

Department of General Services

It No Longer Strategically Sources Contracts and Has Not Assessed Their Impact on Small Businesses and Disabled Veteran Business Enterprises

REPORT NUMBER 2009-114, ISSUED JULY 2010

This report concludes that documents indicate that as a result of its initial strategic sourcing efforts, the State accrued at least \$160 million in net savings from 33 contracts through June 30, 2007. The Department of General Services (General Services) stopped formally calculating savings at that time. Further, although it has not strategically sourced 20 other categories of goods or services that its consultant recommended, General Services indicates that it has used traditional methods to issue statewide contracts for many of the categories. However, it has not determined that these contracts have resulted in savings commensurate with what it would have achieved under strategic sourcing. General Services has not entered into any strategically sourced contracts since July 2006, and it is not reviewing comprehensive purchasing data that will allow it to identify new opportunities effectively.

General Services does not have all the necessary data to determine the change in the number of small businesses and Disabled Veteran Business Enterprises (DVBES) participating in a category of goods that was strategically sourced. Additionally, our review of contracts awarded to small businesses and DVBES by five large state agencies does not indicate a clear relationship. Further, General Services determines whether the planned use of subcontractors complies with statutory requirements designed to ensure that they play a meaningful role in any contract in which they participate. However, it does not monitor to ensure compliance once the contract has been awarded. Finally, General Services does not yet have standard procedures to recover state funds when it identifies a contractor that has not complied with the pricing terms of the contract.

In the report, the California State Auditor (state auditor) made the following recommendations to General Services. The state auditor's determination regarding the current status of recommendations is based on General Services' responses to the state auditor as of July through September 2011.

Recommendation 1.1—See page 21 of the audit report for information on the related finding.

To ensure that it determines savings to the State going forward for strategically sourced contracts, General Services should examine the State's recent purchasing patterns when determining whether to rebid or extend previously strategically sourced contracts and when estimating expected savings. It should subsequently compare the savings it achieves to the expected savings for those contracts.

General Services' Action: Partially implemented.

General Services states that it has developed standards for implementing and documenting the evaluation of recent purchase patterns when determining whether to extend, rebid, or retire previously sourced contracts. It notes that it did so in July 2010 by updating its procedures manual to incorporate detailed requirements for the development of opportunity assessments and sourcing work plans.

General Services notes that it is using a benchmarking procedure that includes the estimation of expected savings for any rebid or extended contracts based on recent purchase patterns. It has developed a work plan template that contains detailed information on savings expected from a proposed sourced contract. General Services indicates that the template is currently being used on the rebid of one statewide contract. It subsequently plans to compare the baseline savings amounts to the actual pricing obtained under an executed contract to calculate achieved savings.

Recommendation 1.2—See pages 22—25 of the audit report for information on the related finding.

To ensure that it has maximized the savings for consultant-recommended categories that it did not strategically source, General Services should conduct its planned review of these categories to determine if there are further opportunities to achieve savings.

General Services' Action: Fully implemented.

General Services completed its review of consultant-recommended categories that it did not strategically source and concluded that none of the 20 categories warranted additional strategic sourcing contracting efforts. General Services noted that its review confirmed that it used other traditional acquisition techniques to acquire those goods or services that accomplished the same goal as strategic sourcing. It noted that for the remaining categories, such as architectural and engineering services, electricity, and leased real property, the review determined that the categories were of such a broad nature that strategic sourcing techniques could not be applied.

In response to our request for documentation of the analysis performed that resulted in its conclusions, General Services provided a document of about three pages. The document commented on the results of each of the categories for which it or others conducted traditional acquisition methods. For many of the categories, General Savings indicated that either savings would be measured by individual contract or savings were not measured. Additionally, General Services described the factors that it believes prevent strategic sourcing of other categories.

However, although General Services completed its planned review, we note that the review was unable to report aggregate savings information for many of the categories for which it indicated traditional acquisition techniques were used. This underscores the need for General Services, as it implements our recommendations regarding future purchases, to ensure that it is tracking actual savings in such a way that it can compare them against expected savings.

Recommendation 1.3—See pages 25—27 of the audit report for information on the related finding.

