

Secretary of State AUDIT REPORT

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Department of Education: Contracting Practices



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Summary

PURPOSE

The purpose of our audit was to determine if the Department of Education's contract procurement and administration practices are adequate and comply with applicable laws and regulations.

BACKGROUND

During our audit period of July 1, 1999 through September 30, 2001, the department entered into approximately 7,000 contracts for a total cost of just over \$48.6 million. Contracts reviewed covered a wide variety of services such as training, management consulting, education and research, translating, investigative, and services for hearings officers.

RESULTS IN BRIEF

Our audit identified opportunities for the department to make improvement in the areas of contract solicitation and selection, contract administration, and the payment approval process. Specifically, our recommendations address such problems as improper or inadequate: solicitation practices, sole source justification, documentation retention, contract approval prior to performance, contract amendments, and retention of deliverables to support payments.

We also identified other issues that we believed deserved the attention of the department, but did not warrant reporting in the audit report. These issues were conveyed to the department in Management Letter No. 581-2003-04-01, dated April 1, 2003.

RECOMMENDATIONS

We recommend that the department:

- Establish clear policies and procedures regarding contract administration, solicitation, selection, and documentation retention. Further, clearly define contracting responsibilities between department staff.

- Establish a standard training curriculum for all staff assigned contracting responsibilities. Also communicate to department staff the importance of competitive bidding practices.
- Establish provisions with the department's new central procurement unit for a quality assurance review of files.
- Consider improving the department's contract database system so that it can be used to notify contract personnel of approaching critical timelines.
- Improve internal policies and procedures to ensure authorized personnel approve payment of invoices.
- Review identified over payment and questioned costs and consult with the Department of Justice to determine appropriateness and potential recovery of any amounts improperly paid.

AGENCY'S ACCOMPLISHMENTS:

Most of the examples that we cite in this report occurred prior to the department's establishment of a procurement unit headed by an individual that holds a state issued procurement certification. To the department's credit, we have found it to be very responsive in dealing with the problems identified in this report and, in many instances, started to institute recommendations prior to the completion of our audit work.

AGENCY'S RESPONSE

The Department of Education generally agrees with the recommendations.

Introduction

The policy of the state of Oregon, as expressed in statute and state administrative contracting rules, is to encourage competition and discourage favoritism among potential contractors. The goal of state contracting activity is to foster open and impartial competition with the aim of obtaining goods and

services at a fair and reasonable price.

The contracting process involves determining that goods or services are needed, soliciting and selecting a contractor, negotiating contract terms, executing a contract, receiving contracted goods or services and making payments according to contract provisions.

Background

During our audit period of July 1, 1999 through September 30, 2001 the department entered into approximately 7,000 contracts for a total cost of just over \$48.6 million.

During our audit we reviewed 114 contracts totaling approximately \$2.4 million that the department entered into with individuals and

non-governmental entities. We also reviewed 13 contracts totaling approximately \$15.8 million that the department entered into with other state agencies or local governments.

The department awarded contracts to individuals and non-governmental entities to acquire a wide variety of services such as training, management consulting, education and research, translating, investigative, and services for hearings officers.

Audit Results

Of the 114 contracts with individuals and non-governmental entities reviewed, 63 were not subject to competitive solicitation requirements.¹ However, 51 were subject to state contracting rules requiring competitive solicitation and were the primary focus of our audit. Eleven of these contracts were with the same contractor, an organization that represents Oregon school administrators. The remaining 40 contracts subject to competitive solicitation rules were with various contractors.

While some of the contracts tested were randomly selected, most were judgmentally selected as described in the “Objectives, Scope and Methodology” section of this report.

During our audit we identified opportunities for improvement in the areas of contract solicitation and selection, contract administration, and in the payment approval process.

Non-competitive Contracting Practices

We identified practices within the department that did not appear to encourage fair, open, and competitive public contracting. These practices included solicitation

¹ Personal Service contracts priced at \$5,000 or less, or Trade Service Agreements under \$5,000 do not require competitive solicitation.

limitations, sole source contracts for specialized but not unique services, and contract files that lacked the required documentation necessary to conclude that contracts were solicited and awarded appropriately.

