

Presented To:	Audit Committee
Presented:	Tuesday, Jun 17, 2014
Report Date	Thursday, Jun 12, 2014
Type:	Presentations

Request for Decision

Audit Report - Competitive Procurement

Recommendation

THAT the City of Greater Sudbury received the report dated June 11, 2014 for information only;

AND THAT the action plans identified in this report be recommended for approval.

Signed By

Auditor General
Brian Bigger
Auditor General
Digitally Signed Jun 12, 14

SUMMARY

Objectives

The objectives of this audit were to evaluate if:

- a) Competitive Procurement activities are being administered in accordance with Finance Services strategy, plans and objectives.
- b) Current internal controls and independent monitoring provided by Supplies and Services are effectively designed and operating to provide assurance that Procurement Objectives outlined in the Purchasing By-Law (2006-270) are achieved by Operating Departments; and
- c) Risks to the City arising from contracts, agreements and commitments are being managed and maintained at acceptable levels.

Background

The City's procurement objectives stated in the Purchasing By-Law (2006-270) are:

- a) *To encourage competition among suppliers;*
- b) *To maximize savings for taxpayers;*
- c) *To ensure service and product delivery, quality, efficiency and effectiveness;*
- d) *To ensure fairness among bidders; and*
- e) *To ensure openness, accountability and transparency while protecting the financial best interests of the City of Greater Sudbury.*

In 2001 the City acquired and rolled out the PeopleSoft finance system. However, thirteen years later, the Auditors found that only 12% of the procurement transactions over \$1500, (25% of the dollar value), are being processed using PeopleSoft. Such underutilization of automated features of a system designed to facilitate compliance with By-Laws, management and monitoring of purchases increases the risk of inadequate monitoring and failure to initiate timely corrective action.

Finance Services strategies, objectives and goals continue to refer to the need for the CGS-wide development and use of PeopleSoft finance system functionality and foundational elements.

Finance Services has identified areas where improvements to internal controls and business processes are required, which are aligned with the Auditor General's opportunities noted in this audit. Action Plans to address these improvements have been reflected in the Finance Strategic Plan and other reports to City Council. For example, Council recently approved a new Purchasing By-Law in February 2014, and in September 2013, a Procurement Contract Administration Policy was approved. These two key policy documents, coupled with management's plans to expand the use of the PeopleSoft system, will improve the framework of internal controls, once implemented over the next few years.

Finance Services have been working on the foundational pieces to improve the City's procure to pay cycle. These foundational pieces include: Purchasing By-Law, business process review / policy development and expansion of PeopleSoft functionality. Once the foundational pieces are complete, and resources are identified in operating departments, Finance had stated that they do plan to amend City policies to make the use of electronic purchase orders mandatory. This strategy has been verbally communicated to the AG, documented in various reports to City Council, and in the Finance Strategic Plan.

Scope

The scope of the audit included:

- PeopleSoft transaction records for the period January 2011 to August 2013 and covered Procurement systems and practices, Policies and Procedures, Purchase Orders issued, Contract Management processes, Vendor Management practices, Blanket Orders, and payments. Records relating to public communication of RFQ, RFI, RFT, RFP, Pre-qualifications, and their results were also included in the review.
- Competitive procurement processes encompassing activities leading to, and pertaining to the acquisition of Materials, Operating Expenses, Equipment Expenses, Purchased/Contract Services. Our focus was on the management and monitoring of competitive procurement activities relating to contracts and agreements provided by Supplies and Services (Purchasing) Division of the Finance Services Department.
- Reviewing records and interviewing select personnel from Accounts Payable, Information Technology and other operating departments.
- Evaluation and assessment of internal control structure (policies and procedures, staff skills, internal reporting and performance measures) with procurement objectives identified by management with the Purchasing By-Law 2006-270.
- Comparison of CGS procurement practices against principles established within the COSO Internal Control – Integrated Framework^[1].
- Our professional standards also required us to consider the possibility of fraud or abuse. Accordingly, we assessed existence and control weaknesses for fraud or abuse.
- We conducted our review in accordance with Generally Accepted Government Auditing Standards (GAGAS). Those standards require that we adequately plan for the audit; properly supervise audit staff; obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions; and prepare audit documentation related to the planning, conducting, and reporting for each audit. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit.

Report Highlights

In conducting the audit, the Auditor General's office has referenced widely accepted frameworks such as the IIA'S "Three Lines Of Defense" for evaluations of governance, risk management and control, and COSO's "Integrated Framework Of Internal Control".

The line of defense most likely to benefit from CGS-wide development and use of PeopleSoft finance system functionality would be centralized finance oversight and monitoring of procurement activities.

According to COSO, "Internal control is broadly defined as a process, effected by an entity's board of directors^[2], management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following three categories: effectiveness and efficiency of operations, reliability of financial reporting and compliance with applicable laws and regulations." COSO considers these categories to be overlapping, yet distinct. The effectiveness of an internal control system is measured by its capacity to provide reasonable assurance to the City Council and management that these three objectives have been met.

COSO identified five interrelated components of internal control.

- 1) The control environment, which includes the integrity, ethical values, and competence of an organization's people.
- 2) Risk assessment.
- 3) Control activities.
- 4) Information and communication, which encompasses the methods for identifying, capturing, and communicating pertinent information in a time frame that enables people to carry out their responsibilities, and
- 5) Monitoring, and oversight.

These components combine to form an integrated system of controls.

To conclude that internal control is effective in any category of objectives; Operations, Financial Reporting, or Compliance, all five components must be present and functioning effectively.

The Auditor General noted:

- A risk of continued slippage in the completion of the planned roll out of foundational pieces to improve the City's procure to pay cycle.
- The need to clean up and improve the administration of Blanket Purchase Order Agreements.
- The need to improve methods used to estimate and report on the value of awarded contracts on the City's website.
- The need to improve use of functionality, features and automated controls in PeopleSoft by replacing manual controls currently being used Citywide.
- The need to improve oversight and monitoring of all purchases through independent spend analysis.
- The need to improve accountability through performance measures in relation to procurement.
- The need to improve the current staffing approach to provide for succession planning and staffing key positions in purchasing.

The full audit report is attached to this agenda. For further information regarding this report, please contact Brian Bigger at extension 4402 or via email at brian.bigger@greatersudbury.ca

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Competitive Procurement

June 12, 2014
FINAL REPORT



SUMMARY

Objectives

The objectives of this audit were to evaluate if:

- a) Competitive Procurement activities are being administered in accordance with Finance Services strategy, plans and objectives.
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The City's procurement objectives stated in the Purchasing By-Law (2006-270) are:

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In 2001 the City acquired and rolled out the PeopleSoft finance system. However, thirteen years later, the Auditors found that only 12% of the procurement transactions over \$1500, (25% of the dollar value), are being processed using PeopleSoft. Such underutilization of automated features of a system designed to facilitate compliance with By-Laws, management and monitoring of purchases increases the risk of inadequate monitoring and failure to initiate timely corrective action.

