



**Office of the City Auditor**

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**Report to the City Council  
City of San José**

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**CONSULTING AGREEMENTS:  
BETTER ENFORCEMENT OF  
PROCUREMENT RULES,  
MONITORING, AND  
TRANSPARENCY IS NEEDED**

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**Report 13-06  
June 2013**

June 12, 2013

Honorable Mayor and Members  
Of the City Council  
200 East Santa Clara Street  
San José, CA 95113

**Consulting Agreements: Better Enforcement of Procurement Rules, Monitoring, and Transparency Is Needed**

In accordance with the City Auditor's Fiscal Year (FY) 2012-13 Audit Work Plan, we have completed an audit of consulting agreements. The purpose of this audit was to assess whether the City's oversight of consulting agreements was sufficient to ensure the City is getting what it is paying for. For purposes of this audit, we used referrals from staff and a risk-based approach to select five consulting agreements for review. Our review of those agreements and resulting conversations with City staff indicated improvements are needed to ensure appropriate procurement, monitoring, and transparency of consulting agreements. This audit is one in a series of contract audits conducted by the City Auditor's Office.

**Finding 1: The City Should Enforce Competitive Procurement Rules and Limit Exceptions to These Rules.** During the course of our review, we identified exceptions to the City's competitive procurement rules including inappropriate exceptions for "unique services," scope expansion, and increased spending without competition. In some cases staff exceeded limits on contract authority, executed contracts after-the-fact, and, in the absence of open competition, grew increasingly reliant on select consultants. Increased oversight is challenging but necessary to improve fairness and competition in City contracting. The City can streamline processes and should provide more information to employees to avoid confusion about those processes.

**Finding 2: Monitoring of Consulting Contracts Should Be Improved.** Consultants are being used for a myriad of reasons including doing analysis, facilitating workshops, and providing advice on policy issues. We found that the City's oversight of the five agreements we reviewed was inadequate. Further we found that City staff had ignored contract terms, changed contract deliverables and payment terms without authorization, and sometimes paid vendors more than required by their contracts. Finally, in some instances staff was unable to provide us with contract-required deliverables. In our opinion, the City needs to ensure that overpayments are reconciled and paid back to the City, staff is trained on how to manage contracts, and consistent policies and procedures are developed.

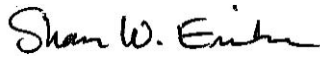
**Finding 3: Transparency and Ethics Policies Should Be Followed and Clarified.** Our review indicates the City can do better at enforcing state and local laws that address consultant agreement ethics, including prohibitions on conflicts of interest and disclosure of economic interests (commonly known as Form 700s). Consulting work is of an advisory nature and deliverables are generally less measurable than for other services, making it important to track spending. Developing and making such

information available will promote transparency, increase oversight and provide assurance to taxpayers that their monies are being appropriately spent.

Our report includes 15 recommendations to improve the procurement, monitoring, and transparency of the City's consulting agreements. We would like to thank the City Manager's Office, City Attorney's Office, City Clerk's Office, Office of Economic Development, and the departments of Finance, Police, Planning, Building and Code Enforcement, and Parks, Recreation and Neighborhood Services for their time and assistance during the audit process.

We will present this report at the June 20, 2013 meeting of the Public Safety, Finance, and Strategic Support Committee. The City Administration's response to the audit is attached on yellow pages.

Respectfully submitted,



Sharon W. Erickson  
City Auditor

finaltr  
SE:lg

Audit Staff: Gitanjali Mandrekar  
Brenna Silbory

cc:	Norberto Duenas	Alex Gurza	Lisa Perez
	Debra Figone	Julia Cooper	Laurel Prevetti
	Ed Shikada	Mark Giovannetti	Toni Taber
	Rick Doyle	Jo Zientek	Julie Edmonds-Mares

# Table of Contents

<b>Cover Letter</b> .....	<b>i</b>
<b>Introduction</b> .....	<b>1</b>
Background .....	1
Audit Objective, Scope, and Methodology .....	7
<b>Finding 1</b>	
<b>The City Should Enforce Competitive Procurement Rules And Limit Exceptions to These Rules</b> .....	<b>11</b>
Why Is Competitive Procurement of Consulting Agreements Important?.....	11
Unique Services Exceptions Carried Over Through Numerous Amendments.....	12
Consulting Contract Scopes Expanded and Spending Increased Without Competition.....	13
Staff Exceeded Council Approval and Authorized Off-Contract Work.....	16
Increased Oversight Is Challenging, but Necessary and Required .....	18
Staff Decisions to Avoid the Competitive Process May Stem in Part from Confusion About How to Employ It.....	19
<b>Finding 2</b>	
<b>Monitoring Of Consulting Contracts Should Be Improved</b> .....	<b>21</b>
What Does Effective Contract Monitoring Look Like? .....	21
Contract Terms Were Ignored and Oversight of Contractors was Inadequate .....	22
Contract Monitoring Requires Consistent Processes, Accountability and Training .....	26
Accountability is Hampered By Lack of Contract Managers and Document Retention .....	28
<b>Finding 3</b>	
<b>Transparency and Ethics Policies Should Be Followed and Clarified</b> .....	<b>31</b>
State and Local Laws Prohibiting Economic Conflicts of Interest Also Apply to Consultants.....	31
Ethics Training For All Contract Monitoring and Procurement Staff.....	33
Promoting Transparency.....	34
<b>Conclusion</b> .....	<b>39</b>
<b>Administration’s Response</b> .....	<b>yellow pages</b>

## **Table of Exhibits**

<b>Exhibit 1: Consulting Contract Responsibilities by Department.....</b>	<b>3</b>
<b>Exhibit 2: City Manager’s Contract Transmittal Form.....</b>	<b>5</b>
<b>Exhibit 3: City Clerk “Status II” Designation.....</b>	<b>6</b>
<b>Exhibit 4: State of Colorado Contract Management Website.....</b>	<b>36</b>

# Introduction

In accordance with the City Auditor's Fiscal Year (FY) 2012-13 Audit Work Plan, we have completed an audit of Citywide consulting agreements. The purpose of this audit was to assess whether the City's oversight of consulting agreements was sufficient to ensure the City of San José (City) is getting what it is paying for. We used a risk assessment approach and staff referrals to identify the agreements that we included as part of our review. This audit is one in a series of contract audits conducted by the City Auditor's Office.

We conducted this performance audit 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. We limited our work to those areas specified in the "Audit Objective, Scope, and Methodology" section of this report.

The Office of the City Auditor thanks the management and staff from the City Manager's Office, City Attorney's Office, City Clerk's Office, the Office of Economic Development (OED), Finance Department, Environmental Services Department (ESD), Parks, Recreation, and Neighborhood Services Department (PRNS), San José Police Department (SJPD) and Planning, Building and Code Enforcement (PBCE) for their time, information, insight, and cooperation during the audit process.

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## Background

### **What is a Consultant? What is a Consulting Agreement?**

The City's Finance department has internally defined consultants as

*Skilled individuals that provide evaluative services or advise departments about policy or strategic questions.*

Finance distinguishes consultant agreements from professional services agreements. Professional services are "services that involve highly skilled, licensed or certified individuals."

The City contracts with consultants for a variety of reasons. These include:

- Lack of in-house expertise,
- Insufficient staff,

- Cost, and
- Short-term services required.

The City contracts with consultants for a variety of purposes including anything from providing answers to specific questions to the design of a system or conducting seminars, workshops, and conferences. The California Public Contract Code<sup>1</sup> describes consultant contracts as providing services of an advisory nature, such as providing a recommended course of action. Consultant contracts usually result in the delivery of a report that is related to the governmental functions of state agency administration and management.

In general, consultants provide an advice-based service, and their deliverables are harder to define, making evaluation of their efficacy all the more important.

### **Contracting Authority for Consulting Agreements**

The City Manager, City Attorney, City Auditor, and City Clerk are authorized to enter into and execute contracts for and on behalf of the City of San José as long as monies have been appropriated<sup>2</sup> for the contract and there is sufficient balance to pay for the expense of the contract. City Council approval is required for most types of contracts that exceed \$250,000<sup>3</sup>, including consulting agreements.

### **Competitive Procurement Required**

The Municipal Code requires consulting agreements to go through a competitive procurement process unless the purchase is under \$10,000.

#### *Exceptions*

The Municipal Code only provides three exceptions to the competitive procurement process for the purchases of services. These exceptions are:

1. *Emergency purchases* – In case of a public emergency involving the threatening of lives, property or welfare of the people of the city or the property of the city
2. *Public agencies purchases* – This relates to acquisition of any supplies, materials or equipment or services from any public or governmental body or agency
3. *Unique services purchases* – Purchases where the procurement authority determines that an unusual or unique situation exists that make the

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<sup>1</sup> Although this Public Contract Code definition is not binding on the City, we are providing it as useful context.

<sup>2</sup> An appropriation is the legal authorization the City Council grants the Administration to make expenditures and incur obligations.

<sup>3</sup> According to the Municipal Code, Section 4.04.085, on July 1, 2013, the applicable monetary amounts shall increase based on the percentage increase from the CPI. That amount will be applicable for the next three years.

application of the requirements for competitive procurement of a services agreement contrary to the public interest. Any special procurement under this section shall be made with such competition as is practicable under the circumstance. A written determination of the basis for the procurement and for the selection of the particular contractor shall be included by the procurement authority in the department files.

**Departments Are Responsible For Procurement and Monitoring of Consultants**

The Municipal Code gives the Finance Director the responsibility for the procurement and provision of supplies, materials and equipment and procurement of contracts for services for the City. In practice, the process is decentralized, with individual City departments responsible for many types of service agreements, including consulting contracts.<sup>4</sup> Exhibit I illustrates the contracting responsibilities for departments under the City Manager’s Office.

**Exhibit I: Consulting Contract Responsibilities by Department**

Contract Process	Department	Finance-Purchasing	Finance-Accounts Payable	City Attorney's Office	City Manager	Finance-Risk Management	City Clerk
Need for service	Determine need						
	Appropriate monies						
Procurement Process	Develop a RFP/RFQ and initiate procurement	May develop RFP/RFQ and initiate procurement					
Contract Formation	Negotiate the contract			Review contract and approve as to form <sup>*</sup> .	Approve and execute contract		
Payment Set-up	Encumber funds in the Financial Management System		Review contract to ensure that encumbered funds match contract terms			Ensure that vendor has appropriate insurance on file <sup>**</sup>	Ensure contract has all required documentation Upload contract to CHAD and designate Status II
Monitoring & Payment	Review & approve invoices & match to deliverables.		Review CHAD for Status II designation				
	Enter payments in FMS		Make payments				

\* Since October 2010, the City Attorney does not review contracts under \$100,000.

\*\* Only for contracts over \$250,000. For all other contracts, the City Clerk reviews the insurance.

