

**Performance Audit:
Annual Contract Administration**

March 2017

City Auditor's Office

City of Atlanta

File #16.09



CITY OF ATLANTA
City Auditor's Office
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Performance Audit:

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What We Found

While city code and the Department of Procurement's standard operating procedures define steps for the city to enter into annual contracts for commodities and for user departments to make purchases against those contracts, user departments have been responsible for enforcing contract terms with little guidance for doing so. As a result, the city may have been over-billed. More than 80% of the 164 invoices we sampled from the city's top twelve supply vendors did not align with the contract price or the contract price list had expired and the city had no current list. The city's competitive process for awarding contracts is based on the American Bar Association's Model Procurement Code and is intended to ensure transparency and fairness in procurement as well as yield the best price. Failure to abide by or enforce the contracts calls into question the extent to which these goals were achieved.

The city spent an estimated \$43.8 million on commodity purchases under annual contracts in fiscal year 2016, but differences in how departments recorded transactions make it impossible to distinguish reliably between purchases made from contracts and purchases made through departments' small purchase authority. Inability to distinguish among types of transactions that are subject to different levels of oversight and competition weakens controls.

The city's recent reorganization of the procurement function provides opportunities to strengthen contract management as former user department buyers, and their role of creating purchase orders, were centralized within the Department of Procurement. Centralizing this function will allow for more consistent quality control, recordkeeping, and enforcement of contract terms. The city's Oracle upgrade provides an additional opportunity to strengthen system controls to capture data needed for effective monitoring of procurement. Enforcing contract terms and analyzing spending to leverage buying power can achieve significant savings

Why We Did This Audit

We undertook this audit to determine whether the Department of Procurement administers annual contracts for commodities in compliance with city code and industry best practices.

What We Recommended

To increase operational efficiency and capitalize on unrealized cost savings, the chief procurement officer should:

- Obtain samples of invoices for each annual contract to ensure that all required fields are completed.
- Develop a template to facilitate compliance with city code in regards to filing estimates of procurement needs for the next fiscal year or require estimates of their procurement needs in the budget proposal.
- Identify and evaluate cooperative agreements related to needs of goods expected to exceed \$20,000 and recur for at least 12 months.
- Use contract clauses, such as tiered-pricing and rebates, to take advantage of unrealized cost savings.
- Update standard operating procedures and training materials to clarify definitions and train staff.
- Determine the feasibility of auto-populating additional contract-related information in Oracle.
- Increase monitoring by reviewing requisitions for completeness, accuracy, and compliance before creating purchase orders, and by generating monthly reporting.

For more information regarding this report, please use the "Contact" link on our website at www.atlaudit.org

Summary of Management Responses

Recommendation #1: We recommend that the chief procurement officer obtain samples of invoices from the Department of Finance for each annual contract with procurement activity to ensure that all contractually required fields are included on invoices.

Proposed Action:

- A. DOP will collaborate with DOF during the 2017 Budget Planning to evaluate the feasibility of a logistics resource within the User Agency or DOF, who would be responsible for evaluating invoices and verifying accuracy of goods received to strengthen contract compliance and three-way match process.
- B. Collaborate with AP and review a sample of invoices to ensure contract compliance.
- C. Strengthen pricing sheet by including a statement indicating the required information e.g., bid number, catalogue item, discount, etc. should be included on the invoice. DOP will include a statement on the pricing sheet for all annual contracts to vendors stating that “In order for vendors to receive payment, the following information must be included on “ALL INVOICES”.

Agree

Timeframe: January 2018

Recommendation #2: We recommend that the chief procurement officer develop a template to facilitate departmental compliance with city code to file estimates of their procurement needs for the next fiscal year or require estimates of their procurement needs for the subsequent fiscal year to be included in the budget proposal.

Proposed Action:

- A. DOP will be included in 2017 Budget Preparedness Process.
- B. Develop a template to capture estimates of the User Agency procurement needs.

Agree

Timeframe: January 2018

Recommendation #3: We recommend that the chief procurement officer identify and evaluate applicable cooperative agreements that relate to current or future needs of goods that are expected to exceed \$20,000 and recur for at least 12 months.

Proposed Action:

- A. Review existing contracts and determine feasibility of potential co-ops.
- B. Review available co-ops to determine suitability for current and future use.
- C. Review co-op opportunities with the State of Georgia where applicable.

Agree

Timeframe: September 2017

Recommendation #4: We recommend that the chief procurement officer use contract clauses, such as tiered pricing and rebates, with invitations to bid for annual contracts to take advantage of unrealized cost savings.

Proposed Action: A. Research other municipalities to assess best practices for bids. **Agree**
B. Consult with the Law Department on modifying the Procurement code if needed.

Timeframe: August 2017

Recommendation #5: We recommend that the chief procurement officer update standard operating procedures and applicable training materials to clarify definitions and appropriate usage of purchase order types. We recommend that the chief procurement officer train staff and user department employees on the updated procedures.

