



AUDIT OF PROCUREMENT PROCESS

Follow Up Report

ABSTRACT

Significant monitoring improvements have been made to facilitate compliance with applicable purchasing laws for about \$203 million in annual expenditures; however, some additional improvements are still necessary especially when sole sourcing goods or services.

City Auditor's Office

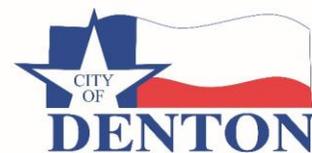


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Executive Summary

Honorable Mayor and City Council Members,

We have completed a six-month follow up review of the Procurement Process Audit, which was originally issued in August 2019. This follow up reviews are intended to provide information on what changes have been made in response to the audit.

Overall, we found that significant monitoring improvements have been made to facilitate compliance with applicable purchasing laws for about \$203 million in annual expenditures including the implementation of an electronic bidding system and additional compliance verifications for every purchase requisition. Still, some additional improvements are necessary as described below:

- Texas law prohibits municipalities from using separate, sequential, or component purchases as a means of avoiding bidding requirements. While new monitoring processes provide assurance requirements are not avoided using multiple purchases, wide-spread use of commodity codes would ensure that expenditures are not divided among suppliers. This type of monitoring would provide further assurance that the City is complying with purchasing laws and could result in additional volume discounts.
- Texas law exempts certain purchase types from its competitive bidding requirements. These sole source purchases require special attention from the Purchasing Division to ensure that the City complies with the law. Purchasing has improved documentation of the department's justification for sole source purchases; however, additional improvements should be made to ensure that Purchasing is performing adequate due diligence when sole source purchase are made. This type of documented due diligence is especially necessary when the department's justification indicates that the purchase may not meet exemption requirements.

The original audit report made 14 recommendations, 12 of which are either implemented or in progress. While additional follow up work is needed in the future, the Purchasing Division has made significant improvements since the issuance of the audit. We appreciate staff's cooperation and time during the audit. Please contact the City Auditor if you have any questions.

Sincerely,
Umesh Dalal, City Auditor

Introduction

The City Internal Auditor is responsible for providing: (a) an independent¹ appraisal of City operations to ensure policies and procedures are in place and complied with, inclusive of purchasing and contracting; (b) information that is accurate and reliable; (c) assurance that assets are properly recorded and safeguarded; (d) assurance that risks are identified and minimized; and (e) assurance that resources are used economically and efficiently and that the City's objectives are being achieved.

The City Auditor's Office has completed an audit follow up of the Procurement Process Audit issued in August 2019. We conducted this follow up review in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Management Responsibility

City management is responsible for ensuring that resources are managed properly and used in compliance with laws and regulations; programs are achieving their objectives; and services are being provided efficiently, effectively, and economically.

Audit Objectives, Scope, and Methodology

This report is intended to provide a progress update on recommendations from the Procurement Process Audit (August 2019), which reviewed the City's compliance with procurement regulations.

Audit fieldwork was conducted during January 2020. The scope of review varied depending on the procedure being performed. The following list summarizes the major procedures performed:

- Reviewed documentation from the issued audit to develop criteria including industry standards, best practices, policies, and procedures;
- Examined a statistical sample² of 91 purchase orders issued between June 2019³ and November 2019 to determine the implementation status of recommended documentation and process improvements;
- Reviewed a judgement sample of 30 solicitations issued since July 2019⁴ to determine if recommended documentation and process improvements had been implemented;
- Reviewed the purchases of a judgement sample of 22 suppliers whose procurements totaled just over \$50,000 (i.e. between \$50,000 and \$70,000) between December 2018 and November 2019; and
- Interviewed Purchasing Management and reviewed provided documentation.

¹ The City of Denton Internal Auditor's Office is considered structurally independent as defined by generally accepted government auditing standard 3.56.

² This sample size provides with 95% confidence that the true population mean is within $\pm 10\%$ of the sample estimate.

³ The scope of this audit is based on the presentation of the report to the Audit/Finance Committee in June 2019.

⁴ Only solicitations issued in the City's new electronic bidding system were considered for review.

Recommendation Status Update

This report summarizes the Audit of Procurement Process's recommendations, management responses, and City Auditor's Office's follow up findings, which described to what degree City Management has implemented the City Auditor's Office's recommendations since publication of the original report (August 2019). Recommendations and their implementation results are grouped as they were in the original report.

