



Douglas County Internal Audit

May 5, 2015

Douglas County Board of Commissioners
1819 Farnam Street, Suite LC2
Omaha, NE 68183

Attention: Mary Ann Borgeson, Mike Boyle, Jim Cavanaugh, Clare Duda, Marc Kraft,
PJ Morgan, and Chris Rodgers

Eric Carlson, Purchasing Agent
1819 Farnam St.
Omaha, NE 68183

Dear Commissioners and Mr. Carlson:

I have completed an audit of the County's contract monitoring processes. The purpose of the audit was to assess the processes used by the County to monitor contract performance and verify the accuracy of the related vendors' billings. The audit revealed that the lack of clearly written guidelines that could be communicated to the employees monitoring contracts resulted in important requirements being overlooked. Additionally, the examination of the vendor billings brought to light other issues not directly related to contract compliance (i.e. inventory management, payment discounts), but present opportunities to improve controls.

Background

The monitoring of contracts within the County is decentralized. Each department where contractual goods or services are received is responsible for monitoring contract compliance. Monitoring for compliance includes making sure that:

- Vendors provide goods and services according to contractual specifications.
- The County fulfills its responsibilities according to contract terms.
- Performance bonds and insurance policies protecting the County are secured and properly maintained.
- Appropriate reporting is provided.
- Vendor billings reflect the actual receipt of goods and services provided and the accurate extension of prices and quantities.
- Ancillary processes provide for effective and efficient operations related to the contractual activities.

In 2011 the County purchased contract database software from Cobblestone Systems. A Contract Administrator as well as other employees are responsible for populating the database. The intent is for all County contracts to reside in the Cobblestone database. Appropriate data input enables the software to automatically alert assigned personnel to help ensure that contract renewal or other efforts are undertaken to secure an uninterrupted flow of goods and services. Cobblestone is also used by personnel in the Clerk/Comptroller's office to help them in their audit of invoices.

Objective

The purpose of the audit was to determine if:

- There were effective county-wide contract monitoring policies and procedures in place.
- There was effective monitoring over specifically selected contracts.
- The contract database was being used effectively to aid departments with contract oversight.

Scope

The policies and processes used during the period January 1, 2014 through February 28, 2015 were assessed. Six contracts in effect during this period were judgmentally selected to test for effective monitoring by individual departments. The six contracts selected were:

- Associated Staffing– provides temporary staffing for laundry, housekeeping and dietary employees at the Health Center
- Central States Petroleum – provides fuel for County vehicles
- Corporate Claims Management – adjusts, supervises, and administers the County's tort claim loss program
- Motorola Solutions – provides 911 system update services
- Nebraska Salt & Grain – provides road salt for winter road conditions
- Omaha Paper Company – provides paper products

Methodology

The information documented by Internal Audit was obtained through interviews and observations of the policies and procedures in place as of the period identified in the scope. Independent verification of specific terms was confirmed with vendors. Contracts and related documents were obtained from the Cobblestone database, department personnel, and vendor submissions. Along with an assessment of the policies and procedures as provided, tests were performed to verify contract compliance and billing accuracy. The tests included but were not limited to the following steps below:

- The data input into the Cobblestone database was compared to the contracts to determine if it was entered accurately.
- Departmental procedures were assessed for adequacy and to determine if there was evidence of a consistent county-wide policy in place for monitoring contract compliance.
- Copies of performance bonds and insurance certificates were obtained to see that they were current and agreed to contract terms.

- Invoices and supporting documentation were obtained to determine if there was evidence to support the receipt of goods and services included in vendor billings.
- Billing rates were agreed to contractual rates, and the invoices were extended.

A minimum of fifteen invoices or at least 50 % of the total amount of invoices paid over the contract term for each vendor were chosen for the invoice testing outlined above. Fifty-one invoices in all were judgmentally selected for testing.

The issues identified appear in the Findings section below:

Findings

Policies and Procedures

Criteria: Management should define and communicate the necessary policies and guidelines needed to effectively monitor contract compliance including vendor billings.

Condition: There were no county-wide policies or guidelines in place to help ensure that all departments had effective contract monitoring and billing verification processes in place. Various aspects of contractual terms and billings were not effectively monitored. This is a repeat finding from the 2013 audit of contract monitoring. Specific findings related to the contracts tested appear below:

- Purchasing tracked the gallons of fuel delivered to the County but not the City of Omaha. The contract is a joint contract. Without monitoring the City's portions, there was no way to know the total gallons purchased and delivered from Central States Petroleum.
- Certificates of Insurance were not obtained prior to the commencement of work as required in the contracts from the following vendors:
 - Associated Staffing
 - Central States Petroleum
 - Corporate Claims Management

Note: Certificates of insurance were obtained during the course of the audit fieldwork for Associated Staffing and Corporate Claims Management.

Effect: Results of ineffective monitoring included the following:

- If Central States fuel deliveries continued beyond the contractual quantity, the County could have suffered a financial loss if current prices were less than the contractual price and Central States continued to bill at the contractual price.
- Without the appropriate certificates of insurance, the County could not be sure that there was adequate insurance to protect the County.

Cause: Management did not provide or communicate appropriate guidance or training to help ensure personnel understood all aspects of how to effectively monitor contract compliance.