Proposed Action: A. Monitor POs, notify user of incorrect entry POs, and provide corrective actions. **Agree**
B. Modify the SOPs to include methods of procurement and PO type to user agencies.
C. Modify number and naming conventions for PO types in Oracle. Assign a required field in Oracle to be populated by the Requester that will validate the purchase order type.

Timeframe: August 2017

Recommendation #6: We recommend that the chief procurement officer collaborate with Atlanta Information Management to determine the feasibility of auto-populating additional contract-related information.

Proposed Action: A. Estimate testing functionality in second quarter of 2017. **Agree**
B. Determine feasibility and timing of automation of procurement functions.

Timeframe: June 2018

Recommendation #7: We recommend that the chief procurement officer increase monitoring by reviewing requisitions for completeness, accuracy, and compliance before creating purchase orders, and by generating monthly reports for vendor activity.

Proposed Action: A. Develop and executed a small purchases pilot in the first quarter of 2017. **Agree**
B. Provide additional training to address requisitions over \$20K ensure accuracy before submitting to DPO for approval and issuance of the PO.

Timeframe: September 2017



CITY OF ATLANTA

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AUDIT COMMITTEE
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March 20, 2017

Honorable Mayor and Members of the City Council:

We undertook this audit of annual contract administration to determine whether the Department of Procurement administers annual commodities contracts in compliance with city code and industry best practices. Our recommendations are intended to strengthen contract management and leverage buying power to achieve savings. The department agreed with all of our recommendations.

The Audit Committee has reviewed this audit of annual contract administration and is releasing it in accordance with Article 2, Chapter 6 of the City Charter. We appreciate the courtesy and cooperation of city staff throughout the audit. The team for this project was Micheal Jones, Randi Qualls, Coia Walker, and Diana Lynn.

Leslie Ward
City Auditor

Marion Cameron
Chair, Audit Committee

Annual Contract Administration

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Introduction

We undertook this audit to determine whether the Department of Procurement administers annual contracts for commodities in compliance with city code, whether annual contracts achieve economies of scale, and whether the standard operating procedures reflect industry best practices.

Background

The Department of Procurement facilitates the purchase of goods and services for all city departments, the City Council, and the Mayor's Office. City code establishes procurement processes for the city and authorizes the chief procurement officer to administer the procurement function, including:

- managing solicitations
- awarding contracts
- creating purchase orders
- renewing annual contracts
- monitoring small purchases

Annual contracts for commodities do not require City Council approval. City code defines an annual contract as any contract entered into with a contractor for a period of one year or multiple one-year periods (including options to renew for additional one-year periods) to provide the city upon request a specified product or service at a predetermined rate or price. Code states that contracts that are valued at less than \$100,000 per year can be authorized by the chief procurement officer once an agreement is reached between the city and the preferred bidder. Service contracts valued at more than \$100,000 must be legislatively approved by City Council before they can be awarded. The chief procurement officer is authorized to enter into contracts for supplies without additional approval from City Council since user departments are responsible for spending and using funding within their individual annual budgets.

The standard operating procedures for annual contracts defines eight steps and considers user departments' needs (see Exhibit 1). Annual contracts are awarded following a competitive sealed bid process. The city issues and advertises an invitation to bid that includes a purchase description and contractual terms and conditions applicable to the procurement.

Exhibit 1 Formal Procurement Process for Commodities



Source: Department of Procurement’s Standard Operating Procedures

Departments have authority to make small purchases outside of procurement. City code delegates to department heads the authority to make purchases for total single orders costing less than or equal to \$20,000, known as small purchases or field purchase orders. City code prohibits artificially dividing a purchase into multiple purchases in order to meet the definition of a small purchase. The chief procurement officer has defined the small purchase limit as \$20,000 aggregate purchases per department per vendor per year. The code further requires departments, “insofar as it is practicable,” to solicit at least three price quotes before making the purchase and to maintain the name of the business submitting a quotation and the date and the amount of each quotation as a public record.

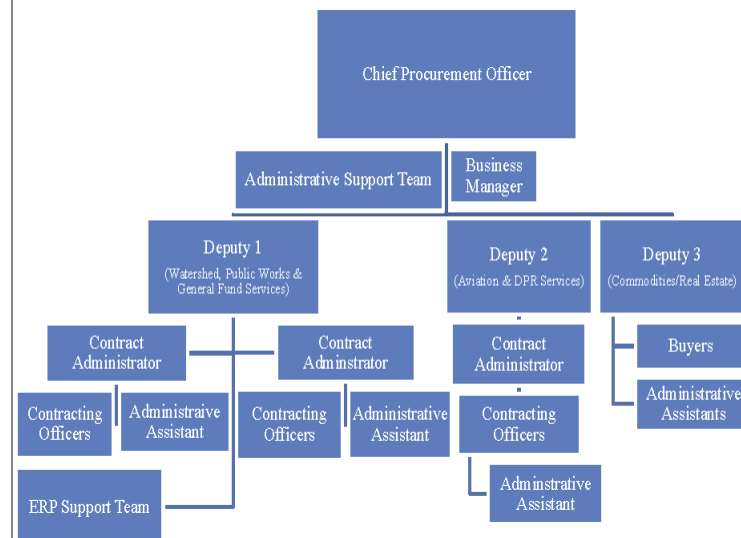
City code provides for additional alternative procurement methods, such as emergency, sole source, special, and cooperative procurements. Emergency procurements occur when the chief procurement officer determines that an emergency exists, where he may authorize others to make emergency procurements for supplies, services, construction items or professional or consultant services. Emergency procurements can only occur when there exists a threat to public health, welfare, or safety under emergency conditions. Such emergency procurements shall be made with as much competition as is practicable under the circumstances.