To ensure that it maximizes the savings to the State for future purchases, General Services should follow the procedures for identifying strategic sourcing opportunities included in the Intake and Analysis Unit's procedures manual. To ensure that it is effectively identifying new strategic sourcing opportunities, General Services should work to obtain comprehensive and accurate data on the specific items that state agencies are purchasing, including exploring options for obtaining such data for agencies that do not have enterprise-wide systems and therefore would not be using the additional functionality of the eProcurement system. Until it obtains such data, General Services should work with state agencies to identify detailed purchases for categories that it identifies through the State Contracting and Procurement Registration System (SCPRS) as viable opportunities for strategically sourcing. For example, if based on its review of SCPRS data, General Services identifies a particular category that it believes is a good candidate for strategic sourcing, it should work with those state agencies that accounted for the most purchases within the category to determine the types and volume of specific goods purchased to further analyze the types of goods to strategically source. General Services should assess any need for additional resources based on the savings it expects to achieve.

General Services' Action: Partially implemented.

General Services indicates that it periodically reviews databases, including the SCPRS data, for items that may indicate a strategic sourcing opportunity. Its procedures manual indicates that this review is to take place quarterly. It states that in consultation with its customers, it uses available data on purchasing patterns to identify if strategic sourcing or another procurement vehicle should be used. General Services believes that these steps are sufficient to allow it to obtain comprehensive and accurate data on the specific items that state agencies are purchasing that are of a volume that warrant an opportunity for strategic sourcing. General Services states that it goes through an extensive search for purchasing data using all available sources and that it requests copies of purchase orders from state agencies to obtain more detailed purchasing data.

However, although General Services notes that it preliminarily identified potential sourcing opportunities through its review of the SCPRS data for quarters ending March 2011 and June 2011, it states that it has not further analyzed these opportunities due to lack of resources.

Recommendation 1.4—See pages 30—31 of the audit report for information on the related finding.

To provide decision makers with the information necessary to determine the true costs and benefits of strategic sourcing, General Services should evaluate any impact strategic sourcing has on small business and DVBE participation in terms of number of contracts awarded and amounts paid to small businesses and DVBEs within the categories being strategically sourced. Specifically, for goods that were strategically sourced, General Services should compare the number of contracts awarded to small businesses and DVBEs before they were strategically sourced with those awarded through such contracts after they were strategically sourced. This effort should include contracts awarded by General Services and other state agencies.

General Services' Action: Partially implemented.

General Services states that before performing an acquisition, it includes an assessment of the number of small businesses and DVBEs that participated in the previous solicitation and the potential number of small businesses and DVBEs that will be participating in the new solicitation. As for tracking the use of small business and DVBE firms after a strategically sourced contract has been awarded, General Services has decided to capture and track that information for statewide contracts under its purview. It has added new off-ramp reporting provisions to three statewide contracts and plans to add this provision to other contracts as necessary.

However, General Services noted that it has not yet analyzed the data it has been tracking for the three contracts currently containing the new off-ramp reporting provision because enough time has not passed to allow adequate usage for analyses. It stated that it plans to conduct its evaluation of small business and DVBE usage in the summer or fall 2012 for off-ramp purchases made under the three statewide contracts.

Recommendation 1.5—See pages 29—31 of the audit report for information on the related finding.

To evaluate the effectiveness of the off ramp in providing opportunities for small business and DVBE participation, General Services should track the number and dollar amounts of contracts that state agencies award through the use of the off ramps in strategically sourced and other mandatory statewide contracts. General Services' evaluation also should consider the extent to which an off ramp affects the monetary benefits that result from statewide contracts designed to leverage the State's purchasing power.

General Services' Action: Partially implemented.

General Services is maintaining a database for tracking purposes of approved small business or DVBE off-ramp purchases, which includes pricing information. It plans to use this information to assess the impact on small businesses and DVBEs after strategic sourcing. General Services has included the new off-ramp usage reporting provisions in three statewide contracts and has begun gathering the usage data. It plans to conduct its evaluation of the off-ramp usage data in summer or fall 2012.

Recommendation 1.6—See pages 35—37 of the audit report for information on the related finding.

To ensure that small business and DVBE subcontractors comply with the commercially useful function requirements, General Services should develop guidance for state agencies on how to ensure that subcontractors perform commercially useful functions if it believes state agencies making the purchases

through statewide contracts should be responsible for this task. In addition, General Services should monitor, on a sample basis, whether state agencies are ensuring compliance with these requirements. General Services could leverage its efforts by working with other state agencies to ensure that subcontractors claiming to have provided the goods and services to the purchasing agency did, in fact, perform the work for which they are invoicing the state agencies.

