
PERFORMANCE AUDIT OF SELECTED CONTRACTS

Review of Selected Contracts Demonstrates
Continued Weaknesses in Contract Oversight
Which Underscores the Need for a
Strengthened Internal Control Environment

Office of the
City Auditor

City of San Diego



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THE CITY OF SAN DIEGO

April 21, 2016

Honorable Mayor, City Council, and Audit Committee Members
City of San Diego, California

Transmitted herewith is an audit report of the City of San Diego's Selected Contracts. This report was conducted in accordance with the City Auditor's Fiscal Year 2016 Audit Work Plan, and the report is presented in accordance with City Charter Section 39.2. The Results in Brief is presented on page 1. Audit Objectives, Scope, and Methodology are presented in Appendix B. Management's responses to our audit recommendations can be found after page 55 of the report.

We would like to thank staff from the Purchasing & Contract, Park & Recreation, and the Public Utilities departments for their assistance and cooperation during this audit. All of their valuable time and efforts spent on providing us information are greatly appreciated. The audit staff responsible for this audit report are Sunny McLernon, Kevin Christensen, and Kyle Elser.

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Results in Brief

The Purchasing & Contracting (P&C) department is responsible for administering the City of San Diego's (City) procurement and materials management. The City's management of contracts is decentralized, and contract administration tasks fall within either P&C, or the client department, depending on the contract and activity.

The Audit Committee asked us to review a selection of City contracts to identify potential impacts of contract oversight deficiencies or loss to the City due to the weaknesses identified in our 2015 audit of Citywide contract oversight. Based on our current review, we found administrative and oversight issues in the limited number of contracts we reviewed. Although the issues we identified in these specific contracts cannot be extrapolated to all contracts under City management, in our view, the issues identified merit additional City executive management attention.

We selected 50 contracts for preliminary review and assigned a risk score based on various factors. Using this risk score and discussions with staff, we selected the sample of six contracts for a comprehensive review. Based on our review, we found the following P&C contract oversight issues:

- Two contracts were not properly executed; three extensions were not completed before the contracts lapsed, and work was performed before the contract finalized in one contract we reviewed. To fully protect the City's interest, it is important that P&C fully and correctly executes all contracts, and extensions are complete and timely in order to ensure that contract terms remain enforceable.
- Purchase orders were not properly tied to existing contracts in two instances. It is more efficient to link the purchase order to an existing contract because it saves time for the department. Also, if purchase orders are not properly tied to a contract, it reduces the transparency of City spending.
- Invoices were paid without verification that contract pricing was charged. Verifying invoices against contracted price lists is essential to ensure that the City is being charged the correct amount by vendors.

In addition, we found the following department contract oversight issues:

- Maintenance Assessment District contract authorization procedures for extraordinary labor were not followed, or written pre-authorizations were not obtained for 76 percent of the invoices we reviewed. Proper authorization is needed for accountability controls and to ensure that public moneys are being spent appropriately and legally.
- In one contract we reviewed, we found that procurement methods may have deviated from established procurement requirements, including the use of using extraordinary labor to pay for goods that should have been purchased by the City under a contract. As a result, those purchases do not go through a competitive solicitation process to ensure the City receives the best value.
- The department approved and paid charges that were not set forth in the contracts including a 10-percent mark-up for certain goods in all three landscaping contracts. Additionally, in one contract, a 15-percent mark-up outside of contract provisions was approved and paid, which totaled more than \$14,600. These mark-ups resulted in vendor overpayments by the City.
- The department did not ensure receipt of available cash discount from vendor for early payments for one contract. The total available discounts not taken over the five years of the contract were estimated at \$19,000.
- For this same contract, the department lacked adequate inventory controls for goods purchased under contract. Inventory controls are essential to ensure city assets are safeguarded.

Many of the issues summarized above are similar to audit findings in prior Office of the City Auditor (OCA) audit and hotline reports over the past several years. Additionally, internal audits issued prior to the creation of OCA in 2008 describe issues similar to those listed above. City Administration officials noted past changes to the procurement and contracting functions, including the upgrade to the City's financial reporting system and updated process narratives and administrative regulations among many other improvements noted. However, contract administration and oversight have continued to face challenges.

The *Standards for Internal Controls in the Federal Government* (Green Book) model provides guidance on improving the kinds of insufficient internal controls described in this report. It indicates that in a strong internal control environment, management should establish organizational structure, delegate authority, and evaluate and hold individuals accountable for their internal control responsibilities. These control activities should be

implemented through detailed policies and procedures which must be communicated “down and across reporting lines.” Management should ensure ongoing periodic reviews of the internal control systems to determine effectiveness.

The ongoing nature of the contract administration deficiencies require that tone be set at the top of the organizational structure to ensure improvements are properly designed, deployed, and continually monitored to ensure effectiveness. In our view, City executive management should take a more active role in designing rules and procedures, overseeing implementation, and monitoring of City contracts to ensure effectiveness and accountability. We made ten recommendations to address the issues identified, and management agreed to implement all of them.

Background

The Purchasing & Contracting (P&C) Department is responsible for administering the City of San Diego's (City) procurement and materials management. The department's responsibilities include the administration of procurement standards including adherence to federal and state procurement law as applicable, and providing customer services and support to internal (City departments) and external (bidders and proposers) customers. Within P&C, the Living Wage and Equal Benefits Program administers the Living Wage Ordinance and the Equal Benefits Ordinance.

As noted in our 2015 Contract Oversight performance audit,¹ in fiscal year 2014 the City managed a minimum of 674 active contracts through the Public Works and P&C departments. The Public Works' Field Division provided contract administration to 177 contracts through the City's Capital Improvements Program (CIP), while City departments administered 497 goods, services, and consultant contracts.

Decentralized Contract Management Responsibilities

City's management of contracts is decentralized. Contract administration involves management of work performed and monitoring quality and quantity of goods, contract close-out and modification, and evaluating the contractor or vendor performance. These are responsibilities that fall within either P&C or the client department, depending on the contract and activity. However, as noted in our 2015 audit, the City does not have standardized contract administration and monitoring processes to ensure compliance with contractual terms for services and goods receipt. For instance, the audit found that 44 percent of contract administrators that responded to a survey, indicated that they had not been provided clear guidance on their roles or responsibilities as the administrator, and only 23 percent reported using a contract monitoring plan.

P&C manages the awarding of contracts for professional and general services that are necessary to support the City's operational and administrative functions. The San Diego Municipal Code (SDMC) generally requires that all contracts be awarded based on best overall value to the City, which can include factors such as quality and cost.² Once contracts are

¹ Performance Audit of Citywide Contract Oversight, *The City Should Strengthen and Standardize the Contract Administration Process to Ensure Contractual Commitments Are Properly Monitored and All Payments Meet Contractual Obligations*, Office of the City Auditor, City of San Diego, April 2015.

² San Diego Municipal Code 22.3203 requires that contracts for amounts between \$25,000 and less than \$50,000 may be awarded based on quotes obtained either orally, or in writing. Contract amounts for more than \$50,000, but equal or less than \$150,000 may be awarded based on the lowest written quote from at least five sources.

awarded, the City client departments are responsible for vendor or consultant oversight. P&C is responsible for initiating the contract extension options, as well as managing the rebid of expiring contracts.

**P&C Initiatives
Intended to Improve
Contract
Administration and
Oversight**

As previously noted, our 2015 audit indicated that the contract administration and oversight processes were not standardized and had weakness such as lack of training, guidance, and internal standards for contract administrators. Generally, the audit findings concluded that:

1. The City does not provide sufficiently accurate and reliable contract award data with supporting documentation through its Citywide financial system, SAP, even though these capabilities and controls exist in SAP;
2. The City's contract modification and closeout processes require improvement; and
3. Although the SDMC allows for the debarment of poorly performing vendors, the City has not defined and developed a debarment process.³

The audit outlined nine recommendations, all intended to standardize and improve Citywide contract oversight operations. Management agreed to all nine of the recommendations. As of the last official reporting period, December 31, 2015, all recommendations are in the process of being implemented.

Prior to that audit report, we released an interim report in January 2015⁴ which found that City contracts, especially Citywide contracts, were not being adequately monitored, and in some cases had no contract administrator. Our department made two recommendations, which as of December 31, 2015, were still in progress.

In response to the audit reports and departmental staffing changes, P&C is currently developing, and in some cases, finalizing improvements to the procurement process and contractor oversight. P&C reports that the

These types of contracts are executed through a purchase order. Contract awards of \$150,000 or more must be awarded through advertised and sealed bids process.

³ In April 2015, the Office of the City Attorney informed the Office of the City Auditor that they are working with the Mayor's Office to update the debarment ordinance. In April 2016, the Office of the City Attorney indicated that the updated ordinance is expected to go to the City Council in the next several months. In addition, it reported that the Purchasing Agent is developing an Administrative Regulation to guide staff through the debarment process.

⁴ Interim report from Eduardo Luna, City Auditor, to Dennis Gakunga, Director of Purchasing & Contracting Department, "The City Needs to Address the Lack of Contract Administration and Monitoring on Citywide Goods and Services Contracts."

department has begun an improvement plan for the contracting process which includes a business process tracking plan to focus on business operations and day-to-day functions, as well as a plan to identify and focus on system strengths that can be enhanced and improved.

Currently, the P&C improvement plan focuses on key areas including master data, contract compliance, requisition sourcing options, and purchase order transmission options. According to P&C, the improvements being completed during the first phase are intended to establish a more comprehensive framework for contract administration.

**Contract Selection
Methodology
Summary**

This audit was requested by the Audit Committee (Committee) after the April 2015 audit report was presented to the Committee. The Committee asked the Office of the City Auditor (OCA) to review a selection of contracts to identify impacts of contract oversight deficiencies or loss to the City due to lack of oversight. Using a risk-based evaluation methodology, we selected six contracts to comprehensively review. This review included review and analysis of the masterfile at P&C; the accounts payable file maintained by the user department; the bid or outline agreement listing expected deliverables and requirements; the signed contract; invoice payments and other supporting documents stored in SAP and maintained by the contract end users; and interviews with department end users and those tasked with oversight, including contract administrators and their supervisors.

To select our sample we used P&C's self-reported "Goods and Services Contracts" list that is published on the department's City website. At the time of our audit fieldwork, this dataset contained more than 1,700 purchase orders for 842 different vendors or contractors. After extracting the data, we excluded all leases, revenue generating contracts, and Capital Improvements Projects (CIP) contracts from our sample selection.⁵

To select the contracts for review, we identified the five departments that had the highest count of contracts for goods, services or consultant services. Of the remaining agreements within these departments, we selected 50 contracts for preliminary review, based on several risk factors. Based on this preliminary review, we assigned a risk score based on certain components of the contracts such as masterfile completeness, information in SAP, and evidence of P&C and City Attorney review. Using this risk score, and through discussions with management and identification of recurring issues in the

⁵ Leases and other revenue generating contracts are subject to different laws and rules than contracts required to go to the lowest reasonable bidder.

contract population, we selected the sample of six contracts from two different departments for an in-depth review.⁶

The results of the reviews of the six contracts are summarized in aggregate in the body of this report. Additionally, issues identified during the preliminary review of a sample of 50 contracts are discussed throughout the report. **Appendix C** provides summary analyses of the contracts we reviewed narratives that provide specific areas of deficiency or concern for each contract.

⁶ To provide context of work performed, OCA reviewed approximately \$2,000,000 worth of invoices during this audit.

Audit Results

Finding #1 Review of Selected Contracts Demonstrates Continued Inconsistencies with Contract Administration, Adherence to Contract Provisions, and City Procurement Requirements, Which Underscores the Need for a Strengthened Internal Control Environment

As reported in our previous audits, over the years the City of San Diego (City) has faced many challenges in managing and overseeing government contracts with private parties. These challenges include a decentralized oversight structure which requires a need for strong and uniformly implemented internal controls over contract management. As a result of our previous work, the Audit Committee asked us to review a selection of contracts to identify potential impacts of contract oversight deficiencies, as well as any financial loss to the City due to the weaknesses identified in the 2015 audit. Based on our review of contract language and applicable City laws, regulations, and policies, we found administrative and oversight issues in the limited number of contracts we reviewed.⁷ Although the issues we identified in these specific contracts cannot be extrapolated to all contracts under City management, in our view, the issues merit additional City executive management attention. Specifically, we found:

P&C Contract Oversight Issues:

- Contracts were not properly executed in two of the six contracts we reviewed; extensions were not completed before the contracts lapsed in three of the six; and work was performed before the contract finalized in one contract we preliminarily reviewed;
- Purchase orders were not properly tied to existing contracts in two instances; and

⁷ The Office of the City Auditor reviewed a total of six contracts during our fieldwork. We selected these six contracts using a risk based examination of the masterfiles of 50 contracts maintained by P&C. The examination of the masterfile was a preliminary desk review designed to review for red flags such as lack of proper signatures, or missing documentation. Although only six contracts were in our sample, in some cases we have also included details of some of the fifty contracts in the cursory review to support that our findings were not isolated events. For more details about our scope of work, see the Objectives, Scope and Methodology in Appendix B.

