

The School District of Lee County



Procurement Audit A1-07

March 9, 2007

**Released by: School Board Audit Office
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PROCUREMENT AUDIT

I. EXECUTIVE SUMMARY

The School Board Audit Office has completed a “Procurement” audit to ascertain whether established internal controls are effective in ensuring consistent compliance to State and District regulations. This audit focused on operational and compliance issues regarding the Procurement process as it relates to the purchasing of goods and services needed for District operations and capital construction projects. The audit crossed over into many departments, including Accounting, Budget, Construction Services, Maintenance, and Procurement Services. Numerous audit hours were spent working with the Information Systems Analysts to design special reports from mainframe data in order to complete the audit process. These reports were invaluable in conducting the various audit analyses done to ascertain whether District procedural controls promoted and encouraged:

- Compliance with applicable procurement and bonding laws and regulations;
- Compliance with provisions of any related bid/contract;
- Reliability of recordkeeping and reporting; and the
- Economic, effective and efficient operations of the District.

In addition to utilizing the system generated data, the audit consisted of selecting a sample of transactions associated with the processes for: 1) vendor setup and change, 2) purchasing, 3) bidding, and 4) performance/payment bonding and liability insurance compliance.

The sample testing results found no signs of fraud or intentional disregard for established policies and procedures. The sample testing results did not find any violations where contracts (resulting from bids) had been issued prior to Board approval. The sample testing results did not find any intentional purchase splitting occurring. However, the audit results do identify twenty (20) audit findings related to weaknesses in procedural controls that affect the efficiency, effectiveness and compliance in operations. To mitigate these weaknesses, thirty-three (33) audit recommendations have been provided to District management as a means to strengthen internal controls and provide greater compliance to State and District laws and regulations.

The School Board Audit Office requested the Superintendent provide a written response/action plan that addressed each of the audit findings and recommendations. The official responses have addressed each recommendation presented in the report and specify whether the recommendation was:

- Accepted and implemented;
- Accepted with implementation pending;
- Under study; or
- Rejected with an explanation of why rejected.

At this time, the School Board Audit Office has accepted the Superintendent's responses/action plan with a condition that an audit follow-up would be conducted in the future to ensure the action plan items have been fully implemented.

As of March 8, 2007, 23 of 33 recommendations have been implemented; another four should be implemented by April 2007. There are two recommendations that should be implemented in FY2009 when the new ERP system is in place. The remaining four recommendations are either under study (3) or rejected (1).

In the case of the one "rejected" recommendation, the School Board Audit Office had recommended a post-processing review (by use of a system generated edit report) be performed by a Budget staff person not responsible for the vendor master file data entry. This was recommended in order to monitor vendor activity; especially frequent changes to any one vendor's address information which is a red flag for possible fraud. At the time this recommendation was made, the significant number of Budget personnel that had access to the Vendor Master file data entry screen was an audit concern and noted in another audit finding. The Budget Department has since reduced the number of employees to only those who need access, thus reducing the risk of unauthorized data entry capabilities. In addition, the Budget Department is now keeping supporting documentation to validate the vendor changes made on the system for longer period of time (another audit finding & recommendation). Although the Budget Department has strengthened their mitigating controls, the School Board Audit Office advises that monitoring through the system should still be considered as a fraud deterrent measure.

The following is a summary of the March 9, 2007 - Procurement Audit Report's findings, recommendations, and management responses for each respective segment of the audit: 1) vendor setup and change, 2) purchasing, 3) bidding, and 4) performance/payment bonding and liability insurance compliance.

Vendor Setup and Changes

Findings: Six

Recommendations: Twelve

Management Responses: Twelve

The audit findings and recommendations are related to system limitations of the current District's information system or weaknesses in established procedures regarding: access, approval, and data entry controls.

Purchasing Process

Findings: Two

Recommendations: Four

Management Responses: Four

The audit findings and recommendations are related to system limitations of the current District's information system and weaknesses in established monitoring procedures.

Bidding Process

Findings: Four

Recommendations: Four

Management Responses: Four

The audit did not find any violations where contracts (resulting from bids) had been issued prior to Board approval. The audit did not find any intentional purchase splitting occurring. The audit findings and recommendations are related to weaknesses regarding: lack of written departmental procedures for monitoring liability insurance coverage and renewal of contracts, and file maintenance procedures.

Construction Contracts

Findings: Eight (2 – Payment Process) (6 – Compliance)

Recommendations: Thirteen (4 – Payment Process) (9 – Compliance)

Management Responses: Thirteen (4 – Payment Process) (9 – Compliance)

The audit findings and recommendations are related to system limitations of the School District's current accounts payable system, lack of written procedural documentation, weak monitoring procedures related to bonding and insurance requirements compliance, and lack of post construction audits corrective steps taken.

As the audit results indicate, many of the audit findings and recommendations are related to limitations of the current District's mainframe information system. These system limitations should be addressed in the new ERP system design. However, until the new system is implemented, the current District procurement practices should be enhanced with additional procedural and monitoring controls in order to maximize efficiencies, effectiveness and keep risk exposure to a minimum.

At this time, the School Board Audit Office would like to thank the District staff who gave their time, insight, and cooperation during the audit process to diligently address these audit issues in a timely and professional manner. In addition, the Information Systems Department Program Analysts that assisted the Audit Office in extracting data from the mainframe and providing it in Access format should be commended for their promptness and thoroughness in providing this much needed data. These reports were invaluable in conducting the various audit analyses done to ascertain whether District procurement controls and procedures were effectively working.

Strategic Plan VIII: We will create an organizational design to achieve our mission and objectives.

The mission of the School Board Audit Office is to help ensure LCSD manages all risks, including financial, operating, and other business risk, by measuring and evaluating the effectiveness of financial and managerial controls and recommending enhancements or corrective actions as needed.