General Services' Action: Partially implemented.

General Services has revised user instructions for new statewide contracts to include instructions and/or direction to user state agencies on ensuring contractors' compliance with the commercially useful function requirements. However, it states that in most cases this task is performed by General Services' staff during the solicitation process. It notes that it has implemented the use of its contract management plan process, which outlines the responsibilities of its contract administrators. Where applicable, these plans are to include a requirement for ensuring contractor compliance with commercially useful function requirements. General Services reports that it is in the early stages of implementing the contract management plan process and has not yet entered into a statewide contract that requires user state agencies to assess commercially useful functions on individual transactions.

Recommendation 1.7—See pages 44—45 of the audit report for information on the related finding.

To ensure prompt recovery of state funds, General Services should implement standard procedures to recover overcharges identified by the Compliance and Savings Administration system. General Services' new procedures should specify the amount of time it considers reasonable to recover funds due back to the State.

General Services' Action: Fully implemented.

General Services has developed standard procedures to recover any overcharges, including the amount of time considered reasonable to recover funds due back to the State. The procedures provide for the issuance of a demand notice for payment of any identified overcharges—normally within 30 days—and monthly monitoring of any outstanding amounts.

Recommendation 1.8—See pages 45—46 of the audit report for information on the related finding.

To improve the integrity of its monitoring of pricing compliance, General Services should implement procedures to help ensure that usage reports reflect the actual items received and prices paid by the state agencies that purchased the items. For example, on a periodic basis, it could select a sample of purchases from the usage reports and work with purchasing state agencies to confirm that the prices and quantity of items reported reconcile with the invoices submitted by the contractor.

General Services' Action: Partially implemented.

General Services has implemented procedures to assist in ensuring the accuracy of the usage reports submitted by contractors. The contract management plan process mentioned in General Services' comments on the recommendations related to commercially useful function requirements include steps for the contract administrator to work with state agencies to confirm the accuracy of contractor reported pricing and other relevant data. To ensure the validity of the contractor's usage reporting, the contract management plans are to include steps requiring the contract administrator to compare, when necessary, the data being reported by contractors with information from purchasing agency documents. General Services notes that the criteria for determining when to perform such comparisons would vary by individual contracts and are influenced by various factors deemed important by contract administrators. However, General Services notes that due to the recent implementation of the contract management plan process, the sampling of agency documentation has not yet occurred.

Recommendation 1.9.a—See pages 38—41 of the audit report for information on the related finding.

The Legislature could revise state law to provide more clarity regarding the use of small business and Disabled Veteran Business Enterprise (DVBE) subcontractors on state contracts. In doing so, the Legislature should consider whether a business relationship such as the one between Office Depot and its subcontractors is what the Legislature envisioned when it created the commercially useful function requirements. It should also consider whether a firm should be required to have demonstrated experience in a particular line of business before being allowed to participate in state contracts.

Legislative Action: Unknown.

The state auditor is not aware of any action taken by the Legislature as of January 5, 2012.

Recommendation 1.9.b—See pages 38—41 of the audit report for information on the related finding.

The Legislature could revise state law to provide more clarity regarding the use of small business and DVBE subcontractors on state contracts. In doing so, the Legislature should consider whether the State should prohibit contractors, which are capable of performing the task contracted for, from subcontracting with small businesses and DVBEs at the cost of eliminating participation opportunities for these entities.

Legislative Action: Legislation introduced.

Senate Bill 817, as introduced in the 2011–12 Regular Legislative Session, includes provisions to allow a vendor to meet DVBE goals from sources other than state contracts and allows the calculation to meet participation goals to include specified direct and indirect costs incurred by the vendor. The bill was held in the committee.

Recommendation 1.9.c—See pages 38—41 of the audit report for information on the related finding.

The Legislature could revise state law to provide more clarity regarding the use of small business and DVBE subcontractors on state contracts. In doing so, the Legislature should consider whether it is in the State's best interest to limit a particular line of business, such as office supplies, to a relatively small number of small business and DVBE subcontractors rather than the many small businesses and DVBEs that could contract with the State in the absence of strategic sourcing.

Legislative Action: Unknown.

The state auditor is not aware of any action taken by the Legislature as of January 5, 2012.