

Date: December 22, 2020 File No.: 0105

To: Angela Shell, Deputy Director
Procurement Division
Department of General Services
707 3rd Street, 2nd Floor
West Sacramento, CA 95605

From: **Department of General Services**
Office of Audit Services

Subject: **Audit Report: Leveraged Procurement Agreement (LPA) Surcharge Fees**

Attached is the final report on our review of the systems of internal control maintained over the collection process of Leveraged Procurement Agreement (LPA) surcharge fees administered by the Procurement Division (PD). Our review was conducted in accordance with the International Standards for the Professional Practice of Internal Auditing.

The Procurement Division's written response to our draft report is included in this final report. The report also includes our evaluation of the response. We are pleased with the actions taken or proposed and commitments made to address our recommendations.

As part of its operating responsibilities, the Office of Audit Services is responsible for following up on audit recommendations. Therefore, please submit on your department's official letterhead a status report on the implementation of each recommendation to us by June 22, 2021.

The necessity of any further status reports will be determined at that time. Please transmit your status report to: DGS – Office of Audit Services, 707 3rd Street, 8th Floor, West Sacramento, CA 95605.

We greatly appreciated the cooperation and assistance provided by PD's personnel.

If you have any questions, please call me at (916) 376-5061, or Victoria LaTour, Management Auditor, at (916) 376-5053.

Gregg Gunderson

Gregg Gunderson, MBA, CIA, CISA
Audit Supervisor, Office of Audit Services

Angela Shell

December 22, 2020

Attachment

cc: Daniel C. Kim, Director
Andy Won, Deputy Director, Office of Audit Services
Carol Bangs, Branch Chief, Acquisitions Branch, PD
Reylina Ruiz, Branch Chief, Operations Branch, PD

**GOVERNMENT OPERATIONS AGENCY
DEPARTMENT OF GENERAL SERVICES**

**AUDIT OF THE
DEPARTMENT OF GENERAL
SERVICES**

**FOR COMPLIANCE WITH STATE
LEVERAGED PROCUREMENT AGREEMENT
SURCHARGE FEES
(REPORT NO. 0105)**

OFFICE OF AUDIT SERVICES

NOVEMBER 2020

**DEPARTMENT OF GENERAL SERVICES
LEVERAGED PROCUREMENT AGREEMENT SURCHARGE FEES
REPORT NO. 0105**

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From: **Department of General Services**
Office of Audit Services

Subject: Audit Report: Leveraged Procurement Agreement (LPA) Surcharge Fees

This summary represents the results of our review of the systems of internal controls maintained by the Department of General Services' Procurement Division (PD). The objective of this audit was limited to reviewing the operations, programs, functions and activities of the Procurement Division's Operations Branch (PD-OPS) for collecting Leveraged Procurement Agreement (LPA) surcharge fees. Specifically, we reviewed both PD-OPS LPA rate calculation methodology and its process for the billing and collection of LPA fees to determine the adequacy of PD's systems for collecting these fees. Our review was conducted in accordance with the International Standards for the Professional Practice of Internal Auditing.

Overall, we concluded that PD has established adequate and effective systems of operational control; however, we identified areas for improvement within programs administered by PD-OPS and the PD's Acquisitions Branch. Specifically, as discussed under the Review Results section of this report, PD-OPS is not adequately administering PD's system for collecting LPA fees. The proper administration of PD's system for collecting LPA fees is extremely important for identifying potential loss in LPA surcharge fee collections.

During our review we also identified another matter requiring attention that we discussed with PD's management but did not pose a significant risk to the program. Specifically, in our review of fifteen local usage transactions, we found two vehicle purchases where the local incentive fees were not collected in the amount of \$2,966. According to representatives of PD-Acquisitions, the fees had yet to be collected, since fees are collected only when the vehicles are delivered, and not at the time of purchase.

BACKGROUND

The Procurement Division (PD) is the state's central purchasing and material management agency, having overall responsibility for ensuring that the state's acquisition system is in compliance with statutory and regulatory requirements and sound business practices. Its mission is to provide effective leadership to deliver innovative procurement solutions enabling its customers to serve the people of California.

PD has identified the following as its core competencies: setting state procurement policies and providing purchasing services; delegating purchasing authority; certifying small and/or disabled veteran businesses to do business with the state; sponsoring the Small Business Council; participating in the Disabled Veterans Business Enterprise Council; and providing innovative purchasing methods that save taxpayers' dollars, integrating quality solutions to meet customers' needs.

Structurally, PD is overseen by a deputy director, and is made-up of five branches: Procurement Operations Branch, Acquisitions Branch, Certification and Outreach Branch, Engineering Branch, and Policy, Training and Customer Services Branch. PD has approximately 188 positions.

SCOPE

As the objective of the audit was the setting, billing and collection of LPA surcharge fees, we selected PD-OPS as the primary operation for review. In addition, we reviewed operational processes of the PD-Acquisitions Branch as it relates to the surcharge fees. Specifically, to ensure PD is recovering its costs of administering the LPA contracts, we reviewed PD-OPS methodology for calculating LPA surcharge fees and reviewed samples of transactions selected from LPA contractor listings for billing and collection. We also reviewed operational processes of both branches to ensure their processes relating to LPA surcharge fees are effective and efficient.

