

California State Auditor

B U R E A U O F S T A T E A U D I T S

State Contracting:

*The State Can Do More to Save Money
When Acquiring Goods and Services*

October 1998
97015

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CALIFORNIA STATE AUDITOR

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October 15, 1998

97015

The Governor of California
President pro Tempore of the Senate
Speaker of the Assembly
State Capitol
Sacramento, California 95814

Dear Governor and Legislative Leaders:

As required by Chapter 1044, Statutes of 1990, as amended, the Bureau of State Audits presents its audit report concerning the State's use of various procurement methods to acquire goods or services and the administration and oversight of these methods by the Department of General Services (DGS). This report concludes that the department paid higher than necessary costs when they purchased goods through the California Multiple Award Schedules (CMAS) program because they did not always compare value among vendors or negotiate price reductions. Our report also states that departments incurred unnecessary administrative costs by using fiscal agents to obtain services from vendors. Further, we point out that weak DGS oversight of the CMAS program led to reduced assurance that vendors adequately complied with program requirements and that departments paid fair and reasonable prices for goods and services. Similarly, weak oversight of master service agreements contributed to the inappropriate use of this procurement method. Finally, departments may experience confusion and lost staff time when guidance from different DGS divisions is inconsistent.

Respectfully submitted,

A handwritten signature in cursive script, appearing to read "Kurt R. Sjoberg".

KURT R. SJOBERG
State Auditor

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SUMMARY

Audit Highlights . . .

Our review of procurement methods used by state departments and the related administration and oversight by the Department of General Services (DGS) revealed:

- Departments do not always obtain the best value when buying goods through the multiple award schedules.*
- The DGS does not adequately administer and oversee use of the multiple award schedules.*
- The DGS does not monitor departmental use of master service agreements.*

Moreover, despite improvements, some departments continue to waste state money by using fiscal agents to obtain contracted services.

RESULTS IN BRIEF

According to the Department of General Services (DGS), the State's departments spent nearly \$5 billion in fiscal year 1997-98 on the procurement of goods and services through the California Multiple Award Schedules (CMAS) program and through contracts approved by the DGS's Office of Legal Services. Under the CMAS program, vendors contract with the DGS to sell specific goods and services at prices discounted from their commercial price list. The above figure does not include those acquisitions not subject to DGS approval, those made under a department's delegation authority, or those made through other procurement methods such as master service agreements.

Because the State spends so much money on procuring goods and services, the DGS must properly administer and oversee the various procurement methods it establishes. However, the DGS has not done so in several ways. First, because the DGS does not require departments to compare value and because it does not adequately facilitate comparing value, the State has missed opportunities to obtain goods and services at a better value. In addition, the absence of sufficient DGS controls has allowed two state agencies to waste money on unnecessary administrative fees by inappropriately using vendors as fiscal agents.¹ Further, weaknesses in its administration and oversight of the CMAS program have led to some departments not obtaining best value when using the program. These weaknesses have also led to the DGS not performing sufficient reviews of CMAS vendors to identify noncompliance with CMAS requirements and not adequately or promptly resolving those instances of vendor noncompliance that it has identified. The DGS has also not reviewed departments' use of master service agreements to identify improper management of such contracts, and, as of this report, has yet to develop and distribute a comprehensive list of services available through master service agreements. Thus, the State cannot take full advantage of its collective buying power. Finally, inconsistent advice from the DGS has the potential to create delays in a department's procurement process.

¹A fiscal agent provides an administrative role between a buyer and seller.

RECOMMENDATIONS

The DGS needs to take several actions to increase the value of the goods and services that departments acquire through its various procurement methods. For instance, rather than merely encouraging departments to compare prices, the DGS should require them to do so when the cost of the good or service exceeds a predetermined amount. The DGS should also require departments to negotiate a lower price when applicable. Finally, the DGS should provide departments with sufficient, easy-to-use tools to help them determine value. Such tools could include improved Internet resources or catalogs organized by product that include price.

Also, to avoid the further waste of money, the DGS should prohibit departments' use of vendors as fiscal agents.

Regarding weaknesses in its administration and oversight of the CMAS program, the DGS has argued that it does not have sufficient staffing to improve its process for reviewing vendors. To address this concern, the DGS should consider alternatives such as providing more resources to the unit currently responsible for conducting vendor reviews, moving responsibility for those reviews to a unit with more experience in reviewing program operations, or hiring a contract auditor on a contingency-fee basis to conduct vendor reviews and any necessary follow-up. The DGS should then take the following actions:

- Increase the number of vendor reviews it conducts annually.
- Use the results of the federal government's reviews as part of a risk-based assessment to choose vendors for review.
- Include within the scope of its reviews an examination of a vendor's compliance with the "price-reduction clause" of the vendor's contract to identify and correct those instances when vendors do not sell goods to the State at the appropriate or best price.
- Communicate the results of its vendor reviews to applicable departments. Appropriate instances include when the DGS identifies departments paying vendors more than the contracted list price for a product or service.

- Develop and implement sufficient procedures that enable effective follow-up on the results of the vendor reviews. These procedures should include demands that vendors promptly refund or credit any overcharges for purchases made and that vendors cease selling to state departments items that the DGS has not approved.
- Develop and implement administrative penalties against vendors that do not comply with applicable procurement requirements.

In addition, the DGS needs to improve its communication with the departments. To avoid hindering a department's ability to efficiently acquire necessary goods or services, the DGS should supply clear and consistent guidance on all state contracting and purchasing issues. The DGS should also provide a complete and accessible list of master service agreements to departments to enable them to take advantage of the State's collective buying power by using such agreements more often and more effectively.

Finally, because of the concerns we identified related to the CMAS program and to master service agreements, the DGS should include a review of the usage of these procurement methods as part of the scope of its existing evaluations of departments.

AGENCY COMMENTS

The DGS agrees with some recommendations in our report, disagrees with others, and, for the remaining recommendations, states that it will either consider the feasibility of implementing them or will review its systems to determine if it should make changes. For example, the DGS agrees with our recommendations that it provide departments with sufficient, easy-to-use tools to help them determine value, and that it include a provision in its upcoming purchasing guidance manual that prohibits the use of any vendor as a fiscal agent. On the other hand, the DGS disagrees with two of the three recommendations concerning ways to increase the value of purchases made through the CMAS program; it states that it will determine whether actions need to be taken to ensure that users of the CMAS program are aware of their responsibilities. Finally, concerning our recom-

mendations related to improved oversight of the CMAS program, the DGS states that it will form a team of DGS staff that will consider the feasibility of specific actions we recommend. ■

INTRODUCTION

The State has established certain processes through which its departments can acquire goods and services. Typically, competition is at the core of these processes. For example, for procurements of \$1,000 or more, state law and DGS policy require departments, with certain exceptions, to offer several vendors a chance to provide price quotes or proposals. This allows departments to fairly select a vendor and ensures that they obtain the good or service with the best possible value for the State.

These two tenets, fairness and value, are required by the California Public Contract Code. Fairness is necessary so that all vendors have an unbiased opportunity to provide their goods or services to the State; no vendor should be improperly excluded from participating in the State's procurement process. Value is necessary so that the State does not waste its resources. Typically, value is measured by the price a department pays for a service or good. However, value can be influenced by other factors such as vendor experience, service after the sale, delivery, training, setup, and warranties or guarantees.

The competitive bidding process that the DGS's policies or the law have required departments to use when selecting vendors for one-time acquisitions of goods or services can be lengthy. A department generally prepares a request for proposal or similar document that, among other things, describes the product or service it wants, invites prospective vendors to submit written proposals that identify their prices, and describes the procedures the department will use to evaluate the proposals. After advertising its request for proposal, the department evaluates the proposals it receives, selects a winning vendor or vendors, issues a notice identifying the winning vendor or vendors, and resolves any protests filed by losing vendors. DGS information indicates that, depending on factors such as the nature of the good or service to be acquired, the number of vendors bidding, and the number of protests filed, this process often takes from three to eight months.

The DGS realizes that departments spend a great deal of time and resources to procure goods and services through competitive bidding. To help reduce acquisition costs and the time involved, the DGS has developed several alternative procurement methods for use by the departments. The DGS refers to several of these alternatives as leveraged procurement methods. We provide a more detailed description of the various procurement methods in Appendix A.

CALIFORNIA MULTIPLE AWARD SCHEDULES

One of the two types of leveraged procurement methods on which we focused during this audit is the California Multiple Award Schedules (CMAS) program. The DGS created the CMAS program from legislation enacted in 1993. In part, this legislation stated that it was the Legislature's intent that procedures created by the DGS provide for "the expeditious and value-effective acquisition of electronic data processing goods and services to satisfy state requirements," and for the acquisition of those goods and services "within a competitive framework." Basically, under the CMAS program, vendors contract with the DGS to sell specific goods or services at prices discounted from their commercial price lists. About 87 percent of the sales under the CMAS program are for computer-related goods or services; the remaining 13 percent are for other goods.

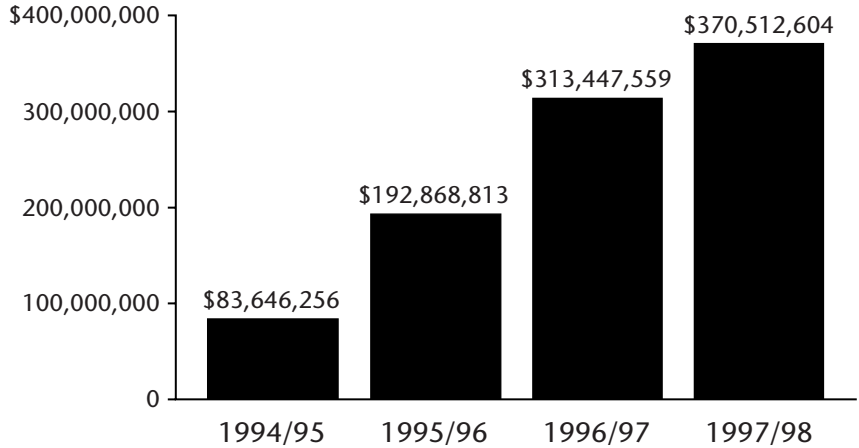
In the past four years, the dollar amount of goods and services purchased through the CMAS program has increased dramatically. This increase is shown in Figure 1.

Examples of the types of goods and services on which this money was spent are described in Appendix B.

Despite this increase in the usage of the CMAS program, some CMAS vendors do not appear to produce many sales to the State. DGS information indicates that, as of May 1998, the CMAS program had 880 active vendors with a total of 1,364 contracts available for use. For those vendors among the top 50 in terms of sales from January 1995 through September 1997, the dollar value of sales ranged from \$1.9 million to \$50.3 million, with only 20 vendors having sales of more than \$5 million each.

