Audit of
Department of Administration
Business Operations Division
Procurement Services Section
Contract Processing

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December 10, 2013

Honorable Tom Barrett, Mayor
The Members of the Common Council
City of Milwaukee

Dear Mayor and Council Members:

The attached report summarizes the results of our audit of the Department of Administration (DOA) Business Operations Division – Procurement Services contract processing. The objectives of the audit were to determine whether the DOA procurement activity is in compliance with the City of Milwaukee Charter and Ordinance requirements; assess the adequacy and effectiveness of internal controls over contract processing; verify whether contracts are recorded accurately and timely on the Financial Management Information System; and assess the adequacy of the policies and procedures for the timely, effective, and efficient acquisition of commodities and services.

Overall, the audit concluded that the internal controls in place surrounding contract processing are operating effectively. However, there are gaps in the control design that expose Procurement Services to risks that were identified in the audit. This report identifies five recommendations to address these issues.

Audit findings are discussed in the Audit Conclusions and Recommendations section of this report, which is followed by management's response.

Appreciation is expressed for the professionalism and cooperation extended to the auditors by the staff of the Department of Administration – Procurement Services.

Sincerely,

Aycha Sirvanci, CPA
Audit Manager

AS:ssm

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I. Audit Scope and Objectives

The audit examined the processes and controls for procurement transactions processed by the Department of Administration's Business Operations Division Procurement Services Section (Procurement Services). The audit also assessed the section's internal policies and procedures for adequacy in addressing the provisions of the Milwaukee City Charter and Code of Ordinances governing City purchases.

The scope of the audit included all purchase requisitions received by Procurement Services through the Financial Management Information System (FMIS) during the twelve month period starting July 1, 2012. The audit excluded contracts entered into by departments with contracting authority since they are not processed by Procurement Services. Additionally, the audit did not include a review of purchases made with Procurement Cards, or the materials management process (the disposal of the City's surplus, obsolete or scrap materials and equipment). Audit procedures were executed during August and September 2013.

The audit methodology included developing an understanding of processes and controls for purchasing transactions processed by Procurement Services. Audit procedures developed to evaluate the processes and controls to meet the audit objectives included process walk-throughs, inspection of relevant control documentation, tests of controls, and detail testing. Procedures and tests conducted included verifying a sample of contracts were processed timely and in accordance with policies and procedures, including the presence of complete and accurate documentation; verifying requisitions contained all required information and were properly approved; confirming contracts were awarded to the appropriate bidders; and assessing internal policies and procedures for adequacy.

Information obtained and reviewed included internal policies and procedures, certain chapters of the City Charter and Code of Ordinances, signed contracts and purchase orders with the supporting documentation contained in the contract file, bid advertising invoices, internal requisition status and monitoring reports, and a list of authorized FMIS requisition approvers. Internal Audit believes that the evidence obtained provides a reasonable basis for the audit's findings and conclusions based on the audit objectives.

The objectives of the audit were to:

- Determine whether the DOA procurement activity is in compliance with the City of Milwaukee Charter and Ordinance requirements;
- Assess the adequacy and effectiveness of internal controls around contract processing;
- Verify whether contracts are recorded accurately and timely on FMIS; and
- Assess the adequacy of the policies and procedures for the timely, effective, and efficient acquisition of commodities and services.

II. Organization and Fiscal Impact

Chapter 16 of the City Charter establishes the Business Operations Division in the Department of Administration with the authority to purchase. The division is under the direction and control of the city purchasing director who has the full power to provide for the purchase of all materials, supplies, and equipment and services. The Business Operations Division serves approximately fifty City departments, boards, and commissions and consists of four sections: Procurement Services, Materials Management, Document Services, and the Office of Small Business Development. The scope of this audit is limited to the Procurement Services Section. Procurement Services is the City's centralized buying and supply management agency responsible for the procurement of approximately $85,000,000 in goods and services annually. All procurement transactions over $5,000 must be authorized in writing by Procurement Services in order for them to be valid and negotiable.[1] Under the management of the purchasing director, the section is staffed with one procurement administrator, one procurement specialist, four senior purchasing agents, one administrative specialist senior, and one contract secretary.