Procurements Exceeding \$50,000

1. Provide training to Procurement staff and departmental liaisons on purchasing regulations.

Management Response: Concur

Training is provided quarterly to department liaisons and as requested for department users, Purchasing staff training is budgeted annually and attended as relevant training is available.

Audit Follow Up Finding: In Progress

The Purchasing Division has provided several trainings to department staff on newly implemented procurement processes including the Requisition Information Form, the Sole Source Justification Form, and applicable changes to the JD Edwards system; these trainings have included references to legal purchasing requirements. In addition, reference materials for the City's new electronic bidding system have been made available to vendors.

In addition, Purchasing staff has received about three and a half hours of procurement training a month since the issuance of the audit. While this is adequate, three staff members were hired at the end of December 2019, and so have not received any procurement training. The training of these staff members will be reviewed during the next follow up report.

2. Use at least five-digit commodity codes for purchases after training departmental and purchasing personnel about their use.

Management Response: Partially Concur

Use of commodity codes will be researched further in partnership with Technology Services; commodity codes are likely not a viable option due to system constraints.

Audit Follow Up Finding: Not Implemented

No purchase orders issued between June 2019 and November 2019 included commodity code references in the JD Edwards system. Purchasing Management stated that they had been focused on implementing other recommendations and so had not yet been able to make progress on this recommendation. Without the widespread use of commodity codes in the City's financial system, the Purchasing Division's ability to monitor purchases for compliance with the law is hindered.

3. Require Purchasing personnel to monitor purchases and seek sealed bidding for expenditures exceeding \$50,000 either as one purchase or cumulatively from several purchases as agreed during this audit.

Management Response: Partially Concur

Monthly monitoring of expenditures is on-going; however, the reviews will be retrospective and will not necessary prevent future purchases from taking place especially if solicitations and contracts cannot be established in a timely manner.

Audit Follow Up Finding: Implemented

The Purchasing Division has implemented a Requisition Information Form, which requires departments to indicate whether the goods or services being requested can be procured under a contract. If a contract is not referenced on this form, Purchasing staff review the vendor's spending history for the past twelve months to ensure that consolidation opportunities are identified when appropriate. We found evidence that the City has initiated negotiations with for at least five vendors based on this process since the audit was issued.

In addition, Purchasing has developed an interactive database of all City contracts, which allows departments to review active contracts and monitor the spending level of each. While not a direct recommendation from the audit, this solution facilitates compliance monitoring for all purchases and the Department should be commended.

4. Require the Purchasing Manager to conduct a periodic spend analysis to identify opportunities for consolidation of purchases to obtain volume discounts.

Management Response: Concur

Beginning in December 2018, staff has been able to report on expenditures by vendor. Monthly monitoring by expenditures is on-going and staff is working to identify contracting opportunities.

Audit Follow Up Finding: Implemented

Purchasing has conducted a three-year spend analysis for each City department and worked with each department's management to identify consolidation opportunities, which will be monitored by a Contract Specialist. Purchasing plans on performing these spend analyses annually. We found evidence that the City has initiated negotiations with at least five vendors based on this process since the audit was issued.

Electronic Bids

5. Require Purchasing to implement an electronic solution to secure electronic bids prior to the bid opening date.

Management Response: Concur

As of 6/12/19, the City has implemented an electronic bidding software.

Audit Follow Up Finding: Implemented

The City has begun using the Ion Wave electronic bidding software.

6. Ensure that the bids, once submitted, cannot be changed.

Management Response: Concur

As of 6/12/19, the City has implemented an electronic bidding software.

Audit Follow Up Finding: Implemented

The implemented electronic bidding software adequately ensure that bids cannot be changed once submitted.

7. Require witnessing of the bid opening, which must be conducted at the designated place.

Management Response: Concur
 Purchasing staff will require witnessing of the bid opening, as stated in the solicitation documents.

Audit Follow Up Finding: Implemented

Purchasing staff has created a standard Bid Opening Form to document public bid openings. We found that ten of twenty-two solicitations reviewed had public bid openings. Of these, seven had completed Bid Opening Forms. The three solicitations with missing Bid Opening Forms all occurred prior to 10/1/2019, indicating that the process has now been fully implemented.

