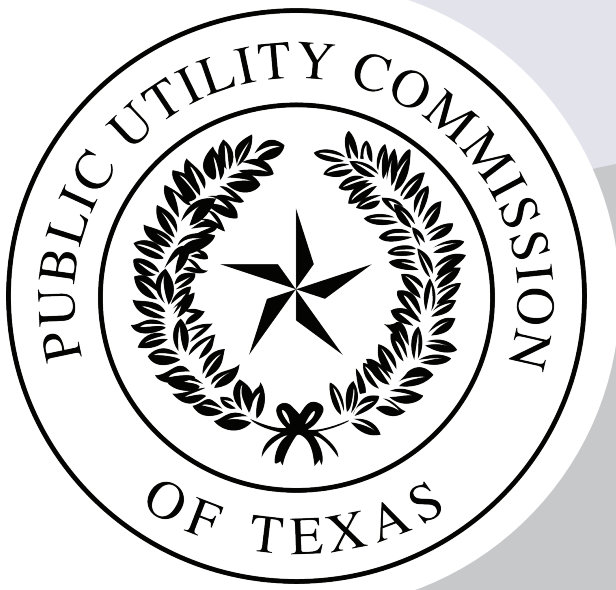


An Internal Audit Report

Contract Oversight at the Public Utility Commission



Report #2021-200, June 2021

Executive Summary

The contract oversight function at the Public Utility Commission of Texas is conducted by the Contract Oversight team. This team is comprised of two staff and is located within the Financial Resources Division. The Contract Oversight team is responsible for all aspects of the procurement cycle. This includes procurement planning, procurement method determination, vendor selection, contract formation and award, and the contract management process.

In addition to the Contract Oversight team, there are Contract Managers at the division level throughout the agency. The Contract Managers are assigned to contracts by the oversight administrator. Each assignment is based on division specific aspects of each contract. The Contract Managers oversee the day-to-day operations of their assigned contract to ensure the service contracted for is being delivered. Any issues noted by the Contract Managers are communicated to the Contract Oversight team. The Contract Oversight team is ultimately responsible for all contracts.

Control weaknesses in the oversight process were identified throughout this audit. The weaknesses were not isolated to one area concerning contract oversight. There is a level of oversight occurring but without clear, documented procedures, the current approach is not consistent and does not satisfy the requirements found in the State of Texas Procurement and Contract Management Guide. During this audit, the Contract Oversight Administrator began working on various issues to strengthen the oversight process. The Financial Resource Division should continue to strengthen the contract oversight process. The following control weaknesses were identified during this audit.

- There are not adequate policies and procedures for contract oversight.
- There is not sufficient training for Contract Managers tasked with the role of contract monitoring.
- There is a lack of segregation of duties between the Contract Oversight team role and the Contract Manager role.
- The factors found in Commission rule 27.170 for identifying contracts deemed high risk and requiring enhanced monitoring are not being used.
- Commission rule 27.170 does not include required clauses found in Texas Government Code 2261.253 (c).
- The onsite monitoring process should be strengthened. Requirements regarding onsite monitoring are not part of the onsite monitoring process.
- Documentation requirements regarding the contract monitoring process is substantially lacking.
- The vendor performance reporting process should be strengthened. Vendor performance reporting participation should be required by all contract managers overseeing contracts that meet the monetary thresholds outlined in the State of Texas Procurement and Contract Management Guide.

The Contract Oversight team should implement a monitoring program that has well defined procedures and follow-up actions. Follow-up is essential, a problem will not correct itself simply by identifying it in a monitoring report.

Summary of Audit Objectives, Scope, and Methodology

The objective of this audit is to determine whether the Financial Resource Division has processes and related controls to help ensure the Contract Oversight function at the Public Utility Commission of Texas is conducted in accordance with applicable requirements and ensures reasonable confidence in the process. The scope of this audit included activities from September 2018 through April 2021. The audit methodology included a review of applicable laws, statutes, and division policy and procedures. It also included an analysis of current contracts, a review of entries in the database maintained by the Contract Oversight team, interviews, and a review of support documentation maintained by the oversight team.