The following attached report is a detail of the audit findings, recommendations and management responses that address where enhancements have been or will be made to increase operational efficiency, effectiveness and compliance to State and District laws and regulations.

II. INTRODUCTION

The objective of the procurement function is to ensure that the District receives the needed quality and quantity of supplies, materials, equipment, and general services at the least expense. All District employees are responsible for compliance with the “Purchasing and Bidding” Policy: 4.44 (**new policy 6.07**); the “Advertising, Contracting, and Bidding” Policy: 4.45 (**new policy # 6.09**) and “Change Orders” Policy 4.42 (**new policy 6.10**). All District purchases (budgeted and internal funds) are accomplished only by the issuance of duly authorized purchase orders. No orders for goods or services (written or verbal) are to be made with respect to District purchases prior to the issuance of a purchase order. Only the Procurement Department is authorized to approve system generated requisitions and issue Purchase Orders to the vendors. The system assigns a sequential purchase order number when the Procurement Department approves the requisition and issues the purchase order. A preventive system control will not allow requisitions on the system to exceed the buying department’s budget for that line item account.

Overall, the implementation of the automated purchase order system (APO) has reduced purchase order cycle time and resulted in fewer hours being spent on purchase order processing. The Budget Department, a critical link in this system, is responsible for setting up new vendors and completing changes to their data.

The Procurement Department evaluates the requisitions and determines whether the product or service should be quoted, formally bid, or subject to a request for proposal (RFP) process. The District also does “piggybacking” on the awarded bids of other governmental entities rather than developing entirely new bids.¹ This is done in order to efficiently reduce the amount of time spent soliciting bids from vendors that have already respond to another governmental entity’s bid for the same type of item / service and to gain large volume purchase discounts.

¹ *Florida Administrative Code FAC 6A-1.012 (5) Purchasing Policy*, state that “in lieu of requesting bids from three or more sources, school boards may make purchases at the unit prices in contracts awarded by other city or county governmental agencies, other school boards, community colleges, or state university system cooperative bid agreements with the bidder awarded a contract by another entity defined herein will permit purchases by a school board at the same terms, conditions, and unit prices awarded in such contract, and such purchases are to the economic advantage of the school board.”

The following authorization limits apply to any item/service or group of related (“like”) items/services:

- (1) **Up to \$4,999.99:** School or Department is encouraged to seek competitive pricing. Documentation is not required.
- (2) **\$5,000 to \$17,499.99:** School or Department shall obtain three (3) informal quotes, verbal or written, and document them on the purchase requisition.
- (3) **\$17,500 to \$24,999.99:** Appropriate information shall be submitted to the Procurement Department for the development of specifications to solicit formal, written quotes from three (3) or more potential vendors.
- (4) **\$25,000 & over:** School Board approval is required, even those that are bid exempt² or that are made from state contracts or other entity bids. Appropriate information shall be submitted to the Procurement Department for the development of specifications to solicit a formal, written bid or proposal from three or more potential vendors. Award recommendations will be forwarded, by the Procurement Department, to the School Board for approval. Once proper authorization is obtained, the Procurement Director reviews and approves all the purchase orders and issues them to the vendors. State and local capital project funds must be spent on capital outlay projects in accordance with Florida Statutes and State Board of Education Rules. Each capital project is tracked on the financial system with an individual project number.

III. AUDIT SCOPE and OBJECTIVES

As part of the annual Audit Plan approved by the School Board, an operational and compliance audit of the Procurement process and other related construction contracting processes was initiated by the School Board Audit Office. The objectives of this audit were to determine whether District procurement controls and procedures promoted and encouraged:

- Compliance with applicable procurement and bonding laws and regulations;
- Compliance with provisions of any related bid/contract;
- Reliability of records and reports;
- Economic, effective and efficient operations of the District.

The scope of the audit consisted of reviewing the original documentation for a judgmental sample of: 114 goods/services purchase orders, 25 formal bids, and 8 construction projects, from the period of July 1, 2005 through June 30, 2006. Audit testing was conducted to ascertain that the processes were in compliance to State and District laws and regulations pertaining to 1) vendor setup/change, 2) procurement, 3) bidding, and 4) performance/payment bonding and liability insurance requirements. The following report is the detail of the audit results and where enhancements could be made to increase operational efficiency, effectiveness and compliance.

² *Florida Administrative Code FAC 6A-1.012 (7)*, “ the requirement for requesting bids from three or more sources is hereby waived as authorized by Section 237.02 Florida Statutes, for the purchase of professional or educational services, educational tests, textbooks, printed instructional materials, computer software, films, filmstrips, videotapes, disc or tape recordings, or similar audio-visual materials, and for library and reference books , and printed library cards where such materials are purchased directly from the producer or publisher, the owner of the copyright, and exclusive agent within the state, a governmental agency or a recognized educational institution.

IV. NEW VENDOR SETUP and VENDOR CHANGES PROCESS

The Vendor Master file (CBVEND) is a separate mainframe file; it contains approximately 30,000 vendor names that include both businesses and individuals. The legacy financial system and the Automated Purchase Order system (APO) both read it to capture vendor data. Setting up a vendor is a separate process from creating a purchase order; therefore, the vendor can be setup anytime prior to a purchase order. Although in most organizations it is the Procurement Department that is in charge with setting up new vendors, at Lee County School District, it is the Budget Department that is in charge of setting up a new vendor and doing any vendor information changes (i.e. change of mailing address).

According to the Budget Department's "process document", the current new vendor setup procedure starts with a requesting department completing a "Request for Vendor Number" form. This form requires a vendor name, address, telephone number and tax ID# or social security number. The fully completed form can be faxed, emailed as an excel form attachment, or sent as a hard copy to the Budget Department. The Budget Department manually assigns a vendor number and enters the data into the Vendor Master file. A hardcopy of the form is then filed for one fiscal period.