- Invoices were paid without verification that contract pricing was charged in all three cases in which we spoke to the person responsible for okaying invoices for payment (specific to goods contracts only).

Department Contract Oversight Issues:

- Of the invoices we looked at related to the Maintenance Assessment District (MAD) contracts, authorization procedures for extraordinary labor were not always followed, or written pre-authorizations were not obtained at all for approximately 76 percent of the invoices we reviewed;
- In one contract we reviewed, we found that procurement methods may have deviated from established procurement requirements, including using extraordinary labor to pay for goods that should have been purchased by the City under a contract;
- Department-approved and paid charges that were not set forth in the contracts. These charges included 10-percent mark-ups for certain goods in all three landscaping contracts we reviewed, and approval and payment of a 15-percent mark-up outside of contract provisions was identified in one contract;
- In one contract that we reviewed, the department did not ensure receipt of available cash discount from vendor for early payments; and
- For this same contract, the department lacked adequate inventory controls for goods purchased under contract.

Many of the issues summarized above are similar to audit findings in several prior Office of the City Auditor (OCA) audit and hotline reports over the past several years and identified in the 2015 audits, as described above. Additionally, internal audits issued prior to the creation of OCA in 2008 describe issues similar to those listed above. For example, many of the issues reported on in this report were also identified in two reports by the Audit Division of the Comptroller's Office in 2004.⁸ The issues include, but are not limited to, problems with invoicing, extraordinary labor charges, and adherence to various procurement rules. Summaries of previous related, key audit findings are provided in **Appendix D**.

During this period, the City Administration officials noted past changes to the procurement and contracting functions, including addressing audit recommendations. For instance, according to an Independent Budget

⁸ June 15, 2004 Audit Report from the Audit Division of the City Comptroller to the then General Services-Central Stores and Print Shop; and June 16, 2004 Audit Report from the Audit Division of the City Comptroller on City-wide Procurement.

Analyst report, in 2009, the City fully implemented the materials management/inventory modules of SAP in accordance with the process design developed by P&C. P&C has also clarified San Diego Municipal Codes (SDMC); updated process narratives and administrative regulations related to purchasing or contracting; standardized forms and created checklists for staff to help ensure processes are followed; provided training and reference materials via the City's intranet; and updated department instructions. However, as noted in the paragraph above, contract administration and oversight have continued to face challenges.

Numerous factors contributed to the ongoing contracting oversight deficiencies. Predominantly, in our opinion, these factors include:

- Decentralized contracting responsibilities;
- Insufficient policies and training for contract administration;
- Lack of coordination of contract oversight between the client departments and P&C;
- The absence of consistent monitoring programs to ensure accountability.

Moreover, in our opinion, these problems have persisted due to a continued long-term absence of leadership in procurement practices caused, in part, by the overarching financial and political strains facing the City, coupled with the frequent turnover of operational and executive leadership. Taking into account the decentralized nature of the procurement and contract administration function, the City's executive leadership is positioned to design, implement, and enforce stronger and more uniform control frameworks across all City departments with contract administration and oversight responsibilities.

The long-standing nature of the issues identified in this audit and in other audits demonstrate the need for the City to develop a stronger internal control framework to improve contract administration and oversight. Specifically, executive management should take a more active role in designing rules and procedures, overseeing implementation, and monitoring to ensure effectiveness and accountability. We make both specific and general recommendations throughout this report to address the issues outlined above.

Previous Audits Prompted Audit Committee's Request for This Review

As a result of our previous audit work on contract monitoring, the Audit Committee asked us to review a selection of contracts to identify impacts of contract oversight deficiency or loss to the City due to lack of oversight. At the onset of our field work, we selected 50 contracts for preliminary review

based on several risk factors.⁹ We prepared contract review criteria checklists to identify potential risks in procurement and administration activities for each contract and assigned a risk score based on information gathered from the masterfile maintained by P&C. Using this risk score and through discussion with departmental staff and identification of reoccurring issues in the contract population, we selected the sample of six contracts from two different departments for a comprehensive review. The results of the reviews of the six contracts and problem areas identified are summarized in **Exhibit 1** and in the body of this report. See **Appendix C** for specific details related to each contract we reviewed.

⁹ A comprehensive Objective, Scope, and Methodology section is presented in Appendix B.

Exhibit 1

Areas of Concern for Contracts Reviewed

Description of Issues	Full Review						Preliminary Review		
	Imperial Sprinkler	Landscapes USA	Shoreline	Cass Plumbing	Bob Crane	Aztec Landscaping	El Dorado Coating	Lopez Concrete	Specialty Seals
Contract not properly executed (lack of signatures)			✓	✓					
Contract lapsed before renewed		✓	✓			✓			
Work performed prior to contract execution								✓	
Purchase orders not properly tied to contracts					✓		✓		
Pricing not verified when invoice paid	✓							✓	✓
Problems with extraordinarily labor authorizations		✓	✓						
Procurement methods potentially not followed as required by SDMC		✓							
Questionable mark ups, or other questionable charges		✓	✓			✓			
Department not ensuring that it receives full available cash discount	✓								
Inventory controls not adequate	✓								

Source: OCA, based on information from P&C masterfiles, department accounts payable files, and other information gathered during the audit process.

P&C Contract Oversight Issues During our audit of selected contracts, we identified issues related to P&C’s oversight of contract administration. Specifically, we found instances in which contracts were not properly executed, were not renewed in a timely manner, and instances in which work was performed before the contract

was finalized. We also found multiple instances in which purchase orders were not properly linked to contracts. Additionally, we found that for goods contracts, the responsibility for ensuring that the contracted price is billed to the City is not clearly assigned. These issues are discussed in more detail in the sections below.

Contracts Not Always Properly Executed

During our review, we found contracts that were not properly executed. For instance, we found at least two agreements without signature by the Office of the City Attorney—a requirement of the City Charter.¹⁰ Improperly executed contracts are not valid under the law and may be unenforceable or put the City at risk of liability. Additionally, signatures are required to ensure that the contracting parties have reviewed and approved all contract terms. In one instance, a contract was not signed by the P&C Director for three years, and not signed by the Office of the City Attorney at all. During this period, more than \$118,500 was charged and paid to the vendor.

The City Charter and the San Diego Municipal Code (SDMC) set forth certain contracting requirements, including provisions for the proper execution of City contracts. The City Charter requires that the Mayor executes contracts, but allows the delegation of this authority. A 2015 memorandum from the Office of the City Attorney states that City contracts typically become effective once they have been executed (signed) by the parties and approved by the City Attorney.¹¹ The memorandum further states that when a charter provides for a certain method of approving a contract, failure to follow that method will render the contract void or unenforceable. The City Attorney's memorandum cited as an example a case in which failure to obtain signatures required by the City of Los Angeles' charter rendered "an alleged City contract unenforceable." In addition, the Charter requires the signature of the Office of the City Attorney's in order to properly execute a City contract, and therefore, the City Attorney's signature is also necessary to the formation of a valid contract.

Contracts Lapsed Before Renewal

Additionally, we found three contracts that were allowed to lapse, then renewed through the extension option as if the contract had never expired. For instance, one open space landscape contract we reviewed was initially executed on September 25, 2012, when it was signed by the Office of the City Attorney. This contract was for a period of one year and included options to renew for up to four one-year periods, for a total duration of up to five years. The contract specified that any renewals were contingent on a mutual agreement between the City and the contractor to be confirmed 60 days prior to the expiration of the contract period. Furthermore, the

¹⁰ San Diego City Charter sec. 40.

¹¹ If the contract stipulates an effective date, it would become effective on that date.

contract language stated that, “[t]he City’s initial letter offering the contractor an opportunity to renew the contract does not constitute an award of the option period. Any option acceptance must be confirmed by the City, in writing, before it becomes valid.”

We reviewed the masterfile for this contract and found that there was no first extension option letter nor other evidence of extension in the file. Additionally, we requested that the procurement agents and the contract administrator provide evidence of the documented contract extension, which they were unable to locate and provide. Daily services and monthly payment continued during this period as if the extension was in place during this second year of service with the landscape contractor. The masterfile did, however, contain extension options for what would have been a second-year extension, as if the contract had never lapsed. In addition, we found three other contracts with vendor charges totaling more than \$1 million that were paid by the City while there was no properly executed contract in place. A summary of the charges is shown in **Exhibit 2**.

Exhibit 2

Summary of Charges Paid to Vendors Without a Properly Executed Contract

Vendor Description	Amount Invoiced Without Contract
Landscaping Vendor	\$368,770
Landscaping Vendor	\$291,088
Landscaping Vendor	\$232,070
Plumbing Vendor	\$118,521
Total	\$1,010,449

Source: OCA, based on contracts reviewed in our contract sample.

We inquired with the Director of P&C about the potential causes of the identified lapses in contract extensions. The Director indicated that the cause could be staff training deficiencies, such as procurement agents’ inability to run proper reports that would show which of their assigned contracts have expired or will soon expire. Additionally, P&C staff reported that during the period of 2013, the department was short-staffed and the heavy transactional workload may have affected its ability to keep up with contract renewal workload.

Contract Not Fully Executed Before Work Began

In addition to contract extension lapses, we identified a contract that appeared to have a delay in its timely execution. In one instance there was a contract for concrete services, and the initial award letter was dated

November 27, 2013—which was 26 days after the effective date of the contract. Additionally, while reviewing invoices that had been paid through this contract, we identified at least three invoices that showed that the work was performed in October and November 2013—either before the effective date or before the award letter. These invoices were approved by staff in the Public Utilities Department and paid by the Office of the City Comptroller. To fully protect the City’s interest, it is important that P&C prioritizes ensuring that contracts are fully and correctly executed, and that extensions are complete and timely in order to make sure that contract terms remain enforceable.

**Purchase Orders Not
Correctly Linked to
Contracts**

During our review of selected contracts, we found instances in which new purchase orders were generated but were not tied to existing contracts, even though the purchase order was for the contracted services with the same vendor.¹² Creating purchase orders that are not linked to a contract is a lengthier and more resource-intensive process compared to using an existing contract to create a purchase order.

Purchase orders allow departments to purchase goods and services from outside the City and then authorize payment to the vendor or service provider through the Office of the City Comptroller. All purchase orders begin with a purchase requisition, which establishes the request and justification for a purchase. The purchase requisition must be approved by the department head, or designee of the requesting department. According to P&C if a contract for the good or service already exists within the City and is identified during purchase requisition development process, the requisition approval does not take as long, and less verification and document request must be made in the creation of a purchase order. However, if no contract already exists for the good or service being sought, then the purchase requisition must go through several potential approvals such as Labor Relations, the Living Wage Program, verification of business and tax certificates, review by the City Attorney’s Office if applicable, and depending on the good or service, may be subject to other reviews. Therefore, it is more efficient to, when possible, link the purchase order to an existing contract when creating a purchase order for a good or services. This saves time for the department in need of the purchase, and saves labor hours for multiple departments. A major exception to this process is the procurement of goods (not services) in the amount of less than \$25,000. In

¹² We also identified this issue in our January 2015 management memorandum to the Purchasing and Contracting Director. Memo. from Eduardo Luna, City Auditor, to Dennis Gakunga, Director, Purchasing and Contracting, *The City Needs to Address the Lack of Contract Administration and Monitoring on Citywide Goods and Services Contracts*, (Jan. 16, 2015)

these instances, a department can auto-generate a purchase order, without the routing of the purchase requisition to the other departments for review and approval.¹³

As mentioned above, creating a new purchase order without a contract is a lengthier and more staff resource-intensive process than using an existing contract to create a purchase order. But, as we found, not having purchase orders properly linked to contracts can also result in a lack of transparency over City expenditures on services and commodity groups. For instance, if a contract has a “not to exceed amount” and purchase orders are issued to that same vendor for same services or goods, yet not linked to the contract, there is risk of surpassing the do-not-exceed contract amount by charging to the purchase orders. Additionally, if purchase orders are coded as the wrong material group, the City will not have accurate data when trying to ascertain how much it spent on certain materials.

Specifically, we found instances in which purchase orders were created for a crane services vendor, even though an existing contract for those same services with that same vendor already existed—yet the purchase order was not linked to the existing contract. In this case, the client department, Public Utilities Department (PUD), miscoded the purchase requisition as an HVAC material group, rather than a crane services purchase. This error—miscoding the purchase requisition as an HVAC purchase request—may have been the reason that neither the PUD analyst creating the request, nor the P&C purchasing agent identified and used the existing crane contract that was already in place. Had either the PUD analyst or the P&C staff identified this existing contract, a purchase order could have been created and linked to that contract immediately and without additional review and approval by other departments.

Moreover, we found more than 15 additional purchase orders with invoices totaling approximately \$47,000 that were issued for this same crane vendor that were also not linked to the established contract. Additionally, during the primary review stage of this audit, we performed a cursory review of metal coating contract. During our review, we identified at least three purchase orders that should have been linked to this contract, but were not. The responsibility to identify contracts that meet the purchasing need resides with the department that is requesting the purchase. However, when the purchase request is finally approved and changed into a purchase order by P&C, P&C staff have a responsibility to ensure that the procurement information is accurate, which includes identifying existing contracts that would meet the purchase requestor’s needs.

