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August 3, 2007

TO: Supervisor Zev Yaroslavsky, Chairman
Supervisor Gloria Molina
Supervisor Yvonne B. Burke
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FROM: J. Tyler McCauley
Auditor-Controller

SUBJECT: **DEPARTMENT OF CHILDREN AND FAMILY SERVICES – PROCUREMENT REVIEW (PHASE I)**

At the request of the Department of Children and Family Services' (DCFS) management, we reviewed the Department's procurement practices to determine compliance with the County Fiscal Manual (CFM) and County purchasing policies, and the Internal Services Department guidelines. Our review focused primarily on the operations of the Department's Procurement and Forms Management Section (Procurement), which has overall responsibility for DCFS' procurement functions.

We evaluated existing controls over the purchasing process, reviewed a sample of purchases, visited the Department's warehouses and regional offices, and interviewed Procurement management, staff and vendors. This report constitutes Phase I of our review. During Phase II, we will evaluate procurement activities outside of the Department's Procurement and Forms Management Section and perform a more focused review of supply inventory controls at the Department's regional offices.

Results of Review

Our Phase I review disclosed a number of significant deficiencies in the Department's procurement operations, including serious violations of County fiscal and purchasing policies, a lack of critical internal controls (e.g., separation of duties, etc.) and recordkeeping. These deficiencies have resulted in a lack of accountability and could have resulted in misappropriation of County property and/or funds going undetected.

The following are examples of the deficiencies we noted:

- **DCFS violated County fiscal and purchasing policies by prepaying a vendor approximately $1.7 million months before the merchandise was received by the Department.** DCFS' prepayment practice is a serious violation of County fiscal and purchasing policies and State claiming practices. Procurement management indicated that prepaid purchases were made primarily to use unspent budgeted funds before the end of the County fiscal year, which is also a violation of County purchasing policies.

- **DCFS Procurement purchased non-agreement supplies from agreement vendors ignoring agreement terms and bypassing established County solicitation requirements.** Such violations of County procurement policies resulted in DCFS overpaying for certain purchases by approximately $51,000.

- **DCFS Procurement made unnecessary purchases of supplies at inflated prices.** For example, DCFS Procurement ordered and received thousands of toner cartridges totaling over $1 million even though the items were not needed. For one of the orders, DCFS paid 15% more per toner cartridges than they had paid for a prior order of toner cartridges. Toner cartridges have a limited shelf life. At the Department's current usage rate, more than 4,500 toner cartridges (or over 70% of the purchases) are expected to expire and may not be usable.

- **DCFS Procurement did not have sufficient controls over Gift Card inventories.** DCFS maintained approximately $160,000 in gift cards but did not maintain perpetual inventory records, proper security or segregation of duties, supporting documentation and did not have controls in place to prevent gift card deliveries to unauthorized personnel.

- **DCFS does not have adequate controls over its equipment and supply inventories.** The Department did not maintain perpetual inventory records and had not conducted a physical inventory of equipment and supplies in over three years. Also, DCFS Procurement did not always inspect, count, and match receiving reports to purchase requests when goods were received, as required.

- **The Department does not have adequate controls over the disposal of surplus/obsolete items.** DCFS Procurement staff did not adequately document disposal of surplus items and did not adequately control or track auction proceeds. Since there was no accountability for auction proceeds, approximately $110,000 of $230,000 in proceeds have not been collected.

- **Procurement staff did not comply with numerous County fiscal and purchasing policies and guidelines.** For example, purchases exceeding the Department's delegated purchasing authority of $15,000 were not always processed through ISD as required; purchases were split to bring transactions within the

delegated authority; and payments were issued without sufficient documentation. We also noted that DCFS did not process requisitions for sole source purchases exceeding $5,000 through ISD as required by County purchasing policy.

We also noted instances where it appears Procurement staff misled Auditor-Controller auditors to possibly conceal excessive inventory items and/or inappropriate purchases. Due to issues of non-compliance with County fiscal and purchasing policies and the significant issues related to internal controls over the procurement process, the Auditor-Controller's Office of County Investigations is conducting additional procedures to determine whether any fraudulent payments or activities have taken place.

During our review, we had several meetings with DCFS management to inform them of the non-compliances and serious violations of County fiscal and procurement policies discussed in this report. Upon learning about our findings, DCFS management immediately began making operational changes, including reorganizing the Department's Procurement and Forms Management Section, by reassigning management and staff, and developing a plan to correct the deficiencies noted.

We will work closely with DCFS and assist them in implementing the recommendations in this report. Details of our findings and recommendations are attached.

Review of Report

We discussed our report with DCFS representatives on July 11, 2007. The Department's initial response (attached) indicates general agreement with our findings and recommendations. The Department will provide a detailed response to the Board of Supervisors on their progress in implementing the recommendations within 60 days.