FIGURE 1

The Cost of Goods and Services Acquired Through the California Multiple Award Schedules Program
By Fiscal Year



Source: Unaudited data from the DGS Procurement Information Network.

MASTER AGREEMENTS

Master agreements typically are created by the DGS to allow departments to obtain needed services quickly and easily, thus avoiding the delays and uncertainties associated with the competitive bid process. The DGS uses three types of master agreements: service, purchase, and rental agreements. Figure 2 shows the types of goods and services departments can acquire under each.

FIGURE 2

Three Types of Master Agreements and the Services or Goods Departments Can Acquire From Each

Master Service Agreement	Master Purchase Agreement	Master Rental Agreement
Consulting Services	Computers	Computers
Maintenance Services	Computer Components	Computer Terminal Equipment
Other Services	Telecommunications Equipment	Other Information Technology Equipment
	Other Information Technology Products	

During this audit, we also focused on master service agreements. Appendix A provides more information about master service agreements while Appendix C lists the types of services available through the agreements as of June 30, 1998.

DGS'S PROCUREMENT RESPONSIBILITIES

Depending on the procurement method used, the DGS and the departments each have different responsibilities. Among other things, the DGS is responsible for developing and administering the various authorized procurement methods, for reviewing and approving those contracts above established delegation limits and supervising purchase orders that exceed those limits, for reviewing requests for exemptions to delegation limits, and for providing guidance as necessary to departments when they are acquiring goods or services. Generally, departments are responsible for identifying the appropriate goods or services that best meet their needs and for obtaining them in a fair manner and at the best value.

The DGS was created in 1963 to provide centralized support services such as building maintenance and purchasing to other departments. It has been redefining itself from a "control agency" to a "customer service agency" since late 1992. According to its former mission statement, the DGS viewed itself as a control agency that provided business services to other departments. However, as part of its quality-management project, the DGS adopted a customer-oriented vision statement in November 1992 and, in 1993, developed a strategic plan to achieve such a vision. The plan states that the DGS will provide purchasing and support services to all departments more economically than the departments can provide such services for themselves. The DGS's objectives include ensuring that the State gets the best service at the best price. The strategic plan also states that the DGS will retain only those control functions that cannot be shifted to other departments or those that the governor or the Legislature mandate that the DGS perform.

Since adopting its service-oriented vision, the DGS has taken a variety of actions to make the State's system of acquisition more responsive to the State's needs. For example, the DGS has done the following:

- Authorized any department that meets the delegation criteria to make purchases of materials, supplies, and equipment of up to \$15,000 without DGS approval.

- Provided some departments with special or expanded delegation authority that increased spending limits for certain items up to \$1 million.
- Implemented new procurement methods, such as the CMAS program and master service agreements, that have delegation limits higher than those for general purchases.²
- Obtained input on how the DGS can make procurement easier and less time-consuming for departments.

Staff of the five departments we visited as part of this audit generally had positive comments about this shift. For example, the California Highway Patrol considers the DGS’s Office of Legal Services and the Procurement Division to be “useful, helpful, and—in fact—valuable.” The Health and Welfare Agency Data Center stated that, “over the last three or four years, the DGS overall has changed from an untimely, bureaucratic impediment to departments’ procurements, to a helpful, service-oriented organization.” In fact, all five departments noted that the DGS had become much more helpful than it used to be.

SCOPE AND METHODOLOGY

Chapter 1044, Statutes of 1990, as amended, requires the Bureau of State Audits to annually evaluate the State’s compliance with laws and regulations for consultant contracts. This audit is the sixth and final report of this series.

To evaluate the State’s compliance with the laws, regulations, and policies governing contracts, we reviewed the California Public Contract Code and the Government Code, the *State Administrative Manual*, and the *State Contracting Manual*; from these sources, we identified provisions and policies pertaining to consulting contracts, interagency agreements, and other types of contracts. In addition, we reviewed the laws and policies regarding acquisitions through the California Multiple Award Schedules (CMAS) program and master service agreements.

² The delegation limit for acquisitions through the CMAS program is \$500,000 for information technology-related goods and services and \$100,000 for commodity purchases. The delegation limits for contracts under master service agreements vary from \$100,000 to no limit.

We then examined the State's use of the CMAS program to determine whether the State is achieving efficiencies from its procurement of goods. In addition, we followed up on our high-level review of master service agreements conducted during our previous state contracting audit, issued in July 1997, entitled *State Contracting: Improvements Are Still Needed To Ensure the Effective Use of Public Resources*, Report 96015.

As part of our examination of the CMAS program and master service agreements, we reviewed the actions of the Department of General Services (DGS) as the administrator of these procurement methods and the actions of five departments as users of them. Based on factors such as recent audit history, audit staff suggestions, and level or nature of usage of contracts or purchasing, we selected the following five departments to review: Franchise Tax Board, Health and Welfare Agency Data Center, California Highway Patrol, Department of Toxic Substances Control, and California Youth Authority.

To determine whether the DGS and the five departments we visited met the standards of fairness and value required by the Public Contract Code, we examined the DGS's administration and the departments' use of the CMAS program and master service agreements. To do this, we reviewed procedures the DGS uses to approve vendors to participate in the CMAS program, to monitor vendors' compliance with CMAS requirements, and to provide services under master service agreements. We also reviewed the procedures the five departments use to select the vendors from which they acquire goods or services through the CMAS program or master service agreements. Further, because our work at the DGS disclosed concerns involving a department other than the five we visited, we cite examples in our report from the California State Lottery.

Also, to establish whether the five departments complied with contracting requirements, we tested samples of consulting services contracts, personal services contracts, and interagency agreements. We also determined the effectiveness of the DGS's directive prohibiting the use of interagency agreements to circumvent competitive bidding as we had indicated we would in our previous state contracting report. We identified no concerns pertaining to these issues at four of the five departments we visited. ■

CHAPTER 1

Departments Can Achieve More Value When Acquiring Goods and Services

CHAPTER SUMMARY

State departments using the California Multiple Award Schedules (CMAS) program, master service agreements, and interagency agreements do not always acquire goods or services at the best value. Our review of the acquisition practices used by several departments identified instances when the departments spent more money than necessary when using these procurement methods. We attribute shortcomings in the use of the CMAS program to three primary causes. First, the Department of General Services's (DGS) written policies and guidance to departments concerning the proper use of the CMAS program are insufficient.³ For example, in its policy bulletins, the DGS strongly encourages departments to compare products among CMAS vendors to obtain the best value but does not require such comparisons. Second, the DGS does not provide adequate tools to facilitate departments' efforts to determine value. For example, the DGS's Web site for CMAS products is limited to just 12 product types or brand names per vendor and does not include the price the vendor charges for the goods offered. Third, some departments are not as diligent in their efforts to obtain best value, regardless of the procurement method used. For example, two departments purchased the same model projector through the CMAS program without considering other CMAS vendors. As a result, each department paid 40 percent more than the price offered for the same model by another CMAS vendor.

Further, the Health and Welfare Agency Data Center and the California State Lottery unnecessarily paid nearly \$70,500 to vendors acting as fiscal agents. When a subcontractor ultimately performs all of the services that a contractor has agreed to provide the State and the contractor only handles the invoicing

³ The DGS uses bulletins to disseminate policies and guidelines concerning the CMAS program. As of August 1998, the DGS had issued 19 separate bulletins. For clarity, we refer to these bulletins collectively as policy bulletins.

of expenditures, then the contractor's role becomes merely administrative in nature. If a contractor's role is just administrative, it is a fiscal agent between the State and the vendor actually performing the work. By using fiscal agents in this manner, the contracting department spends part of the total contract funds to pay unnecessary administrative costs.

DEPARTMENTS ARE NOT ALWAYS OBTAINING BEST VALUE WHEN USING THE CMAS PROGRAM

Although some departments took steps, such as comparing prices, to ensure that they obtained goods and services at a better value when they used the CMAS program, others did not. The DGS could help all departments obtain a better value when using the CMAS program to procure goods and services by requiring departments to compare prices rather than merely encouraging it. Further, the DGS could more clearly explain to departments that they need to negotiate CMAS prices in some circumstances.

Because vendors under the CMAS program do not compete against each other to be approved, a department does not necessarily obtain the best value by merely selecting any CMAS vendor to provide a product or service. Prices can vary for identical products available from different vendors through the CMAS program. For example, one vendor listed the price for a computer interface at \$17,500, while another listed the identical item at \$26,800, a difference of \$9,300, or 53 percent. Therefore, it is to a department's advantage to compare the offered prices and terms.

CMAS prices for identical products can vary significantly.

One department spent \$106,200 for computer equipment that could have been purchased from a different CMAS vendor for \$62,200 less.

Our review revealed that some departments did not take reasonable steps to ensure they were obtaining the best value for products they purchased through the CMAS program. Specifically, some did not compare the value of similar products available through different CMAS vendors. For example, the California Highway Patrol spent \$106,200 on a computer router when a different brand, also available through the CMAS program, would have cost \$62,200 (59 percent) less. Moreover, another less expensive router operated at a faster speed and was a newer generation of computer equipment. Similarly, when the California Youth Authority and the Department of Toxic Substances Control each purchased projectors, they did not consider other vendors offering the identical model projector for sale. Therefore, each spent \$2,100 (40 percent) more than the \$5,200 purchase price offered by another CMAS vendor.

COMPARISON IS NECESSARY TO ACHIEVE BETTER VALUE

Although the DGS encourages departments to comparison shop among CMAS vendors, it does not require them to do so.

Departments do not always take adequate steps to ensure they acquire goods and services at a better value for several reasons. First, although the DGS encourages departments to comparison shop among CMAS vendors to determine which one will provide the best value, it does not actually require them to perform value comparisons. Two departments told us that they did not comparison shop because of this specific language. In contrast, federal regulations provide specific guidance for obtaining best value for purchases through the federal multiple award schedules. Specifically, the Code of Federal Regulations, Title 48, Section 8.404(b), states that, for purchases above a minimum threshold, federal departments should place orders with the vendor that can provide the good or service for the best value.⁴ As part of determining best value, the regulations also state that federal departments should consider reasonably available information, such as catalogs or price lists, of at least three vendors before placing an order. According to these federal regulations, orders placed in compliance with these procedures are considered to be issued pursuant to full and open competition, to represent the best value, and to result in the lowest cost alternative to meet the government's needs.

