Contract and Compliance Monitoring - Building a Successful Program

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Speakers

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Topics

• Current Environment and Relevant Risks

• Contract Monitoring and the Contracting Cycle

Current Environment and Relevant Risks
Current Environment

- Increased focus at the Federal, State, and Local Levels
- Trend of an increased usage of Interlocal and Cooperative Purchasing Agreements to save purchasing costs and avoid costly procurements.
- State Passage of SB 20 in 2015 requiring changes to contract management
- Increased LBB contract oversight in biennial budget

In 2014 GAO reported $125 Billion in improper payments

- Texas State Auditor’s Office has released 14 reports on audits of contracts from July 2012 to December 2014
- Passage of SB 20
- Increased LBB oversight of contracts
- Local scrutiny

SB 20 Key Changes

- Study to be conducted to evaluate consolidating state purchasing functions
- Contract documents to be retained for 7 years
- Restricts officers and employees involved in contract negotiation from employment with vendors for 2 years
- Sets standards for uniform contract and purchasing reporting to the Comptroller
- All DIR contract solicitations must be posted online
- Requires contract managers or procurement directors to certify that Best Value was achieved
- Requires additional training for purchasing personnel
- Requires procurement and contract management personnel to disclose conflicts of interest

IT commodities must be purchased off DIR
- Provides specific requirements for purchasing IT commodities and prohibits commodity contracts over $1 million
- Sets standards for ethics, reporting and contract approval requirements for Higher Education
- Requires certain contracts in excess of $1 or $5 million to be posted online
- Requires increased monitoring of those contracts
- Requires use of vendor performance tracking system

Effective 9-1-2015
Contract Compliance Risks

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Purpose of Contract Monitoring

- Ensures that in the performance of their contract, vendors and contractors comply with Organizations’
  - Programmatic, fiscal, and contractual policies and procedures
  - Interlocal and Cooperative Purchasing Agreement requirements
  - State laws and administrative rules
- Supports operations, as well as finance, legal, and compliance.

Special Considerations

Interlocal and Cooperative Agreement Purchases should be treated the same as any other contract monitoring.
- The following items should be monitored and managed:
  - The number of agreements in use and their duration
  - Evaluation of overall costs, including fees
  - Coordination with the Interlocal or Cooperative Agreement party to ensure compliance with procurement requirements and vendor performance
  - Internal tracking to identify overall purchases and frequency of use

Contract Monitoring and the Contracting Cycle
Contract Monitoring Process

Establish the Program

- Contract monitoring starts with identifying significant contracts in place within the organization.
  - Also, focus on high use contracts/agreements such as Interlocal and Cooperative Purchasing Agreements.
  - Once all contracts are identified, they should be risk-rated to determine the nature, timing, and extent of compliance and monitoring procedures.
- Compliance and monitoring procedures should be integrated throughout the Contracting Process.

Contract Monitoring

- Establishing the Program
- Pre-Award Phase
- Post-Award Phase
- Monitoring Phase

Contract compliance and monitoring procedures should be formally documented.

Personnel responsible for contract management and monitoring should have adequate training and knowledge of appropriate procurement types and methods.
**Risk Assessment**

S.B. 20 requires the following to be considered in the risk assessment process:

- Assessing the risk of fraud, waste, and abuse in the contractor selection process
- Identify contracts that require enhanced monitoring or immediate attention of contract management personnel

The *Texas Comptroller’s Contract Management Guide* also includes the following considerations:

- Complexity of the contract
- Term of the contract
- Dollar value

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**Contract Risk Assessment**

- Risk-rate contracts as high, medium, or low based on specific criteria in the following categories:
  - Financial Exposure Risk (Dollar value)
  - Complexity of the Contract
  - Prior Experience Risk (Risk of Fraud, Waste, and Abuse)
  - Term of the contract
- Assign a risk rating to each contract for each category
- This risk assessment is applied to all contractors and contracts to design and plan the risk monitoring procedures
- Risk levels may change over time with more vendor experience, “clean” monitoring, and changes to other factors.

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**Compliance Monitoring**

- Monitoring frequency and depth should be based on the Contract Risk Assessment
- Monitoring may include multiple touchpoints throughout the contract
  - Invoice/Expenditure Review
  - Desk Reviews
  - Site Reviews
  - Third Party Coordination, i.e. Cooperative Agreement Party
- Monitoring should be performed over the metrics established in the contract negotiation process
- Formal monitoring checklists and programs should be established for all types of monitoring

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**Pre-Award Phase**

Defining the contracting objectives, detailed expectations for the goods and services to be provided in the contract, and the contracting strategy are important factors in effectively managing the contracting process

**Lessons Learned:**

- Documenting the expectations and objectives of contracting establish expectations of the organization and vendors.
- Effective methods include
  - Performing a needs assessment
  - Risk assessment
  - Contacting the State Contract Advisory Team
Bidding Phase

The process of awarding contracts is fraught with risks, and any failures could have significant repercussions to the organization’s operation and reputation.

Considerations:
SB 20 now establishes prescriptive thresholds for certain procurements from cooperative agreements and prohibits contracts for IT commodities in excess of $1 million.