¹³ P&C indicated it is ending the auto-generate purchase orders later this year (2016).

After the April audit was released City management informed us they began the process creating classifications within the P&C Department to perform direct contract administration, monitoring, as well as provide expert advice and training as the contract liaison with all city department staff in contract monitoring. City management informed us in February 2016 the City's Civil Service Commission approved the new classification series. The new Procurement Contracting Officer classifications will have increased responsibilities for ensuring that purchase requisitions are properly assigned, according to the P&C Director.

Further, in December 2015, P&C, in cooperation with the Department of Information Technology, made changes and simplifications to the requisition creation process. Specifically, changes were made to how material groups are coded and assigned in SAP, so that in the process of creating a purchase requisition, SAP will more easily enable client department staff to identify the correct vendors and materials codes. According to the P&C Director, this change will help ensure that purchase requisitions identify contracts already in place during the purchase order creation process.

**Invoices Paid without
Verification of
Contract Pricing**

During our review of selected contracts, we found that staff signing invoice approvals did not always check the price lists to ensure that the contracted pricing was accurately charged. Further, we found that in at least one case, the price list was not available to contract end-users for goods contracts to be reviewed. Verifying invoices against contracted price lists is essential to ensure that the City is being accurately charged.

Goods contracts are generally through a competitive solicitation process to the lowest responsible and reliable bidder. All competing vendors submit their bid which indicates the discount percent they will give off of manufacture's list price (MLP). Vendors are also supposed to provide to P&C the MLP as part of their bid. This MLP is then filed in the contract's masterfile.

The outline agreement, or contract, that is generated in SAP when the contract is awarded does not provide a line item price list for each type of product under the contract but instead provides an estimated total spend by line item. For example, if a winning bid states that it will give 50 percent off MLP for a certain sprinkler head, the SAP contract only indicates that the City estimates to spend a total of \$50,000 for those irrigation heads during the contract period. The agreement in SAP references the percent discount, but no item price is provided. When we spoke to the contract administrators of the goods contracts that we reviewed, they reported that they did not, as a matter of routine, check invoices to ensure that the contracted discount

was invoiced. At least one of the contract end users that we interviewed stated that they did not have access to the MLP, as it was stored in the masterfile at P&C.

As noted before, the MLP is kept in the P&C masterfile. Additionally, several of the contract administrators that we spoke with during our review of contracts indicated they did not typically ensure that contract pricing was billed. In their view, their duty was to ensure that goods were received and that invoiced quantities were correct. During our comprehensive review of one sprinkler parts contract, P&C, the client department contract administrator, and the vendor were all unable to locate and provide us with the MLP. As a result, we were unable to match the actual invoices price to the MLP to verify contract pricing.

City policies do not clearly dictate who is responsible for reviewing invoice pricing to ensure it is correct. The current City process narrative states that the department invoice administrator shall verify invoice information. However, the staff we spoke to construed this to mean that they verify that goods were received and were in good condition. P&C stated that it was the contract administrator's duty to ensure that contracted pricing is received. However, the contract administrators that we spoke to were unaware of this expectation. When price lists are not available to contract end users, or when the responsibility to ensure contract pricing is not assigned, the City runs the risk of being mischarged and introduces a potential risk of waste, fraud, and abuse.

We discussed the issues of price lists not consistently being checked with the P&C Director. The Director stated that it was the contract administrator's job to ensure correct contract pricing. However, P&C intends on implementing new catalog software in June 2017 that would ensure that contracted pricing is billed and paid for goods and services under contract. According to the P&C Director, this software would require that the vendor that is awarded the contract provide to P&C an Excel price sheet for all goods. This price sheet would be uploaded into the ordering software, and would automatically associate the price with the good, which would help mitigate the risk that the wrong price or wrong discount is billed. Further, the Director intends to create a contract compliance unit within P&C in the future. This unit, among other things, would be responsible for periodic monitoring to ensure that contracted price is billed to the City. In addition to these changes, P&C also reported that the department is in the process of creating an all-digital procurement manual for City staff. The creation of a manual provides P&C with an opportunity to offer additional clarity and guidance to all City staff involved in procurement. It is also a mechanism

that would allow P&C to address each of the recurring issues that have been discussed in this section of the report.

Recommendation #1 P&C should ensure that its new purchase requisition procedures and the forthcoming digital procurement manual include a requirement for review by senior procurement specialist to try to reduce errors in purchase requisitions and purchase orders. An emphasis on ensuring that existing contracts are identified when appropriate should be included in the procedures.

Additionally, P&C should develop a monitoring program that periodically reviews, or spot checks, new purchase orders that have been created and were not tied to contracts. This monitoring process should review all purchasing information and vendor assignment to ensure that there was not a contract available for the goods or services. If errors are identified during the monitoring, staff at the client department and P&C should be further trained to help eliminate such errors. (Priority 3)

Recommendation #2 P&C should continue its efforts to obtain and expedite implementation of the catalog software to, among other things, address lapses in contract pricing review of when invoices are processed. P&C should develop a clearly defined and documented plan for training P&C and client department staff as part of the implementation process. (Priority 3)

Recommendation #3 The Office of the City Comptroller should modify its process narrative for invoice payments to clearly assign the responsibility to ensure contract pricing is billed. (Priority 3)

Department Contract Oversight Issues While reviewing specific contracts, we found several issues related to the end-user departments' contract oversight. Specifically, we found that approval procedures for extraordinary labor were not consistently followed. We also found instances in which the procurement rules for the purchase of goods may not have adhered to SDMC requirements. Further, we identified instances in which questionable mark-up charges were approved and paid for by the City. We found one instance in which the department did not ensure that early payment discounts offered by the vendor were received. Finally, we also identified inventory controls that should be strengthened to ensure that goods purchased from City contracts are tracked and accounted for. These findings are discussed in more detail below.

Authorizations for Extraordinary Labor Charges and Invoicing We reviewed three landscape maintenance contracts that were administered by programs within the Park and Recreation Department (P&R). In each of the contracts, we found problems regarding adherence to

contractually-defined elements relating to extraordinary labor provisions. Specifically, we found problems relating to authorizations and approvals and certain mark-ups related to extraordinary labor. A description of the extraordinary labor provisions and processes is provided below, as well as discussion of the related problems.

*Overview of
Extraordinary Labor
Provisions and
Processes*

The contracts we reviewed were competitively bid and were for many types of landscape maintenance services to be performed on a weekly, biweekly, monthly, or quarterly schedule. In addition to scheduled maintenance, each contract had provisions for work termed as extraordinary labor at an hourly rate. The contract terms generally described extraordinary labor as non-routine maintenance such as repairs due to vandalism or graffiti, or replacement of plants or other landscape due to vehicle damage. Terms of the contracts defined that extraordinary labor should be authorized by the contract administrator in writing and that written authorization shall be attached to any invoiced extraordinary labor. Some landscape maintenance contracts that we reviewed did not always adhere to extraordinary labor authorizations, which exposes the City to risk, and does not comply with contract terms.

The landscape contracts we reviewed were for landscaping maintenance work in two types of defined areas. One contract we reviewed was for landscape maintenance in City open space, which are City land areas generally free from development, or development that use the natural environment. The other two landscape maintenance contracts were for Maintenance Assessment Districts (MADs). MADs are areas in which the property owners have voted to assess themselves to pay, and to receive services above and beyond what the City of San Diego normally provides. P&R oversees 55 MADs throughout the City. Within these MADs, P&R oversaw at 33 landscape maintenance contracts in the fiscal year 2014. Although our sample of contracts included only two MADs, it is likely that the issues we describe below would be consistent across MADs with similar landscape contracts, based on our discussions with P&R management regarding the department's general MAD administrative and operations.

The contracts for both the open spaces and the MADs generally specify that maintenance work performed should keep the area safe, attractive and in useable condition, and maintain the plant material in good condition. The contracts also specify that general repair maintenance, such as maintenance and repair of irrigation systems is part of the contracted work.

Both of the MAD contracts we reviewed list work to be performed on weekly, bi-weekly, monthly and quarterly schedules. For instance, part of the scope of work for one MAD contract that we reviewed requested weekly

maintenance for street medians landscaped with trees, shrubs, groundcover; paved street medians, and hardscape; and gutters and curbs and bi-weekly maintenance for street medians landscaped and/or rights-of-way with trees, shrubs, groundcover, and paved areas; paved street medians, and hardscape; and gutters and curbs.

The contracts also allow for what is termed extraordinary labor. Extraordinary labor is work that is outside of the scheduled specified contracted duties. As noted previously, the contracts include removing graffiti or replacing plants that were lost due to vandalism or vehicular damage as examples of extraordinary labor. The extraordinary labor line item is part of the contract and has an hourly extraordinary labor rate. Contract language and P&C's contract General Provisions state that City will not pay contractors for extraordinary work unless the contractor attaches written authorization from the Contract Administrator approving extraordinary work. Additionally, P&R provides further guidance on the extraordinary labor authorization process. Specifically, P&R internal guidance states that contractors shall obtain extraordinary labor authorizations prior to initiating the work.

The contract administrators—in this case, the Grounds Maintenance Managers—should ensure that the scheduled weekly, monthly, quarterly work is performed on schedule and in an acceptable manner. It is also the contract administrator's responsibility to receive extraordinary labor proposals and to use the proposal to create an authorization for extraordinary work. The contract administrator is then supposed to forward the authorization to their managers for approval. Additionally, the contract administrator should also review landscape invoicing to ensure invoices are accurate and that work was performed in conformance with the contract.

*Problems with
Authorization of
Extraordinary Labor*

We found that for two landscape contracts, the correct process for preauthorization of extraordinary labor was not always followed, yet invoicing was paid. In the two MAD landscape contracts we reviewed, we found that about 76 percent of the invoices for extra labor—totaling about \$84,000—were approved without following the required pre-authorization procedure specified in the Extraordinary Labor Authorization forms. Specifically, we found instances in which there was not extraordinary labor preauthorization or proposal, or that the written preauthorization took place at the end of the month after the work was performed. For example, in the month of October 2014, the landscape contractor submitted an invoice for landscape maintenance work performed in one MAD. The invoice was for \$1,068 in extraordinary labor charges for work such as replacing valves and main lines damaged by roots. However, for all six line items of

extraordinary labor, there was no written evidence of prior authorization for this work before it was performed.

We spoke to the contract administrators and their supervisor about the lack of preauthorization of some the extraordinary work that was performed and paid under the contract. They stated that the cases in question were for emergency services that needed to be completed immediately. They said in certain emergency situations that require immediate work, the contract administrator will verbally discuss work that needs to be performed, and then will give the landscape contractor a verbal authorization to proceed. In these cases, the written authorization request (or proposal for work) would not come from the landscape contractor until invoicing, and then would be a summary of work performed.

The contracts we reviewed include language that requires that the landscape contractor complies with all state and City water restrictions due to the current drought. Additionally, the contract terms include requirements that irrigation issues that would result in wasting water be fixed immediately. However, for the period of review for this contract, July 1, 2014, through June 31, 2015, we found that this type of month end summary of preauthorization happened 27 times (76 percent of the invoices we reviewed for this particular contract). Although some of the charges that were not correctly preauthorized reference irrigation, and may have been emergencies services that qualify as immediate services allowed per the contract, we question that this happened more than 76 percent of the time.

We obtained a 2004 internal management memorandum that provided staff with guidance and direction regarding the extraordinary labor authorization process. This memorandum stated that P&R was implementing several controls to enhance contract management, and address business practices related to extraordinary labor. The memorandum specified that "beginning immediately, all extraordinary labor requests require the completion of an Extraordinary Labor/Contractor Authorization Request Form. The policies and producers regarding the use of the attached Extraordinary Labor/Contractor Authorization Form are effective retroactively to July 1, 2004."

The document also noted that a recent audit revealed that the department was not consistent in complying with the authorization requests and that the "use of the form will provide more accountability controls, a better 'paper trail,' and increased transparency to document that public monies are being spent appropriately and legally." The memorandum also indicated that in matters of emergency, the Grounds Maintenance Manager (typically the supervisor of the contract administrator) may verbally provide

extraordinary labor authorization, and initiate the authorization for the next business day.

