



CITY OF SAN ANTONIO

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August 15, 2011

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Mayor and Council Members:

SUBJECT: Audit of Contract Procurement and Monitoring – Office Depot

We are pleased to send you the audit report of the Purchasing and General Services Department. This audit began in May 2010 and concluded with an exit meeting with department management in May 2011. Management's verbatim response is included in Appendix B of the report. The Purchasing and General Services should be commended for its cooperation and assistance during this audit.

The Office of the City Auditor is available to discuss this report with you individually at your convenience.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Kevin W. Barthold".

Kevin W. Barthold, CPA, CIA, CISA
Acting City Auditor
City of San Antonio

Distribution:

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Janie Cantu, Director of Purchasing
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CITY OF SAN ANTONIO
OFFICE OF THE CITY AUDITOR



Audit of Contract Procurement and Monitoring

Office Depot Contract

Project No. AU10-011

August 15, 2011

Kevin W. Barthold, CPA, CIA, CISA
Acting City Auditor

Executive Summary

As part of the annual Audit Plan approved by City Council, we conducted an audit of the Office Depot contract managed by the Purchasing and General Services Department (Purchasing). U.S. Communities Government Purchasing Alliance sponsors this contract through a nation-wide cooperative purchasing program. The audit objective, conclusions, and recommendations follow:

Are controls in place to ensure Office Depot complies with contractual pricing provisions?

No, controls were not in place to ensure the City received appropriate pricing and discounts from Office Depot. The Office Depot contract did not include any additional terms specific to the City environment. For example, the contract's language was not explicit about Office Depot's designation of items not covered under the contract. During the term of the contract, the City's purchases of approximately \$1 million of desk side recycle bins and \$85,000 of pedometers and safety straps for City programs were deemed non-contractual by Office Depot.

Purchasing did not utilize the City's existing procurement process to ensure billings and payments were appropriate. For example, the procurement and accounts payable controls within the City's SAP system were bypassed. In addition, reconciliations were not performed to ensure the City had in fact paid the appropriate amount billed by the contractor. As a result, we identified a possible overage in payments for fiscal year 2008 of approximately \$206,668 that could not be adequately reconciled between usage reports provided by Office Depot and City records.

Overall, the City relied solely on the accuracy and integrity of Office Depot to ensure compliance with contractual pricing. Purchasing did not institute adequate procurement processes to safeguard City's assets when it departed from existing procurement process controls embedded in the City's SAP accounting system. This control deficiency left the City vulnerable to risk of financial loss due to inappropriate or inaccurate transactions.

Although the City has replaced Office Depot as its office supply vendor with Staples, control weaknesses still exist in the payment process. However, the City is in the process of implementing the new San Antonio e-Procurement System (SAePS). The purpose of SAePS is to improve the annual contract procurement process through the use of more advanced technology. According to City management, SAePS should provide the additional controls required due to the systems integration with the City's accounting system SAP.

We recommend that the Chief Financial Officer:

- Clearly define and communicate procurement responsibilities for all City supplies contracts, to include the initiation, usage, payment, and monitoring processes to City staff.
- Ensure adequate controls are included in the City's new automated procurement system to address all contractual pricing provisions, including Cooperative Purchasing Agreements. These controls should include documented order, invoice and payment reconciliation and verification that prices are correct per the contract.

Purchasing Management's verbatim response is in **Appendix B** on page 7.

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Background

The Purchasing and General Services Department (Purchasing) is responsible for the City of San Antonio's (City) bidding and contracting for all supplies and services in accordance with state and local statutes. Included in these responsibilities are City initiated contracts and cooperative purchasing agreements. The City currently has approximately 120 cooperative purchasing agreements (contracts) in place with a combined value of \$94.8 million. Purchasing is also responsible for the procurement of goods and non-professional services requiring expenditure of more than \$3,000 and for the formal procurement procedures set forth in Texas Local Government Code Chapter 252 for all goods and non-professional services that require expenditures of more than \$50,000. City Council approval is required for the procurement of contracts when expenditures are expected to be more than \$50,000.

In September 2006, the City adopted an existing contract between Los Angeles County, California and Office Depot. U.S. Communities Government Purchasing Alliance (U.S. Communities) made this contract available through a cooperative purchasing agreement. Through this agreement, the City was to receive discount pricing on office supplies.

City staff purchased needed supplies through the City's account. Although most transactions were processed through Office Depot's website, City staff was allowed to place orders by phone or email directly to the Office Depot Regional Sales Representative. Users could select any item that appeared on the website to purchase, which also included non-contractual items.