Finance Services strategies, objectives and goals continue to refer to the need for the CGS-wide development and use of PeopleSoft finance system functionality and foundational elements.

Finance Services has identified areas where improvements to internal controls and business processes are required, which are aligned with the Auditor General's opportunities noted in this audit. Action Plans to address these improvements have been reflected in the Finance Strategic Plan and other reports to City Council. For example, Council recently approved a new Purchasing By-Law in February 2014, and in September 2013, a Procurement Contract Administration Policy was approved. These two key policy documents, coupled with management's plans to expand the use of the PeopleSoft system, will improve the framework of internal controls, once implemented over the next few years.

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- Reviewing records and interviewing select personnel from Accounts Payable, Information Technology and other operating departments.
- Evaluation and assessment of internal control structure (policies and procedures, staff skills, internal reporting and performance measures) with procurement objectives identified by management with the Purchasing By-Law 2006-270.
- Comparison of CGS procurement practices against principles established within the COSO Internal Control – Integrated Framework¹.
- Our professional standards also required us to consider the possibility of fraud or abuse. Accordingly, we assessed existence and control weaknesses for fraud or abuse.
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According to COSO, "Internal control is broadly defined as a process, effected by an entity's board of directors², management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following three categories: effectiveness and efficiency of operations, reliability of financial reporting and compliance with applicable laws and regulations." COSO considers these categories to be overlapping, yet distinct. The effectiveness of an internal control system is

¹ Committee Of Sponsoring Organizations for The Treadway Commission. (COSO 2013 - Internal Control — Integrated Framework)

² In the City's case, the Council

measured by its capacity to provide reasonable assurance to the City Council and management that these three objectives have been met.

COSO identified five interrelated components of internal control. 1) The control environment, which includes the integrity, ethical values, and competence of an organization's people. 2) Risk assessment. 3) Control activities. 4) Information and communication, which encompasses the methods for identifying, capturing, and communicating pertinent information in a time frame that enables people to carry out their responsibilities, and 5) Monitoring, and oversight. These components combine to form an integrated system of controls.

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The Auditor General noted:

- A risk of continued slippage in the completion of the planned roll out of foundational pieces to improve the City's procure to pay cycle.
- The need to clean up and improve the administration of Blanket Purchase Order Agreements.
- The need to improve methods used to estimate and report on the value of awarded contracts on the City's website.
- The need to improve use of functionality, features and automated controls in PeopleSoft by replacing manual controls currently being used Citywide.
- The need to improve oversight and monitoring of all purchases through independent spend analysis.
- The need to improve accountability through performance measures in relation to procurement.
- The need to improve the current staffing approach to provide for succession planning and staffing key positions in purchasing.

For further information regarding this report, please contact Brian Bigger at extension 4402 or via email at brian.bigger@greatersudbury.ca

Authored By: Lal Balkaran, FCGA, FCMA, CGMA, CIA and Brian Bigger, CGA, CRMA

OBSERVATIONS AND ACTION PLANS - 1

Achievement Of Purposes, Goals, And Objectives Of The Purchasing By-Law 2006-270

Observation

The auditors noted significant opportunities to improve competitive procurement oversight, monitoring and purchasing practices in the achievement of purposes, goals and objectives of the Purchasing By-Law 2006-270.

1.1 Blanket Purchase Orders

“BLANKET PURCHASE ORDERS (By-Law 2006-270)

12 (2) The Agent shall establish and maintain Blanket Purchase Orders.”

- Administration of Blanket Purchase Agreements is important, as they generally contain negotiated discounts and pricing specific to the City.
- During the audit, we noted that in 2012, and again in 2013 Finance staff had initiated a detailed review of Blanket Purchase Orders that needed further review and updating.
- At the first meeting in October 2013 between the auditors and management, management acknowledged that subsequent to their “clean up” in 2012, Finance had identified further blanket orders that required renewal and further clean up of their central records of blanket purchase orders.
- The audit confirmed existence of numerous agreements in Supplies and Service’s record of Blanket Purchase Order Agreements that were outdated and requiring maintenance and update.
- The status of the joint Finance, Senior Management Team and Operating Department Blanket Agreement Clean-up was provided to the auditors by Finance in October 2013.

A summary of management’s spreadsheets indicated the following:

Action	Number of records	Percent
Population of Blanket Purchase Orders	<u>318</u>	<u>100%</u>
Records removed/deleted	93	29%
Recommended for renewal	76	24%
Recommended for re-tendering	12	4%
Records Requiring Update	10	3%
Still under review (October 2013)	127	40%

- Additional audit testing of City expenditures indicated that an analysis of Operating Division Management’s spending would likely result in a significant increase to the above identified number of Blanket Purchase Orders.

1.2 Independent monitoring of expiry dates of Purchase Contracts

Finance Services does not maintain a centralized list of contracts with their expiration dates. Instead, reliance is placed on the operating departments. Maintenance of Contract records hold the key to

ensuring that competitive bid solicitations are initiated, and communicated to prospective bidders well before the expiration of the contract.

By placing reliance on manual systems and processes, there is a risk that existing vendors and suppliers may enjoy extension of contracts and continue to provide goods and services, contrary to City's procurement objectives.

Example – Illustrating An Impact Of Contracts Expired in 2011:

The Purchasing By-Law (2006-270) requires a competitive process to be initiated when more than \$35 thousand of expenditure is awarded.

- Contract IES06-20 Water/ Wastewater Treatment Chemicals expired on March 31, 2011. However, the City continued and paid 60 invoices between April 2011 and August 2013 totaling an amount of \$388 thousand referencing the expired contracts. No competitive bid was solicited by the City for this procurement over \$35 thousand as required by the Purchasing By-Law.
- Further, no exceptions were reported to Council, nor were Council requested to approve these continued contract extensions beyond their original expiry dates.
- A report should have been provided to Council, requesting approval for the continued contract extensions beyond the original contract expiry dates.

1.3 Opportunities to Improve Purchase/Tendering Practices

Example – Illustrating Small Volume Purchases Accumulating To A Larger Volume:

1. A vendor was awarded Road Maintenance work on a call by call basis.
 - Since the value of each "call" averaged under \$3 thousand, an opportunity to bid or quote on the work was not publicly advertised.
 - During the period of our audit review, 43 individual awards of work were purchased from this vendor (38 charged to the same department and account).
 - The value of work awarded added up to \$127 thousand.
 - No current blanket purchase order or open competitive RFT or RFP process was found.