Detailed Results

Chapter 1

The Contract Oversight Team Should Create Policies and Procedures

In a 2014 audit report it was recommended the Contract Oversight team should create policy and procedures to better facilitate the oversight function. Established policies, procedures, and documentation should provide guidance and training to ensure each division produces consistent performance and meets all requirements. Policies and procedures should be available at all levels of the Public Utility Commission.

Not having documented policies and procedures in place to guide the contract monitoring function has led to inadequate and inconsistent monitoring of contracts across the agency. This increases the risk that agency funds are not being spent appropriately or effectively.

Recommendation:

The Financial Resources Division should develop and implement formal policies and procedures for conducting contract monitoring activities. The policies and procedures should satisfy all requirements found in the State of Texas Procurement and Contract Management Guide.

Response from the Contract Oversight Administrator:

Agree

The Contract Oversight Administrator will be the point of contact and will update the policies and procedures within six months for more adequate and consistent monitoring of contracts across the agency.

Additional Information

The contract oversight team informally meets often with all agency contract managers to discuss monitoring and progression of their specific contracts. Additionally, the contract oversight team verifies all deliverables are received by the agency and appropriate payments are made to contractor.

Training for Contract Managers Should be Provided by the Oversight Team

In the 2014 contract audit, it was reported that staff assigned the Contract Manager role are not sufficiently trained for contract oversight even though they are responsible for monitoring all aspects of various contracts. Currently, staff assigned to contracts are not consistently trained for contract monitoring by the Contract Oversight team. There are no procedures outlining any specific training for those assigned the role of Contract Manager.

Several divisions are doing various levels of contract oversight with no clear strategy or approach. Without training from the Contract Oversight team, the monitoring activities done by the Contract Managers is lacking in meaningful, effective, and consistent oversight.

Recommendation:

The Contract Oversight team should develop a training program for everyone assigned the role of a Contract Manager. Training that aligns with monitoring requirements and best practices can be found in the State of Texas Procurement and Contract Guide and will provide Contract Managers with the knowledge and skills to understand their role in the contract monitoring process.

Response from the Contract Oversight Administrator:

Agree

The Contract Oversight Administrator will be the point of contact and will update the policies and procedures that align with monitoring requirements and best practices found in the State of Texas Procurement and Contract Guide within six months.

Additional Information

The contract oversight team informally meets with the contract manager about the responsibilities of managing the individual contracts.

Segregation of Duties between the Contract Oversight Role and The Contract Manager Role for Six Contracts

The purpose of the Contract Oversight Team is to act as an independent party, separate from daily contract managing activities. The Contract Oversight team is responsible for all aspects of the contract procurement process. This includes procurement planning, procurement method determination, vendor selection, contract formation and award, and overseeing the contract management process.

The contract manager is responsible for the day-to-day activities of the contract and ensures the services contracted for are being delivered. The segregation of duties between the contract oversight team and the contract managers is a good control if the roles are not intermingled.

Currently, the oversight team is also the contract manager for six out of fifteen contracts reviewed. The six contracts are valued at over \$37.8 million, or approximately 53% of the total contract dollars identified during testing. Intermingling the roles of contract oversight and contract manager defeats the control put in place to segregate the job functions. This is a breakdown in the control put in place by the agency.

By overriding the control, there is also a risk of a conflict of interest during the procurement process. A conflict of interest can create the appearance of impropriety that can undermine confidence in the Contract Oversight function even if no unethical or improper act results. There is no documentation found within these contracts or the procurement process acknowledging this conflict. There are no written policies or procedures within the Financial Resources Division providing a clear picture of how the oversight team is managing this dual role and maintaining its independence and segregation of duties.