Procurement Services serves internal and external customers. Their mission is to acquire commodities and services for City departments in the most cost effective, efficient and impartial manner within the appropriate guidelines. Internally, user departments needing to purchase goods and services utilize Procurement Services to execute the contracts. Externally, vendors compete for the contracts through the bidding process, or are selected directly by the user

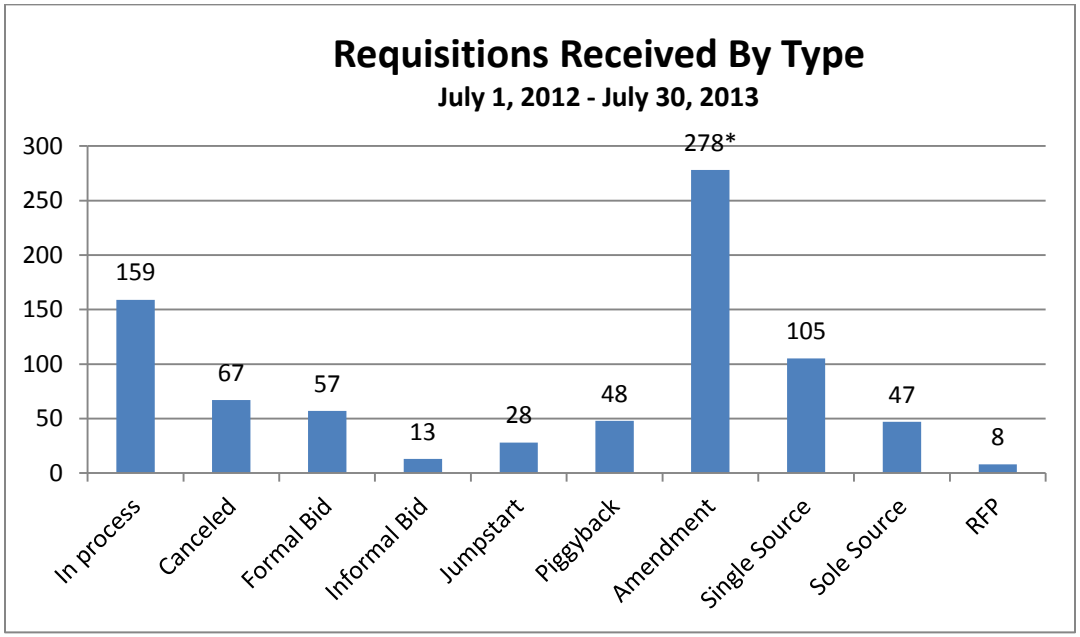
[1] http://city.milwaukee.gov/BusinessOperations.htm

department when granted an allowed exception to bid. Invitations for contracts that are put out to bid are posted online, and vendors can sign up to receive electronic notices of new bids.

All purchases are reviewed by Procurement Services for ethics and social responsibility, price, and quality. There are over 500 active contracts and there were over 200 contracts with effective dates in 2012. Purchasing receives approximately 800 requisitions each year. The bidding process, which is used for the majority of requisitions, should take 30 - 90 days from the time the requisition is received by Procurement Services to the time the contract is signed.

Formal contracts are created for purchases over $30,000.[2] Informal contracts are created for purchases $10,001 - $30,000, and the JumpStart process is used for all contracts $5,000 - $10,000. Requisitions are created through the purchasing module of FMIS. Procurement Services received 810 requisitions between July 1, 2012 and July 30, 2013. Of the 810 requisitions received during this timeframe, 532 resulted in new procurements. In addition, there were 278 amendments to existing contracts. See Table 1 for requisitions by contract award type.