Second, the DGS does not provide departments with adequate catalogs or other similar tools that allow them to easily compare value among vendors. For instance, the DGS's Web site listing of CMAS products is limited to descriptions of just 12 types or brand names of items per vendor. Because some vendors offer thousands of items through the CMAS program, departments may not find all vendors selling a particular product. Also, the Internet information does not allow vendors to list the specific models of goods they offer, nor does it include the prices of the goods offered. Therefore, departments must first search the Web site to identify those vendors selling a certain type of product. Then, they have to contact the identified vendors to determine whether they sell a specific good and ask them the price of that good. On the other hand, the federal government's Web site for its multiple award schedules program provides much more information to facilitate federal departments' evaluation of value. This Web site identifies the specific brands and models of a type of good, the vendors selling it, and the listed prices.

⁴ Until October 1997, the minimum threshold was \$2,500; minimum thresholds are now set in each contract.

Two departments we reviewed were more diligent in their efforts to obtain best value.

Finally, some departments are more diligent in their approach to, and practices for, obtaining best value when using the CMAS program. During our review, we observed that even though some departments did not compare value when they acquired goods and services through the CMAS program, others approached procurement as an opportunity to obtain the best value. For instance, staff of the Health and Welfare Agency Data Center (data center) and the Franchise Tax Board stated that they regularly comparison shop among vendors when purchasing goods through the CMAS program. The data center obtains and evaluates written bids from vendors when making large purchases and the Franchise Tax Board obtains and evaluates bids it takes from vendors by telephone.

We note that the DGS plans to issue written guidance concerning the proper use of purchasing methods such as the CMAS program in a manual similar to its existing *State Contracting Manual*. The DGS anticipates the release of a draft version of this guidance manual, currently referred to as the *California Acquisition Manual*, on to the Internet by January 31, 1999.

Negotiating Lower Prices Adds Value to Acquisitions

In addition to paying higher prices when they do not compare value, we believe that some departments may pay higher prices because they do not seek to negotiate price reductions from the CMAS program's list prices. We believe the opportunity for higher prices exists because the DGS's guidance concerning when to negotiate price reductions is not sufficiently clear. Although the DGS's policy bulletins state, in part, that departments are required to obtain lower unit prices when their orders exceed the higher of either the published CMAS maximum order limit or the federal maximum order limit, the DGS does not require price negotiations under other circumstances. Further, the guidance does not make sense because the CMAS program's order limits refer to maximum dollar amounts of individual purchases above which DGS approval must be sought, not to the number of goods acquired during a single purchase.⁵

⁵ The maximum order limits for acquisitions through the CMAS program are \$500,000 per transaction for information technology purchases and \$100,000 per transaction for commodity purchases.

Unlike the State's guidance, the federal government provides its departments with clear and easy-to-follow directions for negotiating price reductions.

Conversely, the guidance the federal government provides to its departments concerning purchases through the federal multiple award schedules is clear and easy for departments to follow. Specifically, federal regulations state that each contract will have an established threshold above which federal departments must seek price reductions. This threshold is stated as either a quantity or a dollar amount. The regulations further state that, before placing an order that exceeds the threshold, departments will seek price reductions from the vendors appearing to provide the best value. Finally, if a department does not obtain the sought-after price reduction, it may still place the order if it determines that it is appropriate.

If departments do not attempt to obtain price reductions when the size of their orders would otherwise require it, they may unnecessarily pay more for these goods than they should. Although we found no instances during our review in which any of the five departments failed to negotiate prices when the size of their purchase required, the value of negotiating is illustrated by examples we found at the Franchise Tax Board and the data center. Specifically, because the Franchise Tax Board negotiated its purchase of 140 computers, it saved \$95,500 (17 percent) over the vendor's initial price quote, which was already \$136,200 (20 percent) less than the CMAS list price of \$695,700. The data center also negotiated its purchase of 13 computers and a variety of computer components such as memory upgrades, monitors, and hard drives, saving \$79,500 (14 percent) over the CMAS list price of \$553,800.

DEPARTMENTS CONTRACTED WITH AND PAID UNNECESSARY ADMINISTRATIVE COSTS TO FISCAL AGENTS

Our review also disclosed the improper use of fiscal agents. Similar to instances we describe in our last contract report issued in July 1997, the data center and the California State Lottery unnecessarily paid nearly \$70,500 to vendors acting as fiscal agents.

Improper use of fiscal agents wastes State money. When a subcontractor ultimately performs all the services a contractor agreed to provide the State, the contractor's role—the invoicing of expenditures—is merely administrative in nature. The contractor is, in effect, a fiscal agent between the State and the

When a contractor's role is just administrative, state funds are wasted.

vendor actually performing the work. By using fiscal agents in this manner, the contracting department is spending part of the total contract funds to pay unnecessary administrative costs.

The State needs to provide sufficient guidance to prevent abuses of the spirit and intent of its contracting laws and policies. If departments do not have adequate controls to prevent their staff from circumventing laws and policies related to public contracting, they reduce the likelihood of fairly acquiring goods and services at the best value. If a department does want to consider hiring a specific vendor to provide a service, it could, by meeting certain conditions, hire the vendor using a sole-source contract, or it could assist the vendor in becoming an approved CMAS vendor. Both of these methods are preferable to the use of a fiscal agent, which represents an unnecessary cost.

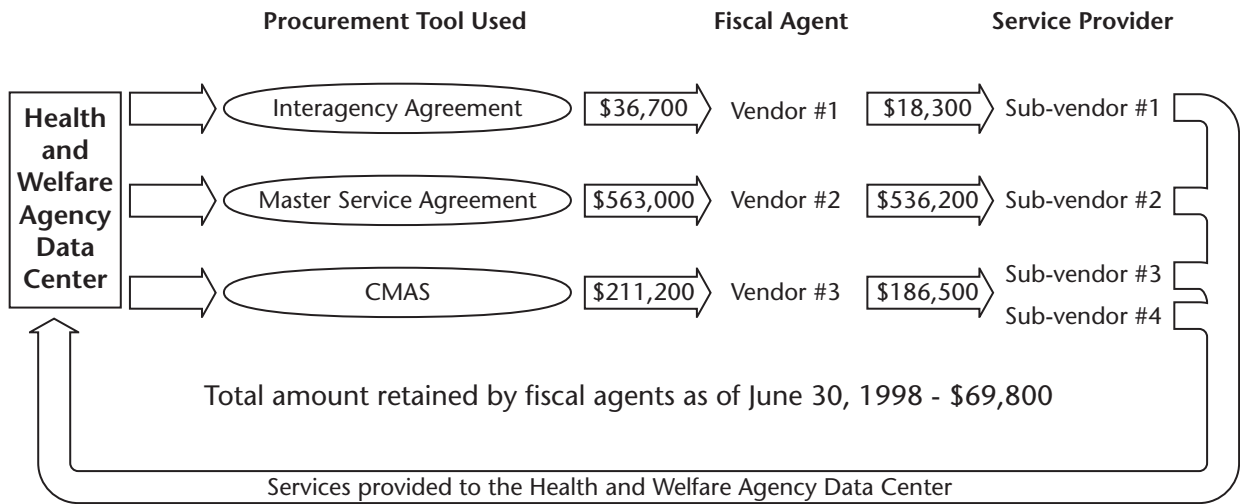
Our review disclosed instances in which two state departments improperly used fiscal agents to obtain services. First, the data center improperly contracted to pay three vendors for their role as fiscal agents. As of June 30, 1998, 9 percent of the \$810,900 the data center had paid for services, or \$69,800, had gone to the three fiscal agents as mere overhead. The data center used as fiscal agents not only another governmental entity with which it had an interagency agreement but also a vendor from the CMAS program and another from a master service agreement. Regarding the instances with the CMAS and master service agreement vendors, the data center entered these contracts because it wanted to hire the specific sub-vendors to perform certain assignments. Regarding the interagency agreement, the data center asked the vendor to provide a consultant from its list of subcontracts. In this instance, the data center used an interagency agreement to contract with the Los Rios Community College District (district).⁶ The district, in turn, hired a subcontractor to perform the services rather than have its own employees or students perform them.

Figure 3 depicts the relationships that existed between the data center, the fiscal agents, and the service providers.

⁶ According to the DGS, because the district is not a state agency, an interagency agreement did not, in fact, exist between the data center and the district. Notwithstanding the DGS's point, the procurement tool used by the data center in this instance was an interagency agreement.

FIGURE 3

Improper Use of Fiscal Agents Resulted in Unnecessary Administrative Costs



The other agency we identified, the California State Lottery (lottery), inappropriately obtained a trainer’s services through an established master service agreement vendor in April 1996. The lottery paid a total of \$7,760 under the contract, of which 10 percent, or \$776, the vendor earmarked as an administrative fee. During our audit, lottery staff provided us with the policies it implemented six months later, in October 1996, that reduced the likelihood of this event happening again.

We stated in our previous contracting report, *State Contracting: Improvements Are Still Needed To Ensure the Effective Use of Public Resources*, Report 96015, that we would determine the effectiveness of DGS’s policy changes regarding fiscal agents and interagency agreements. Except for the previous examples, we found that the use of governmental entities as fiscal agents is not as prevalent as in the past; our review disclosed no other instances in which departments inappropriately used interagency agreements to circumvent laws or policies related to public contracting. In fact, the Department of Toxic Substances Control incorporates as part of its contracts standard language that instructs the other entity to obtain the department’s approval before subcontracting the tasks of the contract. The contract also briefly describes the appropriate procurement method to obtain a subcontractor when it is not an employment contract. Therefore, based on our limited review, the DGS’s policy prohibiting the use of interagency agreements to obtain fiscal agents appears effective. We are concerned, however, that

no such specific policies clearly prohibit the use of the CMAS program, master service agreements, or other leveraged procurement tools in this manner.

CONCLUSION

When departments procure goods and services through the CMAS program, master service agreements, and interagency agreements, they are not always obtaining the best value possible. For example, some departments purchase items through the CMAS program without adequately assessing value, thereby paying more for goods than necessary. Additionally, departments paid unnecessary administrative costs for fiscal agents acquired with contracts entered through the CMAS program, master service agreements, and interagency agreements.

RECOMMENDATIONS

The DGS needs to take steps to increase the value of the purchases that departments make when using the CMAS program. These steps include the following:

- Require departments to compare value when the cost of the good or service offered by a CMAS vendor exceeds a predetermined threshold, rather than merely encouraging them to compare prices for products.
- Require departments to negotiate reductions in CMAS list prices when the size of their purchase warrants it.
- Provide departments with sufficient, easy-to-use tools to help them determine value. Such tools include improved Internet resources or catalogs organized by product that include price.

