seeks to ensure flexibility for Boards. The Commission should reconsider these rules and work with Boards, contractors, and others before adopting the rules.

**Response:** The Commission agrees with the comment and has modified the language in this provision. The revised rule allows the Board to grant exceptions to the 12-month post-employment restriction for a former Board employee to work for the Board's workforce service contractor. Furthermore, the 12-month post-employment restriction does not apply to Boards that want to hire former Board employees from other workforce areas or to former Board employees who want to work for workforce service contractors in other workforce areas.

## **PART V. FINAL RULES**

Sections 2308.264 and 2308.267, Texas Government Code, as amended by §§4.01, 4.02 and 4.09 of SB 280, 78th Texas Legislature, Regular Session, 2003, require the Commission to adopt rules regarding Board contracting guidelines and related provisions referenced in the legislation.

Additionally, §301.0015, Texas Labor Code, provides that the Commission has authority to adopt rules necessary to administer the Commission's policies, including rules necessary for the administration of Title 4, Texas Labor Code, relating to employment services and unemployment.

Section 302.002(d), Texas Labor Code, authorizes the Commission to adopt, amend, or repeal such rules in accordance with Chapter 2001, Texas Government Code, as necessary for the proper administration of the Workforce Development Division.

Section 302.021, Texas Labor Code, which consolidated under the jurisdiction of the Commission job-training, employment, and employment-related educational programs and other functions listed in the section (including, but not limited to, the programs funded under the Workforce Investment Act of 1998 as amended (29 U.S.C. §§2801 et seq.).

Texas Labor Code, Title 4, and primarily Chapters 301 and 302, and Chapter 2308, Texas Government Code, will be affected by the new rules.

*Chapter 801 Local Workforce Development Boards*

*Subchapter C. The Integrity of the Texas Workforce System*

*§801.51. Purpose and General Provisions.*

- (a) The purpose of the rules contained in this subchapter is to implement Texas Government Code, §2308.264 and §2308.267, including provisions relating to directly delivering services, Board contracting guidelines, and other conflict of interest provisions.
- (b) It is the intent of the Commission that these rules strengthen the confidence of the public in the Texas workforce system.
- (c) A Board may set local policies that are more restrictive than those set forth in this subchapter.
- (d) A Board shall develop the policies and procedures required by this subchapter no later than September 1, 2004.
- (e) A Board member with an existing contract for workforce services shall comply with this subchapter no later than the earliest of the following:
  - (1) the expiration of the contract;
  - (2) the contract renewal date;
  - (3) the expiration of the Board member's term or the Board member's resignation; or
  - (4) September 1, 2005.

*§801.52. Definitions.*

The following words and terms, when used in this subchapter, shall have the following meaning, unless the context clearly indicates otherwise.

- (1) Appearance of a conflict of interest -- A circumstance in which the action of a Board member, Board employee, workforce service contractor, or workforce service contractor employee in a decision-making position appears to be:
  - (A) influenced by considerations of one or more of the following: gain to the person, entity, or organization for which the person has an employment interest, substantial financial interest, or other interest, whether direct or indirect (other than those consistent with the terms of the contract); or
  - (B) motivated by design to gain improper influence over the Commission, the Agency, or the Board.
- (2) Board decision-making position -- A position with a Local Workforce Development Board that has final decision-making authority or final recommendation authority on matters that directly affect workforce service contractors. A Board decision-making position is one that performs the function of a Board's executive director, deputy

executive director, chief financial officer, lead contract manager, or lead contract monitor.

- (3) Conflict of interest -- A circumstance in which a Board employee, workforce service contractor, or workforce service contractor's employee is in a decision-making position and has a direct or indirect interest, particularly a substantial financial interest, that influences the individual's ability to perform job duties and fulfill responsibilities.
- (4) Particular matter -- A specific investigation, application, request for a ruling or determination, rule-making proceeding, administrative proceeding, contract, claim, or judicial proceeding, or any other proceeding as defined in §572.054(h)(2), Texas Government Code.
- (5) Substantial financial interest -- An interest in a business entity in which a person:
  - (A) owns 10% or more of the stock, shares, fair market value, or other interest in the business entity;
  - (B) owns more than \$5,000 of the fair market value of the business entity;
  - (C) owns real property if the interest is an equitable or legal ownership with a fair market value of \$2,500 or more used for the business entity;
  - (D) receives funds from the business entity that exceed 10% of the person's gross income for the previous year;
  - (E) is a compensated member of the board of directors or other governing board of the business entity;
  - (F) serves as an elected officer of the business entity; or
  - (G) is related to a person in the first degree by consanguinity or affinity, as determined under Chapter 573, Texas Government Code, who has a substantial financial interest in the business entity, as listed in subparagraphs (A) through (F) of this section. First degree of consanguinity or affinity means the person's parent, child, adopted child, or spouse.
- (6) Workforce service contractor -- A business entity or person, except a state agency or an institution of higher education as defined in §61.003 of the Texas Education Code, that contracts with a Board to provide one or more of the workforce services listed in §801.28 of this chapter, which include core, intensive, training, and other support services such as child care and transportation.
- (7) Workforce service contractor employee in a decision-making position -- A position with a workforce service contractor that includes the ability to commit or bind the contractor to a particular course of action with respect to carrying out the contractor's duties and activities under the contract.