Example – Illustrating Opportunity To Tender Larger Volume Purchases:

- 2) A vendor provides Tires and Tire repair Services to the City.
 - The total amount of Tires and Tire Repair Services purchased from this vendor exceeded \$590 thousand during the period of our audit review.
 - No current blanket purchase order or open competitive RFT or RFP process was found.

Example – Illustrating Opportunity To Tender Larger Volume Purchases:

- 3) Two key vendors provide HVAC and Mechanical Maintenance and Repair services for City facilities.

- Even though both the combined total acquisition costs for HVAC and Mechanical Maintenance and Repairs purchased from these two vendors exceeded \$4.1 million over our period of review, only \$1.1 million of purchases were in reference to a blanket order or contract.
- No current blanket purchase order or open competitive RFT or RFP process was found in Finance Purchasing central files for \$3.0 million or 3,871 of those transactions.

1.4 Inconsistent reporting of the value of contracts awarded

Auditors reviewed the City's Tenders and Results webpage for electronic advertising/announcements and found that methods used to estimate and report on the value of contracts on the City's website were inconsistent.

- Total Acquisition Cost descriptions examined by the auditor that were posted within the City's Tenders and Results webpage between January 2011 and August 2013 ranged from instances of:
 - No description of cost;
 - Unit Price only;
 - An Annual Contract Cost (reflecting a first year / annualized acquisition cost estimation based of the volume of work described in the tender specifications);
 - Total Contract award (reflecting only the first year / annualized acquisition cost based on the volume of work described in the tender specifications); and
 - Total Contract award (reflecting only the base term years acquisition cost based on the volume of work described in the tender specifications but excluding the cost of extension years).
- In only one case out of 337 over the last three years, did the advertisement accurately identify the Total Acquisition Cost reflecting the base term years acquisition cost based of the volume of work described in the tender specifications plus the cost of extension years. Ironically, this interpretation of Total Acquisition Cost was later reversed as a correction.
- "All Bid solicitations over \$35,000" was interpreted as:
 - A one-time expenditure expected to exceed \$35,000;
 - Annual expenditures expected to exceed \$35,000;
 - Responses to bid solicitations (based on hypothetical volumes) expected to exceed \$35,000;
 - Expenditures over the base term of the agreement (excludes extension terms) to exceed \$35,000; and,
 - Expenditures over the base term plus extension terms of the agreement expected to exceed \$35,000.

Quality Of Announcements On Tender Results Web Page (January 2011 to August 2013)		
Total Number Of Announcements	337	
Number Of Announcements With "Price" or "HST" Mentioned	337	100%
Number Of Announcements With "Term" of Contract Mentioned	4	1%
Number Of Announcements With Total Acquisition Cost Provided For Full Term of Award (Including Extensions)	1	0.25%
Number with Award Results But No Minutes	1	0.25%

- Since January 2011, only 4 out of 337 (1%), publicly communicated procurement announcements referred to the term of the contract being awarded.

1.5 Content of RFP/RFT announcements

The content of RFT and RFP public advertisements found on the City's Tender Results Web Page was inconsistent. The Auditors observed that transparency could be improved if the advertisements consistently provided the following information:

- Name of the vendor that the contract has been awarded to;
- Total estimated value of the award;
- The contract or reference number;
- The contract start date;
- The base contract end date;
- The end dates of any contract extensions;
- If the contract is similar to a previous contract;
- The contract or reference number of the previous contract; and
- The previous contract's end date.

1.6 Consistency of the City's conflict of interest rules.

- Conflicts of interest as described in the Purchasing By-Law (2006-270) were not as inclusive as the Municipal Conflicts Of Interest Act.

Business Impact

The City tracks and publicly reports on the "Benefit of The Tendering Process"³ through the annual Ontario Municipal Benchmark Initiative (OMBI). The measure describes the difference between the lowest bid and the second lowest bid when the City has used a formal tender process. This benefit of competitive procurement through a formal tender process has averaged around 10% since 2008 for the City. When independent oversight and monitoring through spend analysis does not exist, or is ineffective, the risk is that those benefits of a formal tendering process will be lost.

- When procurement opportunities are not communicated to prospective vendors on a timely basis, the existing vendors gain an unfair advantage. Such situations are comparable to absence of competitive procurement practices and should be discouraged by Senior Management and Council.
- When the procurement process is not in accordance with the Purchasing By-Law, the City's reputation and legal position may be at risk.
- The Finance Purchasing Division has recognized the need to re-establish their Blanket Purchase Order Agreement records, which at this point requires extensive manual research, going back to source documents.
- Blanket or Standing Order Agreements often contain special pricing and/or discounts. There is a great opportunity for the City to implement independent monitoring, validation and verification of pricing and discounts once Blanket Purchase Order (Standing Offer) Agreement records are re-established.

³ Refer to Appendix 1

- Due to the inconsistent wording of RFT / RFP tender results advertisements and reporting of contract award values (total acquisition values), the objective of transparency is not being met for all bidders (including prospective bidders).
- If organization policies regarding conflicts of interest are not consistently communicated and applied across the organization there may be confusion.

Management's Action Plans

1.1 Blanket Purchase Orders

- a) *As disclosed in the reports to City Council in April 2013 and January 2014, staff in Supplies and Services and the Operating Departments will continue the established work plan to complete the renewal process and ensure existing Blanket Orders are updated via competitive bid solicitations, where required. This work plan also included education to Authorized Employees about the changes to the Purchasing By-Law, and the use of spend analysis tools to identify competitive procurement opportunities. Timeline: On or before June 30th, 2015*

1.2 Independent Monitoring of expiry dates of Purchase Contracts

- b) *The Blanket Orders established under Contract IES06-20, for the purchase of Water/Wastewater Treatment Chemicals have been included in the renewal process as outlined above, and a report to City Council requesting approval for standardization and next steps for the issuance of the Tender will be completed before June 30th, 2015.*

The following is additional information regarding this Contract. Contract IES06-20 for Water/Wastewater Treatment Chemicals was awarded to 5 successful bidders for various chemicals on a per unit price and Blanket Orders were issued.

When Contract IES06-20 expired the City tendered Contract ISD11-6 "for the Supply and Delivery of Chemicals for the City of Greater Sudbury." There were 3 addenda issued. Bids were received from 12 Suppliers. The tender was complicated by issues such as truck sizes, delivery, trials and tests were required for the concentration of solutions and rust inhibitors. Clarifications were requested from a number of Suppliers and were not adequately provided. A decision was not reached before 90 days had lapsed, so the tender was canceled and no award was made.