In addition, when it issues its guidance manual for purchasing, the DGS should include a provision that prohibits the use of any vendor as a fiscal agent, regardless of the procurement method used to obtain the vendor. ■

CHAPTER 2

The Department of General Services Can Improve Its Procurement Administration and Oversight

CHAPTER SUMMARY

The Department of General Services (DGS) provides several different methods to state departments that enable them to fairly procure goods and services at an acceptable value. Our review identified several shortcomings in the DGS's administration and oversight of these methods. For instance, because of weaknesses in its oversight of the California Multiple Award Schedules (CMAS) program, the DGS has failed to ensure that vendors adequately comply with their contractual obligations and has missed opportunities to help departments identify potential weaknesses in their own purchasing procedures.⁷ Similarly, weaknesses in its oversight of master service agreements has led to reduced assurance that departments are properly using this contracting method.⁸ Further, inconsistencies in the advice provided by the DGS may have hindered departments' ability to efficiently acquire the goods or services they need. Finally, as we reported last year, because of the DGS's inability to produce a complete and accurate list of master service agreements, departments cannot always take full advantage of the State's collective buying power. Departments are also hindered in their efforts to determine whether they can receive better value by obtaining services through competitive bids or through master service agreements.

⁷ We more fully describe the CMAS program in Appendix A and Appendix B.

⁸ A master service agreement is a contract between the DGS and vendors from which any state entity may acquire the services described in the contract. For more information about master service agreements, please see Appendix A and Appendix C.

THE DGS DOES NOT ADEQUATELY OVERSEE THE CMAS PROGRAM

Our evaluation disclosed several weaknesses in the DGS's reviews of CMAS vendors. For example, the DGS does not conduct a sufficient number of reviews of CMAS vendors. By not conducting more reviews, the DGS increases the risk that vendors will not comply with their contract obligations. Additionally, the existing scope of the DGS's vendor reviews does not include an examination of whether vendors comply with the price-reduction clause of their contracts. Thus, the DGS fails to identify additional instances when vendors should have sold goods or services to the State at a lower cost. Moreover, the DGS does not adequately resolve instances of noncompliance identified during the reviews; this could give vendors the impression that compliance with CMAS program requirements is not important, leading to further instances of noncompliance. Finally, the DGS does not communicate the results of its vendor reviews to affected departments. As a result, these departments may miss opportunities to promptly correct procedural problems.

The DGS does not conduct a sufficient number of vendor reviews to assure compliance with contract obligations.

The DGS's CMAS unit is responsible for reviewing CMAS vendors to ensure that they comply with the terms of their contracts. Among other things, the unit determines whether a vendor sold items to the State at prices higher than those stated on its CMAS price list or sold items not included on its price list.⁹ To select the vendors for its reviews, the DGS appropriately targets those vendors with the highest dollar amounts of sales. For example, of the 17 vendors the CMAS unit had reviewed as of April 1998, 12 were in the top 20 in terms of sales from January 1995 to September 1997. Also, when it conducts reviews, the DGS is successful in identifying instances of vendor noncompliance. For instance, the results of its review of one vendor indicate that the DGS identified \$311,000 in overcharges and \$4.4 million in services or products sold to the State that the vendor was not authorized to provide.

⁹ The federal government and other entities from which the DGS obtains CMAS vendors agree upon the items the vendor may sell and the prices at which they may sell them. Once approved, the entities consider the vendors' prices for these items to be reasonable, although perhaps not the best value when compared with other vendors approved to sell the same items. When vendors sell items that are not on their approved CMAS price lists, the State has no assurance that it purchased these items at a reasonable price.

The DGS had reviewed only 17 of the 880 CMAS vendors in the four years since the program's inception.

The DGS Does Not Conduct Enough Reviews

We believe that the DGS reviews too few vendors. As of May 1998, the CMAS program had about 880 vendors. While it is reasonable to conclude that not all 880 vendors produced enough sales to warrant attention, the DGS completed reviews of only 17 CMAS vendors from the inception of the program in 1994 through April 1998. Seven other reviews remained in progress at that time. DGS records indicate that CMAS sales during fiscal year 1997-98 totaled \$370.5 million. Although we did not determine an optimum number of reviews to conduct, we believe the DGS increases the risk that vendors will fail to comply with their contractual obligations when it completes so few reviews of a relatively new program. Therefore, the DGS is failing to ensure that the State's best interests are safeguarded.

The value of vendor reviews is demonstrated by the results found by both the DGS and the federal government. For example, in the six vendor reviews that we examined, the DGS identified overcharges of \$376,000 and sales of non-approved CMAS items totaling \$6.7 million. Further, from October 1, 1995, through September 30, 1997, the federal government reviewed nine vendors that were approved for both the state and federal programs and identified more than \$12 million in questionable sales to federal departments. To date, the DGS has reviewed one of these vendors. We believe that a vendor who has not complied with federal requirements is also likely to not comply with CMAS program requirements, and that the DGS should include these vendors in its own review process.

We believe that reviewing CMAS vendors is not a high priority in the DGS. The deputy director of the Procurement Division stated that the staff of the CMAS program are responsible for all aspects of the CMAS program, including processing vendor contracts, conducting training and outreach activities, reviewing vendor activity reports, and performing reviews of vendor compliance. However, he also stated that during the first few years of the CMAS program, CMAS staff have focused on program implementation activities more so than vendor reviews.

Alternatives exist that the DGS should consider to increase the number of vendor reviews. For instance, the DGS could increase the resources in the CMAS program devoted to performing vendor reviews, or it could have staff of other units within the DGS perform the reviews. Further, should it choose to move responsibility for vendor reviews to a unit such as the internal

audit unit that has experience in reviewing programs, the DGS could take advantage of the training and skills these staff possess. Another alternative the DGS could consider is to contract with an auditor on a contingency-fee basis to conduct vendor reviews and any necessary follow-up. In this situation, the DGS would pay a predetermined portion of any recoveries made from instances of noncompliance identified by the contracted auditor.

The DGS Does Not Review for Price-Reduction

In addition to reviewing a small number of vendors, the DGS did not evaluate vendors' compliance with a critical requirement. Although the DGS takes steps to identify whether a vendor charged the State prices higher than those on its CMAS price list or sold the State items not included on the price list, it does not include steps designed to determine a vendor's compliance with the "price-reduction clause" of its contract. The price-reduction clause provides that if a vendor sells any item covered by the contract at a price below the negotiated contract price to a customer comparable to the State, then the vendor must give the State an equivalent price reduction on all subsequent orders for the balance of the contract period or until the price is further reduced. Although this clause is not specifically stated as part of a vendor's CMAS contract, it is incorporated by reference from the vendor's federal multiple award schedule contract. By not including the price-reduction clause as part of the reviews, the DGS fails to identify additional instances when the vendor should have sold products to the State at a lower cost.

By not ensuring vendor compliance with price reduction clauses, the DGS fails to identify instances when products should have been sold cheaper to the State.

The federal General Services Administration's Office of Inspector General believes that vendor audits are one of the most important tools to detect and recover overpricing. These audits give the federal government the ability to monitor vendor compliance with defective pricing. A defective price is one that is higher than that on the federal multiple award schedule price list or not in compliance with the price-reduction clause. The Office of Inspector General also believes that a lack of vendor audits would be "tantamount to handing the contractors 'carte blanche' to violate contract terms." According to reports submitted to the U.S. Congress, the federal government identified \$39.1 million in defective pricing through the 225 reviews it conducted from October 1995 through September 1997.

In response to our question concerning why the DGS does not include the price-reduction clause within the scope of its vendor reviews, the deputy director of the Procurement Division stated that the State generally relies on the federal government to monitor the negotiated price with suppliers for their federal contracts. However, the deputy director's assertion does not respond to our concern that the DGS has little assurance that vendors under California's program comply with the price-reduction clause and give the State all applicable discounts during the term of their contracts.

The DGS Does Not Adequately Resolve Noncompliance Issues

The DGS does not aggressively pursue collection of CMAS vendor overcharges.

The third weakness we identified is the DGS's inadequate resolution of instances of noncompliance found through its vendor reviews. The DGS does not aggressively pursue collection of overcharges by using offsets or credits against future purchases or by charging interest on balances owed, nor does it assess penalties for violations of CMAS program requirements. Such inaction by the DGS enables vendors to take advantage of state departments that purchase items through the CMAS program. For example, in June and July 1998, the California Youth Authority purchased 97 computers from a CMAS vendor that cost a total of \$6,400 more than the CMAS-approved price. Further, the California Youth Authority purchased 26 other computers that the vendor was not approved to sell through the CMAS program. However, nearly 18 months earlier, in January 1997, the DGS had reviewed this vendor, citing concerns such as overcharging departments and selling them items through the CMAS program for which it was not approved.

We examined the actions the DGS took to resolve issues identified in six vendor reviews it conducted. In one review, the DGS notified a vendor in October 1996 of \$311,000 in overcharges and \$4.4 million in sales of non-CMAS items. Although the DGS insisted that the vendor discontinue such practices immediately and required the vendor to submit a plan for corrective action within one month after the review, it did not adequately follow up on the vendor's actions. As a result, it was not until June 1998, 20 months later, that the vendor issued letters of credit to the departments it overcharged.

In another review, issued in November 1996, the DGS identified \$1.8 million in unauthorized products that a CMAS vendor sold to the State as well as \$14,600 in overcharges. Although the DGS notified the vendor of these issues, the DGS provided no

Despite identifying \$1.9 million in unauthorized sales and \$14,600 in overcharges by one vendor, the DGS has not obtained corrective action after 21 months of effort.

evidence that the vendor corrected the overcharges or provided information about measures taken to prevent such problems from happening in the future. A second review of this same vendor seven months later, in July 1997, found an additional \$14,900 in unauthorized sales. Although the DGS directed the vendor to respond in writing to its concerns by August 20, 1997, the vendor did not do so until December 22, 1997, four months after the DGS's deadline. Further, in its response, the vendor acknowledged the findings but did not provide detailed corrective action. In March 1998, the DGS notified the same vendor of the results of a third review in which it identified \$123,900 more in unauthorized sales. The DGS gave the vendor one month to respond in writing and told it that a failure to adequately respond would result in cancellation of its CMAS contract. More than four months later, the vendor had not yet responded to the DGS and the DGS had not canceled the contract. In fact, the DGS notified the vendor on August 17, 1998, that it intended to review the vendor yet again "sometime within the next year." Consequently, despite the efforts of three separate reviews and follow-ups conducted over 21 months, the DGS has not obtained corrective action or disciplined a vendor who sold more than \$1.9 million in unauthorized products to the State and overcharged the State \$14,600. We believe the State has thus received little benefit from the resources spent conducting these reviews.

As of August 21, 1998, the DGS had resolved only one of the six reviews and had not penalized any of the vendors. In fact, although the DGS tells CMAS vendors that they may be removed from the CMAS program for contract noncompliance issues found during vendor reviews, it stated in September 1998 that it has not carried out such ultimatums because there have not been any instances of noncompliance that warrant such actions.