*§801.53. Prohibition against Directly Delivering Services.*

- (a) A Board shall ensure, through the oversight and management of Board policies, that it does not directly deliver or determine eligibility for workforce services in its local workforce development area (workforce area) or contract with the following persons or entities to deliver or determine eligibility for workforce services:
  - (1) a Board member;
  - (2) a business, organization, or institution that a Board member represents on the Board;
  - (3) a Board member's business, organization, or institution in which a Board member has a substantial financial interest; or
  - (4) a Board employee.
- (b) The prohibitions in this section do not apply to public education agencies, such as community colleges and independent school districts, that have Board members who fulfill the requirements set forth in Texas Government Code §2308.256(a)(3)(A).
- (c) A Board may grant a one-year exception to the prohibitions described in subsection (a) of this section for a community-based organization that fulfills the requirements set forth in Texas Government Code §2308.256(a)(2). The exception can only be granted by a two-thirds vote of the members present in an open meeting and may not be granted for contracts for the operation of Texas Workforce Centers.
- (d) A Board shall ensure that the Board, its members, or its employees do not directly control the daily activities of its workforce service contractors. The Agency shall review a Board's compliance through an examination of the Board's exercise of direction and control over its workforce service contractors. The Agency may use the factors for testing the employment status as set out in §821.5 of this title.
- (e) Nothing in this section restricts a Board member or a Board member's organization from receiving Texas workforce system services and thereby being a customer of a Board's workforce service contractors' services.

*§801.54. Board Contracting Guidelines.*

- (a) Fiscal Integrity Provisions.
  - (1) A Board shall develop fiscal integrity evaluation indicators designed to appraise the fiscal integrity of its workforce service contractors.
  - (2) A Board shall assess its workforce service contractors to ensure the contractors meet the requirements of the Board's fiscal integrity evaluation based on the following schedule:

- (A) contracts under \$100,000—the fiscal indicators must be verified prior to the award of the contract and at each renewal of the contract;
  - (B) contracts between \$100,000 and \$500,000—the fiscal indicators must be verified prior to the award of the contract, at each renewal of the contract, and not less than biennially; and
  - (C) contracts over \$500,000—the fiscal indicators must be verified prior to the award of the contract, at each renewal of the contract, and not less than once annually.
- (3) The fiscal integrity evaluation shall include the following provisions for ensuring that workforce service contractors are meeting performance measures in compliance with requirements contained in:
- (A) federal and state statutes and regulations and directives of the Commission or Agency;
  - (B) Office of Management and Budget (OMB) circulars applicable to the entity, such as OMB Circulars A-21, A-87, or A-122, and the Office of the Governor's *Uniform Grant Management Standards*; and
  - (C) any other safeguards a Board has identified that are designed to ensure the proper and effective use of funds placed under the control of its workforce service contractors.
- (4) The fiscal integrity evaluation shall also include the review and consideration of the prospective or renewing workforce service contractor's prior three-year financial history before the Board awards or renews a workforce service contract. The review shall include any adverse judgments or findings, such as administrative audit findings; Commission, Agency, or Board monitor findings; or sanctions by a Board or court of law.
- (5) The fiscal integrity evaluation may include provisions such as accounting for program income in accordance with federal regulations, resolving questioned costs and the repayment of disallowed costs in a timely manner, and safeguarding fixed assets, as well as those referenced in the Texas Workforce Commission's Financial Manual for Grants and Contracts.
- (b) Bonding, Insurance, and Other Methods of Securing Funds to Cover Losses.
- (1) A Board shall ensure that at least 10% of the funds subject to the control of the workforce service contractors is protected through bonds, insurance, escrow accounts, cash on deposit, or other methods to secure the funds consistent with this subchapter. A Board and its workforce service contractors may, consistent with this section, use any method or combination of methods to meet this requirement. At the Board's discretion, the Board may pay for the bonding, insurance, or other protection methods or require its workforce service contractors, to the extent allowable under state and federal law, to pay for such protection.