Water and Waste Water Division management must be very cautious before deciding to change Suppliers, chemicals or concentrations that could affect the quality of the drinking water, to ensure compliance with Ministry regulations. The City continued to purchase the Chemicals from the existing Suppliers/Blanket Orders, in many cases with no or minimal increases to the unit prices.

- c) *The Supplies and Services Section does maintain a list of all Contracts in Excel, by department, by year, as well as a list of Blanket Orders. This information is available to all City staff, and stored in the Supplies and Services Section of City's internal website (City Links). Procedures were modified to ensure that the contract expiration date, or delivery date or substantial completion date is tracked in the excel spreadsheet, until the PeopleSoft functionality (or alternate solution) is developed.*

1.3 Opportunities to improve Purchase/Tendering Practices

- d) *Complete Blanket Order renewal process as outlined above.*
- e) *Implement the communication plan established to educate Authorized Persons in operating departments about the changes to the Purchasing By-Law, and more specifically the Annual Acquisition Cost, Total Acquisition Cost thresholds, and guidelines for the Quotation Process. Timeline : June 2014*
- f) *Review the PeopleSoft functionality to identify tools and develop the framework to assist with spend analysis. Timeline: June 2015*
- g) *Implementation of the Contract Renewal Form : To be rolled out July 1, 2014 with the implementation of By-Law 2014-01*

1.4 Inconsistent reporting of the value of contracts awarded and,

1.5 Content of RFP/RFT announcements

- h) *Supplies and Services will research the websites of other municipalities to determine best practices for the disclosure of the various types of Contract Awards (ie. Unit Price, Fixed Price, Cost Plus, and the disclosure may vary for the purchase of goods, services or construction). Subsequently procedures and updated templates will be developed to ensure consistency in the wording of CGS's Contract Awards and notification of bid solicitations on the City's website. Timeline: September 2014*
- i) *To enhance transparency and accountability, the Purchasing By-Law 2014-01 also included a new requirement for the Purchasing Agent to provide a report to City Council which summarized the contract awards greater than \$50,000. This report will also be posted on the City's website. Timeline: Completed; First Report will be provided in August 2014.*

1.6 Consistency of the City's conflict of interest rules

- j) *The Auditor General provided this feedback in September 2013 during the preparation of the Purchasing By-Law and By-Law 2014-01 includes amended language consistent with the Municipal Conflict of Interests Act. Status: Completed*

Management Comments

1.1 Blanket Orders

The City's Purchasing By-Law 2006-270 authorized the use of Blanket Order Contracts to be established to purchase repetitive Goods or Services for a specified period of time, when convenience and location are significant factors in determining Total Acquisition Cost and the quantity and demand are unknown. Two types of Blanket Orders existed:

- (1) Convenience/Location and Repetitive: where pricing is obtained and a maximum dollar limit per release is established. (Note: Many did not contain expiry dates)*
- (2) Repetitive Supplies/Services: Issued through a Tender/RFP Process*

During 2011 and 2012, staff in Supplies and Services cleaned up the inventory of Blanket Orders and deleted numerous Blanket Orders that were no longer required. During this review, management

identified that additional review, renewal and updating of many Blanket Orders was required. This was reported to City Council in two reports related to the updating of the Purchasing By-Law, in April 2013 and in January 2014.

As a result of management's review, in April 2013 Finance recommended changes to the Purchasing By-Law which would eliminate Blanket Orders, and that these contracts will be replaced with Standing Offers. The By-Law also clarified that total acquisition costs under the Standing Offers must comply with the procurement thresholds and other provisions of the By-Law.

Further, in January 2014, City Council approved the following resolution "That the City's existing Blanket Orders be maintained until they expire, and that any existing Blanket Orders requiring renewal be completed before June 30th, 2015.

1.3 Opportunities to improve Purchase/Tendering Practices

Management concurs with the AG's observation. Management's planned changes as communicated to City Council through the development of the revised Purchasing By-Law will increase opportunities for competitive procurement for low dollar value, repetitive purchases. However, for certain purchases in the AG's sample of transactions the quotation process was utilized by the Authorized Employee in accordance with the Purchasing By-Law 2006-270.

The Purchasing By-Law (2014-01) includes the use of Standing Offers as a tool to achieve purchasing efficiencies and increased competitive procurement for the low dollar value, repetitive purchases. The examples that the AG has provided are included in the Blanket Order renewal process, and will be replaced with Standing Offers, established competitively, where appropriate.

Action Plan Lead

Purchasing Agent and applicable Authorized Employees

Timing

The timing of the action plans are noted above.

OBSERVATIONS AND ACTION PLANS - 2

Optimum Use Of Investments Made In The PeopleSoft System.

Observation

2.1 City wide use of PeopleSoft

- The Auditors noted that Finance purchasing strategies, objectives and goals continue to refer to the need to develop and use foundational elements of PeopleSoft purchasing functionality. The City acquired and rolled out the PeopleSoft Finance system in 2001. This included the Purchasing Module.

- While business plans of the Finance division highlight the importance of City wide use of PeopleSoft functionality, there is a risk that implementation timelines may slip beyond the 2014 timeline established in the Finance Services Strategic Plan.

2.2 Reliance on manual systems and processes

- Currently, operating department staff place reliance on manual off-line processes and workarounds instead of using automated functionality and features of the PeopleSoft system.
- Auditors noted that such reliance on manual off-line purchase order processes has persisted for the past three years.
- Auditors estimated that 75% of dollars or 88% of transactions were supported by freeform references in description fields. Those references were to various forms of manual purchase orders and agreements.
- Only 25% of dollars or 12% of transactions were supported by a PeopleSoft Purchase Order.
- Greater use of electronic, PeopleSoft Purchase Orders could provide the basis for efficient, economical and effective oversight of procurement by management as suggested by the 2nd line of defense of “The Three Lines Of Defense Model”⁴.
- As was previously noted in examples listed in observation 1, this audit revealed significant internal control exceptions that could have been identified and remediated on a timely basis or reported to Council for approval, if automated functionality of PeopleSoft was used for all purchase orders.

2.3 Use of relevant defined fields in PeopleSoft

- Auditors noted that freeform references in description fields do not facilitate meaningful analysis and monitoring. Such inputs need to be made in appropriate fields defined for this purpose in PeopleSoft.

2.4 Internal control framework

- Application of an appropriate effective internal control framework over procurement activities may continue to be negatively impacted until all purchase orders across the City are issued from PeopleSoft.

2.5 Purchasing Activity Report (PARS)

- A manual Purchasing Activity Report (PARS) was developed by purchasing in 2010 as a tool to manage and track the work load of each Supplies and Services Coordinator.
- Our review of the PARS reports revealed that Supplies and Service’s manual records of contracts and blanket purchase agreements often did not contain contract expiration dates, name of the successful bidder, total acquisition costs and/or annual acquisition costs. In the absence of this critical information, effective management, tracking and projection of workloads for individual Supplies and Services Coordinators may be ineffective.