Code also states that sole source procurements can be awarded without competition when the chief procurement officer determines that in the city’s best interest there is only one source for a commodity or service. A sole source procurement could occur, for

example, when an item has only one manufacturer and/or one authorized distributor.

The Department of Procurement is organized into three divisions, with each division managed by a deputy chief procurement officer who is responsible for day-to-day operations (see Exhibit 2). The Commodities/Real Estate division is primarily responsible for annual contracts for goods and for monitoring small purchases.

Exhibit 2 Commodities Contracts under Separate Division



Source: Department of Procurement’s Standard Operating Procedures Manual

In December 2015, the City Council approved the reorganization of the Department of Procurement, moving all buyers into procurement from user departments. Once the restructuring is complete, procurement will also handle all small purchases. The ordinance recognizes the opportunities of standardizing procedures, processes and responsibilities by ensuring that all purchasing and contracting activities are performed under the authority of the department of procurement. The consolidation is intended to:

- leverage general and specialized knowledge
- decrease duplication of procurement functions throughout the city
- ensure the procurement resources are accurately deployed
- consolidate training responsibilities
- improve professional development and career advancement opportunities

The consolidation increased the Department of Procurement staffing from 41 to 79 by transferring staff from the user departments.

The Department of Procurement's standard operating procedures provide guidance to procurement and user departments.

Procurement has also created a supplemental training manual to instruct departments how to create a requisition in Oracle, the city's financial system. The requisition is an electronic record that identifies the department's intent to make a purchase and encumbers funds.

For purchases up to \$20,000, the user department creates the requisition, which is routed to its management for approval. Once approved, the user department generates and approves the purchase order, which is sent to the vendor to place the order. For individual purchases more than \$20,000, the user department creates and approves the requisition, then notifies the Department of Procurement buyer that the requisition is ready for review. The buyer creates the purchase order and sends it to the chief procurement officer for review and approval before it is placed with the vendor. The vendor delivers the purchased goods to the user department and sends the invoice to the Department of Finance. The user department enters a receiving document into Oracle and the Department of Finance enters the invoice into Oracle. Oracle matches the invoice to the purchase order and to the receiving document before processing the payment. This process is called a three-way match. In cases where the documents do not match, the invoice is held and discrepancies must be resolved before the city processes the payment.

The Department of Procurement uses a tool in Oracle to monitor user departments' small purchases.

Audit Objectives

This report addresses the following objectives:

- Does the Department of Procurement manage annual contracts in compliance with city code?
- Are the Department of Procurement's standard operating procedures for commodities consistent with industry best practices?
- Does the city achieve economies of scale from annual contracts?

Scope and Methodology

We conducted this audit in accordance with generally accepted government auditing standards. Our audit methods included:

- reviewing the city's procurement code and standard operating procedures
- reviewing the *Requisition to Purchase Order* training manual
- analyzing closed purchase orders created in fiscal year 2016
- analyzing a judgmental sample of invoices from 12 vendors with annual contract for goods to determine whether the unit price charged matched the contract price, and whether invoices contained required information
- conducting an Oracle simulation of the procurement process
- researching industry best practices for contract management
- interviewing procurement staff, vendors, and other staff

Generally accepted government auditing 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.

Findings and Analysis

Procurement Practices Could Limit the City's Ability to Obtain the Best Price

While city code and Department of Procurement procedures define steps for the city to enter into annual contracts for commodities and for user departments to make purchases against those contracts, user departments have been responsible for enforcing contract terms with little guidance for doing so. As a result, the city may have been overbilled. The unit price charged did not match the contract price list in more than 80% of the invoices we reviewed, in some cases because the contract price list had expired and the city had no current list. About 65% of the invoices contained charges for items not included in the contract, which appears to have violated standard contract terms. The city's competitive process for awarding contracts is based on the American Bar Association's Model Procurement Code and is intended to ensure transparency and fairness in procurement as well as yield the best price. Failure to abide by or enforce the contracts calls into question the extent to which these goals were achieved.

In fiscal year 2016, the city spent an estimated \$43.8 million on commodity purchases from annual contracts. Contradictory guidance and differences in how departments recorded transactions make it impossible to distinguish reliably between purchases made from contracts and purchases made through departments' small purchase authority. Inability to distinguish among types of transactions that are subject to different limits and different levels of oversight and competition weakens controls.