Table 1



* Note: The contract amendment figure of 278 is comprised of various contract types such as formal, informal, piggyback, single and sole source contracts.

[2] At the time of fieldwork. The threshold for formal contracts was increased to over $50,000 as of October 9, 2013.

The City utilizes FMIS to facilitate its purchasing activities. The system houses all created vendor data, serves as the platform for issuing and managing purchase orders, and is utilized to process payments through the accounts payable module.

III. Audit Conclusions and Recommendations

Overall, the audit concluded that the internal controls in place surrounding contract processing are operating effectively, however, there are gaps in the control design that expose Procurement Services to risks resulting from overlong processing times, inconsistent documentation, and confusing ordinances. This report identifies five recommendations to address these issues:

1. Revise the Code of Ordinances to clarify when a written waiver for the ethical purchasing statement is required.
2. Revise the Code of Ordinances regarding recycled content of all paper purchased for achievability, practicality and clarity.
3. Develop and implement a formal quality control process.
4. Provide training to staff on professional (personal) service contracts.
5. Address requisitions at risk for aging.

Additional details regarding the recommendations for improvement are provided in the following sections of this report.

A. Compliance with Milwaukee City Charter and Code of Ordinances

The audit included procedures to determine compliance with the specific provisions of the Milwaukee City Charter and Code of Ordinances that govern procurement. Specifically, purchases are governed by the following:

- City Charter Chapter 3 - Duties and Authority of City Officers, section 3-29
- City Charter Chapter 16 - Purchasing
- Code of Ordinances Chapter 310 - Department of Administration, sections 310-12 through 310-18

- Code of Ordinances Chapter 365 - Local Business Enterprise Contracting Program

Based on audit procedures performed, Procurement Services is processing purchases in compliance with the specific chapters of the City Charter and Code of Ordinances identified above. However, the audit disclosed two subsections of Chapter 310 that warrant revision to provide clarity of intent and consistency in application.

Requirements for Non-apparel Purchases

Section 310-17 of the Code of Ordinances provides that it is in the best interest of the City to procure items from responsible vendors and manufacturers who provide a safe, nondiscriminatory work environment, and who compensate their employees with non-poverty wages. Subsection 310-17-4 requires a sworn report or affidavit including a statement by the bidder that the bidder's facilities are responsible manufacturers for all non-apparel items, materials, supplies and equipment in excess of $30,000 that are bid by the city. The requirements of this section may be waived in writing by the purchasing director if the "items can be furnished from only one source" [single and sole source], "or items constitute a special adaptation for a special purpose, pursuant to s. 16-05-3 of the charter" [includes piggybacks]. However, the ethical purchasing affidavit is not required for single and sole source contracts or piggyback contracts. These contracts are exceptions to the bidding process, therefore, the ordinance would not apply and a written waiver would not be required. The Subsection regarding the waiver of the affidavit for single and sole source contracts and piggybacks is superfluous and leads to confusion.

Recommendation 1: Revise the Code of Ordinances to clarify when a written waiver for the ethical purchasing statement is required.

Subsection 310-17-5-c of Milwaukee City Ordinances should be revised as it relates to Subsection 310-17-4 to clarify when a written waiver is required by the purchasing director. As written, it could lead a reader to conclude that a written waiver is required for certain exceptions to the bidding process, however, the ordinance is only applicable to those contracts that go out for bid.

Purchase of Products Made from Recycled Materials – Paper Products

Subsection 310-15-3 of the Code of Ordinances states "each city public purchaser shall ensure that the average recycled or recovered content of all paper purchased by the city public purchaser in a year is not less than 40% of all purchased paper."

A city-wide paper contract was awarded to two vendors in September 2013. The specifications in the bid prepared by Procurement Services required a minimum recycled paper content of 30 percent. Per the ordinance, it is not clear whether the recycled/recovered content of the paper purchased should be at least 40 percent, or at least 40 percent of paper purchased in a year should have recycled content. Purchasing paper with a minimum 40 percent recycled content may not be achievable or practical based on cost. Ambiguous language in the ordinance increases the risk of noncompliance with the intent of the ordinance.