We discussed the recurring problems with the extraordinary labor authorizations with department management. P&R management indicated that the authorization system is not working as it was intended to and noted that with current technology (such as smartphones and in the field email), the process could be updated and streamlined to be faster and more conducive with technology capabilities, while still providing a record of the requisite extraordinary labor authorization. Based on our discussions with P&R management, the issues described above are likely to be similar in other MAD landscape contracts that were not in our selection sample of contracts. According to P&R management, the extraordinary labor preauthorization process is similar across all of the 55 MADs overseen by P&R. In the fiscal year 2014, according to P&C, there was a total of 33 landscape contracts for landscaping services for City MADs for a total estimated amount of \$8.5 million.¹⁴

Problems with Certain Charges and Markups Related to Extraordinary Labor

During our reviews of the MAD contracts and the open space contract, we found instances of questionable approval and payment of certain charges. These questioned charges include what appears to be an across the board 10-percent markup on goods purchased by the landscape contractor. Throughout our fieldwork, we found instances in which the MAD landscape contractors and the open space landscape contractor would purchase goods and bill for reimbursement of those goods, plus a 10-percent markup. Although the landscape contractor is allowed, per the contract, to assess a 10-percent markup of wholesale goods in certain instances, we found that contractors included the 10-percent markup in instances that were not in compliance with the contract terms. Further, P&R contract administrators have approved the payments in each of these instances.

While the contract language does not allow for a 10-percent markup of materials in general, our review of contracts identified a provision for a 10-percent markup from the wholesale cost of items only under specific circumstances. The contracts allowed for a 10-percent markup from the wholesale cost of plants and materials replaced due to vehicular damage, theft, or vandalism, and allows for the markup in the case of City requested replacement of plant material for aesthetic enhancement. The contract also states that plants and materials shall not be reimbursed for damages related to contractor negligence.

¹⁴ This amount reflects the amount of the original purchase agreements. The actual amount spent could be higher or lower.

It is important to note that the contract does not provide a blanket provision for a 10-percent markup of any and all plants and materials purchased from third-party vendors. Similarly, there is no provision in the contracts for a 10-percent markup on the cost of services performed by subcontractors. We found numerous instances of invoices approved for payment that included a 10-percent markup for various materials not replaced due to vandalism or theft, as well as 10-percent markups for services performed by subcontractors. Specifically, our review of one contract for the period of one fiscal year showed that more than 15 invoices included 10-percent markups on more than 35 job items that were not related to vehicular damage, theft, or vandalism. These charges included a 10-percent markup for goods such as irrigation materials and other supplies. Additionally, we identified a few instances in one MAD contract which the 10-percent markup was whited out on the invoice and written in with a 15-percent markup. These markups, totaling more than \$14,600, were approved by the contract administrator and paid by the MAD. Based on our discussions with P&R management, the issues described above are likely to be similar in other MAD landscape contracts that were outside of the scope of our review.

*MAD Contracts Include
Ambiguous and
Duplicative Descriptions
of Work*

Our review of contracts for landscaping and irrigation work in the MADs identified ambiguous and duplicative definitions of work. These ambiguities create the potential for vendors to charge the City extra funds for work that should be part of standard monthly payments.

As described in greater detail below, these MAD contracts specify different categories of labor that determine different payments. First, the contract sets forth a definition of regular maintenance that is paid at a standard rate. Second, the contract defines extra work that includes tasks beyond regular maintenance. In these cases, the vendor submits separate invoices and receives extra compensation in excess of the standard rate.

Regular Maintenance Work: The scope of work in the contract defines regular maintenance as, "landscape maintenance of designated areas" specified in the contract. This work includes "maintenance and repair of irrigation systems . . . as needed, to ensure proper operation of irrigation systems." Further, in the section of the contract that describes responsibilities for repairs to existing facilities, the contract language states:

The Contractor shall keep controller and valve boxes clear of soil and debris and shall maintain the irrigation system at no additional cost to the City, including, replacement, repair, adjustment, raising or lowering, straightening and any other operations required for the continued proper operation of the system from the "cold" side of that water meter throughout the work site. Repair or replacement includes, but is not limited to" sprinkler system laterals (piping),

sprinkler mains (pressure line), vacuum breakers, sprinkler control valves, sprinkler controllers, sprinkler heads, sprinkler caps, sprinkler head risers, valve covers, boxes and lids (including electrical pull boxes and lids), valve sleeve and lids, quick coupler valves, and hose bibs. Any replacement must conform to the types and kind of existing system. Any deviation must be approved in writing by the Contract Administrator.

The contract appears to include all maintenance and repair work to the irrigation system as regular maintenance work. However, definitions of extra labor elsewhere in the contract cloud this interpretation.

Extra Labor: The contract provides definitions of extraordinary labor that include similar job functions to those listed in the description of regular maintenance. The contract indicates that extra work includes “miscellaneous projects” and states “examples of projects include but are not limited to ... Pour concrete slabs ... Installing irrigation systems as needed ... Excavation, transplanting[,] and replanting, and other associated tree functions as they may arise ... Locate and repair damaged irrigation services or electrical services for broken lines, cut wires to controllers and valves, etc.” These descriptions of projects qualifying as extraordinary labor—such as “replace irrigation controllers”—are very similar to the description of regular maintenance.

We found invoices for one MAD landscape contractor that contained extraordinary labor charges such as “remove and replace valve damaged by tree roots,” or “repair main line vandalized by roots.” Based on the definitions of regular maintenance versus extra labor described above, it is unclear which category of work these charges fall into.

We asked the contract administrators about these invoice line items. They indicated that it was the department’s practice to pay the vendor for certain repairs caused by tree damage, thereby applying the definition of extra labor. Contract administrators explained that the damage was caused because of the age and type of tree, and it would be unfair to the contractor to incur such cost for an unforeseeable condition (such as underground root intrusion).

Nevertheless, we found descriptions of work related to repair of sprinkler systems covered under both the regular maintenance and extra labor overlapping, confusing, and difficult to distinguish. When comparing the regular maintenance language to the extra labor language they both seem to refer to “repair or replace” irrigation services or systems. Further, our review of the two MAD contracts shows a lack of uniformity in how landscape contractors billed this type of repair to the City. One landscape

contractor billed labor costs for repairs as extraordinary labor, plus materials costs and markup. In contrast, the other landscape contractor billed labor for repair work as regular maintenance (no additional hourly rate), and only billed for the cost of materials and mark-up. In both cases, invoices were approved and paid, although the billing practices between the two contractors were inconsistent.

**Questionable
Procurement Methods**

The SDMC has a tiered threshold that determines how a contract can be entered into based on estimated contract prices—oral bids, written bids, or advertised bids. While reviewing some of the landscape contracts, we found instances where, instead of bidding out needed work and projects as required by the SDMC, the department had the landscape contractor perform the work, and billed it as extraordinary labor. This work was billed as extraordinary labor even though the work does not appear to be part of the original scope of work, nor were any amendments made to the original scope of the contract.

We also found that throughout the period of the MAD contracts we reviewed that, instead of using already existing City contracts, or initiating new contracts to procure goods such as sprinkler parts and irrigation supplies, the contract administrators allowed the contract landscapers to procure the goods. As a result, the department missed out on the preferred contract pricing in the existing City contract and paid an additional 10-percent markup on the goods. For instance, we found several invoices for sprinkler goods made by Rainbird that were directly purchased by the landscape contractor through a retailer. First, the City has an existing contract with a different retailer for Rainbird goods in which the City has negotiated more than 50 percent off MLP. Second, the retailer that the landscape contractor was using also had an open purchase order with the City, which would have allowed the City to purchase needed goods through the appropriate channel. Both of these options would have ensured that the MADs were receiving the City negotiated pricing, and would have avoided the 10-percent markup that was being charged by the landscape contractor.

Exhibit 3**Bidding Thresholds and Requirements**

Contract Amount	Bid Requirements	SDMC section
>\$25,000, but equal to or <\$50,000	PA may award contract, shall seek competitive prices either orally or in writing.	22.3203 (a)
>\$50,000, but equal to or <\$150,000	PA may award contract, shall solicit written price quotes from at least 5 sources.	22.3203 (b)
>\$150,000	PA must advertise for sealed bids	22.3203 (c)

Source: OCA, based on based on SDMC, Chapter 2, Article 2, division 32, section 22.3203.

One project that we reviewed that potentially should have been competitively bid was a contract for installation of retrofit irrigation controls. This project totaled more than \$6,000 in labor and \$60,571 in goods—including the 15-percent markup. The total amount was billed under extraordinary labor, with neither labor nor goods put to bid. Further, the invoice showed labor line items for a total of 288 hours, yet billed for 315 hours of labor. We asked the contract administrators why it had the landscape contractor procure the irrigation controls for retrofit mentioned above since the total cost of the goods was more than \$60,000—above the threshold for obtaining five written bids (**Exhibit 3** above describes the SDMC bidding threshold amounts and requirements). They stated that based on research, testing and discussion with the residents in the MAD committee, there was only one type of controller that would meet all their needs and work properly. The department representative stated that if they had gone through a sole source memo, it would have been approved.

We spoke with P&R management about the occurrences of not bidding out labor or goods for special projects such as this retrofit project and instead having the landscape contractor do all enhancements and procure all the goods. P&R management stated that it was best practice to let one contractor do all the work for enhancements to existing systems so that they would have responsibility for all systems. Further, management asserted that because City Council (Council) had already approved the MAD contracts, which were competitively awarded, no further requests for competitive bids were needed for goods or services so long as the amount of the procured good or service did not exceed the total value of the City's contract with the MAD. P&R further asserted that according to the resolution provided to and approved by Council, a fixed cost for routine maintenance and a not-to-exceed cost for Extra Labor was sufficiently vetted through Council via its approval of the contract's resolution.

However, when we reviewed the information provided to Council for approval, we found that the scope of material presented to Council consisted of authorization to assess property owners the additional maintenance fees, overview comments on the scope of the contract for landscape maintenance, and staff recommendations. Based on the information presented to Council, we question whether enhancement projects (rather than repairs), such as the example of irrigation retrofit mentioned above, and the goods used in those projects should have been considered as part of the approved scope of work. Further, although the Council does approve a not-to-exceed amount on each MAD contract, we found instances in both contracts where modifications were made to the purchase orders, and the annual spending on the contract did go over the Council approved not-to-exceed amount.¹⁵

The SDMC requires MADs to adhere to City procurement rules when awarding City contracts.¹⁶ We inquired further with the City Attorney's Office about P&R's procurement of goods through the landscape contractor, rather than using City procurement methods. The City Attorney's Office indicated that, although it did not review the particular circumstances related to this landscape contract, in general, P&R is required to follow procurement rules, including bidding out goods and services above the SDMC mandated thresholds that require a bid. City procurement law requires that purchase of goods and services over \$50,000 be awarded to the lowest of at least five written quotes, follow the correct process for a sole source solicitation, or other allowable procurement options. The P&C Director further confirmed this assessment.

**Department Not
Ensuring it Receives
Full Available Discount**

We reviewed a goods contract that is administered by P&R. This contract, awarded via competitive bid, was for new sprinkler heads, valves, and parts for up to five years. We reviewed the invoices for this contract and found that the invoices stated that early payment will provide an additional two-percent discount. However, P&R had not set up early payment terms with the Comptroller's Office to receive this discount. Instead, the payment terms set in SAP for the invoices we reviewed were 30-day net payment terms, with no discount for early payment—which is the default payment terms. However, default payment terms can be overwritten when a purchase order is created, or a modified payment term can be requested by the department when an invoice is entered into SAP for payment. At the time of field work

¹⁵ Contracts going over the not-to exceed amount was a finding first identified in the audit report that OCA issued in April 2015, addressing Citywide Contracting Oversight. We recommended that P&C fully utilize SAP to ensure that value authorities are not exceeded.

¹⁶ SDMC sec. 65.0213 *et. seq.*

we reviewed the total spend associated with the vendor for this contract and found that the total spend was approximately \$950,000—making the total available discount over the five-years of the contract approximately \$19,000.¹⁷ We did not review every invoice to ascertain if early payment was ever made. However, we did review payment history for this vendor and did not see that any rebates or refunds were provided to the City from the vendor.

We spoke with the contract administrator about receiving this discount. He stated that because the invoices come in the mail rather than email, it may be hard to ensure that the early payment terms are met. Further he indicated that he was unsure that the City could qualify for such a discount. Additionally, we discussed the discount options with the Comptroller's Office, and it stated that the City could obtain the early payment discount. To do so, the department would need to set up new payment terms for the vendor with the Comptroller's Office. The Comptroller's Office stated that the City does not have a written requirement that contract administrators ensure early payment discounts are obtained, but that it is expected that departments will make all efforts to save money.

Need for Improved Inventory Controls

While reviewing P&R's administration of a sprinkler head, valve, and parts contract, we found there were weak inventory controls and no system to track and account for total inventory procured through the contract. We discussed with contract end users the inventory controls for goods purchased through the contract, and they indicated they do not have an inventory count system in place. According to staff, their current practice is to order goods when the inventory shelf is low. Further, staff indicated that there was no count of goods available, and thus no way to accurately reconcile inventory deployed for use against inventory received. We asked staff how they identify if inventory is low, or missing. Staff stated that they "order when the shelf is low," and that they do not have a problem with missing inventory. Internal control standards indicate that it is a best practice to have some method of inventory control and count. P&R does have an electronic inventory system, but it is not implemented at this particular storage location.

We discussed this issue with P&R management. They indicated that although they do track goods ordered, at this time they do not have an inventory system to detect inventory count problems. P&R indicated they are in the process of implementing an inventory tracking system.