Through observation and interviews with Budget staff, several control weaknesses or lack of controls were identified. This increases the risk of unauthorized vendor setup and changes to vendor information. Since the Vendor Master File is the source of the payee names and addresses printed onto checks, integrity of the Vendor Master file data is critical to the District's ability to process its disbursements correctly.

The following is a description of the control weaknesses or lack thereof identified during the audit and the recommendations provided to management to address these issues.

FINDING 1: There are 11 District employees with system user authorization to the vendor master file data entry screen on the legacy mainframe. They include: one IS analyst, all nine budget personnel, and one payroll employee (who formerly was assigned to the Budget Department); however, only two of the budget employees are 'designated' to do the vendor setup/change function (one is backup). The larger the number of authorized users that can edit the vendor master file, the higher the risk for unauthorized data entry and errors into the vendor master file.

RECOMMENDATIONS: To reduce the risk of unauthorized data changes and provide stronger preventive controls, the District needs to improve its access controls over its vendor master file. The following are the recommendations:

1. System access to the Vendor Master file (CBVEND) should be limited to only the necessary few budget personnel needed to complete the vendor setup and maintenance function.
2. The employee from payroll should be removed immediately.
3. A post-processing review by use of an edit report should be performed by a Budget staff person not responsible for data entry to monitor vendor activity, especially frequent changes to any one vendor's address information.

FISCAL IMPACT: These recommendations can be accomplished within existing resources.

MANAGEMENT RESPONSES to FINDING 1 RECOMMENDATIONS:

Response 1: Accepted and implemented February 27, 2007. Access to the budget vendor system to update information has been limited to five budget department personnel. The purpose of the IS analyst access is for a final test when cutting over to the production environment and/or a final check in the Production environment for major upgrades (i.e. mainframe processor upgrade, database conversion, moving of equipment.) Because of this we will continue to authorize access for the IS analyst.

Response 2: Accepted and implemented February 27, 2007. The payroll employee has been removed from vendor master file access.

Response 3: Rejected. The vast majority of vendor changes come from the finance department, and those changes have documentation attached as to why the change is being made. Any vendor changes that are initiated from schools or other departments must have documentation attached from the vendor stating that the change is valid (such as an invoice or letter from the vendor). Based on these controls we have in place, we feel we have addressed the risk of unauthorized vendor changes being made.

Audit Comment: Although other mitigating controls have been strengthened (i.e. reduced number of personnel who have system access to the Vendor master file and longer supporting documentation storage times), **monitoring thru the system** should still be considered as a fraud deterrent measure.

FINDING 2: A vendor application and W-9 “*Request for Taxpayer Identification Number and Certification*” are not required for vendor setup. Only the “Request for Vendor Number” form is completed but it does not require a pre-approval by either the requesting department or the supervisor of Budget prior to input into the system. Due to the high volume of personnel changes throughout the school system, it would be unreasonable to expect the budget clerk assigned vendor setup/changes to know everyone who should be requesting vendor setups/changes. The lack of preventive approval controls increases the risk that bogus vendors could be setup or changes to vendor file information could be done for unauthorized purposes.

RECOMMENDATIONS: To reduce the risk exposure of setting up bogus vendors or changing vendor information for unapproved purposes, the following preventive controls should be implemented:

1. **A new procedure** should be established that requires a vendor application (new vendor information form) along with a W-9³ be completed by the requesting department and

³ Note: Per Department of the Treasury, Internal Revenue Service, the W-9 tax form is used to certify under penalties of perjury that the individual social security number is correct and that it is not subject to backup withholding. If a vendor fails to make this certification on a Form W-9, or similar statement, backup withholding may begin immediately with **28%** of the payments withheld for income tax. There are both civil and criminal penalties if a vendor provides false information to avoid backup withholding.

vendor before a vendor is added to the system. This will help ensure validity of vendor and that proper tax reporting information is provided.

2. **Enhanced current procedures:** written proof of requesting department's supervisory approval should be obtained before a new vendor is setup or changes to vendor information are processed.
3. **Enhanced current procedures:** the vendor setup or change form documentation should be maintained as an audit trail for a reasonable amount of time (3 fiscal periods).

FISCAL IMPACT: These recommendations can be accomplished within existing resources.

MANAGEMENT RESPONSES to FINDING 2 RECOMMENDATIONS:

Response 1: Under study, to be addressed by 7/1/2007. There are many changes inside of our current vendor setup and payment process that will need to be addressed upon implementation of obtaining W-9 forms. The District wants to ensure that we can prevent delays in payment processing and services to schools and departments as a result of this change. The affected departments (Budget, Finance, and Procurement) will meet to discuss how and when this change can be implemented. It was Business Services' plan to implement the W-9 requirement upon deployment our new business software solution. The affected departments will now meet to determine the feasibility of implementing this change before deployment of the new system.

Response 2: Under study, to be addressed by 7/1/2007. We will determine how and if this will be implemented, along with the W-9 requirement.

Response 3: Accepted and implemented, 2/27/2007. All documentation concerning vendor changes and setup will be retained for three fiscal periods.

FINDING 3: The current mainframe vendor master file does not have enough field characters to input a business vendor's 9 digit employer tax ID (TIN) number although there is a separate 9 digit character field for the social security numbers of vendors who are individuals. The current system only allows either a Y (yes) or N (no) or blank in the one space field for employer's TIN. Upon further discussion with Finance, it was learned that the full 9 digit employer TIN will be assigned to a field in the new system software. Since the current vendor master file setup screen does not have the 9 digit employer TIN information electronically stored, the TIN data will need to be recreated prior to input of the data at the time of the conversion. This will involve additional staff time to perform the research needed.