Recommendation: Formally document the policies and procedures needed to effectively monitor contract compliance including assigning responsibilities to appropriate personnel. Train and

communicate to personnel on the proper use of the policies. The policies should include instructions that will answer the following questions:

- Who has overall responsibility for ensuring that contractual obligations are met?
- Who will monitor operational performance?
- What are the key deliverables that need to be monitored?
- How will the deliverables be monitored and how often will it need to be done?
- If appropriate, has an appropriate plan been prepared (e.g., milestones, timelines, dependencies etc.)?
- Are there unique accounting, purchasing, or other aspects that need to be communicated to other personnel within the County?
- Are there other agreements in place that affect how the contract will be administered?
- Who will approve billings/payments?
- Who will verify the accuracy of the billings/payments and how will it be accomplished?
- Is there an appropriate problem/dispute resolution plan in place including how to identify contract noncompliance?
- What documentation needs to be obtained and maintained within the department or forwarded to other departments or entities to ensure contract compliance and billing/payment accuracy, and who will obtain the documentation?
- How will timely procurement of key contractual obligations be ensured (e.g., continued performance bond and insurance coverage)?
- Are there ancillary processes that need to be considered to properly administer the contract?

Management Response: Purchasing Agent & Chief Administrative Officer met with Internal Auditor to discuss the need for a formal contract monitoring process. Purchasing Agent will work with County Administration to create a draft of a Contract Monitoring compliance policy to present to committee for review in the early part of FY 2016.

Criteria: Douglas County purchasing policy and State statute requires, if practical, that the Purchasing Department obtain at least three informal bids for purchases under \$20,000.

Condition: Purchasing used the state contract with the Omaha Paper Company to order numerous paper goods. Paper goods not included in the contract were ordered on the same purchase orders as those items included in the contract. There were no informal bids obtained for the products ordered that were not included in the contract as required by policy and state statute. The amount of these purchases for the invoices examined was approximately \$7,000.

Effect: County policy and state statute were not properly followed. The County could not be sure it had obtained the best price for the product it purchased.

Note: Quotes for the paper product were obtained after the issue was brought to the buyer's attention.

Cause: The buyer did not follow current purchasing policies in place.

Recommendation: Require that purchase documentation, including Oracle purchase order detail, properly reference existing contracts for all product ordered. Hold individual buyers accountable for not following the proper policies and procedures. Consider requiring the Clerk Comptroller's auditors look for required bids for all invoiced product and communicate deficiencies when appropriate.

Management Response: Purchasing management has reviewed procedures regarding documentation of existing contracts on purchase order detail with the responsible Buyer and the entire Purchasing staff. We have also implemented further controls in our office to ensure that purchasing policies are followed. To that end the Assistant Purchasing Agent met with the buying staff to review the documentation required for purchases made on existing contracts. Before a PO is sent to the vendor, a Buyer will review the purchased item(s) to make sure all items are included as part of the contract as listed (description, pricing etc.); contract details should be listed on the Purchase Order detail; the Buyer will follow up with vendor to confirm receipt of PO and request that the PO number be included on any invoicing.

Vendor Discounts

Criteria: Management should take advantage of all reasonable savings opportunities.

Condition: The Omaha Paper contract provides 1% discounts for invoices paid within 20 days from the invoice date. The County does not take advantage of this discount.

Effect: The amount of discount lost for the invoices tested was \$268. The amount of discount lost over the scope period identified above was approximately \$2,600. At current rates of investment for the County, approximately \$880,000 would be needed to be invested over a year to obtain that return.

Cause: The current payment process in place is not designed to take advantage of vendor discounts unless the invoices are designated as rush invoices. The invoices were not designated as such.

Recommendation: Designate all invoices where a discount can be taken as rush invoices to take advantage of the discounts. Change the current accounts payable procedure to provide for immediate processing of invoices that offer favorable payment discounts.

Management Response: Purchasing Agent and staff will meet with the County Clerk's office regarding the accounts payable procedure to determine the feasibility of immediate processing of invoices where payment discounts are offered. This would likely require a change in the policies regarding payables and specifically how "rush invoices" are addressed.

Paper Inventory

Criteria: Inventory should be ordered to ensure adequate quantities are on-hand to meet demand and to keep inventory investment to a minimum.

Condition: Purchasing normally makes large paper purchases each quarter to last for three months of usage. Paper stock generally arrives within 1-3 days of ordering.

Effect: Excessive quantities of inventory were ordered. Keeping one quarter's worth of paper on-hand is not necessary since the lead times are short.

Cause: The Oracle minimum level for non-dietary warehouse inventory is set at one month of usage, and three months of usage is suggested for vendor orders when levels fall below the minimum on-hand quantity. The buyer followed the rules set-up for ordering stock inventory.

Recommendation: Reduce the paper on-hand quantities and orders to no more than one month usage. This would result in a one-time saving of approximately \$25,000 (based upon the largest payments made to Omaha Paper for each quarter of 2014). This would also result in using less space in the warehouse and less effort in rotating stock.

Management Response: Purchasing recognizes that buying less product more frequently could lower costs as suggested by this report. However, given the current workload of the buyer assigned to inventory purchases, an immediate change to the ordering frequency is not feasible (with current staffing and other procurement duties). If staffing constraints are addressed we may be able to implement a change to the ordering. In the near-term, we will continue to monitor the paper on-hand quantities and order using current methodology.

Audit Standards

Internal Audit conducted this audit in accordance with Generally Accepted Government Auditing Standards and the International Standards for the Professional Practice of Internal Auditing. Those standards require that the audit is planned and performed to obtain sufficient, appropriate evidence to provide a reasonable basis for the findings and conclusions based on the audit objectives. Internal Audit believes that the evidence obtained provides a reasonable basis for its findings and conclusions based on the audit objectives. This report was reviewed with the Purchasing Agent, Eric Carlson.

Internal Audit appreciates the excellent cooperation provided by the various departmental directors, managers, and staff. If you have any questions or wish to discuss the information presented in this report, please feel free to contact me at (402) 444-4327.

Sincerely,

Mike Dwornicki
Internal Audit Director

cc: Paul Tomoser
Jude Lui

Richard File
Thomas Cavanaugh
Kathleen Hall
Jerry Prazan
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