¹⁷ This was a five-year contract that had been in place for almost five years when it was selected for review.

Many of the common themes identified during field work were summarized in the body of this report. We have also included in **Appendix C** case narratives for each contract review that was in our sample. These narratives provide a closer look at the details of what we found, and potential causes and recommendations.

- Recommendation #4** Park and Recreation should develop a contract administration training for landscape contract administrators. The training should provide guidance to landscape contract administrators that provide specific direction on allowable charges and allowable procurement methods. The training should focus on methods to control costs and encourage competitive bidding and good stewardship of taxpayer dollars. Specifically, the training should provide guidance in the areas of purchase rules for goods and services. (Priority 2)
- Recommendation #5** Park and Recreation should update its Extraordinary Labor Authorization process to reflect intended, most effective business practices while still ensuring the use of internal controls such as management approval and monitoring. To ensure its authorization process is being used as intended, management should develop a system that performs periodic spot checks of the extraordinary labor preauthorization process. The spot checks should be reported to the deputy directors of the division as to inform them if the process is working as intended. (Priority 2)
- Recommendation #6** Park and Recreation, in consultation with the City Attorney's Office, should review boilerplate language in Maintenance Assessment District and other landscape contracts to clarify language related to allowable extraordinary labor, extraordinary labor authorization processes, the scope of work, and associated markups. (Priority 2)
- Recommendation #7** The Director of Park and Recreation, in consultation with the Office of the City Attorney, should review all line item assessments in invoices submitted by landscape vendors with open contracts with the City of San Diego pertaining to "Contractor's cost of handling" or related "Markup" to determine whether the charges were allowable under the terms of the contract and consider means to recoup any unallowable charges. (Priority 2)
- Recommendation #8** The Office of the Comptroller should develop or include in its invoice payment procedures the written requirements that all departments maximize full early payment discounts to the extent possible. This guidance should be included in any contract administration training that is developed. (Priority 2)

Recommendation #9 The Park and Recreation Director should review inventory practices and direct all of his staff to implement an inventory system at all store facilities. The inventory system should include physical inventory procedures, and should be designed to detect loss and unexpected shortages of critical items. If using an electronic inventory software is not practical at all facilities, then the department should develop and document a process to conduct physical inventory procedures on a periodic basis. The department should monitor and periodically review inventory procedures. (Priority 3)

Previous Audit Findings Illustrate Long-standing Issues Related to Contract Administration and Oversight Since the establishment of the Office of the City Auditor (OCA) in 2008, the OCA has reviewed the City's development and administration of contracts in several capacities. Additionally, internal audits issued prior to the creation of OCA in 2008, describe issues similar to those discussed in this report. The findings in this audit and in audits issued in previous years illustrate the fact that the City has had similar, yet persistent contracting issues over a long period of time. Key selected examples from previous audits are briefly described in **Appendix D**.

Similar Audit Findings Dating Back to 2004 Described by City's Internal Audit Division Additionally, prior to OCA's creation in 2008, the Office of the City Comptroller—Internal Audit Division had issued some internal audit reports that detailed contract administration weaknesses and problems related to not following procurement rules. For example, some of the issues reported on in 2004 by the former Audit Division were similar to issues that we are reporting on in this report. For instance, in 2004, the former Audit Division reported that there were weaknesses in matching contracted pricing to invoices, a problem that we also identified. Again in 2004, a separate audit reported that pricing lists were not always available to contract end users. We identified this same issue 12 years later. Finally, also reported on in the June 2004 audit report titled, *Citywide Procurement Audit*, the Audit Division found that some purchases appeared not to comply with the purchasing rules set forth in the SDMC. We again found similar problems—which are detailed in Appendices C and D of this report—while performing audit fieldwork for this audit.

During this period, the City Administrations have made changes and addressed many recommendations made through the various audits and report. For instance, according to an Independent Budget Analyst report, in 2009, the City fully implemented materials management/inventory modules of SAP in accordance with the process designed developed by P&C. They also have clarified San Diego Municipal Codes (SDMC); updated process narratives and administrative regulations related to purchasing or contracting; standardized forms and created check lists for staff to help

ensure processes are followed; provided training and reference materials via the City's intranet; and updated department instructions. However, as noted in the paragraph above, the contract administration and oversight have continued to face challenges.

This audit identified control weaknesses by both the oversight of P&C and oversight within client departments. One area that we identified contract administration problems with is the two Maintenance Assessment District (MAD) landscape maintenance contracts that we reviewed which are overseen by P&R staff. Among other things, we found problems related to the extraordinary labor approvals and problems related to goods and services procurement which may not have followed procurement rules set forth in SDMC. However, in 2004 P&R had identified these same issues that we are reporting on again in this report.

For instance, in this report, we found that contract administrators did not always follow the required approval process for the extraordinary labor approvals. Despite the requirement that extra labor is authorized in writing prior to the work being performed, some extra labor was authorized in bulk at the end of the month during the invoicing process. According to the department, the preauthorization process serves as an internal control to prevent overspending, inappropriate expenditures, and expenditures which do not comply with City rules. However, in 2004, the then Open Space Deputy Director of P&R issued a memorandum that detailed the extraordinarily labor preauthorization process and clarified in no uncertain terms that all extraordinary labor requires the completion of an extraordinary labor authorization form.

Then in 2012, the P&R Assistant Deputy Director issued a memorandum to City MAD staff to update the purchase request forms and Extraordinary Labor Authorizations forms. This memorandum provided additional reiteration of the Extraordinary Labor Authorization form requirement that was addressed in the 2004 memorandum. The instructions reconfirmed the requirement to request authorization of the work before it was performed, and the requirement for the district managers to sign and return the authorization form to the grounds maintenance managers to hold onto until after the work is completed. The instructions further restated the Extraordinary Authorization form should be attached to the invoice when sent for payment processing. Although the extraordinary labor authorization process was documented in 2004 and 2012 through internal memorandums, and the guidance in the memorandums required a district manager sign off on all extraordinary labor authorizations, department directors have not adequately monitored the authorizations to ensure that the process was correctly followed.

The Green Book indicates that in a strong internal control environment, management should establish organizational structure, delegate authority to achieve the entity's objectives, and evaluate and hold individuals accountable for their internal control responsibilities. The Deputy Directors issuing the memorandums, therefore, should be held accountable for ensuring that monitoring of internal controls are in place to make certain the controls are working as intended. However, Green Book frameworks state that ultimate responsibility lies with the management at the top of the organization.¹⁸ To that end, Directors should develop mechanisms that properly monitor the effectiveness of internal controls related to their departments' procurement activities.

Addressing Long-standing Contract Administration Requires Strengthened Internal Controls Over time, various factors have caused the contracting problems identified in this report. Primarily, the problems have resulted from shortfalls in the City's contracting internal control environment, control activities, and monitoring practices. These deficiencies, coupled with decentralized contracting responsibilities, contributed to the City's on-going contracting problems including insufficient policies and training for contract administration; lack of coordination of contract oversight between the client departments and P&C; and an absence of a systematic, top-down monitoring program by department directors and City executive management. A March 2014 report¹⁹ by Huron Consulting Group (Huron) identified similar deficiencies. Huron found that, among other things, the prolonged and rapid turnover of leadership contributed to a lack of a comprehensive vision and strategy for function.

The City Charter, SDMC, process narratives, and department directives all provide guidance on the proper procedures for creating contracts and purchase orders, approving extraordinary labor in contracts, and administering contract performance.

The Green Book and the Committee of Sponsoring Organizations (COSO) emphasize management's role in establishing an organizational structure, assigning responsibility, and delegating authority to achieve an entity's objectives. A key tenet of the Green Book is that management determines key roles to fulfill the responsibility for internal controls in the organizational structure. The framework requires that to achieve these objectives,

¹⁸ Federal Internal Control Standards sec. 3.07, "Management considers the overall responsibilities assigned to each unit, determines what key roles are needed to fulfill the assigned responsibilities, and establishes the key roles. Those in key roles can further assign responsibility for internal control to roles below them in the organizational structure, but retain ownership for fulfilling the overall responsibilities assigned to the unit."

¹⁹ Huron Consulting Group, *Procurement and Contracting Review: City of San Diego*, March 17, 2014

management should design control activities for the entity's internal control system.

The Green Book further provides these control activities should be implemented through sufficiently detailed policies and procedures which must be communicated "down and across reporting lines" to enable personnel to achieve the objectives. Management should select methods and conduct ongoing periodic reviews of the internal control systems and activities to determine effectiveness. Furthermore, management should remediate identified internal control deficiencies on a timely basis.

Since San Diego voters provided significantly expanded authority to the Mayor under the Strong Mayor form of government, particularly the assumption of the role of the Chief Executive Officer, the executive branch is in a position to take the kind of comprehensive, tone-setting leadership role envisioned in the Green Book and COSO frameworks.

The ongoing nature of the contract administration deficiencies requires that tone be set at the top of the organizational structure to ensure improvements are properly designed, deployed, and continually monitored to ensure effectiveness. In our view, City executive management should take a more active role in designing rules and procedures, overseeing implementation, and monitoring City contracts to ensure effectiveness and accountability.

Recommendation #10

The City's executive management, lead by the Chief Operating Officer, should take a lead role in systematically addressing contract administration and oversight problems. Specific initiatives should include, but not be limited to:

- **Ensuring that City management at the Department Director level provides contract administrators in their departments training and other information to understand and satisfy contract administration requirements, such as, but not limited to:**
 - **Proper and legal contract execution requirements**
 - **Correct creation of purchase requisitions**
 - **Vendor and budget monitoring**
 - **Adequate and complete invoice processing**
- **Setting expectations and establishing standards of performance, or metrics, coupled with ongoing evaluations to ensure that Department Directors are properly overseeing the deployment and execution of contract administration procedures. (Priority 3)**

Conclusion

The Purchasing & Contracting Department (P&C) enters into a large number of contracts annually and City of San Diego (City) departments play a role in administering these contracts. We found that improvements in internal controls and clearly communicated procedures will enhance P&C's adherence to, and enforcement of the City's procurement requirements. Furthermore, we found that improvements in the internal control environment for departments overseeing contract compliance can improve overall contract administration including ensuring vendor adherence to contract provisions. In our view, City executive management, should take a more active role in designing rules and procedures, overseeing implementation, and monitoring City contracts to ensure effectiveness and accountability.

Recommendations

Recommendation #1 P&C should ensure that its new purchase requisition procedures and the forthcoming digital procurement manual include a requirement for review by senior procurement specialist to try to reduce errors in purchase requisitions and purchase orders. An emphasis on ensuring that existing contracts are identified when appropriate should be included in the procedures.

Additionally, P&C should develop a monitoring program that periodically reviews, or spot checks, new purchase orders that have been created and were not tied to contracts. This monitoring process should review all purchasing information and vendor assignment to ensure that there was not a contract available for the goods or services. If errors are identified during the monitoring, staff at the client department and P&C should be further trained to help eliminate such errors. (Priority 3)

Recommendation #2 P&C should continue its efforts to obtain and expedite implementation of the catalog software to, among other things, address lapses in contract pricing review of when invoices are processed. P&C should develop a clearly defined and documented plan for training P&C and client department staff as part of the implementation process. (Priority 3)

Recommendation #3 The Office of the City Comptroller should modify its process narrative for invoice payments to clearly assign the responsibility to ensure contract pricing is billed. (Priority 3)

Recommendation #4 Park and Recreation should develop a contract administration training for landscape contract administrators. The training should provide guidance to landscape contract administrators that provide specific direction on allowable charges and allowable procurement methods. The training should focus on methods to control costs and encourage competitive bidding and good stewardship of taxpayer dollars. Specifically, the training should provide guidance in the areas of purchase rules for goods and services. (Priority 2)

- Recommendation #5** Park and Recreation should update its Extraordinary Labor Authorization process to reflect intended, most effective business practices while still ensuring the use of internal controls such as management approval and monitoring. To ensure its authorization process is being used as intended, management should develop a system that performs periodic spot checks of the extraordinary labor preauthorization process. The spot checks should be reported to the deputy directors of the division as to inform them if the process is working as intended. (Priority 2)
- Recommendation #6** Park and Recreation, in consultation with the City Attorney's Office, should review boilerplate language in Maintenance Assessment District and other landscape contracts to clarify language related to allowable extraordinary labor, extraordinary labor authorization processes, the scope of work, and associated markups. (Priority 2)
- Recommendation #7** The Director of Park and Recreation, in consultation with the Office of the City Attorney, should review all line item assessments in invoices submitted by landscape vendors with open contracts with the City of San Diego pertaining to "Contractor's cost of handling" or related "Markup" to determine whether the charges were allowable under the terms of the contract and consider means to recoup any unallowable charges. (Priority 2)
- Recommendation #8** The Office of the Comptroller should develop or include in its invoice payment procedures the written requirements that all departments maximize full early payment discounts to the extent possible. This guidance should be included in any contract administration training that is developed. (Priority 2)
- Recommendation #9** The Park and Recreation Director should review inventory practices and direct all of his staff to implement an inventory system at all store facilities. The inventory system should include physical inventory procedures, and should be designed to detect loss and unexpected shortages of critical items. If using an electronic inventory software is not practical at all facilities, then the department should develop and document a process to conduct physical inventory procedures on a periodic basis. The department should monitor and periodically review inventory procedures. (Priority 3)
- Recommendation #10** The City's executive management, lead by the Chief Operating Officer, should take a lead role in systematically addressing contract administration and oversight problems. Specific initiatives should include, but not be limited to:
- Ensuring that City management at the Department Director level provides contract administrators in their departments training and

other information to understand and satisfy contract administration requirements, such as, but not limited to:

- Proper and legal contract execution requirements
- Correct creation of purchase requisitions
- Vendor and budget monitoring
- Adequate and complete invoice processing
- Setting expectations and establishing standards of performance, or metrics, coupled with ongoing evaluations to ensure that Department Directors are properly overseeing the deployment and execution of contract administration procedures. (Priority 3)

Appendix A: Audit Recommendation Priorities

DEFINITIONS OF PRIORITY 1, 2, AND 3

AUDIT RECOMMENDATIONS

The Office of the City Auditor maintains a priority classification scheme for audit recommendations based on the importance of each recommendation to the City, as described in the table below. While the City Auditor is responsible for providing a priority classification for recommendations, it is the City Administration’s responsibility to establish a target date to implement each recommendation taking into considerations its priority. The City Auditor requests that target dates be included in the Administration’s official response to the audit findings and recommendations.