⁴ Refer to Appendix 2

2.6 Contract functionality

- In 2012, Finance informed staff that PeopleSoft Commitments Control would be implemented in 2013. In September 2013, the Finance Division reported to Council that the PeopleSoft Purchasing Contracts functionality had been implemented in 2012. However, during the audit, we noted that testing continued for certain contract types during fall of 2013 (e.g. notifications and progress payments).
- During the audit, we were advised that the PeopleSoft program still did not allow for all contracts to be entered (e.g., Revenue Bearing, Multiple Account #s, and Blanket Purchase Agreements)

Business Impact

- Reliance on manual processes by operating staff results in inconsistent application of controls by individual departments using various manual processes.
- The Finance Purchasing Division has recognized the need to re-establish their Blanket Purchase Order Agreement records, which at this point requires extensive manual research, going back to source documents.
- If City use of PeopleSoft Purchase Orders and Procurement Contract Functionality is not expanded, the City will not reap the benefits of its recent investments in PeopleSoft Commitment Control encumbrance system functionality and related reporting strategy.
- Management's current action plans indicate a risk of further timeline⁵.
- If PeopleSoft contracts, contract releases, purchase orders and purchase order releases do not include all procurement activity, the usefulness of the City's PeopleSoft Commitment Control encumbrance system functionality and related reporting strategy will be negatively impacted. Timelines identified in Finance's plan may not be achieved.

Management's Action Plans

Various reports to City Council and/or the Finance and Administration Committee, provided updates on the Finance Department's goals, action plans, and accomplishments, which are summarized in the department's Strategic Plan. More specifically, there are numerous action plans which have been identified to strengthen the City's Procure-To-Pay cycle. Goal #4 in the Finance Strategic Plan states: "Maximize the capabilities and opportunities provided by the financial information systems." To achieve this goal, a number of action items were identified and their status was summarized in the report to City Council in January 2014. The following is an extract of the action items and current status update:

- a) Implement and roll out the Commitment Control functionality in PeopleSoft: This functionality has been operational since February 2014. Roll out and training to Operating Departments will take place in June 2014.*

⁵ Supplies and Services advised the Auditors that they do not have the resources to go back to enter contracts earlier than August 2012. Purchases relating to roads, water, waste water and parks maintenance have largely been managed at the operating department level through the Municipal Maintenance Management System (MMMS), and are not expected to be migrated to PeopleSoft until the second phase of an implementation of a new work order system.

- b) *Expand the use of PeopleSoft Purchase Orders and implementation of recommendations from the Procure to Pay Process review. This is essential to ensure meaningful and reliable encumbrance data in Commitment Control. Timeline: On going*
- c) *Support IT in the development and roll out of Business Intelligence (BI) Reporting Strategy to replace ELinks. These financial reports will contain the Commitment Control encumbrances and pre encumbrances, where a PeopleSoft Purchase Order exists. Roll out and training to Operating Departments will take place in June 2014.*
- d) *Implement and roll out the Procurement Contract functionality in PeopleSoft. As reported to the Finance and Administration Committee in September 2013, challenges were discovered with the functionality and further resources and investigation is required before additional contracts can be entered. Finance has recently completed (in partnership with a PeopleSoft expert hired from Spyre Solutions Inc. the following reports:*
 - (i) *Business Process Review related to the CGS's use PeopleSoft Purchasing Module.*
 - (ii) *Solution Design Report to implement the PeopleSoft Procurement Contract functionality within the Purchasing Module*

Finance is in the process of hiring a temporary contract employee to implement the recommendations and business process changes recommended in these reports, which are required to enhance the City's use of the PeopleSoft Purchasing functionality.

Timeline: To be determined, since it is dependent on availability of resources, with the appropriate expertise.

It must be noted that if the Procurement Contract functionality does not meet the City's needs, Finance will work with IT to investigate options for a more robust Contract Management System.

- e) *Support the implementation of Cityworks, the City's Computerized Municipal Maintenance Management System. Phase 2 of this project includes the interface of PeopleSoft Purchasing and Accounts Payable. Timeline: 2015 to 2016*

Management Comment

The City has made progress on the foundational pieces to improve the City's procure to pay cycle. These foundational pieces include: Purchasing By-Law, business process review / policy development and expansion of PeopleSoft functionality. Once the foundational pieces are complete, and resources are identified in operating departments, management plans to amend City policies to make the use of electronic purchase orders mandatory. Managing the pace of change in the organization has been top of mind to the Chief Financial Officer, and Senior Management Team. The Finance Strategic plan outlined the required action items to achieve the goals, in a balanced approach, at a pace that the organization can manage with the resources it has.

The majority of the remaining Action Plans identified throughout this report, are only some examples of the initiatives that have been underway or completed to build the foundational pieces noted above.

Action Plan Lead

Manager of Accounting and Manager of Supplies and Services

Timing

The timing of the action plans are noted above.

OBSERVATIONS AND ACTION PLANS - 3

Monitoring And Oversight By Finance Over The Initiation Of Contracts, Agreements and Commitments.

Observation

3.1 Effects of manual monitoring processes

The following examples illustrate the need for effective monitoring and oversight of procurement by Finance as a second line of defense, and as part of an effective and integrated framework of internal controls for procurement.