Procurements Exceeding \$3,000 But Less Than \$50,000

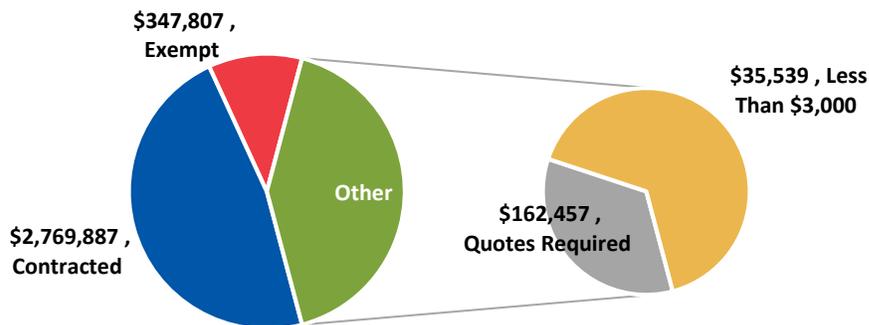
8. Require Purchasing staff to monitor purchases made to ensure that three quotes and the quotes from HUB vendors are obtained for total purchases over \$3,000 but less than \$50,000.

Management Response: Partially Concur
 Monitoring of cumulative purchases will be challenging given that the current policy does not require departments to obtain quotes or comply with HUB requirements for purchases less than \$3,000. Purchasing does not currently have a mechanism to inform departments of when non-contract expenditures with a particular vendor reach a certain dollar amount (e.g. \$3,000).

Audit Follow Up Finding: Implemented

Based on a statistical sample, about 20% of the City’s purchase orders totaled between \$3,000 and \$50,000, do not fall under a contract, and were not procured using an exemption meaning that informal quotes are required (see Figure 1).

Figure 1: Purchase Order Procurement Method Sample Results (June-November 2019)



Of the 18 purchases where quotes were required, we found the following:

- Three purchases were procured as if they were contracted; however, the items procured did not appear to be included in the referenced contract. This resulted in these purchases not having adequate quote documentation.

Based on these results, the Purchasing Division’s monitoring of compliance for purchases between \$3,000 and \$50,000 appears to have significantly improved since the issuance of the audit. Staff

should continue to verify that all items procured under a contract are included in that contract in order to avoid unintentional non-compliance with these regulations.

9. Documentation must be maintained on the record if HUB vendors providing desired products or services are not available in Denton County.

Management Response: Partially Concur

Purchasing implemented a requisition information form that requires documentation of HUB compliance. Certain purchases are exempt from HUB compliance, these purchases will not have documentation of HUB compliance.

Audit Follow Up Finding: Implemented

The Requisition Information Form is adequately designed to facilitate the monitoring of HUB compliance and appears to be effective when it is used.

Bid Evaluation

10. The Director of Purchasing and Compliance must ensure that criteria for best value are included in the request for bids/proposals.

Management Response: Concur

Evaluation criteria are stated in solicitation documents when City issues a Request for Proposal (RFP). Bids are required to meet specifications & minimum qualifications as stated in solicitation documents when City issues Invitation to Bid (IFB) to be considered for award.

Audit Follow Up Finding: Implemented

All thirty non-exempt solicitations reviewed included defined evaluation criteria. In addition, Purchasing appears to have informally adopted a standard set of RFP criteria defined as such:

- Delivery/Project Schedule – 10%
- Compliance with Specifications, Quality, Reliability, and Characteristics to Meet Stated or Implied Needs – 20%
- Indicators of Probable Performance – 10%
- Price – 60%

It should be noted that this follow up report does not express an opinion on the appropriateness of these criteria.

11. The City Council needs to adopt criteria for discussions with offerors submitting qualified proposals in accordance with the Local Government Code 252.042 (b).

Management Response: Concur

Purchasing staff are currently updating the Purchasing Manual which will include evaluation criteria in accordance with Local Government Code 252.042 (b). Council is scheduled to review and adopt the Purchasing Manual updates in August 2019.