RECOMMENDATION: To help reduce the research time involved during the migration of data, the business vendors' TIN information should be recorded in electronic format, preferably by modification to the TIN field size in the Vendor Master file on the mainframe. If this is not possible, then the TIN should be captured and stored on an Excel spreadsheet or Access database file in order to have the TIN data on hand prior to conversion and to significantly reduce the time for researching.

FISCAL IMPACT: This recommendation can be accomplished within existing resources.

MANAGEMENT RESPONSE to FINDING 3 RECOMMENDATION:

Accepted and implemented, 2/27/2007. The TIN for all new vendors will be obtained and input into the system.

FINDING 4: The vendor master file does not have systematic preventive controls that automatically flag duplicate addresses for different vendors. During the audit testing of vendor setup, the mainframe vendor address data was downloaded to an Access table. This table was queried to match duplicate addresses for different vendors. The query identified numerous vendor names which have the same address, many of them for the same vendors but with different spellings of their names (i.e. Paul Lawrence Dunbar and P. L. Dunbar, National Educational Music and NEMC). As a result, additional audit hours were spent to ensure that duplicate payments had not occurred.

RECOMMENDATIONS: To compensate for the lack of a preventive automated system control:

1. The Budget Clerks assigned to data input should be retrained in how they are to enter a vendor name.
2. This procedure should be documented in a "Process Document" in order to ensure consistency for training purposes.
3. In addition, the Budget Department should work with a Programmer Analyst from the Information Systems Department to develop an "exception" report based on program reasonableness checks (a system query could be run routinely to identify matching names, phone numbers or addresses). Once the new system is in place, the query could include tax ID numbers as well.

FISCAL IMPACT: These recommendations can be accomplished within existing resources.

MANAGEMENT RESPONSES to FINDING 4 RECOMMENDATIONS:

Response 1: Accepted and implemented, 2/27/2007. The Budget department currently has a standard for names input into the system. We have reiterated that standard to personnel.

Response 2: Accepted with implementation pending, 3/5//2007. The vendor name standards will be attached to the process document.

Response 3: Under study, to be addressed by 7/1/2007. The Budget department will work with Information Systems to determine the feasibility and time needed to produce the recommended exception report in conjunction with plans for our ASP implementation.

FINDING 5: The current vendor master file system does not automatically assign a vendor number. Instead, the vendor number is manually assigned using a manual log of unassigned alpha-sequential numbers and manually entering the number into the system by a Budget Clerk. Furthermore, the vendor master file does not have a designated field for the vendor setup date; thus, making it difficult to identify how long the vendor has been in the vendor master file system.

RECOMMENDATION: Best practice would be to issue vendor numbers in sequential order. In addition, the vendor setup date should be included as data entered into the system. These features should be included in the new system.

FISCAL IMPACT: This recommendation can be accomplished within existing resources.

MANAGEMENT RESPONSE to FINDING 5 RECOMMENDATION:

Accepted with implementation pending, 7/1/2009. Budget, Procurement, and Finance studied the feasibility of assigning vendor numbers in sequential order. We agree that assigning the vendor numbers in sequential order is the most efficient way to proceed, and have made the decision to implement sequential numbering in the new software system. However, as we examined moving to sequential numbering in the current system, we realized that there are numerous reports that would need to be redone in order to accommodate the sequential numbering. Because of the labor associated with this, we chose to wait until implementation of a new system to change our numbering process.

FINDING 6: Social security numbers for vendors that are individuals are not consistently being entered into the vendor master file as required by written procedure. Approximately 1,330 individuals setup as vendors were identified during the audit analysis as missing a social security number. In addition, as mentioned earlier, a W-9, "*Request for Taxpayer Identification Number and Certification*" is not required.

RECOMMENDATION: The Budget Clerks assigned to vendor data input should be re-trained in the importance of entering the social security number. This procedure should be documented in order to ensure consistency for training purposes.

FISCAL IMPACT: This recommendation can be accomplished within existing resources.

MANAGEMENT RESPONSE to FINDING 6 RECOMMENDATION:

Accepted and implemented, 2/27/2007. The Budget Department makes every effort to enter a social security number for every individual in the vendor system. We will continue to stress the importance of having social security numbers for every individual, and we will document that in our process to ensure consistency. In addition, we will implement sporadic management spot reviews to determine any continued need for retraining.

V. PURCHASING PROCESS

“One Time Purchases” are made when the need for goods and services are satisfied and completed with one transaction. Regular purchase orders are issued and closed after payment is made.

“Annual Contract Purchases” are the purchase of materials, supplies or services which are constantly needed for District operations. The annual contract (purchase order) is a commitment to a supplier for certain goods or services over a period of time at a pre-determined price and the supplier’s commitment to maintain a level of goods and services commensurate with the District’s needs. Purchases are prepared using the informal or formal bid process if greater than \$24,999. The Procurement Services Department may establish an annual contract if the non-professional service is anticipated to re-occur throughout the year.

Ninety-two (92) automated purchase orders generated from the Automated Purchase Order system (APO) and 22 EAM maintenance system purchase orders for a total of 114 purchase orders were tested for accuracy in recording, reporting and compliance to State and District procurement rules, regulations, policy and procedures. In addition, a special report was requested by the School Board Audit Office to ascertain the remaining volume of older open purchase orders that were issued prior to June 30, 2005.

FINDING 1: As of January 3, 2007, there are 344 open purchase orders with original setup dates prior to July 1, 2005. This includes 2 purchase orders dated FY 2002, 7 dated FY 2003, 68 dated FY 2004 and 267 dated FY 2005 for an aggregate encumbered amount of \$1,027,854.25.