Additionally, Procurement Services' internal process manual does not have a procedure to provide guidance to the purchasing agents regarding compliance with the ordinance. Lack of a specific policy and procedure may lead to inconsistent interpretation across purchasing agents, and ultimately noncompliance with the ordinance.

Recommendation 2: Revise the Code of Ordinances regarding recycled content of all paper purchased for achievability, practicality, and clarity.

Subsection 310-15-3 of the Code of Ordinances regarding recycled content of all paper purchased should be revised for achievability, practicality and clarity. Procurement Services Management should then draft an internal procedure to address the process for complying with the ordinance consistently and add it to the Purchasing Internal Processes Manual.

B. Contract Processing Internal Controls

The purchasing process starts with entering a requisition into FMIS by the user department. A requisition is required for all contract purchases. Access to create requisitions in FMIS is limited to authorized individuals. When a requisition is received, purchasing agents verify the budget status is valid.

Chapter 16 of the City Charter requires that formal bids are conducted for purchases valued over $30,000.[3] All requisitions are reviewed by the Office of Small Business Development (OSBD) and the purchasing director before posting. Formal bids are advertised on the city's website, distributed to bidders via E-notify, and published in the official newspaper. When bidding is closed and all complying bids have been determined, the bids are tabulated to determine the lowest compliant bidder. The contract is then created, signed, and distributed after the appeal period expires.

An exemption from the competitive bid process exists for the purchase of goods and services and is permitted when the goods or services to be purchased are impossible or impractical to procure through competitive procurement. The user department enters a requisition and submits the 'Exception to Bid and OSBD Analysis' form. The form requires the signature of the user department and the purchasing agent. When a single or sole source service contract of $50,000 or more is executed or an existing single or sole source service contract of less than $50,000 is amended and the original amount of the contract added to the amended amount of the contract is $50,000 or greater, the contract or amendment must be approved by the Finance and Personnel Committee.

Generally, before contracts are routed for signing, the contract file is reviewed for the proper documentation such as the Ethical Purchasing Affidavit (if the bid is for a non-apparel commodity), the Apparel Affidavit (if the bid is for apparel or textiles), Affidavit of Compliance with Living Wage Provision (for service contracts exceeding $5,000), the Certificate of Insurance and Affidavit of No Interest (if the bid is for a service or for a very large piece of equipment), Local Business Enterprise Affidavit, OSBD Form A (Small Business Enterprise Requirements), the Slavery Disclosure Affidavit (all purchases), and a binding signature page (all bids). These documents demonstrate the expenditure of public funds was made in accordance with the City Charter and Code of Ordinances.

The audit tested 81 files for proper documentation, appropriate approvals, compliance with provisions of the City Charter and Code of Ordinances, and accuracy of recording in FMIS. The

[3] At the time of fieldwork. The threshold for formal contracts was increased to over $50,000 as of October 9, 2013.

audit also verified the bids were properly advertised, and the contract was awarded to the correct bidder based on bid compliance and price.

Quality Control

Testing results indicate the development and implementation of a quality control review could reduce the frequency of errors and missing documents. Approximately 12 percent of contract files reviewed were missing one or more of the required documents or contained documents with errors or omissions. Specifically:

- The Slavery Affidavit was not obtained for one vendor.
- The justification for a sole source purchase and the user department approval was missing from one file.
- Two files for JumpStart contracts did not contain the minimum number (three) of required quotes for pricing.
- Two files were missing the OSBD Participation and Analysis form.
- Two files were missing the Exception to Bid form.
- The term on one of the written contracts did not agree with the term recorded in FMIS.
- The date of award on one contract was incorrect.