We thank DCFS management and staff for their cooperation and assistance during our review. Please call if you have any questions, or your staff may contact Terri Kasman at (626) 293-1121.

JTM:MMO:JLS:TK:YK
Attachment

c: William T Fujioka, Chief Executive Officer
Patricia S. Ploehn, Director, Department of Children and Family Services
Susan Kerr, Chief Deputy Director, Department of Children and Family Services
Raymond G. Fortner, Jr., County Counsel
Dave Lambertson, Director, Internal Services Department
Sachi A. Hamai, Executive Officer
Public Information Office
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DEPARTMENT OF CHILDREN AND FAMILY SERVICES
PROCUREMENT REVIEW (PHASE I)

Background

The Department of Children and Family Services' (DCFS) Procurement and Forms Management Section (DCFS Procurement) has overall responsibility for the procurement functions of the Department, including purchasing services and supplies, reviewing and approving all purchase requisitions and invoices (other than information systems and training-related purchases), receiving supplies, maintaining equipment and supply inventories, controlling fixed assets and disposing of surplus/obsolete items. DCFS' fiscal year (FY) 2006-2007 services and supplies budget was approximately $177 million.

The Bureau of Information Services' (BIS) Procurement Section handles information systems related purchases (e.g., computers, software, servers, etc.) and the Governmental Relations – Legislation Office's Training Section purchases training-related materials and services. Our Phase I review did not include the BIS and Training Section's procurement practices. We will review these Sections' procurement practices during Phase II. In addition, we will evaluate internal controls over supply inventories at the Department's regional offices.

Scope of Review

At the request of DCFS management, we reviewed the Department's procurement practices to determine compliance with the County Fiscal Manual (CFM) and County purchasing policies and Internal Services Department (ISD) guidelines. We reviewed a sample of purchases, visited the Department's warehouses and regional offices, evaluated existing internal controls over the purchasing process and interviewed procurement management, staff and vendors.

Increased Management Oversight

Throughout our review, we noted a number of significant deficiencies in the Department's procurement and fiscal operations, including serious violations of County fiscal and purchasing policies and guidelines, a lack of critical internal controls (e.g., separation of duties, etc.) and recordkeeping. These deficiencies have resulted in a lack of accountability and could have resulted in misappropriation of County property and/or funds going undetected.

We also noted instances where it appears Procurement staff misled auditors to conceal excessive inventory items and/or inappropriate purchases. As a result, a review by our Office of County Investigations is currently underway.

It appears these weaknesses may be attributable to a lack of management oversight, intentional disregard for County fiscal and procurement guidelines, negligence on the part of Procurement staff, and a lack of staff knowledge of procurement guidelines. To

ensure the Department's procurement functions are operating in an efficient and effective manner, and to ensure compliance with County purchasing and fiscal policies and procedures, DCFS management needs to implement the following recommendations.

Recommendations

DCFS management:

1. **Increase the level of management oversight over its procurement functions to ensure Procurement staff comply with County procurement and fiscal policies.**

2. **Provide training on County procurement and fiscal policies and procedures where necessary, monitor staff for compliance, and take appropriate disciplinary action for staff who do not follow required fiscal and procurement policies.**

3. **In conjunction with Human Resources management, take appropriate disciplinary actions for staff who approved inappropriate transactions and/or intentionally violated County fiscal and procurement guidelines.**

Inappropriate Purchases

Prepayments

The County Fiscal Manual and County purchasing policies and guidelines require departments to match various purchasing documents, including matching the vendor's invoice to the receiving report before processing invoices for payment. In addition, paying for merchandise before the goods are received is only allowed under special circumstances and if pre-approved by ISD.

DCFS Procurement inappropriately paid a vendor for office supplies totaling approximately $1.7 million months before the merchandise was received by the Department, without the required approvals. DCFS Procurement submitted Purchase Orders (POs) and Corporate Express's (CE) "temporary invoices" to DCFS Finance for payment. DCFS Finance paid CE without a receiving report. Since the merchandise was not delivered before payment was made, a credit balance was maintained by CE and future orders placed by DCFS were charged to the credit balance. In addition, the supplies listed/ordered on the original POs and "temporary invoices" were not the same supplies which DCFS eventually ordered/purchased and received from CE. For example, DCFS Procurement purchased approximately 1,800 USB flash drives (flash drives) totaling approximately $120,000 using the CE credit balance. However, the list of supplies on the original PO and "temporary invoice" did not include flash drives.

Procurement management indicated that prepaid purchases were made primarily to use unspent budgeted funds before the end of the County fiscal year. CE acknowledged that the company has made arrangements to accept prepayments from DCFS for the past several years.

DCFS' current procurement prepayment practice is a serious violation of County procurement policies and State claiming practices. In addition, DCFS did not adequately keep track of the supplies purchased and applied against the CE credit balance, which could have resulted in DCFS paying invoices multiple times.