Although all schools and departments are provided an electronic version of the “Monthly Detail Activity Report” that includes a section for all open purchase orders for their location, it appears that the schools and departments are not consistently reviewing this report each month. As a result, Financial Services Department is not being notified in a timely manner by the schools and departments to close those open purchase orders that are no longer applicable. In addition, Financial Services Department is not monitoring open purchase orders with use of an “aging report” in order to quickly identify open purchase orders with issue dates that are several years old and may need follow-up with the respective departments and/or schools on their status.

RECOMMENDATION: To help ensure the open purchase order encumbrances are being monitored and removed from the system on a timely basis, the Financial Services Department should:

1. Send a memo to all District schools and departments as a reminder that they should be reviewing their “Monthly Detail Activity Report” each month-end to identify open purchase orders that may need to be closed.
2. Develop a quarterly “Open Purchase Order - Aging Report” in order to monitor older open purchase order activity.

FISCAL IMPACT: These recommendations can be accomplished within existing resources.

MANAGEMENT RESPONSES to FINDING 1 RECOMMENDATIONS:

Response 1: Accepted and Implemented - Schools and departments will continue to be sent an email reminder regarding open purchase orders. In addition, a report of specific open purchase orders will be sent to each school/department annually beginning May 1, 2007.

Response 2: Accepted with pending implementation. Financial Accounting will review the open purchase order – aging report semi-annually to begin February 2007. By April 30, 2007 the report will be disseminated to the Chief Business Officer and Procurement Services. An open purchase order – aging report will be reviewed semi-annually to begin February 2007.

FINDING 2: While District policy prohibits purchase splitting, it relies solely on manual processes to prevent this practice. This was also identified in the Cherry, Bekaert & Holland, L.L.P. 2005 Risk Assessment: *“The only internal control to prevent bid splitting is if someone in finance or procurement notices repetitive purchases occurring in short intervals. As a result, the formal bid solicitation process for purchases of \$25,000 or more could be bypassed and the pricing may not be competitive. We recommend that internal controls be established to prevent bid splitting”*.

During the audit testing for possible purchase splitting, noted was that the current automated purchase order (APO) system does not have a data field for a “commodity code”. A similar finding was also noted in the 2002 OPPAGA Report, p.14-25, as a system problem. As a result of the system’s ineffectiveness to automatically monitor purchases by commodity type, the Procurement Department manually monitors “like-kind” items/services to determine if the requesting department is buying through multiple purchase orders or multiple vendors in order to avoid going through higher levels of approval (purchase splitting). Although this process is in place, there is no written “process document” of how it should be done. **The audit did not find any intentional purchase splitting occurring.**

RECOMMENDATION: According to discussions with the Procurement Director, the new ERP (ASP project) will have a commodity code field and will be capable to automatically flag multiple purchase requisitions for the same item/service. However, until the new system is fully operating, the Procurement Department should:

1. Implement a process document outlining the purchase splitting monitoring steps they are using,
2. Monitor dollar volume by vendor using a BL-016 “Vendor Paid Invoice Report” and pre-defining a threshold amount (i.e. greater than \$17,499 less than \$24,999) for the purposes of identifying other:
 - cost-saving measures that could be achieved District-wide by going to a bid for items/services supplied by those vendors, and
 - monitor for potential purchase splitting.

FISCAL IMPACT: These recommendations can be accomplished within existing resources.

MANAGEMENT RESPONSES to FINDING 2 RECOMMENDATIONS:

Response 1: Accepted and Implemented as of February 2007. Process document for requisition processing and monitoring has been completed.

Response 2: Accepted and Implemented as of February 2007. In addition to our current internal tracking we will utilize the BL-016 "Paid Invoice Report" as a cross check to insure limited risk of potential purchase splitting.

VI. BIDDING PROCESS

The audit scope included reviewing a judgmental sample of 15 bids (District, state contracts, and piggybacking) and their supporting documentation files kept in the Procurement Department for completeness and compliance. In addition, 10 Business Services consent agenda items were randomly selected and traced back to the Procurement Department bid files. Testing was done to ensure the awarded bids were in compliance to contract terms and that the files were complete and current.

FINDING 1: Although bid renewals are done on a timely basis, noted was that a written Process Document does not exist for the steps in this procedure.

RECOMMENDATION: To ensure consistency of the process and to use as a benefit for training purposes, a “Process Document” for the bid renewal procedure should be developed.

FISCAL IMPACT: This recommendation can be accomplished within existing resources.

MANAGEMENT RESPONSE to FINDING 1 RECOMMENDATION:

Accepted and implemented as of February 2007. Process document for the formal solicitation process and subsequent renewals has been developed.

FINDING 2. The awarded bid files were reviewed to ensure proof of liability insurance (required by bid contract) was on file and that the effective dates covered the period of the awarded contract. Noted were that six Acousti Engineering “Q” maintenance purchase orders under bid # BO56355LO were issued in June 2006 but that the certificate of insurance on file indicated coverage expired January 2006. Proof of on-going insurance coverage (updated certificate of insurance) over the term of the contract (contract expired October 15, 2006) was not on file.

RECOMMENDATION: Since insurance coverage usually covers one year (i.e. 1/1/2005 to 1/1/2006), and the effective dates usually are not the same as the awarded bid timeframe (i.e. 10/15/2005 to 10/15/ 2006), the Procurement Department needs to implement a monitoring procedure to ensure awarded bidders are supplying on-going proof of insurance coverage during the contract period.

FISCAL IMPACT: This recommendation can be accomplished within existing resources.

MANAGEMENT RESPONSE to FINDING 2 RECOMMENDATION:

Accepted and was implemented as of December 2006. This issue was addressed during the audit process by utilizing Microsoft task manager and creation of a centralized insurance spreadsheet in conjunction with our current Bid Data Log to insure that all required insurance documents were current and on file.