Priority Class ²⁰	Description
1	Fraud or serious violations are being committed. Significant fiscal and/or equivalent non-fiscal losses are occurring. Costly and/or detrimental operational inefficiencies are taking place. A significant internal control weakness has been identified.
2	The potential for incurring significant fiscal and/or equivalent non-fiscal losses exists. The potential for costly and/or detrimental operational inefficiencies exists. The potential for strengthening or improving internal controls exists.
3	Operation or administrative process will be improved.

²⁰ The City Auditor is responsible for assigning audit recommendation priority class numbers. A recommendation which clearly fits the description for more than one priority class shall be assigned the higher number.

Appendix B: Objectives, Scope, and Methodology

Objectives In accordance with a request made by the Audit Committee, we conducted a performance audit of selected City of San Diego (City) contracts. Specifically, we selected contracts for review based on potential risk, and evaluated the management of each contract selected. The objectives of this audit were to:

- Determine contracts that have risk for mismanagement or loss to the City
- To the extent possible, identify or quantify any loss, or bad effect to the City from poor contract administration controls or oversight.

Scope and Methodology We reviewed laws, rules and standards significant to contract oversight. Additionally, we reviewed other audits related to the City's procurement and contracting management. Using the information gathered through these reviews, we selected 50 contracts for a high level review. To select these 50 contracts, we used Purchasing & Contracting's (P&C) Goods and Services Agreements database that is available on its website. After downloading the database, we attempted to exclude any revenue generating agreements, financial agreements, or Capital Improvement Plan agreements from the dataset. We then used the dataset to identify the four City department with the highest number of total purchase orders. Based on the information that we could obtain through the purchase orders, we used professional judgment to select 50 contracts for a preliminary high-level review.

We requested from P&C the masterfile for each of the 50 contracts that we selected. For each of these contracts we used SAP and the masterfile to evaluate the bid and contract. When reviewing the contracts, we performed a desk evaluation using only the masterfile and SAP based on the following components of the contract:

1. Completeness of bid package
2. Completeness of contract package
3. Clarity and sufficiency of contract scope of work
4. Designation or identification of a contract administrator
5. Sufficiency of price schedules, pricing, and total value
6. Presence of termination clause within contract language

7. Requirements for insurance specified in contract
8. Presence of audit clause within contract
9. Inclusion of City mandated requirements in contract language
10. Inclusion of Conflict of Interest statements
11. Sufficient dispute resolution procedures in contract language
12. Definition of invoicing requirements within contract

For each of the 50 contracts, we issued a risk score based on the components reviewed. Using this risk score, conversations with management, and efforts to diversify the type of contracts selected, we selected six contracts to be reviewed in our sample. For these six contracts selected, we further reviewed the masterfile maintained by P&C. This review included an assessment of the bid, memoranda of agreement (if applicable), contract extension options, communications pertinent to the agreement, and verification that all required signatures were obtained prior to contract execution. We also assessed the method of procurement to determine that it met requirements of the San Diego City Charter, and San Diego Municipal Code.

For each contract in the sample, we evaluated the completeness of the contract, including, but not limited to the inclusion of a specific contract scope, clear compensation details, requirement for insurance, defined conflict of interest, and dispute resolution details. During our fieldwork, we spoke with P&C procurement agents, contract administrators and their managers, department analysts, and staff involved in the purchase request process, and as needed, performed site visits. We reviewed samples of paid invoiced for clarity and evidence of review, and to evaluate the charges against the terms of the contract. If applicable, we identified instances of non-compliance, and if possible quantified any payments made outside of contract terms. As required by government standards, we included fraud detection steps in our field work such as reviewing for on-going or pervasive non-conformance, or systematic accounting issues.

We conducted this performance audit in accordance with Generally Accepted Government Auditing Standards. These 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 the audit objectives.

Appendix C: Selected Contracts' Analyses

Shoreline Landcare, Inc.

Shoreline Landcare, (Shoreline) submitted a bid in July 2012 seeking to perform landscape maintenance on medians within five Maintenance Assessment Districts (MADs) including El Cajon Boulevard, Hillcrest, North Park, Talmadge, and University Heights. The City awarded the contract in November 2012 for a one-year term, beginning on November 1, 2012, with options to renew for four additional one-year periods. According to the bid submitted by Shoreline, the annual value of the contract was \$359,923. The total value of the contract could be as much as \$1.8 million.

Signatures on Contract The bid submitted by Shoreline, which became the contract, was missing key signatures by City officials. The San Diego City Charter requires the signature of the Mayor or a designee, and the City Attorney or a designee in order to formulate a properly executed contract. Specifically, the bid was missing the signature of the City of San Diego Purchasing Agent and the signature from a representative of the City Attorney's Office.

Extraordinary Labor Authorization Pre-Authorization The Park & Recreation Department (P&R) requires that all extra labor projects must be preapproved by the MAD District Manager before work can begin. As part of the authorization process, the Grounds Maintenance Manager is required to receive a proposal, attach it to the completed Extraordinary Labor Authorization (ELA) form, and circulate for approval. After the work is completed, the invoice is attached to the ELA form for approval to pay.

Shoreline submitted more than \$11,000 worth of invoices that may not have included proper authorization required for extraordinary labor, as required by the ELA forms. Examples of instances where ELA procedures were potentially avoided include: missing proposals detailing work; pages missing from the price quote containing the information required to audit; and where a price quote was sent by a Shoreline subcontractor, rather than the contractor.

Shoreline submitted invoices for more than \$17,000 worth of extraordinary labor without submitting sufficient documentation to comply with the instructions on the ELA forms. These issues include: work that was performed without the ELA being completed or approved; work performed the same day the ELAs were approved and on the same date as the invoice;

ELAs approved after the work was completed; and ELAs that were not signed and approved by the proper authorities.

*Support for
Extraordinary Labor*

The P&R Grounds Maintenance Manager, who also serves as the contract administrator for the MAD, is responsible for collecting and ensuring that all invoices are in the accounts payable file, that proper amounts are being charged in invoices, that subcontractor invoices are included to support the invoiced amounts and that these amounts match.

Shoreline submitted more than \$17,000 worth of improper invoices charges and charges without sufficient documentation. These include invoices that do not match amounts in subcontractor invoices; invoices that included improper charges such as "10% contingency"; no description of hours worked; and no description of work.

One charge that may have been unallowable under the contract terms is the "10% contingency." The contract anticipates a 10 percent "handling fee" that a vendor can assess to subcontractor and third party charges. For example, where Shoreline ordered \$100 of trees from a subcontract, Shoreline is permitted to assess a \$10 handling charge. However, Shoreline included a 10 percent "contingency fee" which was not included in the contract in addition to the 10 percent "handling fee." The "contingency fee" was included in numerous proposals and was paid in one invoice. P&R staff were unable to explain the charge or why it was assessed.

*Contract Award and
Extension Lapses*

According to the contract between the City and Shoreline, the City reserved the option to renew the contract after the completion of the original term. The renewal is contingent upon the mutual agreement between the City and Shoreline. A letter from the City offering a renewal does not constitute an award. Rather, the execution of the option requires the City's confirmation in writing.

There were a series of periods when City staff did not ensure the contracts and options were properly or timely executed. As a result, Shoreline completed landscaping work and submitted more than \$523,000 in invoices to the City while there was no contract in place. The initial term of the contract between the City and Shoreline was from November 1, 2012, through November 1, 2013. The first option letter was not confirmed by the City, as required by the contract, until August 28, 2014, which meant that no contract was in place for more than nine months. Shoreline completed and invoiced the City for more than \$291,000 during this period. The term of the first option expired on October 31, 2014. Despite the fact the contract expired in October 2012, the second option to the Shoreline contract was not confirmed and properly executed until June 29, 2015. As a result, again

no contract was in place, this time for more than seven months. Shoreline completed and invoiced the City for more than \$232,000 during this period.

Authorization for Subcontractor Services

In order to employ subcontractors to complete work, Shoreline is required to include the name of the subcontractor in the original bid. However, in instances where a different subcontractor is needed on an emergency basis, the contractor administrator assumes the duty to ensure the selected subcontractors have been vetted by the City.

In one instance, Shoreline used subcontractors to perform work that was neither listed in the bid nor vetted by the contract administrator. The contract administrator notes that in this instance, the work performed was of an emergency nature, and there was not adequate time to go through the purchase order requisition process. Nevertheless, the subcontractor was not on Shoreline's vetted list of approved subcontractors.

Imperial Sprinkler Supply, Inc.

We reviewed the Imperial Sprinkler Supply Inc., (Imperial Sprinkler) contract with the City. This contract was for certain brands of sprinkler heads, valves, and repair parts. This contract was competitively bid and awarded in 2010, as a 2-year contract with three 1-year extension options.

Contract Award and Extension Lapses

The initial award letter was transmitted to Imperial Sprinkler on March 30, 2010, stating that the contract would begin on April 1, 2010, and expire March 31, 2012. The first extension letter in the file is dated April 11, 2012, although the extension is for the period April 1, 2012 through March 31, 2013. The second extension option letter was not in the file, and could not be produced by staff at the Purchasing and Contracting department (P&C) or the Park and Recreation department (P&R). The third extension option letter was in the masterfile and dated September 14, 2014. This is notable because the prior extension should have expired March 31, 2014. This third and final extension states that the "contract is extended until March 31, 2015."

This sprinkler part contract provides goods for multiple P&R operations centers. We reviewed all invoices issued against PO 4500054983, which was a purchase order used by the Raven Street P&R location—totaling about \$35,000. In total, during field work, we found 15 POs issued against this contract for different P&R locations, for a total spend of about \$950,000. We reviewed in whole, or in part, seven of the purchase orders. We reviewed invoices for mathematical accuracy and compliance with contract terms. All invoices reviewed were mathematically correct. We found that generally all

charges appeared correct on the invoice. We did find some instances in which the contract discount appeared to be incorrectly applied at 55 percent, rather than 57 percent. However, the mischarges represented less than half a percent of the total dollar value we reviewed.

Price List Unavailability We attempted to review the invoices to ensure that pricing was in agreement with the awarded contract pricing. However, we were unable to obtain a manufacturer's price list. As noted in the body of the report, goods contracts are generally awarded to the lowest responsible bidder. Although the invoices indicated a manufacturer's price, neither P&C nor P&R were able to provide the price list. As a result, we were unable to verify pricing accuracy.

Cass Plumbing and Heating, Inc.

The City awarded a contract for backwater valve installations to Cass Plumbing and Heating, Inc. (Cass Plumbing) in September 2011. The scope of work included backwater valve installations to prevent City sewers from backing up into private property.

Contract Award and Extension Lapses The San Diego City Charter requires that the Mayor, a designee, the City Attorney and the contracting party signatures in order to effectuate a legally binding contract.

Neither the Director of Purchasing and Contracting (P&C) nor a representative of the City Attorney's Office signed the agreement to formally execute the contract between the City and Cass. The outline agreement was created on October 13, 2011. However, the P&C Director at the time did not sign the contract until October 30, 2014. The City Attorney's Office was not sent a copy of the contract to review until October 31, 2014.

Although the City did not fully execute the contract with Cass Plumbing (as described above), the City continued to order work, and receive and pay invoices to the company. The following table illustrates the amount paid to Cass Plumbing before the Director of P&C signed the contract:

Cass Plumbing Invoiced Amounts Prior to P&C Department Signature²¹

Year	Purchase Order	Total Invoice Amount
FY 2012	4500027519	\$31,410.00
FY 2013	4500033492	\$57,224.25
FY 2014	4500048610	\$25,992.44
Total		\$114,626.69

Source: OCA generated using purchase order details.