Recommendation:

The control structure providing a segregation of duties between the Contract Oversight team and the Contract Manager role should be followed. Management should review this control and determine if any changes should be made concerning the dual role of Contract Oversight and Contract Manager. The division should create policy and procedures explaining how any conflict of interest or lack of segregation of duties is managed within this dual role if the agency continues with this approach.

Response from the Contract Oversight Administrator:

Agree

The Contract Oversight Administrator will be the point of contact and will update the policies and procedures as it relates to internal control when one of the contract oversight team is also the contract manager. This will be implemented within six months.

The contract oversight team consists of two FTE's and understands the auditor's concern with regards to our internal controls. Both FTE's on the contract oversight team are Certified Texas Contract Managers and Certified Texas Contract Developers. When one of the contract oversight team members is the contract manager, the other team member verifies and double checks the deliverables, thus mitigating any optics of impropriety. While this is a difficult area to comply with for most small/mid-size state agencies that have limited staff to complete the various tasks of the agency contract oversight, we will continue to ensure our internal controls are adequate to prevent any fiscal misconduct.

Criteria in Commission Rule 27.170 used for Identifying Contracts Requiring Enhanced Monitoring Should be Followed

Agencies are required to establish by rule a procedure to identify each contract that requires enhanced contract or performance monitoring. According to The State of Texas Procurement and Contract Management Guide, agencies are required to utilize an enhanced monitoring method for high dollar and high-risk contracts.

Enhanced monitoring is an increased level of monitoring, beyond the regular monitoring normally used. Such increased monitoring may include, but is not limited to, the following: frequency of site visits, contractor meetings, and documentation requirements deemed necessary by the agency to assess progress of the contractor toward meeting the identified goals and outcomes established in response to assessments of unsatisfactory performance.

The agency has established the rule required by legislation; however, the oversight team is not using the criteria established by rule to identify contracts deemed high risk. Only one out of the five factors in rule 27.170 is being used to identify contracts that require enhanced monitoring. There are no policies and procedures within the oversight group explaining how to identify contracts needing enhanced monitoring or what the procedures for monitoring enhanced contracts will be.

Recommendation:

The Fiscal Division should create policy and procedures that include the factors found in commission rule 27.170 to identify contracts that require enhanced monitoring. The procedures should also include a plan for monitoring contracts deemed high risk.

Response from the Contract Oversight Administrator:

Agree

The Contract Oversight Administrator will be the point of contact and will update the policies and procedures that include the factors found in commission rule 27.170 to identify contracts that require enhanced monitoring within six months.

The contract oversight team considers all agency contracts as enhanced contracts. All contract deliverables are verified by the contract manager and a member of the contract oversight team.

Commission Rule 27.170 does not satisfy Requirements Found in Statute Regarding Enhanced Monitoring

Commission rule 27.170 does not satisfy the requirements found in Texas Government code 2261.253(c). Specifically, there is no clause in the commission rule requiring the agency's contract management office to submit information to the agency's governing body regarding contracts requiring enhanced monitoring. This is a control designed by the Texas Legislature to provide additional oversight for contracts deemed high risk. The commission rule does include a clause that requires the fiscal division director to notify agency executive staff of contracts needing enhanced monitoring, however it is unclear how this is being done and this does not meet the requirement found in Texas Government Code 2261.253 (c) regarding enhanced contract and performance monitoring.

Recommendation:

The Fiscal Division should develop a commission rule that includes all requirements found in Texas Government Code 2261.253-Required Posting of Certain Contracts, Enhanced Contract and Performance Monitoring.

Response from the Contract Oversight Administrator:

Agreed

The Contract Oversight Administrator will be the point of contact and will work with the legal department to update the commission rule that includes all requirements found in Texas Government Code 2261.253, "Required Posting of Certain Contracts; Enhanced Contract and Performance Monitoring" as soon as possible.