The city's recent reorganization of the procurement function provides opportunities to strengthen contract management as former user department buyers, and their role of creating purchase orders, were centralized within the Department of Procurement. Centralizing this function will allow for more consistent quality control, recordkeeping, and enforcement of contract terms. Greater centralization of the procurement function also provides an opportunity for the city to take advantage of economies of scale and national purchasing agreements. Industry publications estimate that companies can typically achieve savings of 5% of annual supply costs through stronger contract management. Finally, the city's Oracle upgrade provides an opportunity to strengthen system controls to capture data needed for effective monitoring of procurement.

Procurement Reorganization Provides Opportunities to Strengthen Contract Management

User departments have been responsible for enforcing annual contract terms with little guidance for doing so. As a result, the city may have been overbilled for supplies purchased under these contracts.

More than 80% of vendor invoices we reviewed charged prices that didn't match the contract or were unverifiable. We reviewed a judgmental sample of 164 invoices from fiscal years 2013 through 2016 totaling \$2.5 million for commodities purchased from the city's top twelve supply vendors compared to the annual contract terms. Sixty-six of the 164 invoices had unit prices charged that did not match the contract list price, indicating the city has been billed incorrectly for purchased items (see Exhibit 3). We were unable to verify the price on an additional 72 invoices because the vendor did not supply a price catalog or there was ambiguity for an item number with more than one brand of the product. In some cases, unit prices were lower than the contract list price and some were up to 90% higher. According to the vendors, factors that contributed to the price discrepancies included vendor misquotes, market changes, and city staff not using functioning online catalogs managed by vendors. One vendor acknowledged that the company decided to use a different pricing strategy than was provided for in the contract that was expected to yield the same margins. The vendor continued to charge the higher prices after the city renewed the contract in July 2016.

Exhibit 3 Over 84% of Invoices Do Not Match Contract Pricing

Invoice Requirements	Meets Requirement	Does Not Meet Requirement	Unable to Verify	% Not in Compliance
Does Price Match Contract or Catalog?	26	66	72	84.2%
Are All Items on Contract?	57	107	0	65.2%
Is There An Item Identifier?	148	16	0	9.8%
Does the Invoice Reflect A Unit Price?	162	2	0	1.2%
Is the Purchase Order Number On the Invoice?	162	2	0	1.2%
Are Payment Terms Listed On the Invoice?	163	1	0	0.6%
Does the Invoice Include the Total Price?	164	0	0	0.0%

Source: Invoices from twelve surveyed vendors with annual contracts

About 65% of the invoices contained charges for items not included on the contract. We were able to determine that a discount was given for many items, but the discount percentages were inconsistent from invoice to invoice. The city's standard contract states that vendors are responsible for providing only the goods that have been awarded to their company and the city will not pay for items sold that are not listed in the contract. The vendor is responsible for denying unauthorized purchase requests made by city employees and referring the requests to the Department of Procurement, however the commodities contract template also states that the vendor shall provide "like and similar goods not listed on the pricing sheet." Also, about one-third of the contracts we reviewed provided an "average percent discount on all items listed in the catalog that are not specified in the Invitation to Bid." These clauses appear to allow discretion to purchase other items.

None of the twelve vendors complied with all of the contract-mandated invoicing requirements on the invoices we reviewed. The standard language included on every contract for goods requires:

- proper identification of the item(s) sold
- unit price
- total price
- terms of payment (cash discount) allowed
- purchase order number on which the city ordered materials

Lack of accountability leaves city vulnerable to price discrepancies. Purchasing procedures do not clearly define the responsibilities for the Department of Procurement and user departments once a contract is awarded. According to the standard operating procedures, last updated in June 2014, user departments are responsible for creating and approving requisitions and purchase orders for purchases up to \$20,000. For purchases greater than \$20,000, the user department creates and approves the requisition, which procurement professionals are supposed to verify before creating the purchase order and forwarding it to the chief procurement officer for approval. The procedure does not address who should ensure the unit price is correct and how. Procurement staff told us that user departments are responsible for verifying unit pricing because user department staff input the requisition and user department managers approve the requisition before it is forwarded to procurement. However, users may be unaware of contract terms and the proper way to leverage them.

In order to confirm that prices are accurate, user departments must have access to a complete price list, either from the contract or

electronically, that can be used to compare quotes received from vendors. The American Bar Association defines an established catalog price as the price included in a catalog, price list, schedule or other form that:

- is regularly maintained by the manufacturer or contractor
- is published or available for inspection by customer
- states prices at which sales are currently or were last made by a significant number of buyers

The Department of Procurement does not send user departments electronic pricing catalogs to verify unit prices, but maintains a contract master list with contracts and pricing sheets on the city's intranet. The contracts and pricing sheets do not always list unit prices; 21 of the 55 contracts that we reviewed from the twelve vendors offered percentage discounts from a catalog price but the catalog was not attached to the contract. We were able to obtain catalogs from ten of the twelve vendors.