METHODOLOGY

To determine whether PD has an adequate and effective system of operational control, we performed a preliminary survey of its operations related to LPA surcharge fees. The results of this survey provided sufficient information to identify the previously discussed activities for in-depth testing during our audit fieldwork. Our review of these activities included the following:

- reviewing policies and procedures
- reviewing the LPA surcharge fees for fiscal year 2018/2019 to ensure the rate calculation methodology is recovering the costs of administering LPA contracts
- evaluating systems of internal control for setting, billing and collections of LPA surcharge fees
- conducting interviews of appropriate managers and staff
- performing analyses of management and billing and collection systems
- analyzing FI\$Cal and SCPRS data

- performing other tests as deemed necessary

REVIEW RESULTS

We concluded that PD has established adequate operating policies and procedures which provide reasonable assurance that fees are set to recover its costs of administering LPA contracts; collected on LPA purchases; processed properly and timely; reviewed and approved by appropriate levels of management; and supported by sufficient documents for state agency purchases.

However, we identified the following area for improvement in the processing of Leveraged Procurement Agreement surcharge fees. The recommendations presented are to aid management in improving systems of operational control.

COLLECTION OF LOCAL INCENTIVE FEES

PD-OPS and PD's Acquisitions Branch are currently not reconciling reported local entity purchases with the vendor's accounting records. Our review disclosed that PD cannot perform this reconciliation because it does not have access to the purchases made by local entities as it does with state agency purchases. Rather, PD's Acquisition Branch currently relies on the vendor/contractor to submit complete and accurate monthly or quarterly usage report for local purchases, and, in the case of the branch's Pharmaceutical Acquisitions Section, is not requiring vendors to even submit usage reports. Further, in the absence of complete and accurate monthly or quarterly usage reports for local purchases, the local incentive fee checks received by DGS are deposited without additional verification of local government purchases. Therefore, the state may not be collecting its fair share of local incentive fees.

Recommendation

1) Develop a process such as an online portal as a payment mechanism where local governments create a profile and customer account number to conduct their LPA purchases. The vendors will fulfill the local government purchases through the online portal and, after local incentive fees have been collected via the portal, receive payment for the products delivered to local governments.

This process will allow PD-OPS to directly collect incentive fees for LPA purchases made by local entities. In the interim, the PD's Acquisitions Branch, Pharmaceutical Acquisitions Section, should require vendors to submit usage reports.

OUTSTANDING RECEIVABLES

PD-OPS sets and bills for LPA fees; however, it is not following up on outstanding receivables from usage of the departments LPA agreements as required by SRF 1013-Collection Procedures. As of May 29, 2020, outstanding receivables of 120 days or more totaled \$52,300. Of the \$52,300, a total of 10 transactions in the amount of \$35,478 were outstanding over 546 days; 1 transaction of \$177 between 366-545 days; 1 transaction

of \$491 between 181-365 days and 4 transactions of \$16,153 between 120-135 days.

Recommendation

2) Develop, implement, and enforce written policies and procedures that ensure PD-OPS follow current SRF 1013-Collection Procedures.

RECONCILING USAGE REPORTS AGAINST FISCAL AND SCPRS SYSTEMS

PD-OPS has the responsibility of ensuring billing files are sent to the Office of Fiscal Services for invoicing of state agencies; however, because the process does not reconcile the usage reports against the FISCAL and SCPRS systems, the system does not address agencies that have not been previously charged.

We selected for review 33 purchase transactions from state agencies from usage reports for fiscal years 2018/2019 and 2019/2020. Of the 33 purchase transactions, ten (30%) of the purchases could not be found in FISCAL or SCPRS database systems. Further, PD-OPS does not have a process for follow-up on purchases not found in either database or for billing accordingly. As a result, these agencies were not billed an LPA surcharge fee for these transactions. The ten sampled transactions would have yielded a total of \$4,179 in LPA surcharge fees for DGS.

Recommendation

3) PD-OPS should develop, implement, and enforce written policies and procedures and work with the contract managers in the acquisition's branch to ensure full collection of LPA surcharge fees. Contract managers are responsible for ensuring usage reports are submitted by the contractor. However, we recommend an additional step to the process that will ensure that purchases reported on the usage reports are reconciled monthly with FISCAL and SCPRS. If a purchase is not identified in the FISCAL or SCPRS database systems, the contract manager should follow up with the vendor to obtain additional information to ensure the collection of any LPA surcharge fees.

CONCLUSION

The issues presented in this report should be addressed to assist in improving operational policies and procedures. We were pleased that when advised of areas for improvement during our audit fieldwork, PD-OPS management indicated that immediate action would be taken to address our concerns. This provides an indication of management's commitment to improving operational policies and procedures.

We greatly appreciated the cooperation and assistance provided by PD's personnel.

If you need further information or assistance on this report, please contact me at (916) 376-5061, or Victoria LaTour, Associate Management Auditor, Office of Audit Services, at (916) 376-5053.