Source: Auditor summary

<sup>4</sup> Information technology contracts are within the purview of the Purchasing Division.



City departments are tasked with observing all applicable state and local laws and City policies and procedures when they solicit, evaluate, and award proposals and contracts. In addition, each department is responsible for ensuring that it receives deliverables and the vendor performs services per the contract.

The City Attorney's Office has historically reviewed individual contracts and approved them as to form; however since October 2010 it does not generally review the details of contracts under \$100,000. For those smaller contracts it makes standard templates available to departments and does not require a review unless there is a change to the template.

### **City Manager's Office Approval Required for Consulting Agreements**

Although the City Manager has delegated the approval authority for many contracts to the Director of Finance or department heads, approval by the City Manager's Office is required for consulting agreements up to \$250,000 in value. Prior to execution, departments send the proposed consulting agreement to the City Manager along with a "contract transmittal form". The contract transmittal form summarizes basic information such as the contracting department, the purpose of the contract, and the type of procurement. Exhibit 2 below provides a snapshot of this form.

## Exhibit 2: City Manager's Contract Transmittal Form

<b>CONTRACT TRANSMITTAL TO CITY MANAGER</b>	
<b>CONTRACTOR:</b> _____	<b>Business Tax License# (MANDATORY)</b> _____
<b>CONTRACTOR CONTACT:</b> _____	
<b>CONTRACTOR ADDRESS:</b> _____	
NEW CONTRACT <input type="checkbox"/> AMENDMENT <input type="checkbox"/> IF AMENDMENT, LIST NUMBER _____	
<b>TERM OF THIS AGREEMENT:</b> _____	<b>TO</b> _____ <b>AMOUNT OF THIS CONTRACT:</b> _____
<b>TERM OF ORIGINAL AGREEMENT:</b> _____	<b>TO</b> _____ <b>AMOUNT OF ORIGINAL AGREEMENT:</b> _____
<b>COUNCIL DATE:</b> _____	<b>COUNCIL AGENDA ITEM NUMBER:</b> _____
	<b>Council Resolution Number:</b> _____
<b>BUDGET REFERENCE:</b> _____	
<b>BUDGET:</b> _____	<b>APPROPRIATION:</b> _____
<b>DEPT.:</b> _____	<b>CONTACT:</b> _____ <b>PHONE:</b> _____
<b>TYPE OF CONTRACT:</b> Other	<b>CEQA STATUS:</b> Other
<b>DESCRIPTION OF CONTRACT:</b> <i>(What work will the contractor accomplish?)</i>	
<b>CONTRACTOR SELECTION PROCESS (CHECK ONE):</b> RFP <input type="checkbox"/> RFQ <input type="checkbox"/> <b>Date Conducted:</b> _____	
Description of Selection Process (whether RFP/RFQ was conducted or not)	
<b>INFLUENCE OF LOCAL PREFERENCE:</b>	
(Y/N) Local Business – At least one employee in Santa Clara County	
(Y/N) Small Business – 35 or fewer employees companywide	
(Y/N) Award influence by Local Preference Policy	
(\$ Value) Closest non-Local bid	
<b>ISSUES:</b> <i>(Please list any issues of importance.)</i>	
<b>COORDINATION:</b>	

Source: City Manager's Office.

### Contract Documentation and Monitoring

Each individual department is responsible to maintain contract documentation. It also must monitor whether it has received agreed-upon deliverables and whether its invoices are timely and accurate.

In addition to the individual City departments, the City Clerk is responsible for ensuring that all signed consulting contracts are uploaded on its internal website - Council History And Documents (CHAD).<sup>5</sup> The Clerk's Office reviews an executed contract for completeness. More recently, for contracts under \$250,000 it verifies that the department has obtained the necessary insurance documents as required by the contract.

If the contract complies with all document requirements, the City Clerk designates the contract as a "Status 11" when they have received all the required documents. "Status 11" signifies that the agreement has been finalized and that work may proceed. When departments enter invoices into the City's financial system for payment, Finance Department staff verifies that the agreement is "Status 11" in CHAD before authorizing payment. Without this designation, no payment should be made. Exhibit 3 below shows a snapshot of the Clerk's "Status 11" designation.

Exhibit 3: City Clerk "Status 11" Designation

The screenshot displays the CHAD system interface for the City of San José. The header includes the city logo and the text "City of San José Council History And Documents". The main content area shows contract details for "Langham Consulting Services Inc.". A red arrow points to the "Status" field, which is set to "11". Other fields include Contract No / suffix (633260 0), Contractor, Alternate Name, Address (blacked out), Narrative (Consultant services agreement for Recycle Plus & Municipal Water Program), Contract Date (12/12/2008), Term Start Date (11/14/2008), Expiration Date (06/30/2009), and various financial and administrative codes.

Source: City Clerk website

<sup>5</sup> The 2013 Mayor's Budget Message provides direction regarding the proposed purchase of a new electronic document management system.

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## Audit Objective, Scope, and Methodology

Our audit objective was to review a sample of consulting contracts, including their use, procurement, monitoring, and payment, to confirm that the City is getting the service that it is paying for. As described below, we used a risk assessment approach to identify high-risk agreements.

The City does not maintain a complete listing of awarded consulting contracts. In order to identify additional consulting contracts, we reviewed activity that appeared in the 2011-12 Award of Contract (AC)<sup>6</sup> report from the City's Financial Management System (FMS). We screened activity that appeared in the 2011-12 AC spreadsheet from Finance to identify vendors who (a) had a contract relationship with the City extending back to at least 2008-2009 and (b) were possibly consultants. We identified 144 vendors that met this description.

We then cross checked the Clerk's contract database (CHAD) for each vendor and briefly reviewed a sampling of the contract/s listed there (if any) to ascertain:

1. whether one or more CHAD contracts matched the activity indicated in the AC spreadsheet,
2. whether the not-to-exceed term had increased substantially over time pursuant to contract amendments,
3. whether there was indication in CHAD of either a "unique services" or a competitive procurement process, and
4. whether scopes of service had expanded pursuant to contract amendments.

After our first round of screening, 38 vendors emerged from the 144. We then narrowed our scope further by eliminating 1) most airport expansion-related contracts, which are often very high in both cost and complexity but also have generally been subject to separate scrutiny, and 2) contracts with financial analysts working on redevelopment issues, bond issuance, and retirement funds.

Finally, we narrowed the list to those vendors which seemed to us to have the most potential for a problematic vendor-City relationship, potentially characterized by inappropriate scope/cost creep with inadequate controls. Using staff referrals and the risk based approach described above, we selected five consulting agreements for further review. These are described below:

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<sup>6</sup> Generally consulting contracts are entered as an Award of Contract in FMS. "AC" is a term used for encumbrances entered into FMS by departments for executed construction, information technology implementations and professional services contracts, among others. As discussed in Finding I, we found that not all consulting contracts are actually processed as ACs.

1. Community Crime Prevention Associates (CCPA): The City has been contracting with Community Crime Prevention Associates, Inc. (CCPA) to evaluate the City's Parks, Recreation, and Neighborhood Services Department's (PRNS') gang prevention and intervention programs since at least 1992. CCPA has recently provided program evaluation for these programs for the twenty-first consecutive year, in addition to other work for the City. In the thirty months from September 2010 to February 2013, the City paid CCPA over \$456,000; 74 percent of this was for gang program evaluation under three overlapping contracts: one executed January 2010, a second executed November 2010 and amended March 2012, and a third executed November 2012. Our review focused on the gang program evaluation contract executed November 2010 and subsequently amended.
2. Corona Solutions (software agreement)<sup>7</sup>: In 2002, the City hired Corona Solutions, Inc. to provide an Internet-based software product that would help the San José Police Department (SYPD) process data related to crime and police activity. The original contract for \$30,000 had a one-year term, but it was set up to automatically renew on an annual basis, with no end date. The City has paid the vendor over \$586,000 for the software since 2002.
3. Corona Solutions (data and staffing analysis): Additionally, the City in 2010 separately paid Corona Solutions over \$38,000 under a purchase order initially valued at \$3,800 to analyze and report on the data processed using the software product. As of February 2013, the City had spent \$625,000 on these two Corona Solutions agreements.
4. Keyser Marston: In July 2010, the City's Office of Economic Development (OED) hired Keyser Marston for a contract valued at less than \$10,000 to provide analysis on a Zero Waste anaerobic digestion facility.<sup>8</sup> In October 2010, the City's Planning, Building and Code Enforcement Department (PBCE) added an analysis of the fiscal impact of the City's annexation of County land (Cambrian No. 36) to this contract. PBCE's work was valued at \$29,000, bringing the contract total to \$39,000.
5. Langham Consulting: In December 2008, the City entered into a consulting contract valued at \$35,000 to perform a post-implementation assessment of the efficiency and effectiveness of the City's Integrated Billing System (IBS), and to recommend system improvements. The contract and scope of work has been amended

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<sup>7</sup> We ultimately reviewed two agreements related to Corona Solutions. This was because it appeared that one of the agreements had been inappropriately characterized as an open purchase order when it should have been a consulting agreement and because it appeared to have been amended without adequate approval.

<sup>8</sup> We should note that even though OED spent over \$3,000 of its \$10,000 contract, it did not maintain any documentation related to these expenditures or the deliverables received. Therefore we were not able to review those invoices.

five times since 2008 and the current value of the contract is \$950,000. As of 2013, about \$650,000 of that amount had been expended.

We reviewed each of these agreements to answer the following questions:

- Did the department follow a competitive procurement process as outlined in the Municipal Code?
- Was there sufficient oversight of the contract during the life of the contract?

In order to meet our audit objectives we also:

- Reviewed relevant Municipal Code, City Charter and City Policy Manual sections;
- Reviewed CHAD and the AC report to determine vendor history with the City;
- Reviewed contract terms of each individual contract and subsequent contract amendments;
- Interviewed contract managers. Where there were no designated contract managers we interviewed responsible staff;
- Reviewed payments made to the contractor within FMS and compared these to invoices submitted to the department;
- Reviewed contract deliverables as provided by the department; and
- Interviewed Purchasing staff from Santa Clara County for best practices.

We also reviewed best practices documents, including the following:

- *The Request For Proposal Handbook: The best RFP practices, checklists, guidelines, examples and regulations from state and local governments and their agencies*, by Michael Asner;
- *State and Local Government Procurement: A Practical Guide*, by the National Association of State Procurement Officials;
- The Federal Acquisition Regulation (FAR); and
- The 2000 Model Procurement Code for State and Local Governments, by the American Bar Association.

We limited our review to the City's oversight of the contracting process. We did not review each contract to determine whether the department had adequately determined the need for the consultant. Nor did we attempt to determine whether what the City obtained from the consultants was, objectively speaking, good advice.