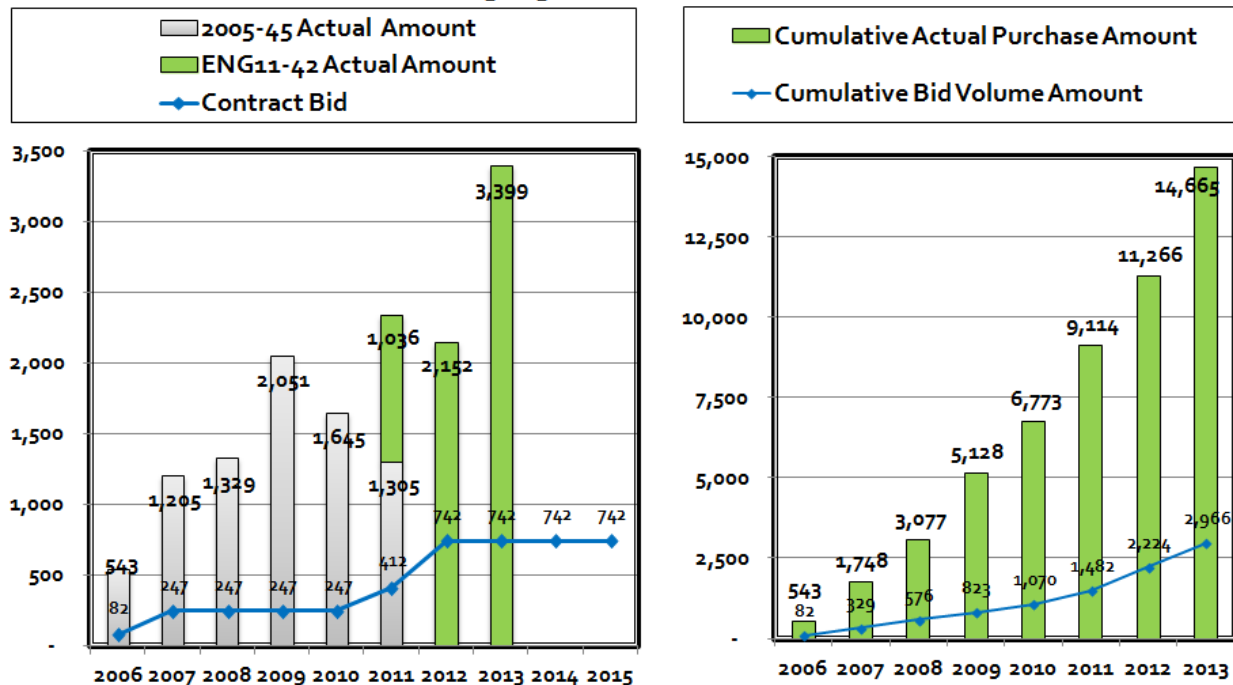
- In 2005, the City issued a tender for Water Main Repairs (the "2005 Tender"). The contract awarded was a unit price contract, but the evaluation was based on an annual estimate that was calculated by multiplying each unit price by the City's estimates of the quantities required. These estimated quantities were based on past volumes of water main repair work. The term of the contract was for three years with the option to extend the contract for two additional one year terms.
- The selected proponent, bid an estimated annual amount of \$247,437.
- The City extended the 2005 Tender contract for the full five years, during the term of which the City spent approximately \$8.1 million under the contract, which was over six times the original estimate bid by selected proponent.

Actual Expenditures Referring To Contract #2005-45		
Contract 2005-45		
Year	#Mths	Expenditures (000's)
2006	4	\$ 543
2007	12	\$ 1,205
2008	12	\$ 1,329
2009	12	\$ 2,051
2010	12	\$ 1,645
2011	8	\$ 1,305
5 YEAR TOTAL		\$ 8,078
YEARLY AVERAGE		\$ 1,616

- In 2011, when the 2005 Tender contract expired, the City put out a new tender for emergency water and waste water repairs (the "2011 Tender"). There were relatively minor variances in volume estimated as between the 2005 and the 2011 Tenders and these variances were inadequate to reflect the significant increases in actual volumes.
- Based on the increased quantities in the 2011 Tender, the amount of the annual estimate that was bid increased. The low bid in the 2011 Tender was again submitted by the same contractor at an estimated annual contract amount of \$740,550. Accordingly, the 2011 Tender contract was awarded to the same contractor. The length of the contract was again a three year term with two optional one year extensions.
- The other two bids submitted in response to the 2011 Tender came in at \$1,036,945 and \$1,381,016.

Actual Expenditures Referring To Contract ENG 11-42		
Contract ENG11-42		
Year	#Mths	Expenditures (000's)
2011	4	\$ 1,036
2012	12	\$ 2,152
2013	12	\$ 3,399
TOTAL		\$ 6,587
YEARLY AVERAGE		\$ 2,823

Contracts 2005-45 and ENG11-42 (\$ 000's)



Section 2 of Part II of the Purchasing By-Law sets out the City's purposes, goals and objectives with respect to its purchasing processes. The following principles are included within this section:

- (a) To encourage competition among suppliers;
- (b) To maximize savings for taxpayers;
- (d) To ensure fairness among bidders.

These principles align with general best practices for public sector procurement across Ontario. The question is whether the facts set out above meet these principles and best practices:

To maximize savings for taxpayers

- Management have stated that they were aware of the increases in contract costs and the annual budget was increased and/or reallocated. The City budget for these activities was doubled between 2008 and 2013.
- According to management, many factors influence the annual number of calls for service and resulting expenses for water and wastewater breaks, such as volumes, severity of the break and duration to repair service, location, weather and timing.
- Management has explained the City's contract cost increased as a result of two main factors.
 - a) Increased call volume of repairs due to aging infrastructure, and
 - b) Improved understanding of cost structure (developed in confirmation with Auditor General) which led to increased use of the Contractor during evening and overnight, especially for more severe breaks
- Management has assured the Auditor General's Office that the contractor has provided exceptional service in responding to the emergency infrastructure repairs requested by the City under the

contracts. Response times and quality of work have been excellent with a minimum impact to traffic and service disruptions.

- The above OMBI Value for the taxpayer is obtained, in large part, by ensuring the best price for services required by a public entity. Only by disclosing the full value of a contract would the City be able to ensure that it is obtaining best value and accordingly, it is not clear that this goal has been met with respect to the 2011 Tender.

To encourage competition among suppliers

- In order for there to be true competition as part of a competitive tender process, all information must be equally known by all bidders. In particular, any estimated quantities must be as accurate as possible in order to ensure fair opportunity to all bidders and that best value is offered by those bidders. Generally, the higher the volume of work that is estimated, the more competitive the rates a bidder will be willing to offer. Based on the information set out above, it appears that the full and accurate value of the work may not have been accurately disclosed in the 2011 Tender. It is possible that another competitor could have provided even more competitive rates had they known the true value of the total dollar spend under the contract.
- With respect to whether the City actually disclosed the full value of the possible work in the 2011 Tender, the Auditors General's Office is concerned that the total dollar spend exceeded the estimate based on the quantities disclosed in the tender by factors ranging from approximately twice as much (over 4 months in 2006) to nine times as much (in 2009). While minor increases above value estimates may be the norm when dealing with contracts with unknown quantities, these variances are clearly outside the acceptable norms for tendered contracts. Further, subject to a decrease between 2009 and 2010, the City's spend on the required services increased on an annual basis.
- While we acknowledge that there may be technical explanations for the increases in the estimated quantities that could factor into the ultimate analysis as to whether the City's estimated quantities in the 2011 Tender were reasonable and accurate, it appears that the City did not increase its anticipated estimated quantities sufficiently in the 2011 Tender to accurately reflect the anticipated spend on water main repair work.