Recommendations

DCFS management:

4. **Ensure Procurement and Finance Section staff immediately discontinue the practice of paying vendors for merchandise which has not been received.**

5. **Provide its Procurement and Finance Sections with a written memo informing staff they are to immediately discontinue the practice of paying vendors for merchandise which has not been received, and that any future non-compliances with County fiscal and procurement policies and guidelines will result in disciplinary action up to and including discharge.**

6. **Ensure the Department received credit for all prepayments by reconciling vendor invoices to internal purchase records and recover funds from Corporate Express which have not been used.**

7. **Consult with ISD and County Counsel to determine possible contract violations by Corporate Express and take appropriate action to penalize the vendor, if appropriate.**

Unauthorized Agreement Purchases

ISD establishes agreements with vendors through the competitive bid process to ensure quality services are obtained at fair, reasonable and competitive prices for commonly purchased supplies and equipment. These agreements allow County departments to pay substantially lower prices than other procurement methods. Departments cannot purchase an item as an agreement purchase (by using an agreement PO) if the item is not covered in the vendor's agreement, and thereby bypass ISD's approval and bid requirements.

DCFS Procurement purchased non-agreement supplies, using agreement POs, from agreement vendors. DCFS Procurement ignored agreement terms, bypassed established County solicitation requirements, and as a result, overpaid for some

purchases. For example, DCFS Procurement purchased 2,700 new laser toner cartridges as an agreement purchase, totaling approximately $450,000 from CE, even though the agreement with CE specifically prohibits buying new toner cartridges from the vendor. Since the purchase exceeded DCFS' delegated authority of $15,000, the purchase should have been submitted to ISD for processing. DCFS' violation of County procurement policies resulted in the Department paying an additional $51,000 for the toner cartridges.

Recommendations

DCFS management:

8. **Ensure Procurement staff do not purchase non-agreement supplies, using agreement POs, from agreement vendors.**

9. **Ensure Procurement Section complies with the agreement terms and submits a purchase requisition to ISD for non-agreement purchases exceeding the Department's delegated authority of $15,000.**

10. **Provide its Procurement Section with a written memo informing staff of the requirements related to recommendations 8 and 9 above, and that any future non-compliance with County fiscal and procurement policies and guidelines will result in disciplinary action up to and including discharge.**

11. **Ensure Procurement Section solicits bids on high-volume/dollar agreement purchases to obtain the lowest possible price.**

Unnecessary Purchases

CFM Section 5.2.3 requires that inventory items should only be ordered when needed and with proper authorization.

In June 2006, DCFS Procurement ordered and received from one vendor over 3,000 toner cartridges for one type of printer, totaling approximately $800,000. Although the quantity they ordered was enough to last the Department approximately three years, DCFS Procurement ordered additional toner cartridges from CE totaling $450,000 in the same month. DCFS paid approximately 15% more per toner cartridge than what they paid for the 3,000 toner cartridges received earlier in June 2006. The Department also prepaid for the $450,000 purchase.

Procurement staff also made multiple purchases of the same toner cartridges from CE Imaging (a CE subsidiary), totaling approximately $150,000, from June 2006 to March 2007. Most of these purchases were made after the Department already spent more than $1.2 million on the same type of toner cartridges.

The manufacturer's specifications indicate that the shelf life of the toner cartridges is two years. However, based on DCFS' printer usage data, the Department's remaining inventory of over 5,500 cartridges would last approximately six years. Since the majority of the cartridges were purchased a year ago, the unused toner cartridges would expire in approximately one year. At the current usage rate, more than 4,500 toner cartridges (or over 70% of the purchases) are expected to expire and may not be usable.

We also noted that only 1,100 of the approximately 1,800 flash drives purchased from CE have been used/distributed to staff. These flash drives were distributed to staff as recently as May 2007, even though most of the flash drives were received in August 2006. In addition, we noted that the Department not only paid more than they should have when the purchase was made, but the identical flash drive is now sold for significantly less, as low as $15, compared to the original purchase price of $67. As prices for computer-related products decrease substantially over time, the Department's savings would have been significant if only required quantities were purchased. We also noted that 78 flash drives, worth over $5,200, are missing, based on our inventory count and Procurement's distribution log.

Recommendations

DCFS management:

12. **Ensure Procurement staff immediately discontinues the practice of ordering excessive quantities of supplies, and that supplies are ordered only when needed.**

13. **Provide its Procurement Section with a written memo informing staff to immediately discontinue the practice of ordering excessive quantities of supplies, that supplies should only be ordered when needed, and that any future non-compliance with County fiscal and procurement policies and guidelines will result in disciplinary action up to and including discharge.**

14. **Work with ISD to determine if the surplus items can be returned to the vendor(s), sold, or utilized by other County departments to minimize waste/loss.**

Gift Cards

DCFS Procurement orders, receives and distributes gift cards to regional offices for the Department's various programs. The gift card purchases require prepayment. When requests come in from the regional offices, Procurement submits a PO to Finance and receives a check made payable to the vendor (e.g., Target, Wal-Mart, Vons, etc.). DCFS Procurement buys the gift cards directly from the vendors or gives the check to regional office staff so they can purchase the gift cards.