Review by the City Attorney's Office In November 2014, the City Attorney's Office returned the contract to P&C with a memorandum outlining issues with the contract and, more importantly, without a signature. Despite the lack of signature from the City Attorney's Office and potential issues with the contract, no remedial action was taken by P&C. It continued with the contract as if it had been signed by all required parties.

Contract Lapse after Completion of Original Contract Term Following the completion of the contract and options, representatives from the Public Utilities Department (PUD) discussed with P&C the possibility of issuing another bid for backwater valve work. PUD officials stated that the total amount of money spent each year on the contract was below the threshold that P&C required for a new contract.

Today, PUD officials enter into purchase orders with backwater valve companies, often Cass Plumbing, when the work is needed or emergencies arise. PUD officials state that this is a very time-consuming process and that during busy times, collecting bids, filling out materials requests, and shepherding the purchase order through review by other departments consumes as much as 90 percent of their time. These PUD officials state that the emergency nature of the work makes creating a sufficiently defined scope of work for an RFP or RFQ impracticable. As a result, individual POs are the only option.

Bob Turner Crane Services, Inc

A job request seeking rental of various operated hydro-cranes was created on April 5, 2009. The estimated cost of the contract was \$150,000. The City issued a Request for Bid for the crane rental with a closing date of May 21, 2009. Bob Turner Crane Services, Inc. (Turner Crane) submitted a bid on May 15, 2009.

²¹ This is shown as a lack of signature in Exhibit 1 of this report.

According to the Purchasing and Contracting (P&C) "Contract Log", the contract was awarded on August 10, 2009. The City awarded four different vendors a portion of the contract. Turner Crane services won the largest portion for \$170,220. The City created an agreement on August 10, 2009, for \$71,133. Notably, there was no award letter in the file maintained by the P&C. It appears the term was from September 1, 2009, through August 1, 2010.

*Contract Award and
Extension Lapses*

P&C personnel completed a "Closeout/Option/Rebid Log" which documented the execution of option contracts for the period September 1, 2010, through August 31, 2011. This document was for the first contract extension option. Notably, Turner Crane was not included in this document.

The contract includes the following language pertaining to options stated; "The renewal is contingent on a mutual agreement between the City and the Contractor with such agreement to be confirmed within sixty (60) days prior to the expiration of the contract period." The contract further stated, "The City's initial letter offering the contractor an opportunity to renew the contract does not constitute an award of the option period. Any option acceptance must be confirmed by the City, in writing, before it becomes valid."

There were no documents in the P&C file to indicate that the first option had been executed between Turner Crane and the City.

The City sent a letter to Turner Crane on July 19, 2012, to provide notification that the contract expires on August 31, 2012, and invited the company to execute an extension of the contract for the period September 1, 2012, through August 31, 2013. A representative of Turner Crane signed the document on July 23, 2012, and returned it to the City.

P&C staff completed a "Closeout/Option/Rebid Log" which documented the execution of option contracts for the period September 1, 2012, through August 31, 2013. Turner Crane was included on the log which noted the company had renewed required insurance policies. This document was for the second contract extension option.

On January 2, 2013, the City sent Turner Crane a letter confirming the execution of the extension for the period September 1, 2012, through August 31, 2013. This means that for the period of August 31, 2012, through January 2, 2013, Turner Crane was performing work for the City without a valid contract in place.

P&C department personnel completed a "Closeout/Option/Rebid Log" which documented the execution of option contracts for the period

September 2, 2013, through August 31, 2014. Turner Crane was not included on the log which noted the company had renewed required insurance policies. This document was for the third contract extension option. Notably, there were not documents in the P&C file to indicate that an option had been executed between Turner Crane and the City.

Purchase Orders Not Correctly Linked to Contracts

As stated in our previous Contracting audit, “the City does not provide sufficiently accurate and reliable contract award data with supporting documentation through its Citywide financial system, SAP, even though these capabilities and controls exist in SAP. As a result, the City cannot determine the level of compliance with contractual terms or the full value and the corresponding commitments of contracts throughout the City.”

The City paid more than \$84,000 in invoices in conjunction with purchase orders not attached to a contract for work completed by Turner Crane during the period the original contract was in place, the period during which the contract lapsed, and during the period when the new contract was in place.

Invoices Issued Before Purchase Order

PUD submitted a materials request to P&C on April 15, 2014. The request sought a total of \$5,000 for crane services and listed the contract number in the request. Attached to the request were a series of documents pertaining to the issuance of the original Turner Crane contract and the original agreement for Turner Crane. The purchase order was issued on May 3, 2014, for \$5,000. However, the first invoice was issued on April 30, 2014, for \$1,472.

The work was completed and the invoice was submitted before the City issued a purchase order, or contract, for the agreement.

LUSA, LP (Landscapes USA)

The City awarded LUSA, LP (LUSA) the landscape maintenance contract for the Carmel Valley Maintenance Assessment District (MAD) on January 6, 2011. The contract term for MAD Area 1 of the contract ran from December 1, 2011, through December 31, 2012, and the term for MAD Area 2 of the contract began on September 15, 2012, and continued through December 31, 2012. The San Diego City Council on May 16, 2012, approved the contract and specified the following scope of work: care and cleaning of street medians, parkway landscaping, sidewalk, curb and gutter, landscaped slopes, mini-parks, greenbelts, and open space areas. The Council approved an amount not to exceed \$4.6 million over five years.

Contract Award and Extension Lapses

According to the contract between the City and LUSA, after the completion of the original contract period, the City reserved the option to renew the

contract for four, one-year terms. The renewal requires the mutual agreement between the City and LUSA. Further, the contract language stated that, “[t]he City’s initial letter offering the contractor an opportunity to renew the contract does not constitute an award of the option period. Any option acceptance must be confirmed by the City, in writing, before it becomes valid.”

In October 2012, the City exercised the first option for the LUSA contract and the term covering the period beginning December 31, 2012, through December 30, 2013. According to documentation maintained by P&C, the contractual relationship may have lapsed for about six months between December 2013 and July 2014. According to documentation maintained by P&C, the City sent a letter to LUSA on June 9, 2014, seeking to exercise an option which stated the term of the contract would run through December 31, 2015. The letter was signed by LUSA on June 11, 2014, and the City on July 1, 2014. During this period when there was potentially no contract in place, LUSA continued to perform landscaping and irrigation services and submitted invoices totaling about \$512,000.

*Extraordinary Labor
Authorization*

P&R requires that all extraordinary labor projects must be preauthorized by the MAD District Manager before work can begin. As part of the approval process, the Grounds Maintenance Manager is required to receive a proposal, attach it to the Extraordinary Labor Authorization (ELA) form and circulate for approval. After the work is completed, the invoice is attached to the ELA form for approval to pay.

In some instances, the City may not have properly adhered to the ELA approval procedure for about \$69,000 (\$34,450 in Area 1 and \$35,000 in Area 2) worth of extraordinary labor projects. Types of instances where procedures were avoided include missing proposals detailing work, missing signatures, and third party vendor purchases made on dates prior to the issuance of the proposal and ELA.

P&R representatives who administer the contract stated that ELA procedures are not followed due to overriding directives to repair water related problems immediately. Water related issues include those such as damaged irrigation lines. However, instances where ELA procedures were not followed occurred in 30 of the 34, or 88 percent, of the total extraordinary labor projects approved. Additionally, the ELA form issued by the P&R had most recently been revised in March 2015.

*Handling Fee Charges
on Invoices*

The contract between the City and LUSA contemplates that LUSA can assess a 10-percent charge on plant materials and the purchase of goods required for repairs on facilities damaged by vandalism or theft. We determined that the contingency may potentially have been mischarged in two ways.

First, LUSA may have been mischarging the 10-percent contingency fee on labor and the purchase of materials for extraordinary labor not resulting from vandalism or theft.

Second, we found five instances where LUSA charged in invoices 15-percent handling fees totaling more than \$14,600 for work. These amounts were paid and approved by the contract administrators.

When asked why the 15 percent was approved as opposed to the 10 percent specified in the contract, the contract administrators stated in these instances LUSA was required to hire a subcontractor to perform work. They stated that in private practice, LUSA would charge a 25 percent markup. The contract administrators stated they felt more comfortable with allowing the 15 percent. However, without a written contract amendment, an increase in markup amount was not allowed under the terms of the contract.

*Third Party Materials
Supply Purchases*

The City's procurement and contracting rules state that where the contract amount is between \$25,000 and \$50,000, the solicitation of one bid is required; for a contract amount between \$50,000 and \$150,000, there needs to be a solicitation of written price quotes from at least five sources. These procedures may be bypassed by seeking sole source authorization or other allowable procurement methods.

During the fiscal year 2015, LUSA purchased more than \$115,000 worth of irrigation-related materials for extraordinary labor projects from one company. Notably, LUSA charged more than \$11,000 in a "10% contingency fee" for the purchase of these items.

When asked whether contract administrators inquired about purchasing the materials through an existing City contract to take advantage of cost reduction and omit the handling fee, the contract administrators stated they asked LUSA to order the parts because the City ordering process takes too long.

In this situation, not only was the City losing out on its preferred pricing, but it was paying a 10 percent markup on the retail price.

*Extraordinary Labor for
Large Purchases*

As stated above, the City's procurement rules require that where contract amounts between \$25,000 and \$50,000 require the solicitation of one bid, amounts between \$50,000 and \$150,000 require the solicitation of written price quotes from at least five sources. These procedures may be bypassed by seeking sole source authorization.

- One extraordinary labor approval covered the first part of a "retrofit" of 21 controllers in the Carmel Valley MAD to "ET Water through

SoCal WaterSmart program” which included the “removal of all existing controllers and replacement.” The materials cost for the project was \$60,571 and the total cost of the project was \$66,584. The second part of the extraordinary labor for the retrofit of “remaining controllers” to “ET Water through SoCal WaterSmart program.” The materials cost for the project was \$40,367 and the total cost was \$53,836.

- When asked why this project was not put out to bid, one of the contract administrators stated that purchasing the SmartMeters through Horizon, the third party vendor used by LUSA, was the direction they received from the MAD committee because LUSA would be monitoring the meters.

This project may have been sufficient in cost to trigger the bid or sole source requirements set forth in the City’s procurement code, but no sole source authorization was sought.

Aztec Landscaping, Inc.

In 2012, the City put out for competitive bid a contract for landscape maintenance services for what was deemed a City open space area. City open space areas are areas within the City that are generally free of development, of low density development areas. These areas are often used for preservation or recreation. Part of this open space contract was awarded to Aztec Landscaping, Inc. (Aztec Landscaping).

Contract Award and Extension Lapses According to the bid, this contract was a one-year contract with four one-year extension options, for a possible total contract period of five-years. This contract was originally awarded in September 2012 for the period September 25, 2012, through September 24, 2013. Through review of the masterfile, we found an extension option award for the period of September 25, 2014, through September 24, 2015. However, we could not locate the option extension letter for the first extension period of September 25, 2013, through September 24, 2014. We reviewed files contained by the contract administrator, and requested the first extension option letter from P&C. However, it could not be located.

According to the contract, any contract extension options were contingent on a mutual agreement between the City and the contractor to be confirmed 60-days prior to the expiration of the contract period. Further, contract language stated that, “The City’s initial letter offering the contractor an opportunity to renew the contract does not constitute an award of the option period. Any option acceptance must be confirmed by the City, in

writing, before it becomes valid." According to this language, if the original contract extension option letter was never sent, or signed, the contract would not have been extended.

Handling Fee Charges on Invoices Contract language allows a 10-percent handling markup for certain goods supplied by the landscape contractor. We found that the contract language explicitly allows for a 10-percent markup for goods used for repairs to facilities or plants damaged by vandalism or theft. However, through our review, we found that the 10-percent mark-up was charged, approved, and paid outside of the terms of these allowances. We spoke to the contract administrator and he stated that if a good was used in order for enhancements, the 10-percent charge was approved because it was beyond maintenance and repair. We reviewed the fiscal year 2015 invoices, and found that in total about \$460 in 10-percent markups were approved which appeared to be outside of the allowable contract terms.

Appendix D: Previous Audits with Contract Administration Findings

The tables below summarize previous audits and the recommendations that were issued by the Office of the City Auditor and which relate to contract oversight or administration. The status of recommendations targeted to improve the contracting process or contract administration process is listed in each table as of the last follow-up period ending December 31, 2015.

Report Title (shortened), Year	Performance Audit of P&C Department, Rules and Practices Should Be Clarified, 2012
Summary of topic	Evaluated the City's contracting process and the adequacy of internal controls
Summary of Findings	That audit found that, among other things, there was ambiguity in some of the San Diego Municipal Code (SDMC) related to contracting rules. We determined that the ambiguity may have led to the City awarding contracts without City Council (Council) approval in instances where Council approval may have been required.
Summary of Related Recommendations	This audit recommended that SDMC section related to the thresholds for contracting that require Council approval be clarified. Additionally, it recommended that the City Administration conduct a full review of the purchasing practices and internal controls to ensure full compliance with the law.
Recommendation Status	All four recommendations implemented.