To ensure fairness among bidders

- Finally, with respect to the goal of ensuring fairness to bidders, it would appear that the incumbent service provider, had access to information that other suppliers did not. That is, the incumbent service provider was aware of the actual amount spent by the City during the years of the 2005 Tender, including the trend towards significant annual increased spending in the area. The other bidders were only aware of the estimated quantities and the original estimated annual amounts tendered for the 2005 Tender. Full and equal disclosure of all relevant information, including volumes, is integral to a fair process and in this regard, this principle of the Purchasing By-Law may not have been met.
- We also note that Section 12(5) of the Purchasing By-Law provides as follows with respect to Blanket Purchase Orders: *"The expected quantity of the specified Goods, Services or Construction to be purchased over the time period of the agreement will be as accurate an estimate as practical and be based, to the greatest extent possible, on previous usage adjusted for any known factors."* Based on our observations above with respect to the significant increased spend between the 2005 and the 2011 Tender, it appears that the City's processes with respect to the 2011 Tender similarly may not have met this requirement of the Purchasing By-Law.

Business Impact

The establishment of effective, independent spending analysis, internal controls and monitoring to identify competitive procurement opportunities, will promote openness, transparency, accountability, fairness to bidders, and encourage competition in accordance with procurement objectives.

What is the benefit to the City when all bidders have access to the same information?

- Supplies and Services has reported “The Benefit Of Tendering Process” which is the difference between the lowest bids and second lowest bids on City tenders as an average of approximately 10% over the last five years (2008 to 2012).

Should the City decline to extend the 2011 Tender contract for the optional extension years and put the value of work out as a new tendering process?

Subject to any commitments already made to the incumbent, the City should consider not extending the existing 2011 Tender contract ENG11-42 for the optional extension years and retender its requirements for its emergency water main and waste water repair work.

- As set out above, given the fact that the estimated quantities were significantly lower than the actual spend, the current 2011 Tender contract may not represent the most accurate and competitive pricing available to the City and therefore could be a breach of the spirit of the City’s Purchasing By-Law. By retendering the value of work with updated estimates that accurately reflect the City’s anticipated spend on water main repair work, the City can assure adherence to the purposes, goals and objectives of its Purchasing By-Law.
- Now that the significant increased spending has been identified by the City, it should consider
 - a) establishing more accurate volume disclosure procedures and
 - b) mitigating against out of scope expenditures through the implementation of contract ceiling limits.

Management’s Action Plans

3.1 Effects of manual monitoring processes

3.1 Effects of manual monitoring processes

a) As noted above under observation #1.4 (pages 7 and 10), Supplies and Services will develop procedures to clarify and ensure consistency regarding the disclosure of Unit Price Contract awards posted on the City’s website.

Timeline: September 2014

b) Management will continue the action plans to increase the use of PeopleSoft Purchasing functionality, as outlined under the Action Plans for Observation #2. The work plans also include a review of the business processes related to procurement contract management for the various types of contracts/arrangements, such as, Standing Offers, Unit Price Contracts, Fixed Price Contracts. Timeline: To be determined, since it is dependent on available resources, with the appropriate expertise.

Compliance with the City's Purchasing By-Law

- c) *Contracts 2005-45 and ENG2011-42 are unit price contracts which were awarded after a competitive Tender, in accordance with the City's Purchasing By-Law. The estimated quantities in 2005 and 2011 were based on management's best estimates at that time. The term of Contract ENG2011-42 for Emergency Water and Wastewater repairs ends August 31, 2014, and the contract contains a renewal option to extend for 2 additional 1 year periods. The City will continue to follow the Purchasing By-Law 2014-01 Section 35 (4) regarding the Contract Extensions.*

Management Comments

Management believes that the issuance and award of these Tenders were in accordance with the Purchasing By-Law. Best and reasonable efforts were made to encourage competition, ensure fairness among bidders, and maximize savings for taxpayers. does not agree that the purchasing objectives were not met.

Action Plan Lead

Noted Above

Timing

Noted above

OBSERVATIONS AND ACTION PLANS - 4

Performance Measures To Enhance Accountability.

Observation

- Recent CGS trends indicate an increase in procurement costs, a decline in the number of bids per bid call, and a decline in the percentage of goods and services purchased through a competitive procurement process.⁶
- It is sound business practice for Management and Council to establish performance measures appropriate for responsibilities at all levels of the entity, reflecting appropriate dimensions of performance and expected standards of conduct, and considering the achievement of both short-term and longer-term objectives.
- Purchasing Metrics and Key Performance Measures are not fully in use to monitor the achievement of objectives for Procurement.
- Only a limited set of information for the Ontario Municipal Benchmarking Initiative or OMBI was prepared for 2011 and 2012.
- For the 2011 OMBI reported statistics, the annual number and \$ value of Purchase Orders awarded by Coordinators was reported.

Business Impact

- When the organization holds individuals accountable for their internal control responsibilities in the pursuit of objectives, there is a greater chance that the objectives will be achieved.

⁶ Source: OMBI (2013) measures reported in the 2014 budget book (Appendix 1)

- The lack of key metrics seriously impacts operations including the performance and productivity of Supplies and Services staff and reduces the effectiveness central purchasing support services.

Management's Action Plan

Supplies and Services will continue to participate in the OMBI Benchmarking Study, and explore opportunities with the OMBI expert panel to expand the number of measures.

Management Comment

None

Action Plan Lead

Manager of Supplies and Services

Timing

On-going

OBSERVATIONS AND ACTION PLANS - 5

Staff Development.

Observation

- Only the Manager, Supplies and Services, Purchasing Agent holds the Supply Chain Management Professional (SCMP) designation in the department. The SCMP is the highest achievement in the field and the mark of strategic chain leadership, administered by the Supply Chain Management Association (SCMA) which is the principal source of supply chain training, education and professional development.
- Staff members of Supplies and Services need to follow the annual SCMP CPD requirements to keep abreast with developments in the procurement profession, training which can help bring leading practices to discharge an effective procurement mandate.
- New staff members in the department should be encouraged to pursue the SCMP as they will be equipped with a technical certificate in purchasing which will professionalize the purchasing effort and bring best practices to the function and City operations.
- With Finance Services plans for major change to decentralized procurement processes through expanded use of PeopleSoft ERP purchase order, contract and commitments capabilities, there will be increased reliance on the capabilities of purchasing staff.

Business Impact

- Professional qualifications of purchasing staff may impact the success and achievement of Finance Services' objectives.
- The current staffing approach does not provide for succession planning and staffing key positions in purchasing.

Management's Action Plan

- Continue to provide training and professional development opportunities for the Supplies and Service staff.*
- Review the organizational structure in Supplies and Services and assess the sufficiency of the resources.*

Management Comment

No additional comments.