Regional office staff typically distribute the gift cards to children and foster parents to purchase necessities (e.g., food, clothing, and other household necessities, etc.), or as incentives for participating in the Department's various programs, such as mentoring and adoptive family recruiting events. The Department purchased at least $1.4 million in gift cards since July 1, 2005.

Internal Controls

Since gift cards are considered cash equivalents, they should be safeguarded in the same manner as cash to prevent theft or misuse. CFM Section 1.1.3 requires departments to maintain logs to document the current inventory balance on hand, the date of usage, amounts issued, and the name and signature of the user. The CFM also requires adequate physical security and an inventory every six months.

In 2003, DCFS reported a theft of approximately $15,000 in gift cards which the Auditor-Controller investigated but was unable to identify the person responsible for the theft. It appears the Department did not strengthen internal controls over gift cards after the investigation.

During our current review, we identified the following:

- **Lack of perpetual inventory records** – DCFS Procurement maintained approximately $160,000 in gift cards but did not maintain perpetual inventory records for all the gift cards. Existing inventory records have not been updated for several months, lacked sufficient details, and were not accurate. Procurement also did not conduct physical inventory counts as required.

- **Lack of segregation of duties -** We found instances in which the same employee ordered and received the gift cards or the check issued by DCFS Finance to pay the vendor. Proper internal controls require that the person ordering gift cards should not also receive the cards/checks.

- **Lack of security -** We noted that not all gift cards were adequately secured. Some gift cards were stored in a locked filing cabinet, but the key was kept in an unlocked drawer. Procurement employees also temporarily maintained gift cards in their desks prior to distribution.

- **Lack of receiving controls -** DCFS does not have controls in place to prevent gift card deliveries to unauthorized personnel. Recently, a box of gift cards valued at $4,999 was mistakenly delivered by the vendor to the Auditor-Controller's Office, via the U.S. Postal Service Priority Mail. The Department should utilize more secure delivery methods (e.g., Registered Mail) for gift card purchases to ensure and verify the delivery of the gift cards to authorized personnel.

- **Overstocked gift cards -** Procurement maintained over $50,000 in unused portrait certificates/gift cards which were purchased several years ago. Procurement staff stated that these gift cards are no longer needed.

- **Insufficient supporting documents -** Procurement could not provide documentation to support approximately $115,000 (16%) of the $700,000 in gift card purchases we reviewed. Consequently, we could not verify that all gift cards were used for appropriate purposes. In addition, for 156 (64%) of 244 gift card transactions reviewed, we could not determine if the regional office staff requesting the gift cards actually received the gift cards. During Phase II, we will perform additional work to determine if regional office staff received the gift cards requested.

During our review, we informed DCFS management of the lack of controls over gift cards and they immediately reassigned gift card responsibilities from the Procurement Section to a Deputy Director's office. The Deputy Director's office now receives, distributes, and maintains the gift card inventories, and maintains perpetual inventory records detailing gift card receipts and distributions with serial numbers. With these changes, Procurement's responsibility is limited to purchasing gift cards upon approval from the Deputy Director. The Department should conduct physical inventories every six months, with at least one person independent of gift card responsibilities.

Our review of gift cards was limited to Procurement's operations. Accordingly, DCFS management should ensure that the regional offices have sufficient controls in place to prevent misuse. In addition, during our review, DCFS management expressed concern about the use of gift cards for certain purposes/programs. DCFS management is working with the State to determine if using gift cards for these programs is allowed. DCFS management should ensure that gift cards are only used for allowed purposes/programs.

Recommendations

DCFS management:

15. **Maintain perpetual inventory records for gift cards and have personnel with no other gift card responsibilities conduct physical inventories of the cards every six months.**

16. **Ensure the functions of purchasing, receiving, and distributing gift cards are adequately segregated.**

17. **Periodically review perpetual inventory records for completeness/accuracy.**

18. **Ensure gift cards are adequately secured at all times and access is limited.**

19. **Require Procurement staff to utilize more secure delivery methods for gift card purchases (e.g., Registered Mail) to ensure only authorized personnel receive gift cards.**

20. **Seek refunds from vendors if gift cards are no longer needed.**

21. **Ensure gift card transactions are adequately supported (e.g., requests for gift cards, receipt of gift cards and/or checks by regional office staff).**

22. **Ensure regional offices have sufficient controls in place to prevent misuse of gift cards.**

Gift Card Purchases without Purchase Orders

County purchasing policy requires a properly executed PO prior to ordering or receiving goods or services. We found that approximately 250 gift card transactions, totaling $700,000, were purchased through DCFS Finance without executing POs and without Procurement's involvement. DCFS Finance incorrectly classified these purchases as miscellaneous charges. However, the CFM only allows certain types of expenditures as miscellaneous charges (e.g., tuition reimbursements, utility charges, etc.). Procurement should have executed POs for all gift card purchases and the Department should have classified the purchases consistent with the gift cards' intended use.