By not vigorously pursuing and penalizing noncompliant vendors, the DGS could give the impression that compliance is not important. This could lead to further instances of non-compliance that could cost the State more money on future purchases. Further, because the DGS does not require prompt repayment of overcharges, vendors can inappropriately hold state funds, thus denying the State the opportunity to earn interest on those funds.

In contrast to the DGS's weak follow-up practices, the Inspector General Act of 1978 and internal departmental policy require the federal government to vigorously pursue recovery from

In contrast to state efforts, remedies employed by the federal government for noncompliant vendors include contract termination, civil lawsuits, and criminal indictments for fraud.

noncompliant vendors through administrative, civil, or criminal remedies. Administrative remedies include suspension or removal of the vendor from the multiple award schedule program, civil remedies include lawsuits to recover overcharges, and criminal remedies include indictments for fraud. In some instances, the federal government can even recover triple damages from a vendor. In one case, the federal government reviewed a vendor's multiple award schedule contract for the years 1990 through 1994 and found that the vendor regularly overcharged federal customers. The vendor agreed to pay \$450,000 to settle a potential civil liability in addition to returning or crediting \$80,000 to federal departments.

The DGS Does Not Notify Departments of Review Results

The final weakness we identified is that the DGS does not inform affected departments of the results of its CMAS vendor reviews. This information could help departments determine whether weaknesses exist in their own purchasing procedures. For example, in one review issued in January 1997, the DGS identified 35 instances in which a vendor charged 14 departments prices higher than those allowed by the CMAS contract. As a result, these departments paid a total of \$15,800 more than necessary to this vendor. Also in this review, the DGS identified more than 300 purchases of items that the vendor was not approved to sell under the CMAS program. If the DGS had informed these departments about the types of issues it found, the departments could have strengthened their procurement procedures to ensure that they did not pay prices for a good or service higher than those on the CMAS price list and did not purchase non-approved items. However, the DGS did not provide the departments with this information. As a result, even though the January 1997 review identified two computers purchased by the California Youth Authority from that were not on the vendor's CMAS list, the California Youth Authority purchased 123 computers from this vendor in June and July 1998 that either cost more than their CMAS list price or were non-CMAS approved items. These purchases occurred about 18 months after the DGS's review was issued to the vendor.

THE DGS PROVIDES WEAK OVERSIGHT OF MASTER SERVICE AGREEMENTS

The DGS provided no evidence that it reviews or evaluates departments' use of master service agreements. For example, although the DGS requires departments to submit a form that describes how they selected a vendor from a master service agreement, the DGS provided no evidence that it reviews these forms to ensure that the selection process used was in accordance with the master service agreement's ordering procedures. The lack of a substantive review of these forms reduces the State's assurance that departments are appropriately using master service agreements. Inappropriate use of master service agreements includes instances when departments purchase services different from those allowed by that master service agreement. For example, we question whether the California State Lottery (lottery) appropriately obtained stress management training from a master service agreement created to provide services related to information technology. The lottery justified its hiring of this trainer by stating on the form, "This vendor ... provides staff [with] knowledge of stressors in a technological age." Even though the lottery obtained these services through the "miscellaneous" category of the master service agreement, the services described in that category are all related to information technology. We do not believe that stress training is an information technology service, but because the DGS does not review these forms, it did not act on the lottery's statement.

Because the DGS does not evaluate departments' use of master service agreements, the State cannot be sure it receives full value for these contracts.

In addition, because the DGS does not evaluate whether departments are properly managing their use of master service agreements, there is no assurance that the State is receiving full value for these contracts. For example, the Health and Welfare Agency Data Center (data center) agreed to pay more than double the original amount of a master service agreement order (contract) without also amending the contract to require the contractor to perform additional tasks or to produce additional deliverables. The data center had entered into a contract for almost \$29,000 for consulting services from a contractor off a master service agreement. The term of the contract was for three months, during which time the consultant was to produce and deliver certain documents. The data center amended the contract three times, extending the contract for an additional three months and increasing the total amount of the contract to more than \$59,000. However, all three amendments stated that the original scope of work would remain the same. Ultimately, the

One department paid a contractor about \$7,000 more than the contract amount without requiring more work.

data center paid the contractor almost \$36,000, or about \$7,000 more than the original contract amount, without requiring the consultant to perform additional tasks.

We asked the data center if the consultant did actually perform additional tasks beyond the original scope of the contract. In addition, we requested that the data center provide documentation to support or justify the additional money added to the contract. Although the data center believes that the consultant might have performed some additional duties beyond the original scope of work, it did not know exactly what was done. Further, it did not provide any documentation to indicate what, if any, duties the consultant performed during the additional three months of the contract other than what was required in the original scope of work.

THE DGS DOES NOT ALWAYS PROVIDE CONSISTENT ADVICE

We found one instance when the DGS provided a department with inconsistent advice. As the State's central source for contracting and purchasing information, the DGS is responsible for providing clear, useful, and consistent guidance for conducting state contracting and purchasing. When such guidance is not present, departments could lose staff time because of the resulting confusion.

The different divisions of the DGS need to give consistent advice to departments; when they do not, it can hinder departments' ability to procure needed goods and services. Specifically, staff of one of the departments we visited sought DGS advice about how to make a particular purchase that involved a product and the labor necessary to modify the product to conform it to department needs. The Office of Legal Services and the Procurement Division each gave the department different advice for determining whether the acquisition should be handled as a contract for services or as the purchase of a good. The department told us that the Office of Legal Services advised that contracts resulting in a product are considered commodity contracts and, as such, should be acquired by using a purchase order. However, the Procurement Division advised the department that a purchase that has more than 50 percent of its total cost as labor charges is considered a service contract and, as such, should be acquired by using a contract. Ultimately, the department obtained the good by using a service contract.

The Office of Legal Services and the Procurement Division are aware of this issue and are in discussions attempting to determine how best to resolve it.

As we note in Chapter 1, the DGS plans to issue written guidance concerning the proper use of purchasing methods in a manual similar to its existing *State Contracting Manual*. The DGS anticipates the release of a draft version of this guidance manual, currently referred to as the *California Acquisition Manual*, on to the Internet by January 31, 1999.

THE DGS MAINTAINS NO CURRENT AND COMPLETE LIST OF MASTER SERVICE AGREEMENTS

As of June 30, 1998, the DGS had not made available to state departments a complete list of all master service agreements, despite our recommendation last year that they do so. In our report, *State Contracting: Improvements Are Still Needed To Ensure the Effective Use of Public Resources*, Report 96015, issued in July 1997, we recommended that the DGS ensure a complete updated listing of all master service agreements is sent to the appropriate personnel at every state department. The DGS created a Web site that lists many master service agreements and distributes a quarterly document that includes many master service agreements, but neither source provides a complete list of all master service agreements in existence. For example, the Internet Web site fails to show the master service agreement for parcel mail sorting and the quarterly list fails to show the master service agreement for local area network computer services. In fact, both sources combined still fail to show all master service agreements in existence. Specifically, neither source shows the master service agreements for unarmed security guards and for credit card processing, which we found listed in a database maintained by the Office of Legal Services.

Without a complete list of all agreements, departments have fewer opportunities to determine whether they can receive better value by obtaining services through a competitive bid or through a master service agreement.

As we reported in July 1997, if the DGS does not make available a comprehensive list of master service agreements, state personnel may not be aware of their existence and cannot take full advantage of the State's collective buying power. Further, without a complete list, departments have fewer opportunities to determine whether they can receive better value by obtaining services through a competitive bid or through a master service agreement. For example, while visiting one of the five departments, we learned that it had competitively bid a contract for shorthand reporting services in June 1996. Although the DGS

had issued a master service agreement for shorthand reporting services in May 1996, the department's purchasing unit was not aware of its existence. As a result, the department was not able to consider whether it would be more cost effective to use the master service agreement.

The DGS stated that it is not practical to distribute a list of master service agreements to appropriate personnel at state departments because it cannot determine which staff should receive such a list. Some purchasing decisions, it argues, are made by staff in the purchasing office while others are made by staff in other offices or in the field. Therefore, the DGS claims, it is very difficult to identify the personnel at each department who would benefit from having a list of master service agreements. The DGS believes that its Internet Web site is a better solution because it is a central location that all staff can access and, therefore, has put a listing of master service agreements there. This is in addition to the list it includes in its hard copy quarterly checklist of statewide contracts that it distributes to departments.

A complete list of master service agreements would enable departments to take full advantage of the State's purchasing power.

While we do not dispute the DGS's contention that it is difficult to identify appropriate personnel, this problem is easily resolved by sending the list to department directors with a request that they forward it to appropriate personnel. However, the DGS's response does not address the issue of completeness. Although the DGS provides state personnel with two listings of master service agreements, neither listing is comprehensive, nor do the two fully agree with each other. Regardless of the method used to distribute the list, it is imperative that the DGS compile a complete list of available master service agreements. This would enable state departments to take full advantage of the State's purchasing power and provide them with an opportunity to determine if there is better value available through these agreements or through competitive bidding.

CONCLUSION

The DGS does not adequately oversee or administer some of its newer procurement methods, which results in departments not always using these methods efficiently. For example, the DGS does not conduct enough compliance reviews of CMAS vendors and does not adequately follow up on those few vendor reviews it does perform. Moreover, the scope of these reviews does not include a critical contractual requirement put in place to help

the State obtain lower prices on goods and services. The DGS also does not provide the results of its vendor reviews to those departments that are affected by vendors' noncompliance. Further, the DGS is not adequately reviewing transactions under master service agreements, and, although we recommended in our last contracts audit that the DGS develop a complete list of all master agreements, it has yet to produce such a listing. Finally, the DGS provided advice that was inconsistent with regards to acquisitions involving a combination of labor and product.

RECOMMENDATIONS

To improve its oversight of the California Multiple Award Schedules (CMAS) program, the Department of General Services (DGS) should take the following actions:

- Optimize its vendor reviews. For instance, the department could devote additional resources to conduct more reviews, move responsibility for performing vendor reviews to a unit that has experience in reviewing programs and following up on identified deficiencies, or contract with independent auditors on a contingency-fee basis to conduct vendor reviews and any necessary follow-up.
- Increase the number of CMAS vendor reviews it conducts annually.
- Consider using the results of federally-conducted vendor reviews to help determine which vendors it will review.
- Include within the scope of its vendor reviews an examination of a vendor's compliance with the price-reduction clause of its contract.
- Communicate results of its vendor reviews to applicable departments when appropriate. Such instances would include when the DGS identifies examples of departments paying vendors more than their CMAS list price for a product or service.
- Develop and implement written procedures for efficient and effective follow-up on the results of the vendor reviews. These procedures should include penalties such as suspending or removing the vendor from the CMAS program.