FINDING 3. It is the policy of the District to seek Board approval prior to notifying the bidder that they have been awarded the contract. **The audit found no violations that sampled contracts were issued prior to Board approval. However, proof of insurance is not required until a bidder has been awarded the contract.** The standard language used in the bid proposal states, *“We understand the insurance requirements contained in these specifications, and that the evidence of said insurance may be required within five (5) business days of the award of bid.”*

Obtaining proof of insurance “post Board approval” presents a risk that the Board is approving a vendor before the vendor fully qualifies to be the awarded bidder. In addition, if the awarded bidder can not demonstrate that proper insurances are in place after being awarded the contract, then the selection and approval process starts all over again, which is time consuming and inefficient.

Audit testing identified that a bidder who ranked third in the awarded bid #B056355LO (approved July 12, 2005 for floor covering) did not have the adequate auto insurance coverage to comply with the contract requirements; thus, did not meet the bid proposal qualifications to be selected as part of the 3 awarded bidders presented to the Board for approval. This issue could have been identified before Board approval if proof of insurance was required prior to awarding the contract.

RECOMMENDATION: To reduce risk and increase efficiency, proof of liability insurances (workers comp, commercial general liability, auto liability) should be required from the bidders during the bid process as a part of the qualifications. The Procurement Department needs to implement a final “pre-contract awarded” quality assurance procedure/checklist to verify that the potential awarded bidder(s) has provided all insurance documents as prescribed in the bid prior to Board approval in awarding / executing a contract.

FISCAL IMPACT: This recommendation can be accomplished within existing resources.

MANAGEMENT RESPONSE to FINDING 3 RECOMMENDATION:

Accepted and implemented as of February 2007. We have revised our current award process to now require proof of insurance within five (5) business days of the “Notice to Award”. This will insure that insurance forms are on file and verified prior to formal Board Award.

FINDING 4: General observation during the audit testing. Bid files kept by the Procurement Department were all available when requested. However, some of them were difficult to navigate through due to no set file format being consistently used.

RECOMMENDATION: To provide easier access to required documents, the Procurement Department’s “bid files” should be kept organized by subsections for: contract documents, insurance documents, approval and renewal correspondence, purchase change orders, to name just a few of the many documents that need to be kept.

FISCAL IMPACT: This recommendation can be accomplished within existing resources.

MANAGEMENT RESPONSE to FINDING 4 RECOMMENDATION:

Accepted and implemented February 2007. A standard operating procedure has been developed to standardize the Bid / RFP / RFQ folder format. This process will again be enhanced with the implementation of the document imaging process, which will allow all district users the ability to view these documents online in a categorized format. Standardization began in 2005.

VII. CONSTRUCTION CONTRACTS

A. Payment Process

FINDING 1: Typically, for a construction contractor, a 10% retainage is held back from each draw request and setup in a liability account. The current automated Accounts Payable system is not capable of automatically reducing the retainage amount from the contractor's progress payments, thus construction draws must be done by a more labor intense manual process.

The reason these payments can not be processed through the automated accounts payable system is because the current system has a system control that automatically matches the check amount to invoice amount. This is an effective preventive control to ensure payments can not be different from the invoice amount. However, this control limits the automated accounts payable system's capability for automatically processing progress payments that have a retainage amount needing to be withheld. To handle these types of payments, the Accounting Department uses QuickBooks Pro software to generate the accounting transaction and "service account check". A journal entry is then posted to the Legacy mainframe financial system to ensure the payment is updated into the financial records.

This has been the District's practice for numerous years and has been included in the financial scope of the External Auditor's annual audit testing to ensure accurate financial recordkeeping and reporting. Based on this audit's review of previous external audit reports, no audit findings have been reported. In addition, the District's Internal Audit Department or Cuthill & Eddy, LLC complete a final review of the construction project's payment activity in order to validate that the contractor's final billing is an accurate representation of the final contract amount due.

RECOMMENDATION: In order to streamline processes to increase efficiency:

1. The "service account check" process should be implemented as an automated process in the new ERP accounts payable system requirements (ASP project) with user stakeholders having an opportunity to make certain that any new computer system meets their reporting and informational needs.
2. The External Auditors should continue reviewing the "service account check" process for financial accuracy in their annual financial audit pursuant to section 11.45, Florida Statutes.
3. The District's Internal Audit Department or Cuthill & Eddy, LLC should continue reviewing all documentation related to the construction contractor's request for final payment and provide a copy of their report to the School Board Audit Office for informational and risk assessment purposes.

FISCAL IMPACT: These recommendations can be accomplished within existing resources.

MANAGEMENT RESPONSES to FINDING 1 RECOMMENDATION:

Response 1: Accepted with implementation expected by 2009, incorporated as a part of Financial Accounting’s software update.

Response 2: Accepted and implemented February 2007. This process has been ongoing and will continue to be reviewed by our external auditors.

Response 3: Accepted and implemented February 2007. This process has been ongoing and will continue to be reviewed by the Internal Audit Department and Cuthill & Eddy, LLC. In addition, copies of their reports will be submitted to the School Board Auditor’s office.

FINDING 2: “Process Documents” are written instructions developed to ensure consistency in performing the required procedural steps. They are critical in training new personnel. During the review of Accounts Payable’s written procedural documentation, a “process document” for completing “journal entries” could not be found in their Department Procedures Manual.

RECOMMENDATION: To ensure current “process documents” are being maintained (using the established District format), it is recommended that a “process document” describing the steps for preparing a “journal entry” be incorporated as its own section of the “Financial Accounting Department Procedures Manual”. In addition, the process document should also be included in Appendix B of the manual, under “Construction Payables”. [Note: Since employee turnover occurs over time, using the job title would be more appropriate when defining the process document steps in this manual.]