Failure to enforce contract terms reduces advantages of competitive pricing. The city's procurement code follows the American Bar Association's Model Procurement Code for State and Local Governments and is intended to foster transparent, competitive and reliable processes for the expenditure of public funds. The model code identifies fair and open competition as a basic tenet of public procurement that promotes public confidence that contract awards are equitable and economical. Failure of the city to abide by the contracts or enforce the contract terms reduces the benefits that should be achieved through competition.

Procurement consolidation offers opportunities to improve contract management. The City Council passed legislation in December 2015 to consolidate 40 employees performing purchasing and contracting functions in various city departments under the Department of Procurement. The consolidation is intended to standardize procurement procedures and processes, leverage general and specialized knowledge, and decrease duplication. Additionally, the Department of Procurement is revising workflows in Oracle so that procurement staff will prepare purchase orders based on department requisitions. This change in workflows provides an opportunity for the department to ensure that items purchased and unit prices comply with contract terms. We recommend that the chief procurement officer revise policies and procedures to clarify the department's responsibilities for contract enforcement. We also recommend that the Department of Procurement periodically request and review invoices from the Department of Finance in

order to ensure that all contractually required fields are included on invoices.

City Could Take Advantage of Economies of Scale and National Cooperative Agreements

Along with enforcement of contract terms, analyzing spending to leverage buying power can achieve savings. Industry experts estimate that companies can typically achieve savings of 5% of annual supply costs through stronger contract management. The city paid its top 12 supply vendors \$22.4 million in fiscal year 2016 and paid an estimated \$43.8 million on commodity purchases from all annual contracts, so the opportunity for savings could be substantial.

Price savings could improve with better annual forecasting and communication during invitations to bid. Half of the city's top 12 supply vendors agreed that knowing the expected volume of purchases on a contract, especially for renewal contracts, would allow for lower pricing. The city includes a price sheet of items that will be purchased from the contract if awarded, but does not estimate annual quantities. City code, however, requires such analysis. Section 2-1139 of the city code states that all user departments shall file with the chief procurement officer, within 30 days after the adoption of the annual budget and quarterly thereafter, estimates of their needs for the procurement of services, supplies, construction, professional or consultant services and real property for the ensuing fiscal year or calendar quarter. The chief procurement officer shall utilize such estimates for the scheduling of work activities and of procurements to compile and consolidate all estimates of supplies needed by user departments, determining total requirements for a given commodity.

The National Institute of Governmental Purchasing suggests procurement organizations analyze spending to leverage buying power, reduce costs, provide better management and oversight of suppliers, and develop an informed procurement strategy. Analysis should include the identification, automated collection, cleansing, grouping, categorization, and analysis of all spending data for the goods and services purchased for the organization. Most of the vendors we surveyed attributed their predicted price reductions to volume discounts and possibly better forecasting that would allow them to negotiate better terms with manufacturers.

Department heads should comply with city code and file estimates of their procurement needs. We recommend that the chief procurement officer develop a template to facilitate compliance.

Three of the vendors we talked to were already offering national cooperative agreements that the city was not using; one of these vendors offered the cooperative agreement price on its bid. National cooperatives are advantageous to the city because they combine the city's total annual spending with other governments to obtain the best possible pricing from the vendors. Cooperative procurement refers to the combining of requirements of two or more public procurement entities to leverage the benefits of volume purchases, delivery and supply chain advantages, best practices, and reduced administrative time and expenses. City code allows the chief procurement officer to participate in a cooperative purchasing agreement for the procurement of supplies, services or construction with one or more public procurement units; amounts where the estimated value of a contract exceeds \$20,000 must receive prior authorization from the City Council. According to the National Institute of Governmental Purchasing, procurement should, after conducting extensive due diligence and market research, consider the use of cooperative contracts in order to lower prices, lower administrative costs, increase competition, and obtain more favorable terms and conditions. The vendors use these programs to reduce costs by leveraging the goods using direct purchasing in bulk from manufacturers, rather than purchasing on a per-order basis.

We recommend that the Department of Procurement identify and evaluate cooperative agreements that are associated with current annual contract vendors. If the agreements appear beneficial to the city, the chief procurement officer should seek City Council authorization to participate in the agreements.

Analysis of spending and strategic procurement could yield lower prices. Five of the twelve vendors also told us they would be open to a tiered-pricing structure, in which the city could receive lower pricing based upon spending trends. At the start of the agreement, the annualized total purchases become the starting base, and at the end of the first year, business growth above this starting base is subject to the rebate. The city would receive greater discounts from increased tiers as the annual spending increases. Half of the vendors were open to a rebate program, especially when associated with annual growth, which would offer an annual rebate back to the city if the city spent a targeted amount.

According to the Institute for Supply Management, initiatives like the volume incentive rebates focus on developing customer/vendor agreements that provide the purchaser with necessary and desired coverage, while also benefiting vendors. Negotiating rebate programs create the benefits to the vendors when there is a lack of reliable quantity forecasting for purchasing, especially in cases where there is uncertainty associated with how much (if any) would be purchased from a specific vendor.