Post-Award Phase

- Processes should be in place to fairly and objectively select the most qualified contractor.
- Evaluation criteria should be pre-defined.
- Conflicts of interest should be considered at all stages of the vendor selection process.

Considerations:
SB 20 requires contract documents, including the solicitation, evaluation and award documents to be retained 7 years.

Bidding Phase

Consider the risks surrounding the advertisement, selection, validation and awarding contracts:
- Misuse/abuse of cooperative agreements.
- Undocumented or informal policies and procedures.
- Unidentified conflicts of interest in the evaluating committee.
- Lack of knowledge and competency on the evaluating committee.
- Inability to identify and select appropriate contractors.
- Inappropriate segregation of duties.
- Design of the evaluation process and monitoring is adequate.

Vendor Selection

- Vendor selection committees should be objective and strategic.
- Questions to ask:
  - What is the desired outcome of the procurement?
  - What is the best way to achieve that outcome?
- Evaluations should be documented, clearly documenting the considerations to determine best value.

Considerations:
- Best value is often not well documented.
- Evaluations of vendors are not retained.
- Unidentified conflicts of interest with contractors and sub-contractors.
Conflict of Interest Prevention and Disclosure

- Preventing fraud and meeting regulatory requirements includes:
  - Processes to ensure that all potential conflicts are known to evaluation committees and appropriately considered during the pre-award process
  - Public information tools that can assist in the identification process and reduce errors

Contract Negotiation and Execution

- Negotiating the details of the contract to include key attributes influences the ability to effectively monitor vendors for performance and compliance
  - Important contract details include:
    - Right to audit clause
    - Performance metrics

Right to Audit

Right to audit clause provides the opportunity to perform a detailed inspection of vendor records to monitor vendor compliance and prevent fraud.

Important considerations to include in the contract:
- Period length of the right to audit
- Provision and timing of audit notice
- Defining the access to records and the vendor's premises
Performance Metrics

- Use the contract negotiation process to define and establish the criteria on which the vendor will be monitored and evaluated.
- Clearly define in the contract:
  - Required deliverables
  - Quality of goods / performance of service
  - Pricing
  - Unallowable costs
  - Reporting requirements
  - Compliance requirements

Monitoring Phase

Effective monitoring occurs throughout the life of a contract and often includes a multi-layered approach including:
- Invoice/expenditure reviews
- Desk Reviews
- Site Reviews
- Third Party Coordination
- Follow up

Monitoring Considerations

Considerations to include when performing contract monitoring:
- Lack of support
- Costs and wage rates
- Performance
- Vendor monitoring of sub-contractors
- Substitution of sub-standard goods
- Billings for unnecessary materials
- Excessive travel
- Cost manipulation between contracts

Invoice/Expenditure Review

- Invoice and Expenditure reviews should be performed over each invoice prior to payment.
- Supporting documents should be requested, if not provided with the invoice, to validate:
  - Costs
  - Subcontractor or 3rd party expenses
  - Quantities of goods/services provided
  - Validation of services performed

Considerations:

- The extent of the monitoring procedures should be based off risk rating assigned to the contract.
- The level of monitoring may vary through the life of the contract, based on experience with the vendor.

SB 20 Considerations:

- Change orders, amendments, renewals, and extensions for contracts >$10 million may be required to be reported to Comptroller.
- Contracts >$1 million must report:
  - Compliance with financial provisions and delivery schedules
  - Vendor corrective action plans and status
  - Liquidated damages assessed or collected
Desk Review Procedures

Desk review procedures not only include invoice/expenditure reviews, but also include reviews of reports (or other documentation of completion of the work) submitted by the contractor. Desk review procedures should include:

- Validation of vendor performance against contract requirements
- Comparing expenditures against the contractor's budget
- Analyzing trends from current compared to prior years
- Evaluation of costs per unit, changes in costs, salaries and wage rates
- Comparing contractors to other similar contractors to evaluate performance

Site Review Procedures

- Full scope site reviews are usually conducted at the contractor’s place of business and cover a broad scope of compliance and performance issues.
- Limited scope site reviews typically focus on a particular problem.

Site review procedures include:

- Confirming goods/services delivered according to terms
- Sampling detailed transactions within each contract to validate expenditures, prices, and quantities
- Validating of performance against progress reported
- Detailed review of sub-contractor invoices and compliance
- Personnel performing the on-site reviews need to have detailed expectations of the documentation required of contractors

Follow-up

For long-term contracts and continued vendor acceptance,

- A mature contract monitoring program includes performing following-up procedures on findings and exceptions identified through the monitoring.
- Contractors should take action to correct findings
- Monitors should identify appropriate timing and test procedures to validate that corrective action was taken

Contract Close-out

- Performance verification - Formal, documented acceptance of goods and services
- Close-out procedures should have formal, written checklists and procedures
- Key financial and performance metrics should be reviewed and validated
- Completing a vendor performance review through Comptroller
- Consider performing a formal audit of the contract for compliance and program performance
**Resources**

- Senate Bill 20
- Texas Comptroller of Public Accounts Contract Management Guide
- Texas Comptroller of Public Accounts Contract Management Best Practices Matrix
- State Contract Advisory Team

**Questions?**

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