Action Plan Lead

Manager of Supplies and Services and Chief Financial Officer

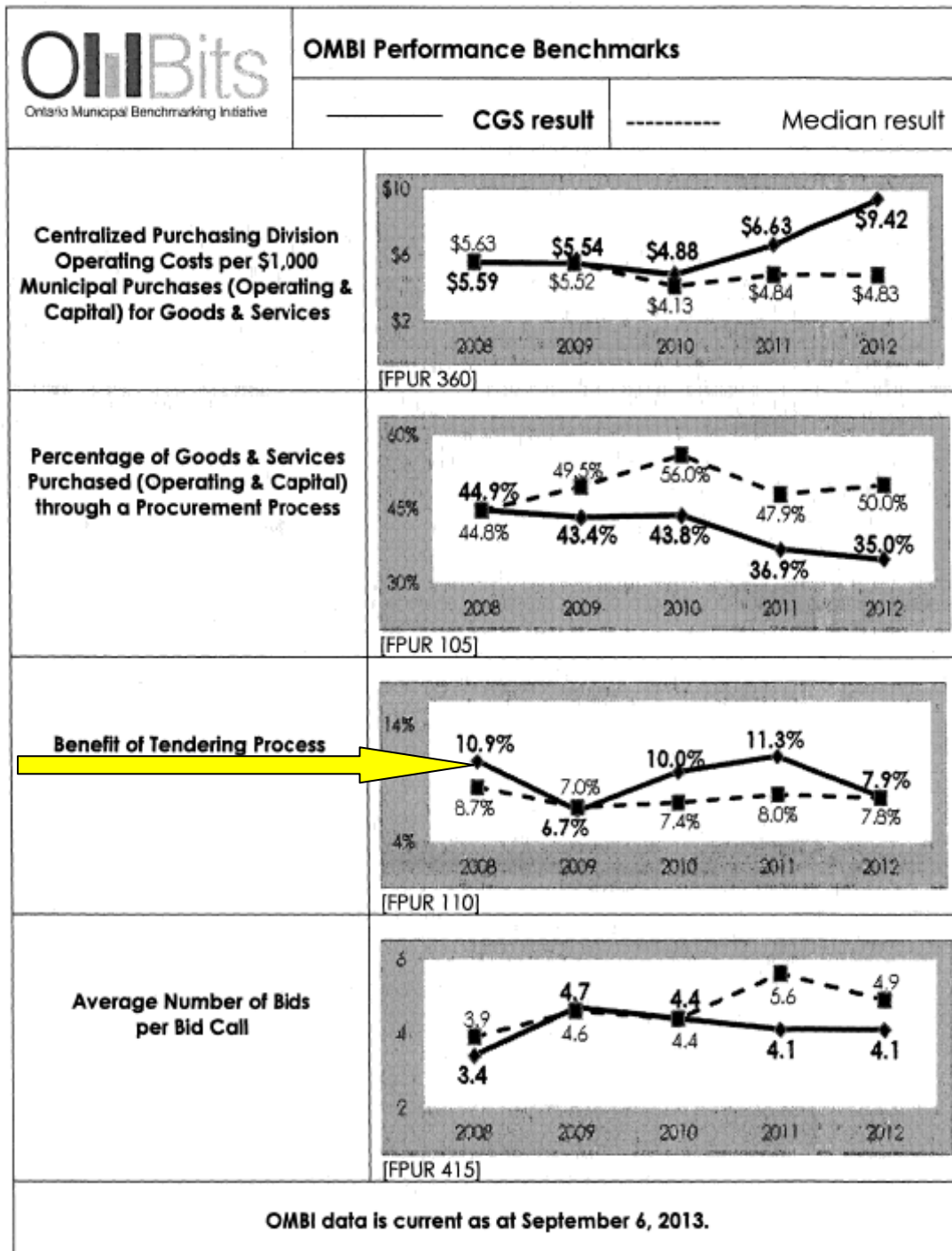
Timing

On going and 2014

APPENDIX - 1

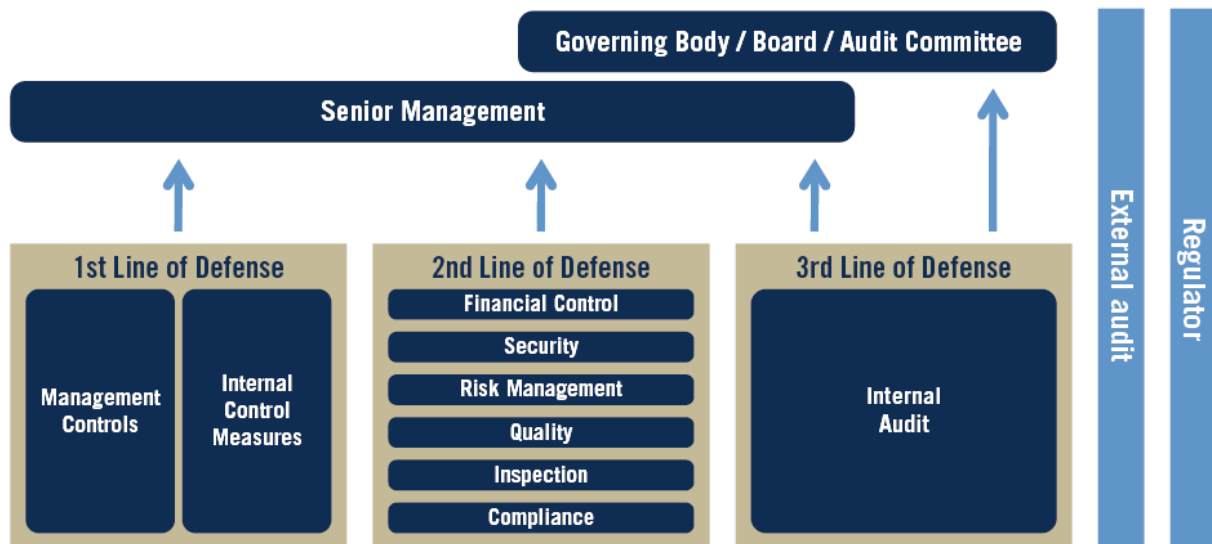
Supplies and Services Performance Measures

SUPPLIES AND SERVICES



APPENDIX - 2

The Three Lines of Defense Model



Adapted from ECIIA/FERMA *Guidance on the 8th EU Company Law Directive, article 41*

APPENDIX - 3

COSO – Integrated Framework Of Internal Controls

Relationship of Objectives and Components

A direct relationship exists between *objectives*, which are what an entity strives to achieve, *components*, which represent what is required to achieve the objectives, and the *organizational structure* of the entity (the operating units, legal entities, and other). The relationship can be depicted in the form of a cube.

- The three categories of objectives—operations, reporting, and compliance—are represented by the columns.
- The five components are represented by the rows.
- An entity's organizational structure is represented by the third dimension.