## Consulting Agreements

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During the course of our review we observed two concerns that we have referred to the appropriate department for further review. One involves a possible violation of the City's Revolving Door Policy. Specifically, a former PRNS employee involved with a vendor contract is currently employed by that vendor. In the other case, a for-profit entity received funds that may have been meant for a non-profit entity. We have referred these concerns to the City Manager, the City Attorney, the Office of Employee Relations, and PRNS for further investigation.

# Finding I The City Should Enforce Competitive Procurement Rules And Limit Exceptions to These Rules

## Summary

During the course of our review, we identified exceptions to the City's competitive procurement rules including inappropriate exceptions for "unique services," scope expansion, and increased spending without competition. In some cases staff exceeded limits on contract authority, executed contracts after-the-fact, and, in the absence of open competition, grew increasingly reliant on select consultants. Increased oversight is challenging but necessary to improve fairness and competition in City contracting. The City can streamline processes and should provide more information to employees to avoid confusion about those processes.

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## Why Is Competitive Procurement of Consulting Agreements Important?

A long-standing notion in government contracting is that public moneys used to purchase goods and services should be spent fairly, without unduly favoring one business over another. To this end, public law and policy promote *competitive procurement*, that is, the buying of goods and services pursuant to a competitive selection process.

Competitive procurement is also intended to:

- Encourage high quality goods and services,
- Lower purchase costs, and
- Foster innovation.

Additionally, because government funds come from the taxpayers, an added benefit to open competition in government procurement is the transparency that it provides. As the Model Procurement Code<sup>9</sup> puts it:

*Fair and open competition is a basic tenet of public procurement. Such competition reduces the opportunity for favoritism and inspires public confidence that contracts are awarded equitably and economically.<sup>10</sup>*

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<sup>9</sup> The American Bar Association's 2000 Model Procurement Code for State and Local Governments is a set of proposed procurement laws that have been adopted in whole or in part by many jurisdictions throughout the United States.

<sup>10</sup> Ibid., 22.



Consulting contracts (the focus of this audit) are by their nature different in many respects from contracts for more concrete goods and services. However, it is imperative that government consulting contracts, like other types of contracts, receive the benefits of fair and open competition.

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### Unique Services Exceptions Carried Over Through Numerous Amendments

As stated in the Background section of this report, the City's Municipal Code allows exceptions to the competitive procurement process for "unique services." During the course of our review, we found instances where the exception was over-used.

For example, in 2008, under the City's "unique services" exception to the competitive procurement process, the City entered into a consulting agreement with Langham Consulting. The original agreement, valued at \$35,000, was for an analysis of the City's Integrated Billing System. By 2013, after five amendments, the agreement had grown to \$950,000. Although four of the five amendments<sup>11</sup> substantially altered the consultant's scope of work, a competitive procurement process was not used for any of the amendments. Each amendment justified the use of this consultant under the "unique services" justification.

The "unique services" justification that was drafted in this case stated that the consultant was chosen in part because the consultant had already (a) done related work for the City; (b) had working knowledge of how the specific software applications were merged; and (c) because time was of the essence. The written justification stated:

*It would be contrary to the public interest and is not practicable to engage in competitive procurement due to the immediate need to begin the system migration upgrade analysis as time is of the essence. In addition it would be cost prohibitive to bring a consultant up to speed on the complexities of the existing system.*

Clearly, a different timeline was present for the four subsequent contract amendments which added over \$900,000 over four years and substantially changed the work to be done under the agreement. Although staff documented the unique services justification for each amendment, the justifications were simply restated year after year even though the scope was changing.

Finally, after several years of working with this consultant, City staff stated that the vendor "has specific knowledge related to the system requirements needed for the City's business operations as it relates to Business Tax billing, Municipal Water billing,

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<sup>11</sup> The second amendment modified the term of the agreement and made some minor changes to the schedule of performance.

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*Sanitary and Storm Sewer billing, and Recycle Plus system requirements and Customer Contact Center operations.”*

This is akin to stating that the vendor was selected because the vendor was previously selected.

### **The City Should Limit “Unique Services” Exceptions**

According to State and Local Government Procurement: A Practical Guide,<sup>12</sup>

*In today’s global economy, it is rare that only one firm can supply whatever the government needs. [...] Much sole source procurement reflects an improper relationship, such as where a “pilot” program managed by a vendor leads to a set of specifications authored by that vendor or favoring that firm.*

Some jurisdictions forbid outright all sole source procurements, such as those permitted under San José’s “unique services” exception. Other jurisdictions limit the exceptions and take additional steps to discourage over-use.

To this end, some jurisdictions require additional publicity of all non-competitive procurements. The Model Procurement Code, for example, requires an annual report describing the year’s non-competitive procurements.

In our opinion, additional controls are advisable to ensure that the initial vendor does not acquire a “lock” on subsequent City business.

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### **Consulting Contract Scopes Expanded and Spending Increased Without Competition**

Other consulting contract procurements we examined did not expressly claim the “unique services” exception, but still avoided competition during the initial procurement. City staff then continued to turn to the same consultants for additional work, and these non-competitive contracts increased in value and scope – still without using competition.

For example, in 2010, the City’s Office of Economic Development (OED) hired Keyser Marston to analyze a proposed project at a cost of \$10,000. Because the agreement was only \$10,000, a competitive procurement process was not required. But then the City’s Planning, Building and Code Enforcement Department (PBCE) “piggy-backed” additional services valued at \$29,000 onto the original agreement to analyze a completely different project. Rather than drafting a separate agreement, PBCE amended the existing OED contract, bringing the contract total to \$39,000. No competitive process was involved. As with some of the other agreements that we reviewed, City staff stated that time constraints required them to use a non-competitive process. Under the City’s

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<sup>12</sup> By the National Association of State Procurement Officials (2008), p. 31

Municipal Code requirements, once the agreement exceeded \$10,000 it should have been competitively procured.

In another example, the City executed a \$3,800 purchase order with Corona Solutions, Inc., in 2010 to use police data to analyze, summarize, and build staffing scenarios. Purchase orders are not intended to be used for consulting agreements. Nonetheless, SJPD ultimately paid \$38,000 on this purchase order (over \$34,000 more than the amount of the original purchase order). It appears that the added payment was for a staffing deployment report that was not part of the original purchase order. Because it was more than \$10,000, this added scope should have been competitively procured, or a unique services exception should have been prepared. It was not.

In addition to enforcing existing rules to ensure competition, we believe the City should implement procedures to limit the life of non-competitive contracts to prevent any one vendor from appearing to have a long-term lock on the City's business.

### **In the Absence of Open Competition, City Staff Can Grow Increasingly Reliant on Select Consultants**

As discussed in the cases above, City staff used the fact that the vendor had been previously selected for work with the City as a major justification for staff's continued reliance on the vendor. Many of the contracts we reviewed showed long-standing relationships between departments and vendors. Specifically:

- ESD staff identified a consultant's expertise with respect to the core system processes as one of the causes to continue to turn to that firm. Some scopes of work that were added to the contract were the result of the consultant's own analysis. The department has continuously used this consultant since 2005 for various contracts and has paid about a million dollars during the same amount of time. The consultant essentially has a "lock" on any work related to that system.
- SJPD staff identified a consultant's eight years of software business with the City as a reason to employ it to do consulting work, and did not look past that consultant to consider any other consultant for that work.
- OED and PBCE chose a consultant as a vendor that had worked extensively with the City before, that was also available to do work on short notice. Staff told us that they had been satisfied with the vendor's previous "high quality impartial analysis".
- PRNS staff has retained the same consulting firm for over twenty consecutive years to evaluate the City's gang programs. Since at least 1992, the City has paid this consulting firm over \$2.5 million for over 30 City contracts. In just the last two-and-a-half years, the City has paid the firm almost \$500,000.

A good reason to retain a consultant is exactly because s/he is bringing outside expertise to the City's work. For example, PRNS staff stated that many years ago the City decided it would benefit from bringing in a third party to provide an objective report on the outcomes of gang prevention efforts. However, the vendor has since become a "major stakeholder" in the process and continues being selected for the same work year after year.<sup>13</sup> In our opinion, the fact that the consultant's knowledge set is informed by *different* experiences than City staff's is what makes the consultant valuable. But consultants who work closely with City staff day in and day out may lose that edge, and the value of the services they provide may diminish.

Finally, the longer a consultant performs the same service and develops close relationships with City staff, the more embedded s/he can get, thereby diminishing the opportunity for fair and open competition to other vendors.

**Recommendation #1: To foster open competition for City contracts, we recommend that the City Manager's Office:**

- a) **Require unique services justifications to describe the department's effort to reach out to other potential vendors;**
- b) **Limit amendments to original agreements for non-competitively procured contracts if there is a substantial change in scope;**
- c) **Limit the number of years that such contracts can be amended or continued (including contract continuation agreements, options to renew and any other instrument that would substantively modify the original agreement);**
- d) **File approved unique services justification memoranda with the City Clerk's office; and**
- e) **Periodically report all non-competitively procured consulting contracts, perhaps in the City Manager's publicly available quarterly contract report.**

<sup>13</sup> While PRNS does go through a Request for Qualifications process every five years, it does not require further competition during the course of those five years.

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## **Staff Exceeded Council Approval and Authorized Off-Contract Work**

### **Spending Exceeded Council Approval**

City Council approval is typically required for agreements over \$250,000. In 2002, the City hired Corona Solutions, Inc., to provide an Internet-based software product that would help the San José Police Department (SJPD) process data related to crime and police activity. This software contract was different from the police staffing analysis described above. This agreement for \$30,000 had a one-year term, but was set up to automatically renew on an annual basis with no end date.

In August 2004, the City Council approved extending the agreement through March 31, 2005; increasing the compensation to a cumulative total of \$135,000; and approving “one-year renewal options without further Council action other than the appropriation of funding, not to exceed 5 years.”

SJPD’s Council authority to exercise up to five annual options to renew the contract expired in March 2010. Since then, payments to this vendor have exceeded \$600,000 without City Council approval.

**Recommendation #2: To ensure compliance with City Council approval authority, we recommend that the SJPD either (a) terminate its unapproved contract with Corona Solutions and/or (b) receive approval from City Council for monies already spent.**

**Recommendation #3: At the same time that it checks the CHAD database prior to authorizing an encumbrance and/or payment, the Finance department should check the agreement’s not-to-exceed amount in CHAD.**

### **Staff Authorized Off-Contract Work**

Our review also revealed instances where the City executed consulting contracts after consultants had already started their work. In one case, most of the contractor’s work was completed by the time the contract was executed. Another contractor continued to work for the City between the expiration of one contract and the effective date of another. In that case, the contract executed in November 2010 authorized payment for work performed in October 2010. Similarly, a contract amendment executed in March 2012 was “retroactive” to January 2012.