The exceptions listed above can generally be attributed to the fact that the procurement process is a highly manual, complex and varied process.

Recommendation 3: Develop and implement a formal quality control process.

The Procurement Services Section should develop and implement a formal file review to ensure all required documents have been obtained and retained, and are properly completed. The quality control review could be performed either on a sampling basis or performed over the entire population of newly generated contracts. Any errors identified should be remedied if possible, and the results of the quality control review should be tracked, documented, and reported to the purchasing director on a periodic basis. The review results could also be utilized to identify trends and training opportunities.

Professional (Personal) Service Contracts

Additional documents are required for professional (personal) service contracts. A professional (personal) service contract is defined in s. 310-13-2-a as any contract in which the majority of workers engaged in the performance of the contract perform work which is predominantly intellectual and varied in nature, as opposed to work which involves routine mental, manual, mechanical or physical labor; and requires advanced knowledge in a field of science or learning customarily acquired by a prolonged course of specialized intellectual instruction and study in an institution of higher education or a hospital. Due to a misunderstanding of the definition of a professional (personal) service contract, Purchasing Agents were not consistently obtaining the required documents. These documents (the request for pricing form, the summary of experience form, the professional services contract questionnaire, and the certificate of professional liability insurance) provide consistency in contracting, protect the city from incurring liability, and mitigate the risk of non-compliance with IRS guidelines for the applicability of payroll taxes when contracting with former employees.

Recommendation 4: Provide training to staff on professional (personal) service contracts.
Management should provide training to applicable staff regarding what constitutes a professional (personal) service contract, when to obtain the required documents, and when professional liability insurance is warranted. Additionally, insurance coverage and professional (personal) service contract documents should be included in the quality control review.

C. Policies and Procedures

Procurement Services maintains the Purchasing Liaison Manual as a guideline for user departments for proper purchasing procedures when needing to purchase items or services. To supplement the information in the Purchasing Liaison Manual, Procurement Services also has a Purchasing Internal Processes Manual (PIP) with comprehensive procedures for the various tasks performed. Purchasing agents and the purchasing director monitor contract processing time to ensure requisitions are processed within a reasonable timeframe using the daily Requisition Status Report and the Bi-weekly Workflow Report.

The audit included an assessment of the policies and procedures for adequately addressing timely, effective, and efficient acquisition of commodities and services. As a result, it was noted

that there are no procedures in place to proactively address requisitions at risk of aging beyond a reasonable timeframe for completion. Testing identified 8 contracts (10 percent of the testing sample) with processing times ranging from 114 to 277 days. The processing time for these contracts is unsatisfactory for the nature of the product or service and the type of contract awarded. Currently, there are only 5 purchasing agents to manage the high volume of requisitions received, meaning at any one time each purchasing agent is managing approximately 25 purchases.[4] The number of purchasing agents and support staff has steadily decreased over the last 20 years while the complexity of the purchasing process continues to increase. Additionally, while progress is monitored routinely, there is no formal process in place to redistribute the work load to address aging requisitions. Overlong processing times can frustrate user departments, and cause service disruptions and unproductive time for employees. Additionally, deadlines may be missed for grant applications impacting the potential to receive a grant award.

Recommendation 5: Address requisitions at risk for aging.

Management should develop and implement procedures to redistribute the work load to address requisitions at risk for aging. The procedures can leverage the monitoring already in place and should include parameters defining when and how to redistribute the work load.

[4] As of September 23, 2013.

City of Milwaukee

Department of Administration
Business Operations Division

Tom Barrett
Mayor

Sharon Robinson
Director of Administration

Rhonda U. Kelsey
City Purchasing Director

December 6, 2013

Aycha Sirvanci, CPA
Comptroller's Office, Audit Section
City Hall, Room 400

RE: Response to the Audit of the Department of Administration-Business Operations Division-Procurement Services Contract Processing

Dear Ms. Sirvanci,

Thank you for your audit of the Department of Administration (DOA)-Business Operations Division- Procurement Services Contract Processing. DOA appreciates the opportunity to work with your staff and appreciates and values the audit's recommendations for improving DOA's contracting processes.