Onsite Monitoring Visits Should be Strengthened

There is not a process in place to evaluate or identify contractors that may require site visits. The Contract Oversight group has chosen to do site visits for the same contractor year after year while omitting others requiring enhanced monitoring. In addition, the site visits completed at this contractor's facilities are not being conducted in accordance with state requirements or best practices. There are no summary reports or deliverables created by the oversight division documenting issues or potential issues. All onsite monitoring reports are completed by the contractor. The contractor also creates the agenda outlining which areas will be reviewed. The oversight group reviews the agenda and the summary report created by the contractor.

According to the State of Texas Procurement and Contract Management Guide, more complex contracts and any contracts that the agency perceives as having a higher degree of risk may require both desk reviews and visits to the contractor's facilities to ensure progress is in accordance with the contract schedule. Site visits may be used to verify actual performance against scheduled or reported performance. These visits can be an opportunity to verify that the contractor is dedicating sufficient resources and appropriate personnel to the contract.

Recommendation:

Onsite monitoring can be an effective tool but should include a plan, tests, reviews, and reporting of what was found as well as a plan for follow up on noted issues. All plans, tests, reviews, and documentation should be completed by the oversight division or contract manager, not the contractor.

To perform a site visit, the agency must develop a comprehensive site monitoring checklist that outlines the contract compliance requirements. The site monitoring checklist should be tailored for each contract. While there may be standard items that the agency will review for all contractors, each contract should be reviewed for specific site monitoring requirements that are unique to the contract and the Contract Manager or Oversight team should document findings from the site visit in a site monitoring report.

Upon completion of a site visit, the Contract Manager or Oversight team must complete a standalone document that serves as a record of the site monitoring work. A copy of the site monitoring report should be sent to the contractor and any others who may benefit from the report. Additional follow-up procedures for identified issues should be included in the monitoring process.

The State of Texas Procurement and Contract Management Guide regarding site visits should be reviewed and policies and procedures regarding site visits should be created by the division. In addition, the contract oversight group should develop risk criteria to identify high risk contractors where onsite visits are necessary. If the current contractor that is visited annually does not have issues, or is being monitored using other effective means, the site visits may not be the best use of agency funds.

Response from the Contract Oversight Administrator:

Agree

The Contract Oversight Administrator will be the point of contact and will update the policy and procedures as it relates to onsite contract monitoring within six months.

The agency will review all current contracts and determine by procedure how to best address the onsite monitoring if warranted.

There is an Overall Lack of Documentation

It was difficult to determine the effectiveness of the Contract Oversight function due to a lack of required documentation. Testing included interviews with various contract managers. All contract managers reported the oversight group provides support when there are issues with contracts. The oversight group is participating in the contracting process and resolving issues presented by the contract managers. However, these are usually informal meetings and documentation of issues and how they were resolved is not being done.

Documentation of contractor performance is an essential part of the contract oversight function. Telephone calls and meetings must be substantiated in writing and maintained as part of the procurement file. Such documentation must include the date and time that phone calls or meetings occurred as well as a summary of topics discussed (e.g., meeting minutes) including pending action items and decisions that were made. The documentation should include the final disposition of all issues related to a contract. Without documentation of contract issues, it is difficult to evaluate the performance of contractors. It also prevents the contract oversight function from consistently making improvements to the contracting process.

Recommendation:

The Financial Resource Division should review the State of Texas Procurement and Contract Management Guide and create policy and procedures that ensure all documentation requirements for contract management are being met.

Response from the Contract Oversight Administrator:

Agreed

The Contract Oversight Administrator will be the point of contact and is working with the IT division to create a database which captures the required information per the State of Texas Procurement and Contract Management Guide. The database will include the date and time of the calls or meetings, summary of topics discussed, pending action items, and decisions that were made.