During our testing of the 51 contracts with individuals and non-governmental entities requiring competitive solicitation, we found exceptions to state contracting rules in 7 of the 11 contracts (64 percent) pertaining to an organization representing school administrators as well as exceptions with 18 of the remaining 40 contracts (45 percent).

By not following and documenting the proper contract awarding practices as delineated in the state contracting rules, the department may not be selecting the most qualified contractor at the best price. Furthermore, contracting decisions may not be defensible if challenged.

Improper Solicitation Practices

State administrative contracting rules specify the solicitation and selection process to be used, which varies depending on the contract amount. These rules were established to encourage competition and discourage favoritism.

We found that, of the 40 contracts reviewed subject to competitive solicitation requirements, six (approximately 15 percent) appeared to have been awarded to preferred vendors.

For example, for two related contracts totaling approximately \$48,000, a proposal was received from the contractors, and contracts were signed before the contracting opportunity was properly advertised. In internal electronic mail communications, department personnel discussed the need to have new contracts written and a new proposal submitted so that they could be dated after the advertisement. Contract file documentation also shows that the contractors’ original proposal was

received approximately five months prior to the department’s solicitation for bids. There was also documentation in the file indicating that the contractors had started work on the contract prior to advertisement.

In another example, a detailed proposal and a bid appear to have been received by the department prior to advertisement. A letter from the contractor to department management, dated approximately one week prior to the advertisement, refers to a planned meeting between the contractor and department management. This meeting was to “...discuss the proposed work scope, and if acceptable proceed with arrangements for the review.” A written bid of approximately \$11,200 was included. The contractor was later awarded the contract for \$11,200.

For the contracts entered into with the organization representing school administrators, we found that contractor selection did not always follow state contracting rules and had the appearance of favoritism.

For the 11 contracts reviewed, we identified seven contracts (64 percent) totaling approximately \$510,000 that had exceptions to state contracting rules.

Although the department often used solicitation practices that require documentation and ranking of proposals received, the department was not able to produce any written proposals supporting any contracts that we selected for review for this contractor. This finding is consistent with information obtained in an interview with the contractor, in which contractor officials explained that contracts with the department were proposed and negotiated verbally.

For example, the department entered into a \$36,000 contract for the performance of administrative duties related to a Legislative interim task force on Education

Service District (ESD) funding. A \$35,500 proposal was received from a competing contractor. No written proposal from the selected contractor or documentation showing scoring of proposals could be located.

In another example, based on our review of existing documentation and interviews, we found that the department entered into a contract and an amendment that appeared to have been arranged as payment for a prior informal work agreement in which a contract and the related \$75,000 payment had been overlooked.

As explained to us by the contractor, arrangements were made for the department to pay \$50,000 to the contractor for administering conferences that the contractor was arranging and had not originally planned on any department financial participation. This was done through the execution of the new \$50,000 contract. The amendment of an existing contract paid the remaining \$25,000 of the informal agreement.

During our audit, we also noted three separate contracts totaling \$12,725, written in amounts less than \$5,000 each, in what appeared to have been an effort to allow direct negotiation with a pre-selected contractor. It also appeared from department documentation that the work was substantially completed prior to contract execution. This exception to contracting rules was identified by department management who informed the contract initiator of the inappropriateness of this practice.

Unjustified Sole Source Contracts

According to state contracting rules, contracts may be “sole sourced” to one specific vendor when only one contractor can provide the services because of unique expertise, or when it is

unlikely that competition will be substantially diminished. Contracting rules require that written justification supporting the sole source determination be kept in the contract files, including evidence of market research.

We found that the department inappropriately applied sole source rules to acquire specialized, but not unique, services for three of the 40 contracts reviewed (approximately 8 percent).

For example, the sole source provision was used for an \$11,050 contract to acquire services for writing and reviewing reading items for student testing. Although contractors would need to have specialized skills to perform these services, they are not unique. This is supported by the fact that the department contracts with other individuals for the performance of similar work.

Lack of Required Documentation

According to state contracting rules, contract files should contain solicitation and selection documentation, a record of the negotiation of the contract terms and executed contracts.