However expedient it may be, permitting vendors to work off-contract is a bad idea. As described above, the Municipal Code requires all agreements with contractors to be in writing, be approved as to form by the City Attorney, and be filed at the Clerk's Office. When City officials authorize the start of work prior to the completion of the City's legal contracting process, they exceed their legal authority.

Furthermore, when contracts are not legally formed, their enforceability is questionable. In those situations, the City may have no obligation to compensate the contractor for the work. We should note that the consultant agreement template the City Attorney's Office provides to departments includes a retroactive provision. According to the City Attorney's Office, the retroactive provision should be used in very limited circumstances where work needs to start while the contract is in the process of execution.

In our opinion, any time a City employee informally authorizes vendor work, they are committing City funds not within their authority to commit. This can give the appearance of favoritism, especially if the contract has not been competitively procured. Moreover, favoring previously employed vendors goes against City policy, which actively attempts to encourage small business contracting and open competition.

As mentioned in the Background section of this report, the City Manager's Office requires each department to fill out a contract transmittal form documenting the type of procurement used. It includes a small space for staff to describe the procurement process, but it is irregularly used. There are no guidelines on what this description should include. In our opinion, the form should also be used to bring attention to those hopefully rare instances when the contractor had already begun work prior to final execution of the agreement.

**Recommendation #4: We recommend the Administration improve enforcement of existing Municipal Code contracting requirements by:**

- a) limiting retroactive contracts to situations where contract execution is in process and the contract has been competitively procured,
- b) including this information on the contract transmittal form, and
- c) periodically reporting on all retroactive consulting agreements regardless of the value or procurement method of the agreement, perhaps in the City Manager's publicly available quarterly contract report.

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## Increased Oversight Is Challenging, but Necessary and Required

As mentioned above, consulting contracts (the focus of this audit) are by their nature different in many respects from contracts for more concrete goods and services. However, it is imperative that government consulting contracts, like other types of contracts, receive the benefits of fair and open competition. As one procurement guide put it,

*While many procurement statutes exempt certain services, such as consultants, from the requirements of competitive selection, procurement officers should use, unless prohibited by law, competitive procurements in these cases as well. Criteria such as reputation, cost, past experience, past performance and historical success can be used to compare competing service proposals. If nothing else, the mere knowledge that a services provider must compete keeps rates lower and performance levels higher.<sup>14</sup>*

Reflecting on the historical omission of professional services from public procurement laws, the guide goes on to note:

*It was ironic that the authority to buy the item that could result in the most subjective decision-making – professional services – was left to vague processes and outside of the purview of the procurement professional. Leaving that unbridled discretion in the hands of untrained persons was an invitation for problems and mistakes, and for fraud and abuse.<sup>15</sup>*

### **A Highly Dispersed Procurement Function Makes Standardization of City Procurement Processes Difficult and Requires Enhanced Oversight**

In the three years ending June 2012, the City reduced staffing by 1,100 persons. City staffing dropped from 8.4 staff per 1,000 residents in 2002, to 5.6 staff per 1,000 residents in 2012. These dramatic reductions meant dramatic changes in the roles of remaining staff, as we previously documented in our 2012 report, *Ten Years of Staffing Reductions at the City of San José: Impacts and Lessons Learned*. As a result, non-procurement and procurement staff alike are spread thin across the City.

The City's Municipal Code gives the Finance Director broad responsibility and authority with respect to procurements, including for the procurement of contracts for services for the City. It requires that deviations from this

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<sup>14</sup> State and Local Government Procurement: A Practical Guide, p. 26.

<sup>15</sup> Ibid., 142.

responsibility be “provided elsewhere in this Code.”<sup>16</sup> The Director is also expected to “endeavor to obtain as full and open competition as possible on all purchases.”<sup>17</sup>

And yet, in interviews with Finance staff, we heard concerns that staff reductions had limited the ability of the Department to exercise this oversight. Since FY 2007-08 the Purchasing Division has seen significant staffing reductions. Specifically, in FY 2007-08, the Division had thirteen staff handling procurements and purchase orders. As of FY 2012-13 the Division had been reduced to seven staff, with the Division Manager also handling some procurements. It should be noted that two of those staff were new.

**Recommendation #5: The City Manager’s Office should revisit the role of the Finance Department with respect to consultant procurements, evaluating whether its current level of involvement and resources is adequate.**

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### **Staff Decisions to Avoid the Competitive Process May Stem in Part from Confusion About How to Employ It**

Departmental staff we interviewed generally found the City’s procurement process intimidating and confusing. The consensus of many was that competitive procurement is difficult, time-consuming, and unfruitful. Individual departments are responsible for their consultant procurements. A 2004-05 Santa Clara County Civil Grand Jury Report on the City of San José Procurement Policies, Procedures and Practices found, among other things, *substantial risks may be incurred by not having professional procurement personnel involvement or oversight in the procurement process*. In response to this report the Finance department developed a web-based Request for Proposals manual. To ensure proper usage of the manual citywide each department was to designate a “Certified Contract Specialist” trained by Finance who would provide guidance in the development and evaluation of RFPs.

However, since at least 2010, there has been no training for staff on how to do a procurement. In addition, the online RFP manual providing such guidance has not been updated since 2006, and does not incorporate updates in the City’s process, including the 2010 changes to the Municipal Code. According to Finance, staffing shortages have prevented both the training program and maintenance of the online manual.

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<sup>16</sup> Municipal Code section 4.12.120

<sup>17</sup> *Ibid.*



**Recommendation #6: The City should implement the “certified contract specialist” program, and/or provide regular procurement training to staff.**

**The City Should Streamline Processes While Enforcing the Competition Requirement**

The City’s procurement policy already allows for a less stringent process for all contracts for services valued at \$10,000 to \$100,000. According to Finance, the City can employ additional mechanisms to shorten the procurement timeline, but still ensure a competitive process. Further, the website where the City posts bids (BidSync) can be used for fast-track, simple procurements. However, staff we talked to in other departments appeared to be unaware of these simple processes. Further, the on-line RFP manual that is the only source of information for the City’s procurement process does not provide guidance on these simplified processes.

In our opinion, the City needs to publicize a simplified competitive process for smaller contracts.

**Recommendation #7: To lessen the burden on City staff while fostering improved competition in consultant procurements, the Finance Department should include in its annual procurement training simplified procurement processes for smaller consulting contract procurements while encouraging full and open competition, and define when these simplified processes can be used.**

## Finding 2 Monitoring Of Consulting Contracts Should Be Improved

### Summary

The City uses consultants for a myriad of reasons including doing analysis, facilitating workshops, and providing advice on policy issues. Our audit identified several agreements for review. We found that the City's oversight of these consultants was inadequate. Further we found that City staff had ignored contract terms, changed contract deliverables and payment terms without authorization, and sometimes paid vendors more than required by their contracts. Finally, in many instances staff was unable to provide us with contract-required deliverables. In our opinion, the City needs to ensure that overpayments are reconciled and paid back to the City, staff is trained on how to manage contracts and consistent policies and procedures are developed.

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### What Does Effective Contract Monitoring Look Like?

The City's online Request for Proposals manual recommends staff monitor contractor performance during the life of the contract. A key to effective contract monitoring is to identify and address all problems promptly. The manual further states monitoring should include:

**Quality** – *Does the contractor's performance meet the performance standard specified in the contract? In instances where the contractor is providing a service for a specified group of people, such as City employees or the general public, you may consider evaluating customer satisfaction through customer surveys or interviews regarding contract services. However, please note that the contractor cannot be held to a quality standard that exceeds the standard specified in the contract.*

**Timeliness** – *Monitor delivery schedules to prevent or minimize lapses in service.*

**Productivity** – *Monitor productivity requirements to ensure that the contract's minimum standards are met.*

Ideally, the compensation structure of an agreement focuses payments on the outcomes the government wants. One way to do this is to specify milestones tied to payment, or delay payment until full performance of the contract. It is also possible to combine two approaches, so that the vendor reports hours to some degree but full compensation is still contingent on accomplishing milestones. This also makes it easier for staff to compare costs during procurement- they can

ask a vendor what it will cost for a given analysis or report and compare that lump sum to its competitors, rather than focus solely on hourly rates.

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### **Contract Terms Were Ignored and Oversight of Contractors was Inadequate**

Our review of the five contracts described in the scope and methodology section of this report revealed instances where staff did not monitor basic contract terms and continued paying vendors without verifying that services were actually rendered. The sections below illustrate the oversight problems that we observed.

#### **Invoices Did Not Provide Sufficient Detail to Ensure Adequate Staff Review**

An important factor in contract review is a close monitoring of contractor payments. This should be done through a thorough review of the payment requests. Thus, the City's contract with Langham Consulting required that each invoice include

*a detailed description of the work completed, the number of hours worked and the applicable hourly rates, a detailed description of the reimbursable expenses incurred and the amount of such expenses, and documents supporting the reimbursable expenses.*

However, each invoice submitted by the consultant since 2008 only states "Project Consulting Services provided by [...]" and the week the work was performed. There was no information on the invoices with regard to the dates of the work or its description, even though the contract requires this detail. Further, the Finance department never received invoices for its review or approval, even though the fourth amendment added additional services that Finance was supposed to manage. ESD, not Finance, continued to approve and make payments on these invoices.

Similarly, we found that the invoices provided by CCPA to PRNS staff made it impossible to confirm actual vendor employees' billable hours, although the payment schedule was structured around them. Invoices lacked basic descriptive information such as which vendor employee charged which hours for which weeks. Staff limited their invoice review to confirming that the total amount for each monthly invoice did not exceed the contract not-to-exceed amount. Furthermore, invoice detail did not always match the compensation schedule in the agreement.

PRNS's Contract Development Guide requires staff to compare invoices to the contract terms, as well as to actual performance, prior to authorizing payment.

*Requests for payments should be reviewed to ensure that items or hours charged match the invoices/reports, contract prices and accurately reflect the services/products received. No payments should be authorized if services/products are not satisfactory. Payments should coincide with the Compensation section of the contract.*

### **Some Contract Terms Were Changed and Deliverables Were Not Documented, Were Informally Changed or Were Never Received**

We found that in the case of the Corona contract the City has been paying more than it agreed to since at least 2007. Specifically, in 2005 the City agreed to pay \$0.12 per police CAD incident processed by the vendor's software. However, since 2007 staff has been approving payments at \$0.13 per incident. Since 2007, that one cent difference has cost the City an estimated \$30,220.

And even though the consultant was required to provide the City with quarterly statements, staff could produce none.