To ensure that departments do not misuse master service agreements, the DGS should begin routinely reviewing departments' master service agreements transactions.

To help minimize confusion in those departments that must follow its guidance, the DGS should provide clear and consistent direction on all state contracting and purchasing issues.

To enable departments to take full advantage of the State's collective buying power, the DGS should make available a listing of master service agreements that is both complete and accessible to appropriate personnel at all departments.

Finally, because of the number of concerns regarding the CMAS program and master service agreements that we mention in this chapter and in Chapter 1, the DGS should include a review of the usage of these procurement methods as part of the scope of its existing evaluations of departments.

We conducted this review under the authority vested in the California State Auditor by Section 8543 et seq. of the California Government Code and according to generally accepted governmental auditing standards. We limited our review to those areas specified in the audit scope section of this report.

Respectfully submitted,



KURT R. SJOBERG
State Auditor

Date: October 15, 1998

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APPENDIX A

Procurement Methods Available to State Departments

Procurement methods generally fall into one of two categories, traditional or leveraged.

TRADITIONAL PROCUREMENT METHODS

Traditional methods include competitively-bid contracts, sole-source contracts, and interagency agreements.

Competitive Bidding

Unless otherwise excepted, the Public Contract Code requires departments to use competitive bidding to acquire goods or services. Under competitive bidding, an agency will prepare a request for proposals, invitation for bids, or similar solicitation. In these solicitations, the department describes, among other things, the good or service it plans to acquire, the procedures bidders should use to submit a proposal or bid, and the factors the department will use to evaluate the proposals or bids. These solicitations are also generally advertised in the *California State Contracts Register*. Typically, the lowest responsible bidder—or in the event factors other than price alone are considered for award, the bidder that best meets the selection criteria—will be awarded the contract for the good or service. With certain exceptions, state law and policies issued by the Department of General Services (DGS) require departments to offer several vendors a chance to provide price quotes or proposals for procurements of \$1,000 or more.

Sole-Source Contracting

On certain occasions, a department may need to contract with a specific vendor. These are referred to as sole-source contracts. The *State Contracting Manual* describes the conditions under which it is appropriate to issue sole-source contracts as well as those under which the DGS's approval is required.

Contracts Between State Agencies

An interagency agreement is a contract between two state agencies in which one is supposed to provide services to the other. These agreements are advertised as a way for departments to use existing state resources and provide improved public service without adding unnecessary costs related to administering the bidding process or profit paid to a private vendor. Because interagency agreements are exempt from competitive bidding requirements, state departments can enter into these arrangements without going through the bidding process. However, in prior audit reports, we disclosed that state departments often used interagency agreements to circumvent existing state laws regarding competitive bidding. Rather than using existing government resources, the departments misused interagency agreements to enter into sole-source contracts with private parties. In some cases, the department desiring the service identified the subcontractors before it entered into the agreement with the other department. These departments have, in effect, awarded sole-source contracts to private vendors without obtaining the approvals that are normally required when following established contracting procedures.

The DGS, however, initiated requirements to prohibit this use of interagency agreements in July 1996. Specifically, if the work specified in the contract is to be accomplished by staff of the other department, that department need not take any additional steps. On the other hand, if a material portion or all of the work is to be performed by a subcontractor to the other department, that department is generally required to competitively bid the availability of the work.

LEVERAGED PROCUREMENT METHODS

Leveraged procurement methods include the California Multiple Award Schedules (CMAS) program, master agreements, state price schedules, and statewide contracts. The DGS intends leveraged procurement methods to provide state departments with lower prices by negotiating bulk discounts based on the purchasing needs of the entire State. In other words, the DGS attempts to use the State's overall purchasing power to bargain from a position of strength.

The California Multiple Award Schedules Program

The DGS implemented the CMAS program in 1994 as an easy and value-effective method through which departments could procure commodities and information technology goods and services. Appendix B lists some of these types of goods and services. The CMAS program establishes contracts with vendors that offer products or services that are already on existing multiple award schedules operated by the federal government or on other approved multiple award contracts. State departments can buy products from a CMAS vendor without going through any bidding process; they simply choose a vendor and place an order. However, with few exceptions, vendors may only sell, and departments may only buy, products and services specifically identified on a vendor's approved CMAS contract. For example, a vendor that is listed to sell desks but not chairs cannot sell chairs through the CMAS.

The DGS has imposed a general spending cap of no more than \$500,000 for each information technology acquisition and no more than \$100,000 for each commodity acquisition made by a specific department. However, on some occasions, the DGS has authorized exemptions to these limits when departments have justified the need to do so.

A vendor can receive DGS approval to sell goods or services through the CMAS in two ways. If a vendor agrees to provide goods or services to the State at the same terms as it does to the federal government or other multiple award contract, the DGS will approve the vendor's application to become a CMAS vendor. The second way to become a CMAS vendor is to agree to provide a good or service at the same terms as a vendor that is already approved as a federal vendor or a CMAS vendor. About 90 percent of the CMAS vendor contracts are based on the federal government's multiple award schedule contracts.

According to the DGS, the federal government and other entities conduct price analyses to determine whether the discounts offered by vendors are reasonable and to ensure that vendors are offering prices that are less than those offered to the general public. The DGS relies on these price analyses because it does not perform any itself and it does not require departments that use the CMAS to perform additional price analyses when procuring from CMAS.

Master Agreements

Master agreements are contracts that the DGS establishes with vendors to provide specified goods or services to any state entity. While many types of services can be acquired through master agreements, only a few types of goods are available. There are three types of master agreements available for departments to use. Master rental agreements allow departments to rent goods such as computer equipment from private vendors. Master purchase agreements allow departments to purchase information technology goods from private vendors. Although the purpose of master purchase agreements overlaps with that of the CMAS, the DGS believes that offering choices to departments helps them meet their individual needs. Finally, departments can use master service agreements to acquire services and some types of goods. A list of master service agreements we identified during our audit can be found in Appendix C.

The DGS normally establishes a master service agreement through competitive bidding and may choose one or more vendors for a particular good or service. When the DGS chooses more than one vendor to provide services, it may, depending on the nature of the master service agreement, prescribe a variety of procedures a department must follow to select the vendor it will use. For instance, one master service agreement requires the department to give the lowest-priced vendor the first opportunity to accept an assignment. If this vendor cannot accept the assignment, the department must then offer it to the second-lowest priced vendor. On another master service agreement, the DGS prescribes no such steps. Also, although several master service agreements encourage but do not require departments to obtain and evaluate proposals from more than one vendor, they explain that doing so enables departments to obtain the most value-effective services. These master service agreements also describe the specific steps departments should take to ensure they obtain the most value-effective acquisition possible.

State Price Schedules

Departments may also use state price schedules to acquire goods. Under the state price schedules, a vendor must agree to provide a specific good at a set price for a specified span of time. A department to which the DGS has delegated purchasing authority need not go through a bidding process when using the state price schedules so long as its order is under \$15,000.

Departments typically are not obligated to purchase from any vendor on the state price schedules. However, there is one vendor on the state price schedules from which departments must purchase. If the Prison Industry Authority (PIA) sells a certain good through a price schedule, departments are required to purchase that good from the PIA and cannot go elsewhere to buy it without the PIA's approval.

Statewide Contracts

Statewide contracts are very similar to the state price schedules; vendors make agreements with the State to provide a specific product or service at a set price for a fixed span of time. However, unlike the state price schedules, there are amounts set forth in each statewide contract that the State is required to purchase; departments cannot procure a product or service through other means if it is available through a statewide contract. For example, because there is a statewide contract for vacuum cleaners, departments are required to buy all their vacuum cleaners through that contract. Also, these departments need not go through a bidding process and there is no dollar limit per order. Many types of products are sold through statewide contracts, but only a few services are available.

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APPENDIX B

Goods and Services Available to State Departments Through the California Multiple Award Schedules

The California Multiple Award Schedules (CMAS) are contracts through which vendors agree to provide products or services at or below a predetermined price to any state department that needs them.¹⁰ Many types of products or services offered on the CMAS have multiple vendors, which allows departments to compare prices and other terms to determine the best value from the CMAS.

The list below is a general description of some of the types of products and services available to departments through the CMAS as of April 14, 1998.

Type of Product or Service Offered	Number of Vendors	Type of Product or Service Offered	Number of Vendors
Anti-Theft Devices (for computers and office equipment)	2	Identification Systems and Materials	3
Bomb, Drug, and Explosive Detectors	2	Internet Security	9
Cash Registers	2	Laboratory Instruments/Equipment	8
Clothing (athletic, recreation, medical, special purpose)	1	Laboratory Supplies	3
Conferencing Equipment	8	Lawn and Agricultural Equipment	2
Construction Equipment and Materials	2	Mailing Equipment and Systems	4
Consulting—Database Design	25	Office Machines	9
Consulting—Information Technology Strategic Plans	16	Optical Readers	3
Consulting—Internet Web Design	5	Photographic Equipment and Accessories	1
Consulting—Network Design	40	Printing Equipment	2
Consulting—Project Manager	4	Project Planning	4
Consulting—Software Design	10	Radio Antennas	3
Consulting—Year 2000 Conversion	15	Radio Receivers	4
Copier Accessories	12	Recording Equipment—Audio	2
Copier Equipment	12	Security—Access Control	2
Copier Supplies	14	Security—X-Ray Equipment	2
Electronic Data Processing Hardware and Peripheral Equipment	22	Service—Equipment Maintenance	24
Facsimile Equipment	15	Service—Hardware Repair	39
Forklifts	2	Service—Network Cabling	9
Furniture	10	Signs	2
Global Positioning Systems and Services	1	Telephone Paging Equipment	3
		Vehicles—Alternative Fuel Sedans	3
		Video Projection Equipment	8
		Voice Mail Systems	19

¹⁰ For more detailed information about the CMAS program, please see Appendix A.

APPENDIX C

Services Available to State Departments Through Master Service Agreements

Master service agreements are contracts through which vendors provide agreed-upon services at a predetermined price to any state department. Although the Department of General Services (DGS) typically creates master service agreements, other state departments can administer them. If more than one vendor is selected to provide the same service, the hiring department must choose one. We present a more detailed description of master agreements in Appendix A.

As we noted in Chapter 2, as of June 30, 1998, the DGS had not made available to state departments a complete list of all master agreements despite our recommendation in last year's state contracting report that it do so. The following list describes the types of services provided under master service agreements current as of June 30, 1998, that we identified from available DGS records during our audit. We also include the number of vendors who provide each type of service.