FISCAL IMPACT: This recommendation can be accomplished within existing resources.

MANAGEMENT RESPONSE to FINDING 2 RECOMMENDATION:

Accepted and implemented March 2007 – A written “process document” to describe the journal entries for payments requiring retainage has been completed.

B. Compliance: Performance & Payment Bonds and Certificates of Insurance Liability

F.S. 255.05, “Bond of Contractor” and F.A.C. section 4.2 (1) “Bonds and Insurance” require “any person entering into a contract with the School District for the construction of a public building, for the prosecution and completion of a public work, or for repairs upon a public building or public work shall be required, before commencing the work deliver to the public owner, and record in the public records of the county where the improvement is located, a payment and performance bond with a surety insurer authorized to do business in this state as surety for construction projects over \$200,000.”

A surety bond is a written instrument in which the Surety (the bond company) promises to answer for the debt or default of the Principal (contractor) to the Obligee (LCSD). The Principal's liability to the Obligee is the obligation to perform and the bond amount. The Surety's liability to the Obligee is the amount of the bond. A **"performance"** bond protects the Obligee from financial loss should the Principal fail to perform in accordance with the terms of and conditions of the contract; assures Obligee of project completion and financial protection. A **"payment"** bond provides a mechanism to ensure that once labor and materials have been furnished to a contractor or subcontractor on a public works project, the provider is assured of receiving payment.

To test compliance, the School Board Audit Office selected a sample of eight (8) construction contracts that were greater than \$200,000. The testing also included reviewing all reports issued by the outside professional services of Cuthill & Eddy, LLC; which the District hired to certify several construction projects' final contract value and certify other project costs at the completion of the project. In addition, an analysis was conducted on one final capital construction payment review performed by the District's Internal Audit Department (IAD) to ascertain the scope of their review steps.

To verify compliance to state requirements under "F.S. 255.05, Bond of Contractor", and "F.A.C., section 4.2 (1), Bonds and Insurance", audit testing was completed to verify both bonds and liability insurance documents were in place prior to start of construction and complied to state laws regarding:

1. Bond Compliance: Timeliness and Adequacy;
2. Bond Compliance: Proper Recording in County records;
3. Insurance coverage: Timeliness and adequacy;
4. Proof of insurance coverage remained effective throughout the construction project.

FINDING 1: Bond Compliance: Timeliness and Adequacy

- Of the seventeen school renovation projects recently completed, a sample of six renovation projects completed by three different general contractors were reviewed for bond compliance. The audit noted that Performance and Payment Bonds were documented in the Construction Services' project files and that the bond amounts covered the initial contract amounts. In addition, change order activity did not result in increases to the original contract amounts of the six projects sampled. **Thus, the bond coverage appears adequate for the six renovations selected for review.**
- A review of two other construction projects related to 1) a re-roofing project and 2) Ida S. Baker Athletic Field indicated that bonds were issued for the original contract amounts. However, additional change orders increased each of those projects' contract amounts. According to F.S. 255.05, bonds should cover the contract amount. It was noted that requiring "addendums" to the bond amount when the modified contract amount increases currently is not a practice used by the Construction Services Department.

RECOMMENDATION: When the original contract amount increases due to change order activity, monitoring steps should be taken by the Construction Services Department to ensure bonding is in full compliance to state law.

FISCAL IMPACT: This recommendation can be accomplished within existing resources.

MANAGEMENT RESPONSE to FINDING 1 RECOMMENDATION:

Accepted and implemented January 2007. We have a process document in place that requires the initial Payment and Performance Bonds prior to construction and also requires a “Consent of Surety” document at the completion of the project. As further assurance, staff has added a procedure to prepare a form letter that will be sent to the Surety each time a change order results in an increase over the original contract price ensuring that the Surety is informed of the change in contract price.

The Bond “follows the contract” and will cover the entire contract even if change orders have been executed. If additive change orders for a project exceed the deductive change orders, the Bonding Company will not sign off on the “Consent of Surety” at the end of the contract until they have been paid their final Bond premium which is based on the final contract amount. The “Consent of Surety” attests that the Bond Company has reviewed the final contract amount and assumes responsibility for that amount over the following next two years. This is the industry standard for Bonding Companies.

FINDING 2: Bond Compliance: Proper Recording in County records.

Compliance to recording requirements is not consistently occurring. Two of six school renovation construction projects’ performance and payment bonds were recorded within a week of the contract date (prior to construction) with Lee County Clerk of Court as required by state law (it should be noted that both were filed by the same general contractor). The other four renovation projects were not recorded by the other two general contractors as required by F.S. 255.05. Although the contract language specifies it is the responsibility of the contractor to ensure bonds are filed with the County, the Construction Services Department does not have a monitoring procedure in place to ensure bonds are properly recorded prior to commencement of construction.

RECOMMENDATION: To ensure performance and payment bonds are in full compliance with Florida Statute 255.05, the Construction Services Department needs to implement a consistent monitoring procedure to ensure compliance to the county recording requirements. Documentation should exist in the departmental files that performance & payment bonds have been filed with the county as required. A “Pre-construction” checklist would help to effectively implement this recommendation.

FISCAL IMPACT: This recommendation can be accomplished within existing resources.

MANAGEMENT RESPONSE to FINDING 2 RECOMMENDATION:

Accepted and implemented October 18, 2006. A pre-construction checklist has been developed for utilization in monitoring full compliance to the recording requirement of the statute. Construction project files now have proof of Bond being recorded prior to construction as evidence of compliance.

FINDING 3: Insurance coverage: Timeliness and adequacy.