We found that for nine of the 40 contracts reviewed (approximately 23 percent), contract file documentation did not contain the documentation necessary to ensure that vendor proposals were consistently and objectively evaluated and that contracts were fairly awarded.

For example, for a \$25,000 contract, auditors were provided documentation showing that five proposals were received. A scoring sheet for the selected contractor was also provided; however, there was no documentation available to indicate how the other proposals were scored.

Contract Administration Needs Improvement

In addition to the issues identified surrounding the awarding of public contracts, we identified other contract administration processes that needed attention. We found that the department did not always follow state contracting rules when administering contracts and contract amendments, which resulted in questioned costs and increased risk of financial loss to the state should disagreements with contractors occur.

Written contracts and amendments help protect the interest of the state by ensuring that the responsibilities of the parties, definition of deliverables, compensation and other agreements are documented in writing.

Services Performed Without a Contract

According to state contracting rules and standard language within personal services contracts, all requisite approvals must be obtained before any service may be performed under a contract. During our audit we identified instances in which work was performed prior to the creation of an approved contract.

For example, the department created three contracts totaling \$5,250 after work was completed.

We also identified one contractor who performed personal services without a contract and was reimbursed through three purchase orders totaling approximately \$1,470. In addition, the contractor was overpaid on one of the purchase orders by approximately \$265.

Amendments Did Not Follow State Rules

According to state contracting rules, personal services contracts may not be amended after the original contract expires without formally reinstating the contract

within 60 days. State contracting rules have specific requirements for agencies to follow for reinstatements. For example, the agency should document that the failure to extend or renew the personal services contract in a timely manner was due to unforeseen or unavoidable conditions. During our audit we identified four amendments that did not follow these state contracting rules.

For example, we found three amendments that were signed after the original contract had expired. Two of these had no reinstatement, and one amendment had a reinstatement but was signed after the 60-day time limit.

We also noted one contract that should have been treated as an amendment to an expired contract. The new contract was directly negotiated even though it exceeded the \$5,000 threshold for direct negotiation by \$20,000 and was an extension of work included in a prior contract.

Payment Approval Process Does Not Meet Guidelines

We found that the approval process for contract payments was not performed as required by state guidelines. Payments totaling approximately \$37,600 related to 12 contracts were either not adequately supported by contract deliverables or not properly approved for payment.

Deliverables Not Retained

The *Oregon Accounting Manual* (OAM) states that by approving an invoice for payment the approver is attesting that the materials, services, or other expenses covered by the claim have been furnished, rendered, or expended on behalf of the state.

The contract files for six of the 114 contracts with individuals and non-governmental entities reviewed during our audit, for contracts totaling approximately \$165,000, did not contain evidence of deliverables

to support all contract payments made. After additional research and inquiry some documentation of deliverables were obtained; however, the department could not provide documentation supporting payments totaling approximately \$19,000 for four contracts.

Due to insufficient documentation of deliverables, we could not determine if the department received the deliverables for which it contracted.

Approval by Unauthorized Individuals

We found that eight of the 114 contracts with individuals and non-governmental entities reviewed had payments totaling approximately \$18,600 that were either not approved or not approved by an individual with delegated authority. There were also eight contracts with payments approved by contract administrators named in the contract, but who did not have written delegated authority to approve expenditures as required by the OAM. The OAM allows agency heads to delegate their expenditure decision authority in writing to subordinates.

Typically, written delegated authority identifies the individuals responsible for ensuring the appropriateness of expenditures. Written delegated authority is not only a requirement of the OAM, but it is an important control designed to control access to assets and reduce the risk of loss.

Contributing Factors

These conditions existed due to several factors, including:

- The department delegated responsibility for contracting to the program offices without adequate monitoring by the management services section, and without adequate policies and procedures in place. The department also does not have

adequate policies and procedures to ensure only authorized personnel approve payment of invoices.

- Lack of training provided to program personnel assigned contracting duties. During our audit we noted that personnel were sometimes confused about which state contracting rules to follow.
- Lack of timely notification of contract personnel when follow up was needed to ensure that critical time requirements were met.