Type of Service Offered	Number of Vendors	Type of Service Offered	Number of Vendors
Automated Federal/State Legislative Bill Tracking and Related Services	4	Maintenance Services for AM Multigraphics Brand Equipment	1
Certified Shorthand Reporters	16	Maintenance Services for CP Bourg Brand Equipment	1
Claims Adjusting & Investigative Services	1	Maintenance Services for Dictaphone Brand Dictation Equipment	1
Computer Programming/Systems Analysis (Short-Term Personnel Services)	7	Maintenance Services for Neopost Brand Equipment	1
Computer-Related Project Management Services	56	Maintenance Services for Pitney Bowes Brand Equipment	1
Computer-Related Services to Fix Year 2000 Problems	43	Pagers and Pager Services	4
Conversion of Documents to Microfilm	16	Parcel Mail Sorting and Expedited Delivery	1
Credit Card Issuance	1	Public Access Telecommunications Services	2
Credit Card Processing	4	Quality Management Training Services (administered by the Department of Personnel Administration)	165+
Debt Collection Services	33	Specialized Restoration Services	1
Document Imaging and Records Consulting Services	8	Strategic Management Consulting	20
Electronic Legal and General Information Libraries	2	Telecommunications Billing Auditing	2
Internet Services	5	Telecommunications Consulting Services	8
Key Data Entry Services	3	Unarmed Security Guard Services (administered by the California Highway Patrol)	2
Legislative Bill Delivery	1	Utility Bill Auditing	3
Local Area Network Services	5		

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Agency's response to the report provided as text only:

State and Consumer Services Agency
Office of the Secretary
915 Capitol Mall, Suite 200
Sacramento, California 95814

September 29, 1998

Kurt R. Sjoberg, State Auditor
Bureau of State Audits
555 Capitol Mall, Suite 300
Sacramento, California 95814

Dear Mr. Sjoberg:

RE: STATE CONTRACTING: DEPARTMENTS COULD SAVE MORE MONEY WHEN
ACQUIRING GOODS AND SERVICES

Enclosed is our response prepared by the Department of General Services to the Bureau of State Audits' Report No. 97015 entitled "State Contracting: Departments Could Save More Money When Acquiring Goods and Services," as well as a copy of the response on a diskette.

If you have any questions or need additional information, please contact me at 653-4090.

Sincerely,

Original Signed by:

George Valverde
Deputy Secretary

Enclosures



MEMORANDUM

Date: September 30, 1998 File No.: 97015

To: Anne E. Sheehan, Secretary
State and Consumer Services Agency
915 Capitol Mall, Room 200
Sacramento, CA 95814

From: Department of General Services
Executive Office

Subject: **RESPONSE TO BUREAU OF STATE AUDITS' REPORT NO. 97015 –
"STATE CONTRACTING: DEPARTMENTS COULD SAVE MORE
MONEY WHEN ACQUIRING GOODS AND SERVICES"**

Thank you for the opportunity to respond to Bureau of State Audits' (BSA) Report No. 97015 which addresses recommendations to the Department of General Services (DGS). The following response addresses each of the recommendations.

OVERVIEW OF THE REPORT

The DGS has reviewed the findings, conclusions and recommendations presented in Report No. 97015. As discussed in this response, the DGS will take appropriate actions to address the recommendations.

Overall, the DGS is pleased that the BSA found that all of the departments included in the audit had positive comments related to the DGS' shift from a control orientation to a customer service orientation. These comments reflect favorably on the DGS' role in developing and implementing acquisition systems that are more responsive to customer needs. These systems include the California Multiple Award Schedules (CMAS) and Master Service Agreement (MSA) systems addressed in the audit scope.

Although, as with any new operating systems, there may be additional areas for improvement, we believe the acquisition staff within the Procurement Division (PD) and the contracting staff within the Office of Legal Services (OLS) should be commended for their roles in implementing and/or expanding two major acquisition methods, i.e., CMAS and MSAs, over the last few years. These acquisition methods allow a significantly less complex and costly acquisition process to be used which results in substantial savings to state and local government entities when compared to the costs of using formal competitive bidding procedures.

① *

Chapter 1 of the report primarily presents the BSA's view that the DGS should require departments using CMAS to value shop, instead of the DGS' current policy of encouraging this activity. A change from encouraging value shopping to requiring this activity would represent a fundamental shift in the CMAS program and be contrary to legislative intent and best procurement practices. In general, best procurement practices have been found to be those that are value-driven and not process-driven. The CMAS is an example of a value-driven, highly successful procurement process that has resulted in a significant reduction in duplication of

②

efforts among governmental entities and, therefore, substantial savings to the state's taxpayers. The DGS is not aware of any desire by its legislative, state agency or local government customers to add additional control requirements to this program.

①

It is our belief that a significant contributing reason to the success of the CMAS program has been the DGS' philosophy of keeping required processes, such as requiring value shopping, to a minimum and assigning accountability and responsibility at the procurement entity level. The DGS believes its role related to value shopping should continue to be limited to communicating the responsibility of being smart shoppers to CMAS users. This responsibility is communicated to the users through the CMAS agreements which contain language that strongly encourages each user to optimize the benefits of the program by comparing different schedules for varying products, services and prices, and carefully reviewing all contract terms and conditions to obtain the best value available. In addition to the language contained in the CMAS agreements, the users' responsibility for being a smart shopper has been emphasized in over 100 outreach activities performed by CMAS program staff. These activities included staffing booths at conferences and forums, making presentations to interested parties, and providing onsite training for various users. The onsite training has included such large CMAS users as the Departments of Transportation, Social Services, Water Resources, Forestry and Fire Protection and Justice.

③

While the PD has oversight responsibility for the CMAS program, each state or local government entity is ultimately responsible for its own purchasing program. Under the CMAS program, it is the procurement entity that is responsible for determining the degree of effort to be made in obtaining best value for the commodity or service being procured. By placing this responsibility at the procurement entity level, the party with direct knowledge of the circumstances of a particular procurement is making operational decisions and, therefore, accountable for the procurement. This placement of responsibility is a key ingredient in ensuring that the procurement process is streamlined to remove repetitive, resource intensive, costly and time consuming processes.

③

Chapter 2 of the report identifies several shortcomings in the DGS' oversight of the CMAS program. It is not surprising that there are areas that could be improved in a new program that has grown to approximately \$437 million in a four year period. As with any new program, during the first few years of the CMAS program resources have been focused on implementation activities such as determining the eligibility of suppliers, processing contracts and conducting outreach and training activities. However, even with this focus, the CMAS Unit managed to conduct desk reviews of a significant number of the program's most frequently utilized suppliers. In fact, the BSA notes in its report that 12 of the top 20 suppliers in terms of sales had been reviewed by the CMAS Unit. These suppliers represent 43% of all sales activity during the period referred to in the audit report, January 1995 to September 1997.

④

As with all operating activities, management assesses risks and benefits in assigning staff to different functions. We believe the CMAS unit has done an exceptional job in allocating staff resources during a period that state government was operating with limited resources. The DGS is pleased that, while finding areas for additional improvement, the BSA found that the CMAS Unit has focused its reviews on those suppliers with the highest dollar amounts of sales and that, in the reviews that have been conducted, has been successful in identifying instances of supplier noncompliance.

④

The following response only addresses the recommendations. Since they have been extensively discussed in past meetings with the BSA's staff, our disagreements with some specific findings and resulting conclusions will not be repeated in this response. It is also our understanding that specific findings pertaining to other departments have been discussed with those departments. Therefore, the DGS has not attempted to verify the accuracy of those findings and will not respond to those issues.

RECOMMENDATIONS

CHAPTER 1

RECOMMENDATION # 1: *The Department of General Services (DGS) needs to take steps to increase the value of the purchases that departments make when using the California Multiple Award Schedules (CMAS). These steps include the following:*

- *Rather than merely encouraging departments to compare prices for products offered by CMAS vendors, the DGS should require departments to compare value when the cost of the good or service exceeds a pre-determined threshold.*
- *Require departments to negotiate reductions in CMAS list prices when the size of their purchase warrants it.*
- *Provide departments with sufficient, easy-to-use tools to help them determine value. Such tools include improved Internet resources or catalogs organized by product that include price.*

DGS RESPONSE # 1:

The DGS' position for the first two recommended actions related to requiring value shopping are extensively discussed in the Overview section of this response. Although not believing that the CMAS procedures should be revised to require value shopping, the DGS will determine if additional actions need to be taken to ensure that CMAS users are aware of their responsibility for being smart shoppers. Specifically, the PD will review its education and training processes to ensure that they sufficiently disseminate to CMAS users their responsibility for attempting to achieve the best possible value in the circumstances which may necessitate price comparison and negotiation.

In addition, the PD will determine the feasibility of enhancing its commodity delegation compliance review activity to include CMAS transactions. Further, the DGS Audit Section will consider adding CMAS value shopping issues to its comprehensive compliance audit activity conducted at the largest state departments. Through the compliance reviews and audits, the DGS will be able to identify additional education and training opportunities.

Through a policy bulletin, the PD will also communicate to CMAS customers the BSA's concerns related to value shopping. Further, PD staff will discuss the results of the BSA's audit at the next meeting of the Business Expansion Council which includes purchasing professionals from state departments.

Additionally, as noted in the report, the PD initiated a project in March 1998 to develop a comprehensive system of policies and procedures related to the acquisition of commodities (i.e., material, equipment and supplies) and information technology. The resulting policies and procedures will be contained in a new manual, i.e., the California Acquisition Manual (CAM). The PD will ensure that the CMAS value shopping issues raised by the BSA are addressed in this manual.

For the third recommended action which involves providing departments with additional tools to more easily comparison shop, the DGS is developing a new information technology resource which addresses this need. Specifically, as discussed with the BSA during the audit, the PD is committing significant resources to developing and implementing the California Statewide Procurement Network (CSPN). The CSPN contains a module that addresses database limitations that have prevented the DGS' Internet Web site from containing more extensive information on CMAS suppliers, products and prices.

The CSPN project is a powerful and flexible statewide procurement system due to commence in October 1998 that will span approximately sixteen to eighteen months at an estimated implementation cost of \$9.4 million. The CSPN system will provide customers with the capability of conducting procurement transactions electronically and searching for products across all catalogs (on-line catalog shopping) whether the products are available on a CMAS contract or some other statewide master contract.

5

RECOMMENDATION # 2: ***When it issues its guidance manual for purchasing, the DGS should include a provision that prohibits the use of any vendor as a fiscal agent, regardless of the procurement method used to obtain the vendor.***

DGS RESPONSE # 2:

The acquisition manual, CAM, discussed above will include provisions that prohibit the use of fiscal agents to circumvent the state's contracting and purchasing requirements. These provisions will be based on those contained in the State Contracting Manual (SCM). The SCM includes provisions which state that it is not appropriate to use pass-through contracts to circumvent state contracting requirements.