We have reviewed the audit and offer the following responses to its recommendations:

<u>Recommendation 1</u>: Revise the Code of Ordinances to clarify when a written waiver for the ethical purchasing statement is required.

DOA-Procurement Services shares the audit's concern about ensuring that city ordinances that govern the complexities of the procurement process are clear and looks forward to working with the legislative branch and the City Attorney's office to provide clarity when a written waiver for the ethical purchasing statement is required. As the audit states, the waiver applies to bids and does not apply to exception to bid contracts or piggybacks and therefore it is not necessary to require a written waiver.

DOA-Procurement Services has informed the legislative branch and the City Attorney's office that these legislative changes should be made to the Code of Ordinances along with additional changes to Chapter 310 as a result of recent changes made to Chapter 16. DOA-Procurement Services has scheduled a meeting with the City Attorney's office for December 23, 2013 to begin this process.

Implementation Date: April 1, 2014

<u>Recommendation 2:</u> Revise the Code of Ordinances regarding recycled content of all paper purchased for achievability, practicality, and clarity.

With regard to Subsection 310-15-3 of the Code of Ordinances (Purchase of Products Made from Recycled Materials – Paper Products), it is important to point out that all bids issued by DOA Procurement Services for the purchase of paper have included a 30% recycled paper content

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requirement in accordance with federal Environmental Protection Agency (EPA) standards. All bids that are issued for the purchase of paper by PSS are reviewed to ensure that the 30% paper content requirement is included in an effort to meet EPA standards. As a result, DOA-Procurement Services has not awarded any contracts for the purchase of paper that are not in alignment with federal EPA standards. Simultaneously, DOA-Procurement Services shares the audits concerns that this section of the code of ordinances is vaguely written, as it may be difficult to determine if the ordinance references a 40% recycled paper content requirement or an overall 40% paper purchase requirement for each city public purchaser. DOA-Procurement Services will work with the legislative branch to craft language that attempts to make the intent of the policymakers that adopted the recycled paper content language almost two decades ago clear, practical, and achievable. In addition, DOA-Procurement Services will include a section in its internal Purchasing Internal Procedures Manual that speaks specifically to the purchase of recycled paper.

Implementation Date: April 1, 2014

Recommendation 3: Develop and implement a formal quality control process.

DOA-Procurement Services shares the audit's concern that the procurement process is a highly manual, complex and a varied process with many layers. Unfortunately, the existing purchasing module that is in use does not provide for a "formal" quality control process. The quality control process currently in place utilizes existing resources such as a Requisition Tracking form. The Requisition Tracking form is utilized with each requisition received via the FMIS system and provides a checklist of applicable city ordinances for all procurements. This tool is used as a guide for Purchasing Agents and the Contract Secretary to ensure that all applicable city ordinances and purchasing procedures are followed. The Contract Secretary serves as the sole administrative support staff person in conducting a secondary review of the Requisition Tracking form to ensure that all required documentation is received and complete prior to contract execution. It is important to point out that the purchasing staff was significantly larger a number of years ago, at a time when the purchasing process was far less complex and layered. In light of the increased complexity of the city's contracting processes, and in spite of significantly reduced staffing levels, DOA-Procurement Services has a fairly solid record of minimizing the number of bid and specification appeals from 2008 to present. This indicates that a high level of integrity and fairness is maintained by DOA-Procurement Services in its bidding and contracting processes.