Recommendation

23. **DCFS management ensure that all gift card purchases are processed through Procurement with a purchase order and that they are not classified as miscellaneous charges.**

Warehousing/Inventory

Internal Controls Over Equipment and Supplies

CFM Section 5.2.2 requires departments to establish controls to ensure supply inventories are safeguarded from theft or personal use. The CFM also requires departments to maintain perpetual inventory records; conduct annual physical inventories; review inventory records periodically; and identify slow moving, obsolete, and/or overstocked items. Departments are also required to inspect, count, and match items received to the receiving report and purchase order.

DCFS did not have adequate controls over its equipment and supply inventories. The Department did not maintain perpetual inventory records and had not conducted a physical inventory in over three years. DCFS Procurement also did not always inspect, count, and match receiving reports to purchase requests when goods were received.

We visited DCFS' warehouses and found multiple receiving reports (i.e., packing lists) attached to original shipments indicating that Procurement staff did not inspect, count, and match the goods received to receiving reports and purchase requests.

Because the Department did not maintain perpetual inventory records, Procurement staff ordered inventory items when there was no need. As a result, we noted significant quantities of obsolete and/or overstocked inventory items, which were purchased as long as several years ago. For example, we found pallets containing over 1,000 outdated legal reference books, hundreds of obsolete toner cartridges and printers, and approximately 120 office cabinets costing more than $700 each. We also found 70 unused digital cameras purchased over a year ago and 60 obsolete digital cameras.

We also noted instances where the same person ordered and received the goods. For proper internal controls, an individual should not order and also receive goods.

Recommendations

DCFS management:

24. **Ensure staff independent of Procurement conduct Department-wide physical inventories of warehouses and stock/supply rooms annually.**

25. **Ensure staff periodically evaluates inventory for obsolescence.**

26. **Ensure perpetual inventory records are maintained and updated timely as additions and deletions occur.**

27. **Ensure the functions of ordering, receiving, conducting physical inventories, and recording transactions are adequately segregated.**

Undisclosed Warehouses

DCFS has three main warehouses and several storage locations where they maintain supplies and equipment. DCFS Procurement management did not disclose all warehouse locations when asked. We found a number of undisclosed warehouse locations/supply rooms through staff interviews, invoice reviews, and unannounced site visits. Most of the undisclosed warehouses were used to store surplus and/or obsolete items.

One of the undisclosed warehouses was an offsite storage facility which the Department rented for $3,000 per month. At this location, we found one shipping/freight container, 42 storage crates (equivalent in size to a typical office cubicle), and seven pallets containing office furniture (both new and used), office supplies, obsolete supplies, etc. We questioned DCFS' need for renting warehouse space to store excessive supplies and obsolete items.

DCFS Procurement also did not properly manage the offsite storage facility, resulting in past due invoices totaling $26,000. The Procurement supervisor responsible for approving the invoices did not review the invoices or forward them to Finance for payment. When we visited the offsite storage facility, the vendor stated that they planned to auction the Department's inventory to recover the past due amounts because their attempts to contact Procurement had failed. Procurement staff maintained this offsite storage facility for at least three years.

We discussed this issue with DCFS management and they immediately paid the past due amounts. DCFS management also assigned non-Procurement staff to arrange a transfer of the inventory to a County facility. The Department plans to conduct an inventory and distribute or dispose of any obsolete items.

Recommendations

DCFS management:

28. **Ensure Procurement staff approves and forwards vendor invoices to Finance timely.**

29. **Inventory the offsite storage items and work with the ISD Surplus Property Coordinator to dispose of any obsolete/surplus items.**

Warehouse Security

Supplies and equipment inventories need to be properly secured to minimize the risk of theft. We noted the Department's three main warehouses were secured with access limited to two or three Procurement staff. However, Procurement also keeps surplus items in unsecured areas where DCFS field staff and other unauthorized employees have access.

Recommendation

30. **DCFS management ensure supplies and equipment inventories are properly secured and access is limited to authorized personnel.**

Disposal of Surplus/Obsolete Items

The County has agreements with auction companies to sell surplus/obsolete items at auction. The Department's Surplus Property Coordinators (Surplus Coordinators) approve and forward items for disposal to the auction company, and the auction company issues checks to the Department through the Surplus Coordinators, or in some cases through ISD. The auction company also sends a copy of the checks to ISD. The DCFS Surplus Coordinators are required to forward checks to the Department's Finance Section for deposit.