Gregg Gunderson

Gregg Gunderson, MBA, CIA, CISA
Audit Supervisor
Office of Audit Services

Staff: Victoria LaTour, Associate Management Auditor
Christopher Harris, Associate Management Auditor, MPA

cc: Daniel C. Kim, Director
Andy Won, Deputy Director, Office of Audit Services
Carol Bangs, Branch Chief, Acquisitions Branch, PD
Reylina Ruiz, Branch Chief, Operations Branch, PD

December 7, 2020

Gregg Gunderson, MBA, CIA, CISA
Audit Supervisor
Office of Audit Services

**Audit Report: Leveraged Procurement Agreement (LPA) Surcharge Fees
File No. 0105**

The Procurement Division (PD) appreciates the opportunity to provide comments and address the recommendations outlined in the Office of Audit Services (OAS) Audit Report No. 0105. Please find our comments below in the response to the findings of the audit.

COLLECTION OF LOCAL INCENTIVE FEES

Recommendation 1

Develop a process such as an online portal as a payment mechanism where local governments create a profile and customer account number to conduct their LPA purchases. The vendors will fulfill the local government purchases through the online portal and, after local incentive fees have been collected via the portal, receive payment for the products delivered to local governments.

This process will allow PD-OPS to directly collect incentive fees for LPA purchases made by local entities. In the interim, the PD's Acquisitions Branch, Pharmaceutical Acquisitions Section, should require vendors to submit usage reports.

Response

PD agrees with the findings in part. PD has no authority over local agencies and will not be able to enforce payment collection. Once local governments create a PO and have the LPA information, they can conduct POs from the LPAs on their own, bypassing the system. Collecting the fee from the vendor allows PD to pull their contract if they do not pay. Remedies for non-payment would consist of requiring PD to bar non-paying locals from using LPAs and would impact economies of scale on those contracts and agreements. PD has created a portal to collect payment online from contractors, which will speed up the

payment process. Moving forward, PD will require usage reports in upcoming Pharmaceutical Acquisitions Section contracts.

OUTSTANDING RECIEVABLES

Recommendation 2

Develop, implement, and enforce written policies and procedures that ensure PD-OPS follow current SRF 1013-Collection Procedures.

Response

PD-OPS brought this issue to the DGS Revenue Generation Workgroup and DGS collection procedures as a whole are being evaluated within this group. PD-OPS will wait and follow the new policies and procedures that are established for DGS. PD-OPS is also working with OFS on changing its biggest debtor from a non-EFT to EFT CAN, which will alleviate the great majority of PD's outstanding invoices.

RECONCILING USAGE REPORTS AGAINST FI\$CAL AND SCPRS SYSTEMS

Recommendation 3

PD-OPS should develop, implement, and enforce written policies and procedures and work with the contract managers in the acquisition's branch to ensure full collection of LPA surcharge fees. Contract managers are responsible for ensuring usage reports are submitted by the contractor. However, we recommend an additional step to the process that will ensure that purchases reported on the usage reports are reconciled monthly with FI\$Cal and SCPRS. If a purchase is not identified in the FI\$Cal or SCPRS database systems, the contract manager should follow up with the vendor to obtain additional information to ensure the collection of any LPA surcharge fees.

Response

PD agrees in part. PD-OPS will continue to send the billing files to OFS and PD Acquisitions will intermittently audit LPA reports for this purpose.

If a purchase is identified in SCPRS but not in a usage report, the contract manager in the Acquisitions Branch would follow up with the contractor to ensure that information is being reported correctly. If a purchase is identified in a usage report but not in SCPRS, it is the department that has not been reporting correctly and would be referred to the Policy Branch to have the department correct their action.

If you need further information or assistance on this report, please contact me at (916) 375-4417, Carol Bangs, Branch Chief, Acquisitions Branch at (916) 375-4540 or Reyлина Ruiz, Branch Chief, PD Operations at (916) 375-4945.

Sincerely,

A handwritten signature in black ink that reads "Angela Shell". The signature is written in a cursive, flowing style.

ANGELA SHELL
Deputy Director, Procurement Division

cc: Daniel C. Kim, Director
Andy Won, Deputy Director, Office of Audit Services
Reyлина Ruiz, Branch Chief, Operations Branch, PD
Carol Bangs, Branch Chief, Acquisitions Branch, PD

**PROCUREMENT DIVISION
LEVERAGED PROCUREMENT AGREEMENT (LPA) SURCHARGE FEES**

EVALUATION OF PD'S RESPONSE

We have reviewed the response by the Procurement Division (PD) to our draft audit report. The response indicates that appropriate actions are being taken in addressing our recommendations except for the collection of local incentive fees. The current operational process poses a risk of not fully collecting local incentive fees that the state may be entitled to. PD should continue to find a method for minimizing this risk and create policy or procedures to ensure that the state is fully recovering local incentive fees it may be entitled to.

We appreciate the efforts taken or being taken by PD's personnel to improve operational controls. The promptness of these efforts continues to disclose their significant commitment to improving operating policies and procedures.