CHAPTER 2

RECOMMENDATION # 1: *To improve its oversight of the California Multiple Award Schedules (CMAS) program, the Department of General Services (DGS) should take the following actions:*

- *Optimize its vendor reviews. For instance, the department could devote additional resources to conduct more reviews, move responsibility for performing vendor reviews to a unit that has experience in reviewing programs and following up on identified deficiencies, or contract with independent auditors on a contingent fee basis to conduct vendor reviews and any necessary follow up.*
- *Increase the number of CMAS vendor reviews it conducts annually.*
- *Consider using the results of federally conducted vendor reviews to help it determine which vendors it will review.*
- *Include within the scope of its vendor reviews an examination of a vendor's compliance with the "price-reduction clause" of its contract.*
- *Communicate results of its vendor reviews to applicable departments when appropriate. Such instances would include when the DGS identifies examples of departments paying vendors more than their CMAS list price for a product or service.*
- *Develop and implement written procedures for efficient and effective follow-up on the results of the vendor reviews. These procedures should include penalties such as suspending or removing the vendor from the CMAS program.*

DGS RESPONSE # 1:

As discussed in the Overview section of this response, during the first few years of the CMAS program resources have been focused on implementation activities such as determining the eligibility of suppliers, processing contracts and conducting outreach and training activities. With the maturing of the CMAS program, additional resources will now be focused on performing compliance reviews. As part of this process, the PD will form a team with representatives from its CMAS and System Integrity Units and the DGS Audit Section with a goal of optimizing the supplier compliance review function.

The team will fully consider the feasibility of the specific actions recommended by the BSA. However, as previously discussed with the BSA, we have concerns with the feasibility of the

BSA's recommended actions related to examining for supplier compliance with the price reduction clause and communicating the results of supplier reviews to departments. Specifically, although willing to relook at the issue, when the PD previously considered the price reduction issue it concluded that a review of vendors for compliance with this clause would be a costly and duplicative process. The Federal General Services Administration's monitoring of negotiated prices at the time of contract renewal and continual monitoring of changes during the term of its contracts was found to be sufficient in determining compliance with price reduction requirements.

For the recommended action involving communicating results to applicable departments, the team will relook at this issue, however, the PD has tentatively concluded that providing additional training to departments that are consistently found to be not complying with CMAS provisions may be the best approach. This action would avoid the incurrence of significant costs in notifying applicable CMAS users of compliance review findings. Further, this practice would avoid any kind of a public disclosure that could expose the state to liability if not preceded by a legal action. An informal finding resolution process limited to the PD and the supplier avoids this risk. (6)

For the last recommended action related to follow-up, it should be noted that the PD is aware that more efficient and effective follow-up procedures are needed within the CMAS program's review activity. However, although the results of the compliance reviews have not justified the termination of any supplier, the PD has not hesitated to terminate contracts with CMAS suppliers who have not been responsive to program requirements. Although not removed due to the results of a compliance review, hundreds of suppliers have been terminated as a result of noncompliance with program requirements, e.g., not submitting timely quarterly reports and being nonresponsive to Year 2000 requirements. (7)

RECOMMENDATION # 2: *To ensure that departments do not misuse master service agreements, the DGS should begin routinely reviewing departments' master service agreements transactions for propriety.*

DGS RESPONSE # 2:

The PD will review its current systems of administrative oversight to determine if additional actions should be taken related to monitoring departments' MSA transactions. As presented in the State Contracting Manual, each state agency is responsible for its own contracting program. To assist state departments in complying with their responsibilities and to accomplish its oversight responsibilities, the DGS has implemented numerous administrative control activities. For MSA transactions, as part of its administrative control process the PD, depending upon the type of agreement, requires various reports and forms to be submitted for its review. Currently, the degree of review depends on staffing priorities and an assessment of risk.

RECOMMENDATION # 3: *To help minimize confusion in those departments that must follow its guidance the DGS should provide clear and consistent guidance on all state contracting and purchasing issues.*

DGS RESPONSE # 3:

The DGS continually strives to provide clear and consistent guidance on state contracting and purchasing issues. However, due to the complexity of state statutes on acquisitions, on occasion there are acquisitions that require the involvement of both the department's purchasing and contracting experts to determine the appropriate acquisition method. In the one instance noted in the report, the complexity of the acquisition, which involved both services and a product, required the expertise of staff from both the OLS and PD.

8

We do not believe that the one instance noted in the report should be used to reflect negatively on the customer service orientation of the DGS' staff. As noted in the Introduction section of the report, the DGS' procurement and contracting staff have been extremely successful in implementing the customer-oriented mission of the department. This success is shown by the positive comments related to the DGS' services made by the five departments which were audited by the BSA. Included in these comments is a statement by the entity, California Highway Patrol (CHP), involved in the acquisition that resulted in this recommendation. The CHP indicates that it considers the OLS' and PD's services to be "useful, helpful, and—in fact—valuable."

RECOMMENDATION # 4: *To enable departments to take full advantage of the State's collective buying power, the DGS should make available a listing of master service agreements that is both complete and accessible to appropriate personnel at all departments.*

DGS RESPONSE # 4:

The PD is taking action to ensure that its listing of master service agreements is both complete and accessible to appropriate personnel. Specifically, policies and procedures are being developed that provide for the PD's Internet Web site to include MSAs developed not only by the PD but those developed by other state entities. Further, when fully implemented the previously discussed CSPN will greatly improve the accessibility to MSAs and provide for greater functionality.

In addition to the Internet solution, the DGS will continue to communicate with its client agencies through such media as Management Memos, presentations to user groups and issuance of written announcements whenever such communications are considered advantageous.

RECOMMENDATION # 5: *Finally, because of the number of concerns regarding the CMAS and master service agreements that we mention in this chapter and Chapter 1, the DGS should include a review of the usage of these procurement methods as part of the scope of its existing evaluations of departments.*

DGS RESPONSE # 5:

Currently, the DGS Audit Section includes CMAS and MSA transactions within its general testing of purchases and contracts when conducting compliance audits of state agencies. However, the Audit Section has recognized the growing significance of these transactions and is taking steps to perform more indepth tests of these acquisition methods. In addition, the PD's System Integrity Unit is exploring an expansion of its routine information technology and commodity delegation reviews to cover the use of CMAS and MSA transactions.

CONCLUSION

The DGS has a firm commitment to provide efficient and effective oversight of the state's procurement and contracting programs. As part of its continuing efforts to improve policies over these programs, the DGS will take appropriate actions to address the issues presented in the report.

If you need further information or assistance on this issue, please call me at 445-3441.

Original signed by:

PETER G. STAMISON, Director
Department of General Services

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COMMENTS

California State Auditor’s Comments on the Response From the Department of General Services

To provide clarity and perspective, we are commenting on the response to our audit report from the Department of General Services (DGS). The numbers below correspond to the numbers we have placed in the responses.

- ① The DGS’s conclusion that governmental entities achieved “substantial” savings through the use of these two acquisition methods is not supported by documentary evidence. Despite several requests during our audit, the DGS did not provide support for amounts of savings that departments achieved by using these methods. The DGS does not track this information. Although it is logical to conclude that the use of these methods can save some amount of resources when compared to those consumed during a competitive bid, any savings achieved must be offset by losses due to misuse of these methods. As we indicate in our report, departments do not always use these methods properly.
- ② The DGS’s opinion that it is “contrary to legislative intent” to change from **encouraging** value shopping to **requiring** value shopping simply reflects its interpretation of the law. We disagree with the DGS’s opinion. As we state in our report’s Introduction, the intent behind the legislation authorizing the creation of the CMAS program includes the acquisition of goods and services within a competitive framework. Competition ensures value to the State and fairness to the vendors. Because vendors do not compete against each other to be approved under the CMAS program, value is not achieved when departments simply select any vendor from the CMAS program to provide a good or service. Departments must compare products from different vendors to achieve value. As we point out on page 13, some departments do not always value shop because the DGS does not require them to do so.

- ③ The DGS mistakenly believes that requiring value shopping creates unnecessary bureaucracy and misaligns responsibilities. Departments most certainly should exercise discretion in determining the level of effort to use when determining value. However, direction provided by the DGS requiring departments to value shop when a purchase exceeds a minimum threshold sets a benchmark that helps the departments determine the applicable level of effort to apply; it does not create unnecessary bureaucracy nor does it misalign responsibilities. In fact, providing such direction is consistent with the DGS's own stated objective to ensure, as we point out on page 8, that the State obtains the best service at the best price. In comparison, as we note on page 13, federal regulations state that orders above a minimum threshold in which a federal department considered reasonably available information from at least three vendors are considered to be issued pursuant to full and open competition, to represent the best value, and to result in the lowest cost alternative to meet the federal government's needs.
- ④ Although these DGS statements do not mischaracterize information presented in our report, they do minimize the seriousness of the issues. As we point out in Chapter 2, the DGS does not adequately resolve issues of vendor noncompliance nor does it communicate the results of its vendor reviews to affected departments. In fact, one of the examples we cite on page 23 concerning vendor noncompliance and the one cited on page 25 regarding lack of notification refer to the same vendor. This vendor led all other CMAS vendors with sales of \$50.3 million, or nearly 11 percent of CMAS sales, occurring from January 1995 through September 1997.
- ⑤ Although the DGS proposes a longer-range response to our concern that departments cannot easily compare value, it fails to provide any interim, or nearer-term, solutions.
- ⑥ The informal finding resolution process and the departmental training described by the DGS do not adequately address our concern regarding its not notifying departments of the results of vendor reviews. Further, the DGS has other methods available to it for communicating this important information that are not costly and do not expose the State to liability. For example, the DGS could add the specific departments involved to a risk-based selection for its existing departmental reviews and communicate more specific information during the review process itself.

- ⑦ The DGS's statement that the results of its vendor reviews have not justified the removal of any vendors from the CMAS program is curious. As we note on page 24, despite the efforts of three reviews and the associated follow-up conducted over 21 months, the DGS has not obtained corrective action from a vendor who sold \$1.9 million in unauthorized products to the State and overcharged the State \$14,600. Further, rather than suspending or terminating this vendor from the CMAS program, the DGS has scheduled this vendor for a fourth review. If the DGS is willing to terminate a contract because a vendor did not submit a quarterly report on time, surely it should at least suspend, if not terminate, the contract of a vendor such as the one we described.

- ⑧ The DGS does not adequately respond to this recommendation. In fact, the response contradicts information the DGS gave to us during our audit. Specifically, we discussed this issue with DGS staff who agreed that consistent advice was necessary. Further, as we point out on page 28 of the report, the DGS's Office of Legal Services and its Procurement Division are in discussions attempting to determine how best to resolve the issue.

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