CFM Section 6.10.2 requires that the manager/supervisor approving surplus items for disposal should not have purchasing or fixed asset responsibilities. In addition, the CFM and/or ISD policies require departments to develop written procedures for the disposal of surplus County property and to document disposed surplus items.

DCFS does not comply with the CFM and/or County purchasing policies and guidelines. All three of the Department's Surplus Coordinators (the Procurement manager and two Procurement employees) can authorize surplus items for disposal and have purchasing and/or fixed asset responsibilities.

DCFS also does not have written procedures for the disposal of surplus property, as required. We noted that Procurement staff did not adequately document disposed surplus items, nor did they adequately control or track auction proceeds. As a result, approximately $110,000 of $230,000 in total auction proceeds between July 2000 and April 2007 was unaccounted for. We found that one auction company voided 45 checks, totaling $110,000, because the checks were not cashed within 180 days as noted on the company's checks. The checks were made payable to DCFS and addressed to DCFS Procurement.

We could not confirm that DCFS Procurement received the missing checks. The Surplus Coordinators stated that they did not receive the checks, although the auction company claims they were mailed. ISD, however, had documents indicating that ISD received and forwarded four of the 45 checks, or approximately $16,000 of the $110,000, to the DCFS Surplus Coordinators. At a minimum, the Department's Surplus Coordinators should have followed up to ensure auction proceeds were received.

Based on our findings, DCFS management immediately replaced the Surplus Coordinators with staff having no procurement or fixed asset responsibilities. DCFS management should also periodically review disposed surplus/obsolete items for appropriateness and to ensure the items were properly approved.

Recommendations

DCFS management:

31. **Develop written procedures for the disposal of surplus property.**

32. **Work with ISD to collect the $110,000 in auction proceeds from the auction company.**

33. **Ensure the Department's Surplus Coordinators complete all required auction documents and establish controls to account for future auction proceeds.**

34. **Continue to ensure the Department's Surplus Coordinators have no procurement or fixed asset responsibilities.**

35. **Periodically review disposed surplus/obsolete items for appropriateness and ensure the items were properly approved for disposal.**

Compliance with County Purchasing Guidelines

Non-Agreement Purchases

County purchasing policies require departments to submit a requisition to ISD for non-agreement purchases over $5,000. However, some departments, including DCFS, have increased purchasing authority to make non-agreement purchases up to $15,000 without ISD's involvement. These departments must obtain at least three quotes/bids for purchases between $1,500 and $15,000. The departments are allowed to make purchases without bidding (i.e., sole source purchase) but only under special circumstances (e.g., emergency purchases, etc.). Sole source purchases under $5,000 can be processed by departments but must be justified in sufficient detail; while all sole source purchases over $5,000 must be processed through ISD for approval, as the County Purchasing Agent.

We reviewed ten purchases over DCFS' delegated purchasing authority of $15,000 and noted that six (60%) were not processed through ISD as required. We also reviewed 17 transactions between $1,500 and $15,000 and noted that Procurement processed seven (41%) transactions as sole source purchases. Three of the seven transactions were under $5,000, which the Department could have processed, if justified. However, none of the three purchases were properly justified. The Department did not obtain ISD approval for the remaining four sole source purchases over $5,000.

In addition, during our review of gift cards, we noted that DCFS did not obtain ISD approval for sole source purchases of gift cards over $5,000. These inappropriate purchases totaled approximately $250,000 since July 2005.

Recommendations

DCFS management:

36. **Ensure purchases in excess of the Department's delegated purchasing authority are processed through ISD.**

37. **Ensure price quotes are obtained in accordance with County purchasing policies.**

38. **Ensure sole source purchases are justified in sufficient detail and those over $5,000 are processed through ISD as required.**

Frequently Purchased Items

ISD solicits and establishes purchasing agreements to obtain favorable purchasing terms for commonly used items. County purchasing policy requires departments to notify ISD of non-agreement items that are purchased frequently where an agreement may be desirable.

DCFS does not notify ISD of frequently purchased items. For example, we noted that the Department purchased over 130 similar/identical furniture items for its program clients between September 2005 and June 2006, from one vendor. The Department continued to purchase the same furniture items after this period, but did not notify ISD.

Recommendation

39. DCFS management require Procurement to monitor frequently purchased items and notify ISD of items that may warrant a vendor purchasing agreement.

Splitting Transactions

County purchasing rules prohibit departments from splitting purchases to bring transactions within the department's delegated purchasing authority. For example, if a department has a $15,000 limit for non-agreement purchases, and wants to make a $30,000 purchase, the department should not issue two $15,000 purchase orders to the same vendor at the same time to avoid having to send a $30,000 purchase order to ISD.