In the case of the Langham agreement, City staff allowed changes to contract deliverables. For example,

- The agreement required the contractor to "Prepare quarterly status reports to assess process and schedule and financial feasibility forecasts documenting status for all projects considered by the strategic plan". The budget for this line item was set at \$21,000. However, according to ESD, the City requested that the contractor instead provide a "verbal" update. There was no reduction in the price.
- Although the agreement required the consultant to "document position requirements for Application Manager role" for \$5,600, City staff reported they had cancelled this deliverable. We were unable to determine whether the City had paid for this deliverable because the department does not track individual budget items.
- Four deliverables were also dropped from the second Langham contract amendment after the City paid for them. There was no explanation whether the deliverables were received or whether the requirements changed. According to City staff, many of the deliverables were changed because the direction of the project changed. But because staff has not been tracking the contract budget and checking off deliverables as the City received them, we have no assurance that the City has actually received all the deliverables that the contract required and the City paid for.

None of these scope changes were highlighted to the contracting authority (whether to the City Council, the City Manager, or her designee) when contracts were amended and, to our knowledge, did not result in a reduction of fees.

### **The City Overpaid for Some Services and Reimbursable Expenses and Did Not Follow its Own Approval Processes for Additional Work**

#### *Overpayments*

Among the contracts we reviewed, we found some overpayments, including \$2,418 for CCPA surcharges for “fringe benefits” and “indirect costs.”

We also found that PBCE paid about \$279 more than the Keyser Marston contract allowed for reimbursable expenses. This included reimbursements for reports that the contractor used (with a 10 percent or \$48 mark-up over cost). The contract did not allow reimbursements for these items or the mark-up. Furthermore, the contract required allowable expenses to be pre-approved in writing by the Chief Development Officer. We did not find any written pre-approvals that would allow these payments.

#### *Undocumented “Additional Services”*

Similarly, the CCPA contract required prior written authorization and separate negotiation for charges against its “additional services” budget. We found that the contractor charged, and the City paid, a total of \$11,050 for “additional services” without prior written authorization from the City. The vendor provided minimal description of what these charges were for. City staff stated the vendor was provided verbal authorization. For another charge, staff provided assurances, but could not provide documentation that “additional services” did not overlap with work already contemplated in the contract.

#### *Budget and Task Order Process Ignored*

The Langham contract prescribed a tentative budget for each task in the consultant’s scope of work, but staff cannot provide assurance whether they were within those budgeted limits because these were never tracked. According to the contract, “the tentative budget for each Task [...] shall be consistent with the [...] Schedule of Compensation.” We found that dollar amounts for two budget line items were changed in the fourth amendment without explanation. As stated above, staff does not track individual line item budgets, therefore changing these budgets is a “guess” at best. And, although the contract required task orders to describe what work the consultant was supposed to do and for what price, staff never used this process. Instead, staff continued paying the consultant on an hourly basis.

Similarly, PRNS staff allowed CCPA to exhaust the budget for some types of meetings before completing all of the meetings. Then, after budgets had been replenished under a subsequent contract or amendment, staff authorized retroactive payments for the remaining meetings.

*Compensation Exceeded a Not-To-Exceed Task Amount*

When PBCE “piggy-backed” on OED’s \$10,000 contract, it agreed to a not-to-exceed contract amount of \$29,000. It exceeded this by \$1,380 even though the contract expressly disallowed it. The consultant’s invoices themselves highlighted that they had exceeded the agreed-upon-amount. The excess PBCE portion was “covered” by OED’s original contract encumbrance of \$10,000.<sup>18</sup>

**Staff Relied on Vendor’s Invoices and Did Not Verify Their Accuracy**

One agreement implied a truing-up process that, according to staff, has not been happening. Specifically, one of the Corona contracts requires the City to pay in advance based on a projected number of CAD police incidents processed by the software product. The City agreed “to pay an annual fee in advance calculated on the anticipated volume of incidents”. However, we found that although this contract compensation was tied to the number of CAD incidents, staff never verified that the number of CAD incidents the City paid for matched the number of incidents that actually happened. The contract expressly required overpayments from one year to be applied to the following year’s contract. Staff should have been “truing up” expenses at the end of the year to ensure that there were no over/underpayments. However, it does not appear that this was ever done.

**Recommendation #8: We recommend that the City**

- a) Reconcile overpayments as described above and get reimbursed for these overpayments,**
- b) Document any changes in consulting contract terms or requirements through a formal contract amendment, and enforce existing contract terms. If the contract allows for changes in terms without amendments, such changes should be documented in writing, and**
- c) Require contract managers to reconcile previously received deliverables to contract payments during the contract amendment process, prior to increasing contract amounts.**

<sup>18</sup> OED has been unable to provide the Auditor’s Office with any invoices or work product of its original contract with Keyser Marston.

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### **Contract Monitoring Requires Consistent Processes, Accountability and Training**

According to the Georgia State Auditor's Best Practices in Government: Components of an Effective Monitoring System: "Contract monitoring is an essential aspect of all three phases of contracting – the pre-contract period, contract period, and post-contract period." The Auditor identified the following components as necessary for an effective contract monitoring system:

- *Training employees in contract monitoring;*
- *Written policies and procedures for contract monitoring;*
- *Contingency plans;*
- *Clearly communicating expectations to vendors through a detailed statement of work, performance measures, and post-award meetings;*
- *Contract administration plan;*
- *Organized contract files;*
- *Payments linked to satisfactory performance;*
- *Regular programmatic reports;*
- *Access to records and right to audit; and*
- *Dispute resolution procedures.*

#### **Lack of Training and Inconsistent Policies and Procedures**

In our opinion, the City faces significant financial and programmatic consequences from inadequate contract monitoring. As discussed above, consequences ranged from overpayments to contractors, to not receiving the very advice or reports that were the original purpose of the contracts.

We found that the City does not have any Citywide policies governing contract monitoring. Staff has dual responsibilities of program management along with monitoring contracts, for which they have received no training.

We also found that Department contract files were incomplete and in some cases did not exist, requiring extensive effort and coordination on the part of staff to find basic contract-related documents. The City does not provide any training to staff on the appropriate level of oversight for contract monitoring. It is left up to individual staff to determine what level of oversight they should provide.

Further, staff appeared to rely heavily on consultants to determine contract scope and compliance. Staff focus was on developing a “partnership” rather than enforcing rules, regulations or contract provisions. In our opinion, it should be both.

### **Effective Contract Management Depends on Staff’s Understanding of Internal Controls**

According to the U.S Government Accountability Office (GAO),

*an entity’s management should establish and maintain an environment that sets a positive and supportive attitude towards control and conscientious management. A positive control environment provides discipline and structure as well as a climate supportive of quality internal control, and includes an assessment of the risks the agency faces from both external and internal sources.*

*Control activities are the policies, procedures, techniques, and mechanisms that enforce management’s directives and help ensure that actions are taken to address risks. [...] Control activities include both preventive and detective controls. Preventive controls—such as invoice review prior to payment—are controls designed to prevent improper payments (errors and fraud), waste, and mismanagement, while detective controls—such as incurred cost audits—are designed to identify errors or improper payments after the payment is made. Further, preventive controls such as accounting system reviews and invoice reviews help to reduce the risk of improper payments or waste **before** [emphasis added] they occur. [...] Generally, it is more effective and efficient to prevent improper payments. A control activity can be preventive, detective, or both, based on when the control occurs in the contract life cycle.*

### **The City Requires All Employees to Certify Understanding of Its Procurement Card Policy, But Not to Monitor Millions of Dollars of Contracts**

The City’s Finance department administers the citywide procurement card program. In order to ensure successful utilization of the program, all procurement cardholders have to sign a Procurement Card Program Cardholder Agreement acknowledging that the cardholder has read and understood the procurement card policy and will abide it.

Additionally, all employees receiving a procurement card have to take and pass a quiz as part of the application process and certify to the following:

*I am responsible for the card's safekeeping at all times. I will immediately notify the financial institution, which issued the Procurement card, the Approving Official, Department Procurement Card Coordinator, or the Citywide Procurement Card Administrator*



*when the card is lost or stolen or if I believe the card was used in a fraudulent manner. I will review the Monthly Statement within five business days of billing statement date and forward verification of charges and all required supporting materials to the Approving Official. If I dispute a charge, I will immediately seek to resolve the problem with the vendor, and follow the process as outlined in the Procurement Card Policy.*

Many of these employees' monthly spending limits are between \$500 and \$10,000.

However, employees monitoring millions of dollars of taxpayer funded consulting contracts require no such accountability and receive no training on how to monitor these contracts. In our opinion, the City needs to develop a consistent contract monitoring process and ensure that staff is empowered and accountable for contract administration.

**Recommendation #9: We recommend the Administration develop Citywide policies and procedures on contract monitoring and management including:**

- a standardized contract management process,
- organization of contract files,
- checklists for tracking agreed-upon deliverables and line item budgets,
- components of invoice review which link payments to contract deliverables, and
- documenting deliverables prior to payment.

**We further recommend that the City require contract administrators to annually certify they have reviewed and understand those policies and procedures.**

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## **Accountability is Hampered By Lack of Contract Managers and Document Retention**

### **No Contract Manager Requirement**

The City does not require its departments to have a contract manager for each contract. We observed contracts lacked a central contract manager. For example, the Langham consulting contract has no contract manager. Oversight has been further hampered because it spanned three departments - ESD, Finance

and ITD. In addition, contract terms have been amended multiple times, over multiple years, with direction being provided by a Steering Committee made up of senior members of the three departments. Staff turnover in all three departments has meant that the consultant was one of the few original participants over the course of the project.

**Recommendation #10: For inter-departmental contracts, we recommend the Administration require staff to designate a responsible staff member who would be accountable for all aspects of contract monitoring, including invoice approval and review.**

### Document Retention Requirements Were Not Followed

The Citywide retention schedule for contracts states “Service and other contracts, and any records (including insurance certificates) needed to document contract compliance and/or performance” is “Term +5 Years.” The Citywide retention schedule is “4 Years” for

*“Procurement and purchasing records – Records documenting procurement and contracting activities not conducted by the Finance Department/Purchasing Division or involving capital construction including but not limited to Qualifications Based Selection, Request for Proposal, Request for Qualifications, Request for Information, proposal evaluation forms, confidentiality agreements, conflict of interest forms, and unsuccessful bids”*

During our review, staff seemed genuinely unaware of the retention requirements for some of these agreements. For example, we found that SJPD has not maintained complete files even though the City’s retention policy clearly required it. Furthermore, one of the contracts is still active. SJPD staff appeared to be unaware of the documentation retention requirement and told us that they routinely destroy contract related files/documents after two years.<sup>19</sup>

With respect to ESD’s agreement, staff was not able to provide us with many deliverables/reports that staff says the consultant provided. According to staff, these files may have been destroyed.