We recommend that the Department of Procurement include provisions for incentivized contract clauses, including tiered-pricing and rebates, on invitations to bid for annual contracts.

The city paid its top twelve supplies vendors \$22.4 million in fiscal year 2016 (see Exhibit 4). The city spent an estimated \$43.8 million on commodity purchases in fiscal year 2016 from all annual contracts. Some industry experts estimate that stronger supply contract management can yield 5% or more of annual spending, so potential savings could be substantial.

Exhibit 4 City Paid the Top 12 Supply Vendors \$22.4 Million in Fiscal Year 2016

Vendor Name	Total \$ Closed Purchase Orders FY2016
CDW Government Inc.	\$8,148,862
Allan Vigil Ford Lincoln	\$3,849,851
Rush Truck Centers	\$2,886,370
Grainger Industrial Supply	\$1,671,399
Applied Industrial Technologies	\$1,360,796
Nelson Business Products Inc.	\$1,063,662
Freeman Forms	\$932,718
SA White Oil Co Inc.	\$644,823
Technology Integration Group	\$631,279
GC Electrical Solutions, LLC	\$629,333
Ag Pro LLC	\$393,526
GT Distributors Of Ga, Inc.	\$201,016
Total	\$22,413,634

Source: Oracle Discoverer Report, July 2016

Procedures Should Provide Consistent Direction

Contradictory guidance and differences in how departments recorded purchasing transactions in Oracle make it impossible to distinguish reliably between purchases made from competitively bid contracts and purchases made through departments' small purchase

authority. Inability to distinguish among types of transactions that are subject to different rules weakens controls and limits the city's ability to analyze spending.

The Department of Procurement's standard operating procedures and Oracle training materials define different types of purchases that are subject to different limits, different levels of approval, and different amounts of competition:

- Field purchase orders - a requisition that is created and sourced by the user department for goods or services up to \$20,000 annually per supplier.
- Blanket purchase orders - a requisition created to procure goods from an awarded blanket purchase agreement that can exceed \$20,000 and does not require procurement's approval.
- Procured goods - a requisition for goods that is created by the user departmental, but sourced by the Department of Procurement, generally created for a one-time purchase in excess of \$20,000.

Guidance for processing transactions appears to contradict definitions. While purchases of goods under an annual contract appear to meet the definition of a blanket purchase order, Department of Procurement staff told us that the city does not use blanket purchase orders. Guidance from the chief procurement officer directs departments to classify all individual purchase orders that are less than \$20,000 as field purchase orders made under the department's small purchase authority even when the items are purchased under an annual contract. This guidance appears to limit both the city's ability to monitor how much is spent under annual contracts and to monitor departments' compliance with their small purchase authority.

Our analysis of fiscal year 2016 purchase order types found apparent inconsistent use by user departments. We saw purchase orders greater than \$20,000 categorized as field purchase orders. According to the chief procurement officer, these should have been classified as procured goods. While procurement staff said that no transactions should be classified as blanket purchase orders, we saw 209 instances of blanket purchase orders in excess of \$20,000 and 37 blanket purchase orders that were not directly associated with an annual contract. We provided a list of anomalous transactions to the Department of Procurement for further analysis. Procurement staff

told us that the purchase order type field is unreliable and the department does not use it for monitoring or analysis.

Lack of input controls make effective monitoring a challenge.

According to the Department of Procurement's training manual, for items on an annual contract, a contract number should be included in the requisition to identify purchase orders that are associated with an annual contract. The contract number, or contract purchasing agreement number, is a numerical identifier specifically tied to each individual contract. The information is not mandatory, but is typed into a free-form field by the user department when completing a requisition. As a result, user departments do not consistently include the contract purchase agreement number on the requisition or purchase order.

About half of the purchase orders issued to the top twelve supplies vendors in fiscal year 2016 were missing a contract purchasing agreement number (see Exhibit 5). Based on our review of sample invoices, some of these purchases were for items listed in annual contracts. We also saw instances of the incorrect contract purchasing agreement number listed on the requisition and purchase order.

Exhibit 5 Contract Number Missing on 53% of Purchases from Top 12 Supply Vendors in Fiscal Year 2016

Vendor Name	% of Purchase Orders w/o Contract Number
GT Distributors Of GA, Inc.	88.6%
Allan Vigil Ford Lincoln	85.1%
Rush Truck Centers	74.9%
CDW Government Inc.	62.4%
Technology Integration Group	57.5%
GC Electrical Solutions, LLC	44.9%
Nelson Business Products Inc.	32.3%
Freeman Forms	12.0%
Ag Pro LLC	9.5%
Grainger Industrial Supply	1.8%
Applied Industrial Technologies	0.2%
SA White Oil Co Inc.	0.0%
Total	53.0%

Source: Oracle Discoverer Report, August 2016

The Department of Procurement uses the field purchase order enhancement tool in Oracle to flag small purchases that exceed the limit. It was initially designed to monitor user departments' use of

small purchases, especially amounts in excess of \$20,000 per department per vendor per year, but it is structured to flag any small purchase that approaches the annual limit. Flagged purchase orders are routed to procurement for review. These purchase orders are manually processed in two steps, initially sending them to procurement employees who forward them for final review by the deputy chief procurement officer.