Recommendations

We recommend that department management:

- Establish clear written policies and procedures defining contract administration responsibilities. These policies and procedures should clearly assign responsibilities between department staff for standard procedures, including contract solicitation and selection responsibilities. Documentation retention requirements should also be addressed.
- Establish a standard training curriculum for all staff assigned contracting responsibilities. Training should include basic principles of state contracting rules and responsibilities of contract administrators, including approval of invoices for payment.
- Establish provisions with the department's new central procurement unit for a quality assurance review of files to ensure compliance with state contracting rules.
- Provide a written directive to managers, program staff, and procurement unit staff regarding the importance of competitive bidding practices.
- Consider improving the contract database system so that it can be

used to notify contract personnel of approaching critical timelines.

- Improve internal policies and procedures to ensure that authorized personnel approve payment of invoices. If the department's director chooses to delegate expenditure approval authority to contract administrators named in the contract, this intent should be included in the department's internal policies.
- Review overpayment and questioned costs identified in this report and consult with the Department of Justice to determine appropriateness and potential recovery of any amounts improperly paid.

Agency's Response:

We have reviewed the audit of the Department of Education Contracting Practices. The audit findings reflect practices that do not meet Superintendent Castillo's management standards. As it noted in the audit, the Department instituted corrective action during the course of the audit work. We intend to use these final audit findings and recommendations to complete corrective action.

Agency Accomplishments

We commend the department on the actions it has taken to improve some of the conditions noted in our audit. For example, in May 2002 the department hired an individual who holds a state-issued procurement certification to manage a newly created procurement unit. The department has also developed contract training classes for individuals with contract responsibilities and is working on enhancements to its contract management information system.

Objectives, Scope and Methodology

The objective of our audit was to determine if the department's

contract procurement and administration practices are adequate and comply with applicable laws and regulations. Specifically, we tested contract files to determine if:

- Contracts complied with applicable statutes and state administrative contracting rules.
- Contracts and disbursements were properly approved.
- The department received all contracted services or goods.
- Contract disbursements were based on a bona-fide liability.
- Contract disbursements were accurately recorded.

We also performed procedures to determine if:

- Contracts were entered into with contractors who were department employees, or with contractors related to department employees that may have violated state ethics laws.
- Specific allegations that came to our attention contained any merit.
- Large contracts were written as multiple smaller contracts in order to avoid competitive bidding.
- The price of intergovernmental agreements for individuals who were on job rotation agreements was reasonable.
- Intergovernmental and Interagency agreements are in compliance with state laws and rules.

To accomplish these objectives we:

- Reviewed pertinent laws, state administrative rules, and department policies and procedures.
- Interviewed or contacted department staff, Department of Justice attorneys, Department of Administrative Services purchasing staff, and other individuals deemed necessary.

- Judgmentally selected contracts to review because of allegations received or based on risk. For example, we performed analytical procedures on accounting, payroll and business registry records in order to identify contracts that may have been entered into in violation of state ethics laws. State ethics laws do not allow public officials, including employees, to personally benefit from their official position.
- The department did not have a reliable contract database available to select contracts for testing. We therefore randomly selected contract payments made to individuals and non-governmental entities from all contract payments recorded by the department into the Statewide Financial Management System (SFMA) from July 1, 1999 through September 30, 2001. We then tested the related contract. We considered the data extracted from SFMA used to select our sample to be sufficiently reliable for our purpose, based upon prior application control reviews performed by our office and selected file reviews performed during the course of our audit.
- We judgmentally tested additional payments related to contracts reviewed.
- In total we reviewed 127 contracts, of which 114 were personal services contracts and trade services agreements, and 13 were Intergovernmental or Interagency Agreements. Twenty of the contracts reviewed were randomly selected. The remaining contracts were judgmentally selected for review.

We conducted our fieldwork from January 2002 through August 2002. Our audit was conducted in accordance with generally accepted government auditing standards.

This report, which is a public record, is intended to promote the best possible management of public resources. Copies may be obtained by mail at Oregon Audits Division, Public Service Building, Salem, Oregon 97310, by phone at 503-986-2255 and 800-336-8218 (hotline), or internet at Audits.Hotline@state.or.us and <http://www.sos.state.or.us/audits/audithp.htm>

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The courtesies and cooperation extended by the officials and staff of the Department of Education were commendable and much appreciated.

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