<sup>19</sup> We could only provide a limited review of both SJPD agreements because both contracts’ files had been prematurely destroyed. Specifically, SJPD Fiscal staff informed us that they have already destroyed the file for the consulting contract (which was last paid in 2010). Staff stated that they did not believe the retention policy applied to this type of contract. In addition, SJPD Fiscal was able to provide only limited billing-related information for the software contract dating back to 2007, but none for the first five years of the contract. Some, but not all invoices (“estimates”) were available. There was no record of substantive contract monitoring for either contract.

Finally, we were not able to provide any review for portion of one agreement because OED does not have documents describing what the purpose of the original contract was, or invoices related to the about \$3,000 already spent on the contract. It appears that OED did not get the final report that it had contracted for, but there is no explanation as to what happened.

The Clerk's Office also had difficulty locating some previously filed contracts. The original 2002 Corona contract was still on file, but subsequent documents had been misfiled. In addition, the CHAD database had staff entry errors which made location of the files difficult. Annual renewals or amendment filing can get confusing because these renewals may be viewed as expired after the one-year term, prompting premature document destruction.

**Recommendation #11: We recommend the Administration ensure that:**

- a) Staff managing contracts conform with current City contract retention policies and, consistent with those policies, keep all documents related to contract procurement, compliance and monitoring, including all documents related to contract renewals, amendments, continuation agreements, and other contract modifications; and**
- b) Require staff to include a notation regarding the City's retention policies in each individual contract file.**

## Finding 3 Transparency and Ethics Policies Should Be Followed and Clarified

### Summary

Our review indicates the City can do better at enforcing state and local laws that address consultant agreement ethics, including prohibitions on conflicts of interest and disclosure of economic interests (commonly known as Form 700s). Consulting work is of an advisory nature and deliverables are generally less measurable than for other services, making it important to track spending. In our opinion, developing and making such information available can only promote transparency, increase oversight and provide assurance to taxpayers that their monies are being appropriately spent.

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### State and Local Laws Prohibiting Economic Conflicts of Interest Also Apply to Consultants

State law prohibits self-dealing in government. The California Political Reform Act of 1974 spelled out a system whereby local governments must track potential conflicts of interest among their employees and consultants. It requires cities to adopt a local “Conflict Code” that designates which local individuals must file “statements of economic interest” (commonly called “Form 700’s”), and what they must disclose on those statements. The City last updated its Conflict of Interest Code in December 2012.

The City’s Conflict Code requires “consultants” as defined by the Political Reform Act to file disclosure Form 700s. A “consultant” is defined as an individual who pursuant to a contract with the City

- serves in a staff capacity and in that capacity participates in making a governmental decision, or
- makes one or more of a number of types of government decisions (such as approving contract specifications, approving a report or study, or adopting policies, standards, or guidelines).

In other words, when a person, for example, writes a report to aid a government decision, that person’s work is “participating in making” that government decision. When that person is working under contract with the City, that person is a consultant who needs to file a Form 700.<sup>20</sup>

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<sup>20</sup> Note that multiple Form 700’s may be required for an individual filer: assuming office forms, annual forms, and leaving office forms. For the sake of brevity, we are focused on whether *any* of these forms are required for an individual, rather than which forms are required. We are also not touching on *what* the individual must disclose in the event they do have to file.

### **Previous Audit of Form 700 Filers**

This Office previously audited the City's Form 700 filing system. In our 2010 audit, we noted that only 45 of 142 consultants filed the annual Form 700. We further noted the need for improved guidance on the question of which City consultants are required to file Form 700s, and improved processes to clarify the responsibilities of firms to ensure their employees are filing. Pursuant to the 2010 audit, the current Conflict Code now requires the City Clerk to notify Department Directors when required filers have not filed. The report's five recommendations have yet to be fully implemented.

### **Almost None of the Consultants Whose Contracts We Examined Filed the Necessary Form 700's**

None of seven CCPA employees who have worked on the City's gang programs in the last three years have filed Form 700's in spite of the fact that the CCPA contract explicitly requires the vendor to file Form 700's. The City relies on CCPA's reports and advice to assess the efficacy of its gang programs and to make decisions about how to spend program funds.

The Langham contract, too, required Form 700 filing. The principal employee who works with City staff did not file Form 700 for 2011, though he did file for other years. All 5 of the other employees who worked at different points of time with City staff did not file Form 700's for any of the relevant years. The City is relying on this consultant's advice to determine the methodology for billing garbage services when the Integrated Billing System loses software support in 2015.

No Form 700s were filed by Keyser Marston employees. While the contract did not require a Form 700 filing, the City relied on these individuals' advice to determine whether it was in the best interest of the City to annex some County property, and the contract should have required it.

No Form 700 was filed by Corona Solutions employees, even though the purpose of its report was to influence SJPD staffing deployment decisions.

Without Form 700s, the City and the public are unable to determine whether any of these consultants violated the law against self-dealing in their work on City contracts.

Although Form 700 filing requirements exist independent of contract language, the City's objective of discouraging conflicts of interest is ill-served when the consultants' duty to file is not clearly articulated in the contract. Violation of state law provisions related to Form 700 filing, as incorporated by the City, can make consultants subject to fines, and in some cases civil and criminal sanctions. These include fines of \$10 per day for late filing.

**Recommendation #12: We recommend that:**

- a) **The City Clerk in consultation with the City Attorney's office provide training to City staff on Form 700 filing requirements for consultants, follow-up on missing Form 700s for current agreements, and penalize consultants who do not comply, and**
- b) **The City Clerk, prior to providing Status II payment authorization, require Form 700s from those consultants whose contracts require them.**

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**Ethics Training For All Contract Monitoring and Procurement Staff**

All staff who are involved with consulting contract monitoring and procurement should have adequate training and experience to recognize and prevent behaviors that compromise wise stewardship of public moneys.

Public procurement is both a field and a profession, and many existing resources provide excellent guidance applicable to the City's procurement challenges. Aside from training about the mechanics of how the contract procurement process should work, other programs should be available.

For example, one checklist of public procurement official ethics<sup>21</sup> includes the following:

1. Be independent (from vendors, prospective bidders, elected officials and political appointees, and other interested parties),
2. Act only in the public interest,
3. Remain a trustee of the public's money,
4. Follow the law,
5. Strive for efficiency,
6. Protect the economy (by discouraging the bundling of contracts and other practices that erode a diverse marketplace),
7. Take nothing, ever (gifts, which can give the appearance of favoritism),
8. Do not socialize with vendors,

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<sup>21</sup>State and Local Government Procurement, p. 27

9. Maintain confidentiality (avoid providing insider information to vendors), and
10. Do not play favorites (each vendor must stand on level ground).

The City's conflict of interest, revolving door policies and ethics principles should also be highlighted to contract monitoring and procurement staff.

**Recommendation #13: We recommend that the City Administration include the City's Conflict of Interest and Ethics policies in its annual procurement and contract monitoring training.**

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## Promoting Transparency

Transparency with regard to taxpayer funds paid to consultants helps provide public officials and residents with assurance that the services paid for are being delivered, and that the consulting agreements are monitored by the City on an ongoing basis.

### **The City Does Not Track Total Spending on Consultants**

Neither the City's Financial Management System (FMS) nor the contract database maintained by the City Clerk's office has standard definitions that would allow easy compilation of the City's total expenditures on consultants. Each City Department is responsible for monitoring its own consulting contracts, and departments may classify consulting expenditures differently.

As stated previously, consulting work is of an advisory nature and deliverables are generally less measurable than with other types of contracts. In our opinion, this makes it especially important to track and "daylight" spending on these advisory services.

### **Definition of a Consultant**

In order to begin tracking these expenditures, the City should develop and make available to staff a more precise definition of what a consultant is. For example, the County of Santa Clara defines consultants as professional services that *provide support to and facilitate department operations and the governmental functions of the County administration/management, program management or innovation.*

In our opinion, more clearly defining and making information available about the City's use of consultants will promote transparency, increase oversight and provide assurance to taxpayers that their monies are being appropriately spent.

### Other Cities Track and Publish Spending on Consultants

The City of Seattle publishes a publicly accessible roster of consultants. The City of Seattle Consultant Roster Program is an internet-based program that features numerous categories of consultant services routinely utilized by city departments. Consultants who wish to do business with the city may apply to one or more of these categories by completing and submitting an application online. Applicants who adequately demonstrate experience and capability in a category are added to the Consultant Roster. City departments may use any approved consultant in the Consultant Roster Program for projects totaling \$260,000 or less. Departments select consultants based on their expertise and abilities outlined in their applications. The City makes this list publicly available.

The City of Chicago also maintains a publicly accessible database of all awarded contracts. This database can be searched by type of contract, dollar amount, vendor name, type of procurement, etc. According to its website,

*...the City of Chicago's Data Portal is dedicated to promoting access to government data and encouraging the development of creative tools to engage and serve Chicago's diverse community. The site hosts over 200 datasets presented in easy-to-use formats about City departments, services, facilities and performance.*

Similarly, the State of Colorado also maintains a database of contracts that are searchable by department, contract date, contract terms, positions created, work performed, and vendor performance rating.<sup>22</sup> Exhibit 4 shows a snapshot of the searchable database.

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<sup>22</sup> The State of Colorado's contract close-out process requires a vendor performance evaluation rating.



**Exhibit 4: State of Colorado Contract Management Website**

Colorado The Official State Web Portal  
Department of Personnel & Administration  
Office of the State Controller  
633 17th Street - Suite 1520, Denver, Colorado 80202  
Good Government Starts Here

Help Comments

**State of Colorado - Contract Management System**  
**Public Website Search Form**  
Powered by: Cobblestone Systems Corp.

**General Information**

State Entity  
--Select One--

Vendor  
Contract Purpose

**Contract Dates**

Effective Date  
Begin  
End

Period of Performance  
Begin  
End

**Vendor Performance Rating**

Final Vendor Rating  
--Select One--

**State Personnel Positions Affected**

# of New Positions Created  
--Select One--

**Contract Terms**

Maximum Contract Amount  
--Select One--

Vendor Solicitation Method  
--Select One--

**Location of Work Performed**

% Outside CO  
--Select One--

% Outside US  
--Select One--

Search Records  
Back

Source: <http://contractsweb.state.co.us/default.aspx>

**The 2013 Mayor’s Budget Message Directs Expenditure on an Electronic Data Management System**

The current CHAD system is outdated and limited. It is also not accessible to members of the public. The 2013 Mayor’s Budget Message provides direction to the City Clerk to work with the City Manager’s Office to use savings within the City Clerk’s current year appropriations to fund an electronic document management system. The City Clerk anticipates that the system will act as a self-service file storage system where City staff and members of the public can obtain documents such as agendas, minutes, resolutions, ordinances and contracts without staff assistance. In our opinion, the new system should also incorporate the recommendations stated below.