Upon completion of an order, Office Depot delivered the item to the prospective buyer within one to two business days. Office Depot billed the City twice monthly by email with an attached spreadsheet listing the invoice numbers processed for the period, the cost center or internal order number to be charged, and the final amount. Purchasing uploaded the spreadsheet into the City's SAP system and processed the payment based on the batched total. As of September 2010, the City had expended over \$8.9 million and processed approximately 42,000 invoices through the Office Depot contract.

In May 2010, we received information that Office Depot had allegedly over billed several government agencies. Of these, eight state and local agencies published audit or investigation reports totaling over \$16 million of alleged over billings by Office Depot. **Table 1** on page 2 lists the reports released from these agencies.

Table 1: List of Alleged Overbilling by various Government Entities

Government Entity	* Total Loss Reported	Date of Report
San Francisco, California	\$ 5,752,848	12/18/2009
United States Justice Dept.	4,750,000	9/19/2005
State of Florida	4,500,000	10/8/2009
State of Missouri	320,000	4/29/2010
State of Washington	306,017	9/6/2010
State of North Carolina	294,413	9/9/2008
City of Clearwater, Florida	** 166,331	10/8/2009
Lee County, Florida	** 63,786	9/22/2008
Summary Total of Losses Reported	<u>\$ 16,153,395</u>	
<small>* All dollar figures are taken from published audit reports and Attorney General Press Releases ** Totals may also be included in the State of Florida figure. The Attorney General's Office's press release did not itemize the \$4.5 million.</small>		

Audit Scope and Methodology

The audit scope was from October 2006 through September 2010. We interviewed staff, obtained payment and usage documentation, and researched potential issues experienced by other government agencies contracting with Office Depot. Our testing criteria included Texas Local Government Code Chapter 252, City Administrative Directives, and the Office Depot contract.

Our testing methodology was to compare sales transactions to contractual pricing. However, we were unable to complete our testing since detailed sales transactions could not be successfully traced through the procurement process to specific contractual pricing. Instead, we requested usage reports from Office Depot and compared report totals to the amounts billed and paid by the City. However, we were unable to verify the data within the usage reports due to the lack of documentation retained by the City.

We relied on computer-processed data in the City's accounting system (SAP) to validate the amount paid to Office Depot. Our reliance was based on performing limited testwork of the data rather than evaluating the system's general and application controls. We do not believe that the absence of testing general and application controls of the SAP system had an effect on the results of our audit

We conducted this audit from May 2010 to April 2011 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our audit results and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable

basis for our audit results and conclusions based on our audit objectives. Our audit included tests of management controls that we considered necessary under the circumstances.

Audit Results and Recommendations

A. City's Contractual Interest Not Protected

Purchasing facilitated the City's utilization of a cooperative contract between LA County and Office Depot without any additional terms specific to the City environment. For example, the contract's language was not explicit about Office Depot's designation of items not covered under the contract. During our review, we determined that some departments were unaware that certain items may not be included under the contract. During the contract term, the City purchased approximately \$1 million of desk side recycle bins and \$85,000 of pedometers and safety straps for City programs. While invoices for these items were paid under the contract, Office Depot staff deemed these purchases as non-contractual. This may have occurred because no City department took responsibility or was clearly tasked with monitoring the Office Depot contract. Although Office Depot usage reports were available that identified items considered off contract, these reports were not requested and monitored to ensure contract compliance.

B. Required Procurement Controls Not in Place

Purchasing did not utilize the City's existing procurement process to ensure billings and payments were appropriate. For example, the procurement and accounts payable controls within the City's SAP system were bypassed because purchase requisitions, purchase orders, and good receipts were not created in the system. According to the City's Administrative Directive for Accounts Payable, proper approvals are to be accomplished within SAP throughout the various steps of the procurement process from the initiation of a purchase requisition, issuance of a purchase order, and entry of the goods receipt through the resulting payment of an invoice for the goods and/or service received.

The City made payments to Office Depot without requiring and verifying adequate support documentation, such as sales invoices and receipt documents. City staff only received emails from Office Depot with an Excel spreadsheet attached. The spreadsheet listed invoice numbers, accounts to be charged and the total amount due. The spreadsheet was then entered into SAP and a check was issued for the total amount due. There was no verification process to determine whether the items billed were actually received, accurate, or appropriate before payments were sent. In addition, reconciliations were not performed to ensure the City had in fact paid the appropriate amount billed by the contractor. As a result, we identified a possible overage in payments for FY2008 of approximately \$206,668 that could not be adequately reconciled between usage reports provided by Office Depot and City records.

Overall, the City relied solely on the accuracy and integrity of Office Depot to ensure compliance with contractual pricing. Purchasing did not institute adequate procurement processes in which to safeguard the City's assets when it departed from the City's existing procurement process embedded in the City's SAP accounting system. This control deficiency left the City vulnerable to risk of financial loss due to inappropriate or inaccurate transactions.