We reviewed 12 transactions that appeared questionable and identified three instances (25%) where Procurement split purchases to stay under the Department's delegated purchasing authority of $15,000. For example, DCFS paid a vendor approximately $17,000 for recruiting and outreach promotional items. Although Procurement received one request from a regional office for the purchase, Procurement prepared two POs. One PO was just below the Department's delegated purchasing authority at $14,671, with the second PO covering the difference. The vendor issued two invoices to match the POs, and the Department subsequently issued two payments.

DCFS must ensure that individual purchases are not split to stay under the Department's delegated purchasing authority by retraining all managers who authorize purchase requisitions and monitor compliance.

Recommendation

40. DCFS management ensure that individual purchases are not split to stay under the Department's delegated purchasing authority by retraining all managers who authorize purchase requisitions and monitor compliance.

Agreement Vendor Purchases

As previously mentioned, it is a violation of County purchasing rules to use agreement POs to purchase non-agreement items and thereby bypass the County's bidding and the delegated purchasing authority requirements.

In addition to the violation noted in the "Inappropriate Purchases" section above, three (25%) of 12 agreement purchases reviewed should have been processed as non-agreement purchases. In one of the three instances, there was no agreement with the vendor. In the remaining two instances, non-agreement items were purchased from an agreement vendor. Procurement staff indicated that they do not regularly review agreements before making purchases and rely on vendors to provide the prices and payment terms.

Recommendation

41. DCFS management require Procurement staff to review agreements prior to making purchases to ensure items are covered by the agreement and that the Department receives the negotiated prices and payment terms.

Payment Practices

Payment without Sufficient Documentation

The CFM requires that vendor invoices must be properly matched with a receiving report/shipping document and purchase order before being paid. This ensures payments are made for goods actually ordered and received, and that the correct price is paid.

We noted that DCFS is not complying with these basic control requirements. DCFS Finance frequently issued payments without receiving reports, purchase orders, and/or invoices. Payments are sometimes issued based on memos from the Procurement manager. To ensure the accuracy of prices, cash discounts, quantities ordered, and delivery terms, and whether the Department actually ordered and received the goods, DCFS management should require Finance to match vendor invoices with purchase orders and receiving reports prior to paying vendors.

Recommendation

42. DCFS management ensure Finance staff match invoices with purchase orders and receiving reports prior to paying vendors.

Cash Discounts and Timeliness of Payments

Many vendors offer cash discounts to encourage early payments. CFM Sections 4.3.1 and 4.3.4 require departments to take all available discounts. We reviewed 17 invoices that offered cash discounts and noted that Finance staff did not take discounts, totaling $337, on any of the invoices.

The CFM also requires departments to pay vendors within 30 days of receipt of the vendor's invoice. We noted that 25 (56%) of 45 payments reviewed were not made within 30 days, including seven that were more than 60 days late and three that were more than 90 days late.

Recommendation

43. DCFS management ensure the Department maximizes cash discounts and that payments are made to vendors within 30 days.

Monitoring Pending/Rejected eCAPS Payments

The County's accounting and accounts payable system, eCAPS, maintains pending/rejected files for payment transactions entered into the system with errors or transactions that have not obtained all the required approvals. Eighty-two of 354 transactions in pending/rejected files (or 23%) were more than 14 days old, including 31 (9%) that were older than three months.

DCFS should periodically review the pending/rejected files to identify and resolve transactions that have been pending/rejected for extended periods of time. Proper monitoring of these files helps ensure timely payments to vendors.

Recommendation

44. DCFS management ensure Finance staff periodically reviews the eCAPS pending/rejected files to identify and resolve transactions that have been in these files for extended periods.

Marking Invoices Paid

DCFS Finance does not consistently mark vendor invoices "paid." Eight (18%) of 45 invoices reviewed were not marked "paid." Vendor invoices should be marked "paid" to prevent reuse/duplicate payments.

Recommendation

45. DCFS management ensure Finance marks invoices "paid" to prevent reuse.

Internal Control Certification Program

The Auditor-Controller developed the Internal Control Certification Program (ICCP) to assist County departmental managers in evaluating and improving internal controls in all fiscal areas, thereby reducing the risk of error, fraud and other improper activities. Under the ICCP, County departments are required to annually review and evaluate controls in key areas and certify that proper controls are in place or note that action is being taken to correct any deficiencies or weaknesses noted.

Many of the non-compliances and other procurement problems we noted in DCFS' procurement and payment operations should have been detected when completing the Department's annual ICCP. However, the Department's FY 2005-06 certification, submitted May 15, 2006, certifies that appropriate procurement and payment controls were in place or were not applicable to the Department's operations. For the areas we reviewed, the FY 2005-06 certification only identified weaknesses related to annual physical inventories.