**Recommendation #14: We recommend that the Finance Department, in consultation with the City Attorney's Office, develop a more clear definition and list of what services would fall under the consultant services category.**

**Recommendation #15: Once a new electronic data management system is available, we recommend the City Clerk prepare and annually post a listing of payments to consultants over the previous year, including: (a) the consultant's name, (b) the general nature of the work performed, (c) the type of procurement process used, (d) the department, and (e) the amount paid.**

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# Conclusion

For purposes of this audit, we used a risk-based approach to select five consulting agreements for review. Our review of those agreements and resulting conversations with City staff indicated improvements are needed to ensure appropriate procurement, monitoring, and transparency of consulting agreements.

## RECOMMENDATIONS

Recommendation #1: To foster open competition for City contracts, we recommend that the City Manager's Office:

- a) Require unique services justifications to describe the department's effort to reach out to other potential vendors;
- b) Limit amendments to original agreements for non-competitively procured contracts if there is a substantial change in scope;
- c) Limit the number of years that such contracts can be amended or continued (including contract continuation agreements, options to renew and any other instrument that would substantively modify the original agreement);
- d) File approved unique services justification memoranda with the City Clerk's office; and
- e) Periodically report all non-competitively procured consulting contracts, perhaps in the City Manager's publicly available quarterly contract report.

Recommendation #2: To ensure compliance with City Council approval authority, we recommend that the SJPD either (a) terminate its unapproved contract with Corona Solutions and/or (b) receive approval from City Council for monies already spent.

Recommendation #3: At the same time that it checks the CHAD database prior to authorizing an encumbrance and/or payment, the Finance department should check the agreement's not-to-exceed amount in CHAD.

Recommendation #4: We recommend the Administration improve enforcement of existing Municipal Code contracting requirements by:

- a) limiting retroactive contracts to situations where contract execution is in process and the contract has been competitively procured,
- b) including this information on the contract transmittal form, and
- c) periodically reporting on all retroactive consulting agreements regardless of the value or procurement method of the agreement, perhaps in the City Manager's publicly available quarterly contract report.

## Consulting Agreements

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Recommendation #5: The City Manager's Office should revisit the role of the Finance Department with respect to consultant procurements, evaluating whether its current level of involvement and resources is adequate.

Recommendation #6: The City should implement the "certified contract specialist" program, and/or provide regular procurement training to staff.

Recommendation #7: To lessen the burden on City staff while fostering improved competition in consultant procurements, the Finance Department should include in its annual procurement training simplified procurement processes for smaller consulting contract procurements while encouraging full and open competition, and define when these simplified processes can be used.

Recommendation #8: We recommend that the City

- a) Reconcile overpayments as described above and get reimbursed for these overpayments,
- b) Document any changes in consulting contract terms or requirements through a formal contract amendment, and enforce existing contract terms. If the contract allows for changes in terms without amendments, such changes should be documented in writing, and
- c) Require contract managers to reconcile previously received deliverables to contract payments during the contract amendment process, prior to increasing contract amounts.

Recommendation #9: We recommend the Administration develop Citywide policies and procedures on contract monitoring and management including:

- a standardized contract management process,
- organization of contract files,
- checklists for tracking agreed-upon deliverables and line item budgets,
- components of invoice review which link payments to contract deliverables, and
- documenting deliverables prior to payment.

We further recommend that the City require contract administrators to annually certify they have reviewed and understand those policies and procedures.

Recommendation #10: For inter-departmental contracts, we recommend the Administration require staff to designate a responsible staff member who would be accountable for all aspects of contract monitoring, including invoice approval and review.

Recommendation #11: We recommend the Administration ensure that:

- a) Staff managing contracts conform with current City contract retention policies and, consistent with those policies, keep all documents related to contract procurement,

compliance and monitoring, including all documents related to contract renewals, amendments, continuation agreements, and other contract modifications; and

- b) Require staff to include a notation regarding the City's retention policies in each individual contract file.

Recommendation #12: We recommend that:

- a) The City Clerk in consultation with the City Attorney's office provide training to City staff on Form 700 filing requirements for consultants, follow-up on missing Form 700s for current agreements, and penalize consultants who do not comply, and
- b) The City Clerk, prior to providing Status II payment authorization, require Form 700s from those consultants whose contracts require them.

Recommendation #13: We recommend that the City Administration include the City's Conflict of Interest and Ethics policies in its annual procurement and contract monitoring training.

Recommendation #14: We recommend that the Finance Department, in consultation with the City Attorney's Office, develop a more clear definition and list of what services would fall under the consultant services category.

Recommendation #15: Once a new electronic data management system is available, we recommend the City Clerk prepare and annually post a listing of payments to consultants over the previous year, including: (a) the consultant's name, (b) the general nature of the work performed, (c) the type of procurement process used, (d) the department, and (e) the amount paid.

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# Memorandum

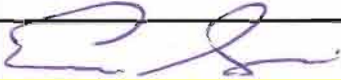
**TO:** SHARON WINSLOW ERICKSON  
CITY AUDITOR

**FROM:** Norberto Dueñas

**SUBJECT:** SEE BELOW

**DATE:** June 12, 2013

Approved:



Date

6/12/13

**SUBJECT: ADMINISTRATION'S RESPONSE TO "CONSULTING AGREEMENTS: BETTER ENFORCEMENT OF PROCUREMENT RULES, MONITORING, AND TRANSPARENCY IS NEEDED"**

The Administration has reviewed the City Auditor's final draft report "*Consulting Agreements: Better Enforcement of Procurement Rules, Monitoring, and Transparency is Needed*" and agrees with many of its findings and recommendations. The Administration values the City Auditor's examination of this issue and her recommendations for improving City procurement and contract management practices.

The Administration also has identified specific audit findings where additional analysis is needed to better evaluate implementation options and recommendations. Further analysis will focus on operating efficiencies, service delivery tradeoffs, and potential customer impacts, particularly where the audit has identified reduced staffing levels and resources.

The City organization prides itself on innovation, efficiency, transparency and effective service delivery to our businesses and residents while maintaining critical community services without disruption and performing other core activities of local government during a period of significant fiscal challenges. Over the past several years, staffing reductions have shifted resource allocation away from many desirable priorities, including Citywide training and support for consultant procurement and contract management. The audit and its findings should be considered in this context.

In light of the audit recommendations, the Administration will identify and implement changes in our processes and procedures for procuring and managing consulting agreements. In particular, these issues will be addressed in a revised administrative policy to enhance clarity and improve guidelines to departments and contract managers. In addition, the Finance Department and City Clerk's Office have begun reviewing processes and procedures that can be streamlined, and will add resource materials on the City's intranet, and reinitiate Citywide training on procurement and contract management.



## **RECOMMENDATIONS AND RESPONSE**

**Recommendation 1:** To foster open competition for City contracts, we recommend that the City Manager's Office:

- a) Require unique services justifications to describe the department's effort to reach out to other potential vendors;
- b) Limit amendments to original agreements for non-competitively procured contracts if there is a substantial change in scope;
- c) Limit the number of years that such contracts can be amended or continued (including contract continuation agreements, options to renew and any other instrument that would substantively modify the original agreement);
- d) File approved unique services justification memoranda with the City Clerk's Office; and
- e) Periodically report all non-competitively procured consulting contracts perhaps in the City Manager's publicly available quarterly contract report.

**Administration Response:** The Administration partially agrees with recommendations 1a through 1c.

1a-1c. Current City policy requires open competition. Although situations exist, justifying departments' selected process of outreach to potential vendors, the Municipal Code does allow exceptions to this policy ("unique services") for services where a business case can be made that following a competitive process is contrary to the public interest. The Administration has existing informal controls that ensure each justification for a unique service depends on specific facts and circumstances associated with that situation. Therefore, the Administration partially disagrees with the recommendations 1a through 1c. For example, it is not clear there would be benefit from reaching out to other potential vendors (Recommendation 1a) if the basis of the unique services justification is that no other vendors could perform the service. Additionally, there are some circumstances where a unique service can be justified even when other vendors might be capable of performing the work. The Administration can approve these on a case-by-case basis when this path is to be found necessary and critical for service delivery.

As an alternative, the Administration recommends that a unique service justification minimally include the following criteria: a) a maximum validity term, b) a maximum dollar value, and c) require the approval from the department director or purchasing officer approval. If any of these parameters are exceeded, then the original justification must be updated with reasons, and the director must approve the extension. The Administration will develop a policy that further clarifies and provides guidance to staff on these audit issues.

**Administration Response:** The Administration agrees with recommendations d and e.

1d. The Administration will ensure that the approved unique services justification memoranda are included in the documentation of the contract agreements, submitted for execution to the City

SHARON WINSLOW ERICKSON, CITY AUDITOR

June 12, 2013

**Subject: Consulting Agreements - Better Enforcement of Procurement Rules, Monitoring and Transparency is Needed**

Page 3 of 9

Clerk's Office, in order to be filed and uploaded with the agreements in the Council History and Documents (CHAD) internal database.

1e. The Finance Department will review the existing quarterly report to the City Council on executed agreements between \$100,000 and \$250,000 in value and coordinate with City departments to include reporting on the data pertaining to all non-competitively procured consulting contracts.

**Recommendation 2:** To ensure compliance with City Council approval authority, we recommend that the SJPD either (a) terminate its unapproved contract with Corona Solutions and/or (b) receive approval from City Council for monies already spent.

**Administration Response:** The Administration agrees with this recommendation. The San José Police Department staff will begin a Request for Proposal process for these professional services in order to achieve compliance. This process is expected to take approximately six to eight months since staff involved in this project is also heavily involved in the current implementation of the Automated Field Reporting/Records Management System implementation. Terminating the current agreement is not advisable given the valuable crime data staff receives from the system. As such, the Department will seek approval from City Council for work that has been performed and paid for by the City.

**Recommendation 3:** At the same time that it checks the CHAD database prior to authorizing an encumbrance and/or payment, the Finance Department should check the agreement's not-to-exceed amount in CHAD.

**Administration Response:** The Administration agrees with this recommendation. The Finance Department will coordinate and review the process of incorporating this procedure into existing processes and procedures in Accounts Payable.

**Recommendation 4:** We recommend the Administration improve enforcement of existing Municipal Code contracting requirements by:

- a) limiting retroactive contracts to situations where contract execution is in process and the contract has been competitively procured.
- b) including this information on the contract transmittal form, and
- c) periodically reporting on all retroactive consulting agreements regardless of the value of procurement method of agreement, perhaps in the City Manager's publicly available quarterly contract report.