Insurance coverage must exist prior to commencement of construction. Of the seventeen school renovations recently completed, a sample of six renovation projects were reviewed for timeliness and adequacy of required liability insurance coverage. The audit noted that the original Certificate of Liability Insurance was obtained in a timely manner (pre-construction) and kept in the Construction Services' files. **The coverage amounts of the six sampled projects complied with the contract terms.**

- and -

FINDING 4: Insurance coverages should remain effective throughout the contract.

Evidence of on-going current insurance (updated Certificate of Liability Insurance) was on file for all six projects sampled, but all the Certificates were dated on either January 18 or 19, 2007 (after the School Board Audit Office notified Construction Services which project files were to be pulled for review, the School Board Auditor arrived on January 20th). This indicates that a process to monitor on-going proof of insurance coverage had not been occurring prior to the audit.

RECOMMENDATION: Since insurance coverage usually covers one year (i.e. 1/1/2005 to 1/1/2006), and the construction projects usually begin and end in different periods (i.e. 4/1/2005 to 10/15/2006), the Construction Services Department needs to implement a monitoring procedure to ensure contractors are supplying timely on-going proof of insurance coverage over the life of the project.

FISCAL IMPACT: This recommendation can be accomplished within existing resources.

MANAGEMENT RESPONSE to FINDING 3 & 4 RECOMMENDATION:

Accepted and implemented January 22, 2007. A tickler reminder system has been implemented, using the scheduler feature on Outlook that notifies staff 30 days prior to the expiration date of the insurance policies. At that time, a new certificate will be requested from the contractor and all pertinent information verified.

FINDING 5: Post - Construction Audit Services: Internally performed.

- At the time of this audit testing (Dec 2006), it was noted that the post construction review process conducted by the Internal Audit Department did not have established audit steps in the scope of their work to review for bond and insurance compliance. After identifying this limited scope issue, the School Board Auditor contacted the District's Internal Audit Department (IAD) to discuss implementing additional review steps. The IAD concurred and have incorporated additional audit steps to the scope of their reviews. These additional steps now address: 1) bond and insurance compliance and 2) that total project costs are not exceeding the amount approved by the School Board.

- The District's Internal Audit Department provides a final report of their review to the Construction Services Department. However, the Construction Services Department is not providing a written respond / action plan back to Internal Audit that addresses the Internal Audit Department's findings and recommendations.

RECOMMENDATION: For construction cost reviews that are internally performed by the District's Internal Audit Department:

1. The Construction Services Department should provide a written response to the Internal Audit Department as to what steps they will take to address the findings and recommendations.
2. The Internal Audit Department should perform follow-up testing to ensure the recommendations have been implemented.
3. The Internal Audit Department should prepare an annual summary of the various construction projects' findings, recommendations and status of corrective steps taken by School Support Division management. This report should be provided to the Chief Administrative Officer who oversees the School Support Division as a means for him to monitor the continuous improvement progress made by the School Support Division and Construction Services Department.
4. The Internal Audit Department should provide copies of all reports generated from their department to the School Board Audit Office for informational and risk assessment purposes.

FISCAL IMPACT: These recommendations can be accomplished within existing resources.

MANAGEMENT RESPONSES to FINDING 5 RECOMMENDATIONS:

Response 1: Accepted and implemented March 2007. The process document for Construction Projects Final Payment Review now includes a step that indicates a response letter will be written indicating how all recommendations made in the report will be resolved. The response letter will be addressed to the Internal Audit Department and copied to Executive Director of School support and the Project Manager. The Construction Services Department will have ten (10) days to respond. If no response has been received a reminder will be sent to the Director of Construction Services.

Response 2: Accepted with pending implementation March 2007. The Internal Audit Department will perform follow up testing to assure that recommendations made in our report are being implemented. We now have a process in place as part of the audit program we use for construction project final payment reviews that requires follow up testing to document that the recommendations are being implemented. This document will be part of the review work papers.

Response 3: Accepted with pending implementation March 2007. The Internal Audit Department will prepare a summary document that lists the construction projects that we have reviewed on a six month basis. The summary document will show all projects reviewed, the recommendations we have made, and comments as to how the recommendations have been implemented. The summary documents will be discussed with the Chief Administrative Officer and the Executive Director of

School Support as a means for them to monitor the progress made by the School Support Division and the Construction Services Department.

Response 4: Accepted and implemented March 2007. The process document for Construction Projects Final Payment Review now includes a step that indicates a final report for each construction project reviewed will be sent to Executive Director of School Support and the School Board Audit Office.

FINDING 6: Post - Construction Audit Services: Externally performed.

- At the time of this audit testing (Dec 2006), it was noted that the current post construction review process conducted by Cuthill & Eddy, LLC did not have established audit steps in the scope of their work to review for bond and insurance compliance.
- The School Support Division which receives the Cuthill & Eddy, LLC reports does not have written procedures in place for addressing the findings and recommendations. After reading the 8 issued reports by C&E, LLC, it appeared that many of the same findings were noted in several construction projects reviewed.

RECOMMENDATION: For the construction cost reviews that are externally performed by Cuthill & Eddy, LLC:

1. The Construction Services Department should implement written procedures that address C&E, LLC finding and recommendations, with management responses provided to executive management. This would help ensure the District is addressing audit concerns in a timely fashion; thus, strengthening controls for greater accountability of project costs.
2. The School Support Services Division should provide copies of all C&E, LLC reports as well as their action plan reports to the School Board Audit Office for informational and risk assessment purposes.

FISCAL IMPACT: These recommendations can be accomplished within existing resources.

MANAGEMENT RESPONSES to FINDING 6 RECOMMENDATIONS:

Response 1: Accepted and implemented January 2007. Responses to Cuthill & Eddy, LLC reports were prepared in January 2007 and items requiring changes have been implemented for future projects.

Response 2: Accepted and implemented February 2007. Copies of C&E, LLC reports and our responses will be submitted to the School Board Audit Office when completed.