User departments can bypass this control by entering any numerical value in the contract field. The field purchase order enhancement tool only takes into account those purchase orders without a contract purchase agreement number entered into the contract field. The tool does not verify that the value entered is a valid contract purchasing agreement number or is associated with the specific vendor listed on the requisition and purchase order.

The National Institute of Governmental Purchasing recommends that procurement organizations develop a comprehensive policy manual that clearly defines authority and responsibility and establishes guidelines for the organization and the procurement professional to follow when carrying out their responsibilities. The manual should include a definition section that:

- clearly defines the use of terms as they are used in the policy (e.g., annual contract, blanket purchase agreement, and procured goods)
- clearly defines criteria for any procurement decision that may be unclear without further explanation (e.g., using a field purchase order type for an annual contract purchase)

We recommend that the Department of Procurement update its standard operating procedures and training manual to clarify the definitions and appropriate uses of different types of requisitions. Field purchase orders should only be used for true small purchases, not purchases made from an annual contract. We also recommend that the Department of Procurement train staff and user department employees on the updated procedures. As part of the revised workflow, the Department of Procurement should review requisitions for completeness, accuracy, and compliance with procedures before generating purchase orders.

Oracle Upgrade Should Capture Data Needed For Effective Monitoring

The Oracle upgrade provides an opportunity to strengthen system controls. Best practices for contract management encourage organizations to develop an infrastructure to track contract

compliance and an organizational commitment to increase visibility of contractual and non-contractual spending.

Expanding auto-populated fields would improve data reliability. Oracle has the capability to auto-populate fields when configured. User departments start a requisition by filling required fields, such as item description, category, quantity, unit of measure, unit price, and currency. The current Oracle interface auto-populates default fields when a user creates a requisition.

Best practices associated with contract management suggest that the system should be automated wherever feasible in order to reduce manual error and increase data reliability. The user departments could input a contract purchase agreement number, which would auto-populate necessary contract related information throughout the procurement process. For example, when the user department inputs the contract purchase agreement number when starting a requisition, that number would auto-generate the vendor name. In cases with a multiple vendor contract, the departments could choose from the vendors related to that contract only. The requisition data could carry over to the requisition checkout and auto-generate the purchase order type.

We recommend that the Department of Procurement work with Atlanta Information Management to explore the feasibility of auto-populating additional contract-related information, especially required fields. These additional controls would reduce manual inputting by user departments thereby improving data reliability.

Methodical reporting would strengthen city's ability to monitor spending on annual contracts and small purchases. Our interviews reflect the Department of Procurement has no formal, automated reporting process in place for monitoring contracts. The Department of Procurement process requires their buyers to create purchase orders for user departments that exceed \$20,000, even if on an annual contract. Small purchases associated with an annual contract are not directly monitored unless they are flagged by the field purchase order enhancement tool. If the Department of Procurement limits the user departments' use of certain purchase order types for annual contracts, it will be able to generate reports to monitor annual contracts.

We recommend that the Department of Procurement implement more frequent monitoring of spending and compliance by generating and reviewing monthly reports according to purchase order type.

Recommendations

In order to increase operational efficiency and capitalize on unrealized cost savings, the chief procurement officer of the Department of Procurement should:

1. Request and review a sample of invoices for each annual contract with procurement activity from the Department of Finance in order to ensure that all contractually required fields are included on invoices.
2. Develop a template to facilitate departmental compliance with city code to file estimates of their procurement needs for the next fiscal year or require estimates of their procurement needs for the subsequent fiscal year to be included in the budget proposal.
3. Identify and evaluate applicable cooperative agreements that relate to current or future needs of goods and services that are expected to exceed \$20,000 and recur for at least 12 months.
4. Use contract clauses, such as tiered pricing and rebates, with invitations to bid for annual contracts to take advantage of unrealized cost savings.
5. Update its standard operating procedures and applicable training material to clarify definitions (e.g., small purchases and blanket purchase agreements) and appropriate use of each purchase order type. Train staff and user department employees on the updated procedures.
6. Collaborate with Atlanta Information Management to determine the feasibility of auto-populating additional contract-related information.
7. Increase monitoring by reviewing requisitions for completeness, accuracy, and compliance before creating purchase orders, and by generating monthly reports for vendor activity.