DOA-Procurement Services agrees with the audit recommendation regarding the need for the implementation of a formal quality control process. This could be achieved via the use of an efficient E-Procurement module that interfaces with the City's Financial Management Information System (FMIS) or an enhancement of existing functionality in FMIS which would automate and formalize the tracking of procurements throughout the contracting process to ensure accuracy. DOA – Procurement Services has scheduled meetings with the DOA-Information Technology Management Division (ITMD) regarding the purchase and implementation of an E-Procurement module as a result of funding that was recently approved in the 2013 Capital Improvements Budget and is excited about the promise that this purchase might provide in helping to automate and streamline the procurement process. Additionally, in an effort

to be proactive, DOA-Procurement Services will enhance its internal controls by re-designing the Requisition Tracking Form and bolstering the Contract Secretary's responsibilities in serving as a secondary review to ensure that all required document is received prior to contract execution. Furthermore, and in agreement with the audit recommendation**,** DOA-Procurement Services will conduct a quarterly compliance review of a sample of contracts that have been created in an effort to identify issues or trends. The results of the compliance review will be shared with all PSS staff and training will be provided in an effort to increase accuracy in areas found to be problematic, and corrections will be made immediately. Finally, any files determined during the audit to have missing, incomplete or inaccurate documentation have been reviewed and the discrepancies have been rectified.

Implementation Date: Action already in progress with an anticipated completion date of July 1, 2014.

Recommendation 4: Provide training to staff on professional (personal) service contracts.
A re-training session regarding what documentation is required was held with Procurement Services Staff on October 3, 2013. The reference to the word "personal" was removed from the forms, the Purchasing Internal Procedures manual and the Purchasing Liaison Manual to further clarify that a "personal" service contract can be provided by either an individual or an actual business/firm where it might not be clear the business is ran by an individual. Additionally, the Requisition Tracking Form was updated to include the Professional Service Contract Questionnaire and the Summary of Experience form to improve and allow for increased quality controls.

It is important to point out that the distinction between professional and non-professional service contracts has always been apparent and DOA-Procurement Services did not fail to obtain appropriate insurance coverages. However, the issue that contributed to confusion, as highlighted in the audit, is the lack of a distinction between a "personal" service contract with an "individual (doing business in his/her name)" as opposed to a contract with a formal business entity where it was not immediately evident that the service being provided was with an individual who owned a business utilizing a formal business name as referenced on the W-9's that are submitted by vendors. Again, this has been addressed in the DOA-Procurement Services internal procedures manual and staff has already been directed to probe deeper to determine if the service is actually being provided by an individual or an actual company/firm.

Implementation Date: October 3, 2013

Recommendation 5: Address requisitions at risk for aging.

The existing procedure that the DOA-Procurement Services has in place to monitor and reassign aging requisitions includes the use of the following workload reports: Daily Req Status Report; Biweekly Requisition Status Report; and a Biweekly Workflow Review Report. These reports are used as project management tools for Purchasing Agents to manage their workflow and stay on target with meeting PSS contracting processing timelines when possible. In addition, the Purchasing Director meets with all Procurement staff members on a biweekly basis to review the status of all requisitions received as well as to resolve any procurement issues or questions that

Procurement staff may have. The need to reassign requisitions is assessed at the biweekly meetings upon review of each Purchasing Agents workload and does occur when deemed appropriate. In addition, the Procurement Administrator meets on a biweekly basis with the Contract Secretary to ensure that the appropriate documentation is received and contracts are fully executed. It is important to point out that the reasons for aging requisitions varies and can be dependent on a number of factors to include but not limited to: user department need; status of receipt of pending information to process the procurement and overall prioritization of citywide procurements based on need or importance. Although the DOA-Procurement Services has an existing procedure in place via the use of workload reports and regular staff meetings, it is a very manual based system and should be automated to minimize the number of aging requisitions. Again, and as stated earlier the DOA-Procurement Services is excited about the opportunity to implement a new purchasing module and/or upgrade existing functionality in an effort to address the audit's concern is this area.

Implementation Date: Action already in progress with an anticipated completion date of July 1, 2014.

Sincerely,

Rhonda Kelsey
City Purchasing Director