Audit Follow Up Finding: Not Implemented

The Materials Management and Payment Procedures Manual (i.e. the Purchasing Manual) has not been updated since the Procurement Process Audit was issued in August 2019, though this update is in process. The current Manual – updated May 2018 – does not include any standard criteria for

RFP solicitations, indicating that the City Council has yet to adopt criteria for discussions with offerors submitting qualified proposals.

12. Require retention of all bid evaluation sheets along with detailed explanation of the scores assigned to each bid.

Management Response: Partially Concur

Purchasing will maintain bid evaluations with explanations of the scores for the evaluation team, individual notes from each evaluation team member will not be maintained.

Audit Follow Up Finding: In Progress

Of the thirty non-exempt solicitations reviewed, fifteen had proceeded to the bid evaluation stage. Thirteen of these solicitations had adequate bid evaluation documentation. The details of this finding are further illustrated in Table 1.

Table 1: Bid Evaluation Documentation Summary

Solicitation Type	# Reviewed	Adequate Bid Tabulation	Adequate Evaluation Explanation
Invitation for Bid	7	100%	Not Necessary
Request for Proposal	6	100%	67%
Request for Qualifications	2	100%	100%
All:	15	100%	87%

According to Purchasing Management, all evaluations are being performed in the Ion Wave system as of January 2020. The implementation of this process should increase assurance that adequate evaluation score explanations are documented in the future.

Sole Source Purchases

13. Require the Department Directors to ensure that the products or services requested for sole-source procurement are not available from any other source.

Management Response: Concur

Purchasing has implemented a sole source justification form requiring Department Directors signature when requesting a sole source purchase.

Audit Follow Up Finding: In Progress

The Procurement Division has implemented a Sole Source Justification Form, which requires department directors to certify that a purchase qualifies for the Local Government Code Chapter 252 sole source exemption. We found that all Sole Source Justification Forms reviewed were signed by a department director; however, three of the seven Sole Source Justification Forms reviewed had statements indicating that there were other vendors of a potential commodity and so may not qualify for the sole source exemption. Purchasing Management stated that these exemptions were allowed because the department was able to justify why the specifications of a particular product were considered necessary.

These statements are shown below:

- *“Several software vendors were available at the Fall National Community Development Association Conference in January 2019.”*

- *“Currently only two companies have the equipment that will work and survive in this harsh environment and have a reputation for quality and a track record of meeting the goals of the customer.”*
- *“The only other vendor with a comparable hosted and fully supported ILS software for public libraries is SIRSI/Dynix’s BLUEcloud.”*

We found that this type of justification practice was taught as part of the Purchasing Division’s department sole source justification trainings; however, the availability of other vendors for a commodity indicates that a purchase is not sole source.

14. **Require the Purchasing Division to conduct due diligence to research and obtain all pertinent information related to the sole source purchase request for analysis and determine if the request complies with the state regulations. The following procedures may also be used to determine if the request for the sole source is valid:**
- Advertise in the newspaper the City’s intention to procure a product or service as sole source and invite proposals/information from potential vendors related to the procurement.**
 - Consult the City Attorney’s Office to verify if any additional inquiries or information is necessary to justify the sole source procurement.**

Management Response: Partially Concur

Purchasing staff check cooperative purchase agreements, other municipalities, and consult with the City Attorney’s Office when verifying sole source claims. Not all research is documented in a central location.

Audit Follow Up Finding: In Progress

The Sole Source Justification Form implemented by Procurement staff generally requires the department to provide appropriate information; however, it does not require Purchasing to document due diligence performed. Of the seven Sole Source Justification Forms reviewed, we found evidence of due diligence for only one purchase and we found evidence that at least four of the reviewed purchases may not meet the legal requirements for a sole source exemption. In addition, only four of the seven reviewed forms were certified by the Purchasing Manager.

This being said, a revised Sole Source Justification Form was introduced as of November 2019, which may improve the documentation of Purchasing’s due diligence. Similarly, Purchasing has issued two “Notice of Intent to Award Sole Source” (SSA) via the new electronic bidding software. Issuance of an SSA provides evidence of Purchasing’s sole source due diligence.

According to Purchasing Management, the decision to issue an SSA is based on Purchasing’s discussion with the department during a Solicitation Review Committee (SRC) meeting, which reviews all sole source procurements over \$50,000. Increasing documentation of the discussion and direction given at these meetings may further demonstrate Purchasing’s sole source due diligence.