In January 2011, the City replaced Office Depot as its office supply vendor with Staples. Nevertheless, control weaknesses still exist in the payment process. Currently, transactions are not being reconciled before payments are disbursed. However, the City is in the process of implementing the new San Antonio e-Procurement System (SAePS). The purpose of SAePS is to improve the annual contract procurement process through the use of more advanced technology. According to City management, SAePS should provide the additional controls required due to the systems integration with the City's SAP accounting system.

Recommendations:

We recommend that the Chief Financial Officer:

- Clearly define and communicate procurement responsibilities for all City supplies contracts, to include the initiation, usage, payment, and monitoring processes to City staff.
- Ensure adequate controls are included in the City's new automated procurement system to address all contractual pricing provisions, including Cooperative Purchasing Agreements. These controls should include documented order, invoice and payment reconciliation and verification that prices are correct per the contract.

Appendix A – Staff Acknowledgement

Brian K. Williams, MBA, CFE, CIA, CGAP, Audit Manager
Kimberly A. Weber, CFE, CIA, CGAP, Auditor in Charge
Sylvia Esparza, MBA, CFE, Auditor

Appendix B – Management Response



CITY OF SAN ANTONIO

SAN ANTONIO TEXAS 78283-3966

July 28, 2011

Kevin Barthold, CPA, CIA, CISA
Acting City Auditor
San Antonio, Texas

RE: Management's Corrective Action Plan for the Audit of Contract Procurement and Monitoring Office Depot Contract

The Finance Department has reviewed the audit report and developed the Corrective Action Plans below corresponding to report recommendations.

Recommendation					
#	Description	Audit Report Page	Accept, Partially Accept, Decline	Responsible Person's Name/Title	Completion Date
A.	<p>City's Contractual Interest Not Protected</p> <p>The Chief Financial Officer should clearly define and communicate procurement responsibilities for all City supplies contracts, to include the initiation, usage, payment, and monitoring processes to City staff.</p>	5	Accept	Janie Cantu / Troy Elliott	Dec 2011
<p>Action plan:</p> <p>The City utilized a cooperative contract and all of the terms therein. No additional terms & conditions specific to COSA were applied. However, since 2009 the Purchasing & General Services Department has incorporated a new form when using cooperative contracts that is an improvement in our process and allows the COSA terms & conditions to be included and clearly identifies items covered by a contract, as evidenced in the newly awarded Staples contract.</p> <p>The Auditor's Office identified two (2) purchases which may have been non-contract items, recycle bins and pedometers. It is recognized that there were some ambiguities which made it difficult to determine the full nature of those purchases. Shortcomings in the process and City staff's understanding of their responsibilities for contract compliance and use of this contract contributed to the occurrence of these transactions. The Purchasing and Finance Departments will address these issues by providing training to applicable staff on procurement roles and responsibilities.</p>					

Recommendation					
#	Description	Audit Report Page	Accept, Partially Accept, Decline	Responsible Person's Name/Title	Completion Date
B	<p>Required Procurement Controls Were Not in Place</p> <p>The Chief Financial officer should ensure adequate controls are included in the City's new automated procurement system to address all contractual pricing provisions, including Cooperative Purchasing Agreements. These controls should include documented order, invoice and payment reconciliation and verification that prices are correct per the contract.</p>	5	Accept	Janie Cantu / Troy Elliott	Dec 2011
<p><u>Action plan:</u></p> <p>Because of the decisions that were made at the outset of this contract regarding the management and methodology chosen to process payments and govern transactions, the built-in control features of SAP were bypassed (i.e., contract, PO releases, GRs, etc.). As part of the original introduction of this program citywide, the Purchasing & General Services Department took steps to communicate responsibilities for monitoring transactions under this contract.</p> <p>The SAePS system is now implemented and provides the electronic platform for the proper front end controls for contract purchases. Also, the Purchasing & General Services Department is developing and enhancing the system so all necessary back end controls are supported for verification of goods received prior to release of payment. The implementation of the new Staples contract into SAePS will eliminate the shortcomings identified in this audit and provide controls that had previously been lacking on the office supplies contract. It is anticipated that the Staples Contract will be in the SAePS System by October 2011.</p> <p>Additionally, through the Shared Services Project which is currently underway, the Purchasing & General Services Department and Finance Departments will develop and provide additional training for staff responsible for compliance, to include Procurement Policy and Procedures Manual training for contract monitoring.</p>					

We are committed to addressing the recommendations in the audit report and the plan of actions presented above.

Sincerely,



 Ben Gorzell
 Chief Financial Officer

7/28/2011

 Date