- (2) In conducting the fiscal integrity evaluation required in this section, a Board may determine that more than 10% of the funds subject to the control of its workforce service contractors shall be secured through bonds, insurance, escrow accounts, or other methods consistent with this subchapter.
  - (3) Escrow of funds may also be used to satisfy the requirements of §801.54(b) provided that:
    - (A) the funds placed in escrow require the signature of persons other than the persons with signatory authority for the Board's workforce service contractors;
    - (B) the funds do not lapse due to requirements for timely expenditure of funds; and
    - (C) this provision does not conflict with any provision in contract, rule, or statute for the timely expenditure of funds.
  - (4) If a bond is used, a Board shall ensure that the bond is executed by a corporate surety or sureties holding certificates of authority, authorized to do business in the state of Texas.
  - (5) A Board shall ensure, based on the schedule referenced in §801.54(a)(2) of this section, that each of its workforce service contractors is required to verify that:
    - (A) the insurance or bond policy is valid, premiums are paid to date, the company is authorized to provide the bonding or insurance, and the company is not in receivership, bankruptcy or some other status that would jeopardize the ability to draw upon the policy;
    - (B) the escrow account balances are at an appropriate level;
    - (C) the method of securing the funds has not been withdrawn, drawn upon, obligated for another purpose, or is no longer valid for use as the method of security; and
    - (D) other such protections as are applicable and relied upon by the Board are verified as in force.
  - (6) A Board shall ensure that the workforce service contractors are required to disclose any changes in and circumstances regarding the method of securing or protecting the funds under the workforce service contractors' control.
- (c) Standards of Conduct. A Board shall ensure that the workforce service contractors:
- (1) comply with federal and state statutes and regulations regarding standards of conduct and conflict of interest provisions including, but not limited to, the following:

- (A) 29 C.F.R. §97.36(b)(3), which includes requirements from the Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments;
  - (B) professional licensing requirements, when applicable; and
  - (C) applicable OMB circular requirements and the Office of the Governor's *Uniform Grant Management Standards*.
- (2) avoid any conflict of interest or any appearance of a conflict of interest; and
- (3) refrain from using nonpublic information gained through a relationship with the Commission, an Agency employee, a Board, or a Board employee, to seek or obtain financial gains that would be a conflict of interest or the appearance of a conflict of interest.
- (d) Disclosures. A Board shall require its workforce service contractors to disclose the following:
- (1) Matters Subject to Disclosure. A Board shall ensure that its workforce service contractors promptly disclose in writing the following:
    - (A) a substantial financial interest that the workforce service contractor, or any of its workforce service contractor employees in decision-making positions, have in a business entity that is a party to any business transaction with a Board member or Board employee who is in a Board decision-making position;
    - (B) a gift greater than \$50 in value given to a Board member or Board employee by a workforce service contractor or its employees; and
    - (C) the existence of any conflict of interest and any appearance of a conflict of interest, or the lack thereof.
  - (2) Content of Disclosure. A Board shall ensure that its workforce service contractors' written disclosures contain the following:
    - (A) information describing the conflict of interest; and
    - (B) information describing the appearance of a conflict of interest, and actions the workforce service contractor and its employees will take in order to prevent any conflict of interest from occurring.
  - (3) Frequency of Disclosure. A Board shall ensure that its workforce service contractors disclose:
    - (A) at least annually, and as frequently as necessary, any conflict of interest and any appearance of a conflict of interest;

(B) within 10 days of giving a gift greater than \$50 in value as referenced in this section; and

(C) at least annually that no conflict of interest and no appearance of a conflict of interest exists.

(4) Matters Not Subject to Disclosure. This provision does not apply to:

(A) a financial transaction performed in the course of a contract with the Board; or

(B) a transaction or benefit that is made available to the general public under the same terms and conditions.

*§801.55. Employment of Former Board Employees by Workforce Service Contractors.*

(a) Post-Employment Restriction. In order to avoid a conflict of interest, a Board shall ensure that the Board's workforce service contractors shall not employ or otherwise compensate a former Board employee who:

(1) was in a Board decision-making position as defined in §801.52 of this subchapter; and

(2) was employed or compensated by the Board anytime during the previous 12 months.

(b) Exceptions. Where there is no actual conflict of interest, but there is an appearance of such a conflict, a Board in an open meeting may provide for an exception to the period described in subsection (a) of this section by a vote of two-thirds of the membership present. In making such a determination, the Board shall assess all relevant factors, including but not limited to, whether there is a critical need for the skills involved, the relative cost and availability of alternatives, and the need to protect the integrity and stability of the Texas workforce system. In such an instance, the Board shall impose whatever terms and conditions it deems necessary to mitigate the appearance of a conflict of interest.

(c) Corrective Actions. A Board shall ensure that its contracts with workforce service contractors require compliance with this section and provide effective enforcement mechanisms allowing it to impose corrective actions, up to and including contract termination, for violation of this section.

(d) Particular Matter. A Board shall ensure that its workforce service contractors shall not employ or otherwise compensate a former Board employee to work on a particular matter that the employee worked on for the Board, as defined in §801.52 of this subchapter. Nothing in this section shall prohibit a Board's workforce service contractor from employing or otherwise compensating a former employee of the Board who worked on a particular matter for the Board as long as the former Board employee never works on that same particular matter once employed or otherwise compensated by the Board's workforce service contractor.

*§801.56. Enforcement.*

If a Board fails to adhere to the provisions of this subchapter, the Agency may impose corrective actions, up to and including sanctions.