Appendices

Appendix A: Management Review and Response to Audit Recommendations

Report # 16.09 Report Title: Annual Contracts		Date: 1/31/2017
Rec. # 1	We recommend that the chief procurement officer obtain samples of invoices from the Department of Finance for each annual contract with procurement activity to ensure that all contractually required fields are included on invoices.	Agree
<u>Proposed Action:</u>	<p>A. DOP will collaborate with DOF during the 2017 Budget Planning to evaluate the feasibility of a logistics resource within the User Agency or DOF, who would be responsible for evaluating invoices and verifying accuracy of goods received to strengthen contract compliance and three-way match process.</p> <p>B. Collaborate with AP and review a sample of invoices to ensure contract compliance.</p> <p>C. Strengthen pricing sheet by including a statement indicating the required information e.g., bid number, catalogue item, discount, etc. should be included on the invoice. DOP will include a statement on the pricing sheet for all annual contracts to vendors stating that “In order for vendors to receive payment, the following information must be included on “ALL INVOICES”.</p>	
<u>Implementation</u>	January 2018	
<u>Timeframe:</u>		
<u>Comments:</u>		
<u>Responsible Person:</u>	DOP/DOF	
Rec. # 2	We recommend that the chief procurement officer develop a template to facilitate departmental compliance with city code to file estimates of their procurement needs for the next fiscal year or require estimates of their procurement needs for the subsequent fiscal year to be included in the budget proposal.	Agree
<u>Proposed Action:</u>	<p>A. DOP will be included in 2017 Budget Preparedness Process.</p> <p>B. Develop a template to capture estimates of the User Agency procurement needs.</p>	
<u>Implementation</u>	January 2018	
<u>Timeframe:</u>		
<u>Comments:</u>	Involvement in the budgeting process will enhance DOPs opportunity to capitalize on potential cooperative agreements.	
<u>Responsible Person:</u>	DOP	

Rec. # 3	We recommend that the chief procurement officer identify and evaluate applicable cooperative agreements that relate to current or future needs of goods that are expected to exceed \$20,000 and recur for at least 12 months.	Agree
<u>Proposed Action:</u>		
A. Review existing contracts and determine feasibility of potential co-ops.		
B. Review available co-ops to determine suitability for current and future use.		
C. Review co-op opportunities with the State of Georgia where applicable.		
<u>Implementation</u>		
September 2017		
<u>Timeframe:</u>		
<u>Comments:</u>		
<u>Responsible Person:</u> DOP		
Rec. # 4	We recommend that the chief procurement officer use contract clauses, such as tiered pricing and rebates, with invitations to bid for annual contracts to take advantage of unrealized cost savings.	Agree
<u>Proposed Action:</u>		
A. Research other municipalities to assess best practices for bids.		
B. Consult with the Law Department on modifying the Procurement code if needed.		
<u>Implementation</u>		
August 2017		
<u>Timeframe:</u>		
<u>Comments:</u>		
Utilization of tiered pricing and negotiating rebates may allow COA to take advantage of unrealized savings.		
<u>Responsible Person:</u> DOP		
Rec. # 5	We recommend that the chief procurement officer update standard operating procedures and applicable training materials to clarify definitions and appropriate usage of purchase order types. We recommend that the chief procurement officer train staff and user department employees on the updated procedures.	Agree
<u>Proposed Action:</u>		
A. Monitor POs, notify user of incorrect entry POs, and provide corrective actions.		
B. Modify the SOPs to include methods of procurement and PO type to user agencies.		
C. Modify number and naming conventions for PO types in Oracle. Assign a required field in Oracle to be populated by the Requester that will validate the purchase order type.		
<u>Implementation</u>		
August 2017		
<u>Timeframe:</u>		
<u>Comments:</u>		
This situation requires the need to train the User Agency on the new operating procedures and system processes. Training on system processes will not occur until R12 implementation in 2018. This situation also requires the need to reiterate to the vendor the need for accurate information on the invoice to insure prompt payment. The goal is to mitigate mismatches and improve invoice accuracy.		
<u>Responsible Person:</u> DOP/DOF		

Rec. # 6	We recommend that the chief procurement officer collaborate with Atlanta Information Management to determine the feasibility of auto-populating additional contract-related information.	Agree
<p><u>Proposed Action:</u> A. Estimate testing functionality in second quarter of 2017. B. Determine feasibility and timing of automation of procurement functions.</p> <p><u>Implementation</u> June 2018</p> <p><u>Timeframe:</u></p> <p><u>Comments:</u> Feasibility of auto-populating information will be assessed with R12 design.</p> <p><u>Responsible Person:</u> DOP/AIM</p>		
Rec. # 7	We recommend that the chief procurement officer increase monitoring by reviewing requisitions for completeness, accuracy, and compliance before creating purchase orders, and by generating monthly reports for vendor activity.	Agree
<p><u>Proposed Action:</u> A. Develop and executed a small purchases pilot in the first quarter of 2017. B. Provide additional training to address requisitions over \$20K ensure accuracy before submitting to DPO for approval and issuance of the PO.</p> <p><u>Implementation</u> September 2017</p> <p><u>Timeframe:</u></p> <p><u>Comments:</u> Small purchases pilot commenced in January 2017. The DOP consolidation will enable more oversight and control of the small purchases process. Additional training provided to agencies will occur during the Small Purchases Pilot.</p> <p><u>Responsible Person:</u> DOP</p>		