**Administration Response:** The Administration agrees with the recommendations.

June 12, 2013

**Subject: Consulting Agreements - Better Enforcement of Procurement Rules, Monitoring and Transparency is Needed**

Page 4 of 9

4a. Staffing reductions over the years have led to some certain contracts being executed after the start of the contractor's work. The Administration agrees that this practice is less than ideal and will work diligently towards remedies. Additionally, the Administration will establish further guidelines that delineate when retroactive agreements may be acceptable, such as low risk versus high risk agreements. The Finance Department and the Workforce Training and Development Division in Human Resources will incorporate the guidelines into the development and implementation of a Citywide training on procurement and contract management for individuals responsible for contract management and compliance

4b. The Administration regularly reviews agreements before their execution and will incorporate additional guidelines into the contract transmittal form to ensure that department contract managers and liaisons have a better understanding of the limitations of the contract authority that is delegated to the City Manager and Council Appointees.

4c. The Finance Department will review the existing quarterly report model and determine the proper approach and guidelines to include reporting on the data pertaining to agreements. The Administration will also incorporate additional guidelines and update the contract transmittal form in order to include this information on the contract transmittal form.

**Recommendation 5:** The City Manager's Office should revisit the role of the Finance Department with respect to consultant procurements, evaluating whether its current level of involvement and resources is adequate.

**Administration Response:** The Administration agrees with this recommendation. The Finance Department will evaluate whether its current level of involvement and resources are adequate. The evaluation will include analysis of the costs associated with the Finance Department's more integrated role in procurements, mechanisms to enhance procurement throughout the City, and staff development. The resource assessment could include various levels of Finance Department assistance in the consultant procurement process.

**Recommendation 6:** The City should implement the "certified contract specialist" program, and/or provide regular procurement training to staff.

**Administration Response:** The Administration agrees with this recommendation. The Finance Department and the Workforce Training and Development Division in Human Resources will coordinate the development and implementation of a Citywide training on procurement and contract management for individuals responsible for contract management and compliance. Additionally, in mid- June, two new managers commence employment with the City in the

Finance Department, Purchasing Division, and recruitment is underway for two additional management positions. Filling these critical vacancies should provide sufficient capacity to re-examine and streamline procurement processes, update resource materials such as an online Request for Proposal (RFP) Guide, and re-initiate a training program. It will take six months to one year to complete hiring and training new staff, and we estimate these related work efforts can be started at least by June 2014.

In the past, departments were responsible for designating Certified Contracting Specialists (CCS) who were tasked with ensuring all City policies and procedures are observed when Request for Proposals (RFPs) are solicited, proposals evaluated and contracts awarded. Under this program, in order to be designated as a department CCS, an individual was nominated by the respective department director, attended a series of training sessions to learn the basics of purchasing and contract writing for consulting/professional services requirements. To ensure continued enhancement of procurement knowledge, skills, and abilities, CCSs were required to attend regularly scheduled meetings with the City's Chief Purchasing Officer or designee. It was the expectation that CCSs serve as a valuable resource for their respective department staff, as well as providing assurance that all contracting efforts were conducted appropriately, ethically, and in accordance with all applicable laws, guidelines, and regulations.

Over the past several years, turnover and re-assignments within the organization has diluted the CCS pool, and the Finance Department/Purchasing Division has not been able to maintain this program given significant staffing reductions, vacancies and turnover during the last several years. As noted above, it is anticipated that commencing in FY 2014-15, the Finance Department will be able to develop and re-establish a new training program for Department purchasing liaisons. Finance will coordinate with City departments and the City Clerk's Office to regularly keep an updated list of the staff designated as Department Purchasing Liaisons.

**Recommendation 7:** To lessen the burden on City staff while fostering improved competition in consultant procurements, the Finance Department should include in its annual procurement training simplified procurement processes for smaller consulting contract procurements while encouraging full and open competition, and define when these simplified processes can be used.

**Administration Response:** The Administration agrees with this recommendation. The response to Recommendation 6 provides an outline of the preliminary plan for the Finance Department to re-initiate training related to procurements and contract management. Coordination with the Workforce Training and Development Division in Human Resources will be important for pooling resources and communicating training opportunities in this area to City departments and employees.

**Recommendation 8:** We recommend that the City

- a) Reconcile overpayments as described above and get reimbursed for these overpayments,
- b) Document any changes in consulting contract terms or requirements through a formal contract amendment, and enforce existing contract terms. If the contract allows for changes in terms without amendments, such changes should be documented in writing, and
- c) Require contract managers to reconcile previously received deliverables to contract payments during the contract amendment process, prior to increasing contract amounts.

**Administration Response:** The Administration agrees with this recommendation. Specifically, the Environmental Services Department has already implemented procedures to document director-approved changes to scope of services and/or task budget, as allowed by agreement language. ESD has also implemented procedural changes to ensure that contract payments are tracked with contract deliverables, including associated budget limits assigned to tasks. Additionally, the commitment to develop and train contract managers will lead to overall continuous improvement.

**Recommendation 9:** We recommend the Administration develop Citywide policies and procedures on contract monitoring and management including:

- a standardized contract management process,
- organization of contract files,
- checklists for tracking agreed-upon deliverables and line item budgets,
- components of invoice review which link payments to contract deliverables, and
- documenting deliverables prior to payment.

We further recommend that the City require contract administrators to annually certify they have reviewed and understand those policies and procedures.

**Administration Response:** The Administration agrees with this recommendation. The Administration will assemble a team led by the Finance Department, City Attorney's Office, and other key departments to review the existing Contract Administration and Management Guidelines. Additionally, the Administration will incorporate additional analysis into the review of these guidelines and update the manual to address the audit suggestions and enhance Citywide policies and procedures on for contract monitoring and management.

**Recommendation 10:** For inter-departmental contracts, we recommend the Administration require staff to designate a responsible staff member who would be accountable for all aspects of contract monitoring, including invoice approval and review.

**Administration Response:** The Administration agrees with this recommendation. City departments will coordinate with the City Clerk's Office to record and track the contracting manager responsible for each agreement. Currently, the Administration collects this information through the Contract Transmittal Form (CTF). The Administration will include additional

guidelines/or notifications in the CTF to ensure that the contract person is the appropriate staff person responsible for monitoring the contract.

**Recommendation 11:** We recommend the Administration ensure that:

- (a) Staff managing contracts conform with current City contract retention policies and, consistent with those policies, keep all documents related to contract procurement, compliance and monitoring, including all documents related to contract renewals, amendments, continuation agreements, and other contract modifications; and
- (b) Require staff to include a notation regarding the City's retention policies in each individual contract file.

**Administration Response:** The Administration agrees with this recommendation. City departments will ensure staff managing City contracts are trained and informed of the existing Records retention schedules. Currently, the retention schedule for contracts, procurements and purchasing, calls for related records and documentation to be retained for four years. The record management and retention policy pertains to each of the documents noted in this recommendation. Technical advice and assistance is available to departments on record management topics (e.g. preservation of records, developing, updating, and using records retention schedules). The Administration will coordinate with the City departments to ensure that staff managing contracts utilize the technical assistance including the notation and retention of the policy in each individual contract file.

**Recommendation 12:** We recommend that:

- a) The City Clerk in consultation with the City Attorney's Office provide training to City staff on Form 700 filing requirements for consultants, follow up on missing Form 700s for current agreements, and penalize consultants who do not comply, and
- b) The City Clerk, prior to providing Status 11 payment authorization, require Form 700s from those consultants whose contracts require them.

**Administration Response:** The Administration agrees with this recommendation. Recognizing that the Form 700 compliance rate for consultants has been historically low, the City Clerk's Office has been working on improvement of the Form 700 process to improve compliance. In March 2013, the City received approval from the Fair Political Practices Commission to allow electronic filing of Form 700s without the need for a signed hard copy, which will allow the filers to store information and make annual filings simpler. Furthermore, the City Clerk's Office, in partnership with the City Manager's Office, has updated the contract transmittal form, and we have been working together to develop a contract training program for employees. We agree with the recommendation to work with staff to make sure the Form 700 is submitted at the same time the contract is submitted for approval.

**Recommendation 13:** We recommend that the City Administration include the City's Conflict of Interest and Ethics policies in its annual procurement and contract monitoring training.

**Administration Response:** The Administration agrees with this recommendation. The City's Conflict of Interest and Code of Ethics policies will be included in its annual procurement and contract monitoring training.

**Recommendation 14:** We recommend that the Finance Department, in consultation with the City Attorney's Office develop a more clear definition and list of what services would fall under the consultant services category.

**Administration Response:** The Administration agrees with this recommendation. However, it is not clear to the Administration why a distinction between consultant and other professional services is required. All agreements need to be managed effectively and require the same level of transparency and accountability. The Administration also recognizes that the list of consultant services may change over time and an ongoing consultation between the Finance Department and City Attorney's Office will occur as part of the review.

**Recommendation 15:** Once a new electronic data management system is available, we recommend the City Clerk prepare and annually post a listing of payments to consultants over the previous year, including: (a) the consultant's name, (b) the general nature of the work performed, (c) the type of procurement process used, (d) the department, and (e) the amount paid.

**Administration Response:** The Administration agrees with these recommendations. The Administration and the City Clerk's Office will ensure all of the data, including consultant's name, nature of work performed, procurement process, department and amount paid, is available once the new electronic data management system is operational. In the meantime, this data is submitted on the Contract Transmittal Forms and recorded upon the execution of each agreement. The City Clerk's Office reviews and verifies the executed contract for completeness and uploads the agreements and attached documents into the internal Council History and Documents (CHAD) database, which includes the Contract Transmittal Form details (e.g. consultant name, scope of work, procurement process, department contact, term and compensation.)

## **CONCLUSION**

The Audit has surfaced concerns and provides recommendations that speak to the need for revising and improving our practices with respect to better enforcement of procurement rules,

SHARON WINSLOW ERICKSON, CITY AUDITOR

June 12, 2013

**Subject: Consulting Agreements - Better Enforcement of Procurement Rules, Monitoring and Transparency is Needed**

Page 9 of 9

monitoring and transparency of consulting agreements. Responsive actions will be taken to thoroughly address the above recommendations over the coming months.

Budget reductions in prior years have negatively affected staffing and training related to contract management and procurement, with the unfortunate result that some of our current practices are not aligned with best practice. The Audit highlights the need for a comprehensive administrative policy that will provide the appropriate guidance to address these issues while also ensuring the City remains dedicated to providing innovative solutions, operational efficiency, and strong customer service.

In an effort to provide a road map and additional guidance to departments to the issues highlighted in this audit regarding the procurement and management of professional and consulting service agreements, the Administration will update the relevant administrative policy. The policy will outline the detailed procedures for management of contracts and include a checklist. In addition, the policy will establish guidelines and administrative procedures for managing contracts. The goal will be to improve the knowledge and skills of employees in this area.

The City Manager's Office would like to thank the City Auditor's Office for conducting this audit.



NORBERTO DUEÑAS  
Deputy City Manager

For more information, please contact Ernest Azevedo, Executive Analyst at (408) 535-8119