Report Title (shortened), Year	High Mark-up of Goods Purchased through Cooperative Agreements, 2012
Summary of topic	An interim memorandum to P&C to make management aware of costly findings identified during an audit of General Services Department's Facilities Division.
Summary of Findings	We found that the City was paying high priced markups for supplies and equipment under newly established maintenance, repair and operations (MRO) cooperative agreements.
Summary of Related Recommendations	Our office recommended that P&C immediately work with the City Attorney to review the MRO terms and find a solution.
Recommendation Status	Implemented.

Report Title (shortened), Year	Performance Audit of the Procurement Card Program, Oversight Can Be Strengthened, 2012
Summary of topic	Review of the Procurement Card program which at the time was administered by P&C.
Summary of Findings	We found that in some cases, total spending with one vendor by one department was high enough to warrant competitive bidding per the SDMC.
Summary of Related Recommendations	We recommended that P&C track and monitor procurement card spend totals by vendor, and ensure that the appropriate procurement methods were utilized to procure City goods.
Recommendation Status	Of the five recommendations, two have been implemented and three are in progress.
Report Title (shortened), Year	Performance Audit of the Graffiti Program, Oversight of the Vendor Contract Needs Improvement, 2014
Summary of topic	Reviewed the City's Graffiti Control Program, including the contracted third party for graffiti abatement.
Summary of Findings	The report concluded that oversight of the City's contract for third party graffiti abatement was minimal and did not conform to industry best practices.
Summary of Related Recommendations	This report recommended a monitoring program for the vendors, as well as directing the Chief Operating Officer to instruct the responsible departments to renegotiate the contract to include performance standards.
Recommendation Status	Both recommendations have been implemented.
Report Title (shortened), Year	Responses to Key Questions Pertaining to Balboa Park Celebration Contract, 2014
Summary of topic	This report examined the adequacy of City oversight regarding the Balboa Park Celebration planning.
Summary of Findings	The audit found that there were problems not only with contractor oversight (contract administration) that led to the contractor repeatedly missing deliverable dates, but also problems with the clarity of the broad scope of work.
Summary of Related Recommendations	This audit report did not have recommendations to particular departments involved in the contract, but it did suggest issues for consideration, which included comments related to requiring detailed invoicing, and ensuring general contractor accountability.
Recommendation Status	We did not make any recommendations in this audit.

Report Title (shortened), Year	Performance Audit of Citywide Contract Oversight: The City Should Strengthen Oversight, 2015
Summary of topic	This audit assessed the control environment of the Citywide contracting practices.
Summary of Findings	The report concluded that there were not sufficient controls in place to assure quality and completeness of contract deliverables, or to determine the total contractual commitments of the City.
Summary of Related Recommendations	The audit recommended some specific internal controls that should be developed or strengthened in order to provide stronger contract administration Citywide.
Recommendation Status	The City Assistant Chief Operating Officer has stated that these changes are in process.

Similar Audit Findings Dating Back to 2004 Described by City's Internal Audit Division

Prior to the Office of the City Auditor's creation in 2008, the City had issued some internal audit reports that detailed contract administration weaknesses and problems related to not following procurement rules. A brief summary of some of the contracting audits is below.

Audits Issued by the Former Audit Division Within the Office of the City Comptroller	
Summary of Finding	In 2004, the former Audit Division reported that there were weaknesses in matching contracted pricing to invoices.
2015 Condition	We found instances in which this issue is still a current problem. Additionally, we found that some contract administrators were not aware it was their responsibility to ensure that contracted pricing was billed.
Summary of Finding	Pricing lists were not always available to contract end users.
2015 Condition	We found that one contract administrator that we spoke to did not have the contract price lists available to them.
Summary of Finding	The 2004 Citywide Procurement Audit found that some purchases appeared not to comply with the purchasing rules set forth in SDMC.
2015 Condition	We found purchases that were made by vendors that may not comply with the rules set forth in the SDMC.



THE CITY OF SAN DIEGO

M E M O R A N D U M

DATE: April 15, 2016

TO: Eduardo Luna, City Auditor

FROM: Stacey LoMedico, Assistant Chief Operating Officer

SUBJECT: Management Response to the Performance Audit on Selected Contracts

This memorandum is in response to the audit recommendations within the Performance Audit on Selected Contracts. We would like to thank the Office of the City Auditor for their work and efforts on this performance audit.

Recommendation 1

P&C should ensure that its new purchase requisition procedures, and the forthcoming digital procurement manual include a requirement for review by senior procurement specialist to try to reduce errors in purchase requisitions and purchase orders. An emphasis on ensuring that existing contracts are identified when appropriate should be included in the procedures.

Additionally, P&C should develop a monitoring program that periodically reviews, or spot checks, new purchase orders that have been created and were not tied to contracts. This monitoring process should review all purchasing information and vendor assignment to ensure that there was not a contract available for the goods or services. If errors are identified during the monitoring, staff at the client department and P&C should be further trained to help eliminate such errors.

Management Response:

Agree. P&C began a complete overhaul of the procurement processes in the SAP MM Module, as a joint project with the City's Department of Information Technology (DoIT). This effort began in summer 2015 and the scope includes system controls to ensure that requisitions are appropriately linked to contracts.

Additionally, P&C is in the process of drafting a comprehensive procurement manual which will be available to all City staff in a digital format. This comprehensive manual will provide processes and guidelines for both P&C staff and contract administrators citywide. A portion of the recommendation is anticipated to be completed this calendar year, but the complete solution is not anticipated to be completed until early 2018.

Target Implementation Date: January 31, 2018

Recommendation 2

P&C should continue its efforts to obtain and expedite implementation of the catalog software to, among other things, address lapses in contract pricing review of when

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invoices are processed. P&C should develop a clearly-defined and documented plan for training P&C and client department staff as part of the implementation process.

Management Response:

Agree. This was outlined in a previous audit recommendation. The Procure to Pay (P2P) project scope includes the investment in a contract sourcing solution that will provide P&C the tools needed to effectively manage the City's contracts centrally. P&C successfully reclassified the position of core procurement staff and as part of implementation of these new positions, will have a detailed training and transition plan.

Target Implementation Date: November 30, 2016

Recommendation 3

The Comptroller's Office should modify its process narrative for invoice payments to clearly assign the responsibility to ensure contract pricing is billed.

Management Response:

Agree. The Comptroller's Office will work with P&C to strengthen controls over contract pricing review and monitoring, and will incorporate all resulting process changes into the appropriate process narrative.

Target Implementation Date: June 30, 2016

Recommendation 4

Park and Recreation should develop a contract administration training for landscape contract administrators. The training should provide guidance to landscape contract administrators that provide specific direction on allowable charges and allowable procurement methods. The training should focus on methods to control costs and encourage competitive bidding and good stewardship of tax payer dollars. Specifically the training should provide guidance in the areas of purchase rules for goods and services.

Management Response:

Agree. The Department will create a formalized training to ensure clear guidelines and procedures specific to landscape contracts.

Target Implementation Date: September 30, 2016

Recommendation 5

Park & Recreation should update its Extraordinary Labor Authorization process to reflect intended, most effective business practices, while still ensuring the use of internal controls such as management approval and monitoring. To ensure its authorization process is being used as intended, management should develop a system that performs periodic spot checks of the extraordinary labor preauthorization process. The spot checks should be reported to the deputy directors of the division as to inform them if the process is working as intended.

Management Response:

Agree. The Department agrees to the recommendation with the exception of authorizing emergency-related Extraordinary Labor activities immediately in the field due to the emergency, safety considerations. All work authorized will be documented via written documentation from the contractor and will have corresponding documented city approval which will be kept in the contract file unless inputted into SAP.

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The Department will ensure the process as outlined in the 2004 memorandum is updated through a department instruction, training, or other formal process narrative.

Target Implementation Date: September 30, 2016

Recommendation 6:

Park & Recreation, in consultation with the City Attorney's Office, should review boiler plate language in Maintenance Assessment District and other landscape contracts to clarify language related to allowable extraordinary labor, extraordinary labor authorization processes, scope of work, and associated mark ups.

Management Response:

Agree.

Target Implementation Date: November 30, 2016

Recommendation 7:

The Director of Park & Recreation, in consultation with the Office of the City Attorney, should review all line item assessments in invoices submitted by landscape vendors with open contracts with the City of San Diego pertaining to "Contractor's cost of handling" or related "Mark-up" to determine whether the charges were allowable under the terms of the contract and consider means to recoup any unallowable charge.

Management Response:

Agree.

Target Implementation Date: November 30, 2016

Recommendation 8

The Office of the Comptroller should develop or include in its invoice payment procedures the written requirements that all departments maximize full early payment discounts to the extent possible. This guidance should be included in any contract administration training that is developed.

Management Response:

Agree. The Comptroller's Office will add language to the process narrative for invoice payments indicating that all departments should maximize full early payment discounts to the extent possible. P&C will incorporate this guideline into any future contract administration training that is developed.

Target Implementation Date: June 30, 2016

Recommendation 9

The Park and Recreation Director should review inventory practices and direct all of his staff to implement an inventory system at all store facilities. The inventory system should include physical inventory procedures, and should be designed to detect loss and unexpected shortages of critical items. If using an electronic inventory software is not practical at all facilities, then the department should develop and document a process to conduct physical inventory procedures on a periodic basis. The department should monitor and periodically review inventory procedures.

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Management Response:

Agree. The Department will develop and document an inventory process within 90-days. Implementation will begin immediately and completion is expected in early 2017.

Target Implementation Date: April 30, 2017

Recommendation 10

The City's executive management, led by the Chief Operating Officer, should take a lead role in systematically addressing contract administration and oversight problems. Specific initiatives should include, but not be limited to:

- Ensuring that City management at the Department Director level require contract administrators in their departments trainings and other information to understand and satisfy contract administration requirements, such as, but not limited to :
 - Proper and legal contract execution requirements
 - Correct creation of purchase requisitions
 - Vendor and budget monitoring
 - Adequate and complete invoice processing

Setting expectations and establishing standards of performance, or metrics, coupled with ongoing evaluations to ensure that Department Directors are properly overseeing the deployment and execution of contract administration procedures.

Management Response:

Agree. In October 2013, a report was issued to City Council outlining improvements to City governmental operations. The report was unanimously approved by City Council. The report, Improvement to City of San Diego Governmental Operations, No. 13-076 outlined steps and actions to make significant and meaningful changes to provide for "*stability, accountability, transparency, efficiency, effectiveness, fiscal discipline...*" within the City of San Diego. The report includes a discussion about the development of contract management training for the management, oversight and supervision of city contracts due the City's decentralized contract procurement process. This began last year with the recommendation to create a new job classification which will provide the core knowledge and expertise for contract monitoring and management throughout the city.

In early 2014, the Chief Operating Officer (COO) with the Mayor's leadership moved quickly to create an atmosphere of strong policies and procedures within the operations of the city as a whole. More than 50% of the Directors and Executive Directors of the 27 Mayoral departments/programs are new since early 2014. With the city leadership in these positions and throughout the unclassified service, in 2014 the Mayor and COO rolled out annual performance plans for all unclassified staff. As is quoted within the memorandum to staff "a robust and on-going personnel evaluation program is critical to establishing goals and setting expectations in related performance of all employees." While there are no specific metrics for contract management within evaluations it does not reduce or diminish the importance that management has placed on contract management and overall internal controls.

Because the new contract management positions authorized via the Civil Service Commission in March 2016 will not be in place until July 1, 2016 a staff member will be selected to assist the P&C Director for a 90-day special assignment to assist with collecting data from the largest city departments to outline how they are providing contract monitoring. This

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information along with the information obtained through the previous performance audits on this topic will identify the areas that need to be emphasized and prioritized within the procedural manuals and training.

Target Implementation Date: November 30, 2016



Stacey LoMedico
Assistant Chief Operating Officer

SLM/tm

cc: Stephen Puetz, Chief of Staff, Office of the Mayor
Scott Chadwick, Chief Operating Officer
Mary Lewis, Chief Financial Officer
Paz Gomez, Deputy Chief Operating Officer, Infrastructure & Public Works
David Graham, Deputy Chief Operating Officer, Neighborhood Services
Ronald H. Villa, Deputy Chief Operating Officer, Internal Controls
Rolando Charvel, City Comptroller
Judy von Kalinowski, Director, Human Resources Department
Kristina Peralta, Director, Purchasing and Contracting Department
Herman Parker, Director, Park and Recreation Department
Halla Razak, Director, Public Utilities Department
Marshall Anderson, Director of Council Affairs, Office of the Mayor
Lee Ann Jones-Santos, Assistant Director, Public Utilities Department
Andrew Fields, Assistant Director, Park and Recreation Department
Seth Gates, Deputy Director, Public Utilities Department
Chris Zirkle, Deputy Director, Park and Recreation Department