Vendor Performance Reporting Should be Strengthened

Vendor performance reports have not been a part of the contract oversight process in the past and has been an issue communicated to the contract oversight group in previous audits. The oversight group recently began the process of requiring contract managers to complete vendor performance reports. Not all vendor performance reports had been completed at the time of testing.

The State of Texas Procurement and Contract Management Guide requires agencies to report vendor performance using the Vendor Performance Tracking System (VPTS) maintained by Statewide Procurement Division. Accurately reporting contractor performance allows agencies to share vendor information and facilitates better oversight of state contracts (e.g., aid in identifying vendors that have exceptional performance, protect the State from vendors with unethical business practices).

Recommendation:

This is a new process at the agency and should be strengthened by reviewing all requirements found in the State of Texas Procurement and Contract Management Guide. In addition, this process should be included in the policies and procedures regarding contract management. It is statutorily required yearly and when certain milestones within the contract are met if the value is over \$5 million. Otherwise, contracts with values greater than \$25,000 only need to be done at the end of the contract or upon contract termination.

Response from the Contract Oversight Administrator:

Agree

The Contract Oversight Administrator will be the point of contact and will update the policies and procedures related to vendor performance as found in the State of Texas Procurement and Contract Management Guide within six months.

The contract oversight team has been receiving vendor performance reports for all contracts semi-annually for the past 1 ½ year's regardless of the contract amount. Additionally, as part of the contract closeout, a vendor performance report is completed.

Appendix

Objectives, Scope, and Methodology

Objective

The objective of this audit is to determine whether the Financial Resource Division has processes and related controls to help ensure the Contract Oversight function at the Public Utility Commission of Texas is conducted in accordance with applicable requirements and ensures reasonable confidence in the process.

Scope

The scope of this audit included activities from September 1, 2018, through April 2021.

Methodology

The audit methodology included a review of applicable laws, statutes, and division policy and procedures. It also included an analysis of current contracts, a review of entries in the database maintained by the Contract Oversight team, interviews, and a review of support documentation maintained by the oversight team.

Sampling Methodology

Sampling was done using nonstatistical samples from databases, spreadsheets, and all means of data collection used for contract oversight included in the scope of this audit. The samples were used to determine if controls were operating effectively.

Information collected and reviewed includes:

- Contract details maintained in the contract database.
- Supporting documentation maintained by the contract oversight team.
- Previous audits concerning the contracting process at the PUC.

Testing

Testing included the following:

- Interviewed contract oversight personnel and contract managers.
- Reviewed contracts and related monitoring activities.
- The process for identifying contracts requiring enhanced monitoring.
- Reviewed the quality assessment process.

The criteria used during the audit was:

- Texas Government Code § 2261-State Contracting Standards and Oversight

- Commission Rule 27.170-Enhanced Contract Monitoring
- State of Texas Procurement and Contract Management Guide version 1.3
- Agency policies and procedures if available.

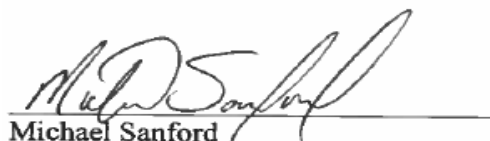
Project Information

Audit fieldwork was conducted from May 2021 through June 2021. This was a performance audit conducted in accordance with Generally Accepted Government Auditing Standards. Internal Audit believes that the evidence obtained provides a reasonable basis for the conclusions based on the audit objectives.

PUBLIC UTILITY COMMISSION OF TEXAS

Internal Audit Project #2021-100

February 2021



Michael Sanford
Internal Auditor, Public Utility Commission

This report has been provided to the following:

Mr. Peter Lake, Chairman, Public Utility Commission
Mr. Will McAdams, Commissioner, Public Utility Commission
Ms. Lori Cobos, Commissioner, Public Utility Commission
Mr. Thomas Gleeson, Executive Director, Public Utility Commission

Copies of this report have been distributed to the following in accordance with Government Code §2102.0091:

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