Recommendation

46. **DCFS management ensure that the ICCP questionnaires are accurately completed by conscientious, qualified staff independent of the function for all applicable assessable units, that all weaknesses are identified, and that an improvement plan is developed to address each internal control problem identified.**

Operational Efficiency

Throughout our review, we noted a number of ways in which the Department can improve the efficiency and effectiveness of its procurement operations, such as:

- **Reduce the number of purchase requests from regional office staff.** We noted that one office submitted a similar/identical supply request on each of four consecutive days and submitted an average of two supply requests per week. To save processing time and prevent backlogs, DCFS management should develop procedures related to the purchase request process. These procedures should require staff to combine similar/identical supply requests where possible and limit the number of staff authorized to order supplies.

- **Limit emergency purchase requests.** We noted emergency requests that were unnecessary and/or did not allow sufficient processing time. For example, 27 (56%) of 48 supply requests from one office over a six-month period were processed as emergency requests. We also noted instances where regional office staff did not request supplies until the supply inventory was gone, and also noted emergency supply requests for community events that were submitted just days before the

event. Regional office staff needs to periodically evaluate and anticipate supply needs and submit requests timely to reduce emergency supply requisitions.

- **Utilizing automation tools.** DCFS Procurement manually tracks purchases, supply inventories, etc. However, given the size of the Department, including multiple regional offices and the number of transactions processed, maintaining accurate perpetual inventory records can be difficult using a manual system. We noted that other County departments (i.e., Department of Public Social Services and the Department of Public Works) utilize some form of automated inventory system. Although there is no Countywide automated inventory system available at this time to assist the Department in automating their inventory/procurement processes (i.e., monitor inventory transactions and levels on-line), we noted that an automated inventory module will be available through eCAPS in the future. The eCAPS inventory module is scheduled to be implemented with the Department of Public Works on a "pilot" basis in July 2008, with other departments to be implemented over the ensuing 12 month period. The Department needs to closely monitor implementation of the eCAPS inventory module at DPW and implement it at the earliest opportunity.

- **Improve staff knowledge through training.** We noted Procurement staff are not proficient in basic computer programs (i.e., Excel), essential in performing their jobs, nor are all Procurement staff knowledgeable regarding County purchasing policies and guidelines. DCFS management should ensure that staff receive appropriate computer training and require all procurement staff to attend ISD's Countywide Procurement Training program.

- **Evaluate Procurement management level.** During our review period, an Administrative Services Manager (ASM) II oversaw DCFS' procurement operations. Given the significance of our audit findings, the Department temporarily placed a higher level manager (i.e., ASM III) over the Procurement Section. Due to the complexity of certain program purchases and the need for critical decision making skills for purchasing matters that have Department-wide impact, we believe DCFS needs to assign a permanent manager at or equivalent to ASM III over the Procurement Section.

We will continue to work with DCFS in evaluating areas where the Department can improve its Procurement operations including evaluating Procurement staffing levels.

Recommendations

DCFS management:

47. Ensure supply requests are combined where possible and limit the number of staff authorized to order supplies.

48. **Ensure staff periodically evaluate and anticipate supply needs and submit requests timely to reduce emergency supply requisitions.**

49. **Closely monitor implementation of the eCAPS inventory module at DPW and implement it at the earliest opportunity.**

50. **Ensure staff receive appropriate computer training and require all Procurement staff to attend ISD's Countywide Procurement Training program.**

51. **Consider placing a permanent manager at or equivalent to ASM III over the Procurement Section.**

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July 30, 2007

To: J. Tyler McCauley
Auditor-Controller

From: Patricia S. Ploehn, Director
Department of Children and Family Services

RESPONSE TO PROCUREMENT REVIEW - PHASE I

Thank you for the opportunity to review the draft report of Phase I of the Auditor-Controller's review of the Department of Children and Family Services' (DCFS) procurement processes.

We generally agree with all of the recommendations contained in the report and implemented a number of the recommendations throughout the review process as issues were brought to our attention. In the near future, we will provide the Board a detailed report on our progress in implementing the recommendations identified in the Phase I report.

As you may know, the reason DCFS requested the Auditor-Controller review our Procurement Section was to get assistance in establishing whether the volume of complaints we receive about the Procurement Section is attributable to insufficient staffing, poor processes, lack of necessary tools to do the job, etc. We certainly had not anticipated that such serious violations of County fiscal and procurement policies would be identified and require so much of your staff resources. So I would like to take this opportunity to thank you for the level of staff resources you devoted to helping DCFS to improve its operations. Your staff has been great to work with; even under the stressful situations, they maintained their professionalism and good humor.

If you have any questions, please let me know; or your staff may contact Claudine Crank, Deputy Director, Bureau of Finance and Administration, at (213) 351-5847.

PSP:SK
CC:cc