



ARLINGTON
VIRGINIA

Internal Audit Report – Sole Source Procurement Process

Report Date: March 8, 2018

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TRANSMITTAL LETTER

March 8, 2018

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Purchasing Agent, Purchasing Office

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Pursuant to the contract and related statement of work for Arlington County, Virginia (“the County”), we hereby present the internal audit of sole source procurement process. Our report is organized in the following sections:

Executive Summary	This section includes a background summary of the function, the objectives and approach, and a detailed description of the observations noted during this audit. Identified with each observation is the recommended action(s), and management’s corrective action plan, including the responsible party and estimated completion date.
Background	This section provides an overview of the function within the process and pertinent operational control points and related compliance requirements.
Objectives and Approach	The internal audit objectives and focus are expanded upon in this section as well as a review of the various phases of our approach.
Process Maps	This section illustrates process maps, which depict data flow, key control points and any identified gaps.

As described in our objectives and procedures outlined on page 8 and 9 of this report, the observations noted are based on our analysis of the processes, documents, records and information provided to us by the County. This audit focused on evaluating the soundness of internal control policies to safeguard assets and on reviewing compliance with County policies. We offer no assurances that schemes or fraudulent activities have not been, or are not currently being perpetrated by any person within the areas reviewed.

We would like to thank the staff and all those involved in assisting RSM US LLP with this internal audit of sole source procurement process.

Respectfully Submitted,

RSM US LLP

RSM US LLP

EXECUTIVE SUMMARY

Background

The mission of the County’s Purchasing Office (“Purchasing”), which is within the Department of Management and Finance (“DMF”), is “*To provide and administer procurement solutions that support the community through county operations.*” For the best interest in the public body, as mandated by the Commonwealth of Virginia, all procurement procedures must be conducted in a fair and impartial manner, and all qualified vendors should have a competitive chance for winning a bid.

Laws relative to the procurement process, in general, are found in the Code of Virginia, *Virginia Public Procurement Act § 2.2-4300*. The County also maintains the *Arlington County Purchasing Manual (“Purchasing Manual”)*, prepared in accordance with the *Arlington County Purchasing Resolution (“Purchasing Resolution”)*, in order to provide clear direction to all County employees regarding purchasing policies.

In certain cases, a vendor may be selected without going through a competitive bid process. One case is described as ‘sole sourcing’ and should only be used when necessary.

Common justifications for the County’s need of sole source procurements include:

- Original manufacturer or provider (no regional distributors)
- Only greater Washington area distributor of the original manufacturer or provider
- The parts/equipment are not interchangeable with similar parts of another manufacturer
- Only known item or service that will meet the specifications
- Parts/equipment are required from this source to permit standardization

Overall Summary / Highlights

The observations identified during our assessment are detailed within the pages that follow. We have assigned relative risk or value factors to each observation identified. Risk ratings are the evaluation of the severity of the concern and the potential impact on the operations of each item. There are many areas of risk to consider in determining the relative risk rating of an observation, including financial, operational, and/or compliance, as well as public perception or ‘brand’ risk.

Objectives and Scope

The objectives of this internal audit were designed to assess whether the system of internal controls surrounding sole source procurements are adequate and appropriate for effective purchasing in compliance with County policies and the *Virginia Public Procurement Act*. This included validating:

- Sole source declarations are warranted, no reasonable alternatives exist, and conditions supporting sole source declarations are present;
- An appropriate level of management, following County policies, is making sole source declarations;
- Sole source procurements are not being made without prior approval; and
- The requirements of sole source procurements occur as prescribed in County policies and the *Virginia Public Procurement Act*.

The scope of this internal audit included all identifiable sole source procurements entered into between July 1, 2016 and June 30, 2017. The County entered into 36 sole source contracts during this timeframe, which was the basis for our sample selection.

Number of Observations by Risk Rating

(See page 9 for rating definitions)

	High	Moderate	Low
Internal Audit – Sole Source Procurement Process	-	1	-

Fieldwork was performed September 2017 through February 2018

We would like to thank all Arlington County team members who assisted us throughout this internal audit.

EXECUTIVE SUMMARY (CONTINUED)

Detailed Observation(s)

<u>Risk Rating</u>	<u>Observation</u>	<u>Recommendation</u>	<u>Management's Action Plan</u>
Moderate	1. Inadequate Documentation to Substantiate Sole Source Determination		
	<p>The County's <i>Purchasing Manual</i> stipulates the requirements as it relates to Sole Source purchases, including valid justifications. We noted the below exceptions regarding inadequate documentation to substantiate the sole source determination for 3 of 15 sole source purchases selected for testing.</p> <p>Per Code of Virginia, <i>Virginia Public Procurement Act § 2.2-4300</i>, jurisdictions may procure goods and services via sole source "...if there is only one source practicably available for that which is to be procured, a contract may be negotiated and awarded to that source without competitive sealed bidding or competitive negotiation."</p> <p><u>Solicitation #17-207-SS – Forest City LLC</u> Change order for additional work related to 'Ballston Garage Concrete Repair' amounting to \$5,311,150.72 by the Department of Environmental Services:</p> <ul style="list-style-type: none"> A Sole Source Justification Form was not completed as required per the County's <i>Purchasing Manual</i>. A sole source memorandum and approval, from the County Attorney, was retained separately. <p><u>Solicitation #17-144-SS Environment Systems Research Institute, Inc</u></p> <ul style="list-style-type: none"> Solicitation #17-144-SS with a contract value of \$17,608 by Department of Technology Services (DTS), did not have a written letter from the manufacturer confirming there were no regional distributors, as required to support the Sole Source Justification Form. 	<p>The level of accountability and transparency of governments far exceeds that of private industry, and in instances in which private industry and governments mix, it is even more important that the accountability and transparency address the appearance of any potential conflicts. In this case, the Public-Private Partnership entered into for community redevelopment included a sole sourced general contractor, which requires a high level of scrutiny. Given the unique relationship between parties, minimal sole source documentation, and resulting change orders we recommend a review of the contract execution and contract compliance to address the potential appearance of inappropriate actions.</p> <p>We recommend that additional scrutiny on sole source procurements be made by the Purchasing Department even if approved by the County Board to strengthen the documentation to support the procurement. Supporting documentation should clearly justify the sole source procurement without exception, so there is no uncertainty as to whether the procurement can be a sole source purchase in accordance with code of Virginia, <i>Virginia Public Procurement Act § 2.2-4300</i>.</p>	<p>Response:</p> <p>For each of these findings, while the sole source determination was appropriate but the appropriate documentation was either not included in the file or the official "Sole Source Justification Form" was not used. All purchasing staff will be reminded about the need to use standard forms and what should be included in the file as appropriate backup.</p> <p><u>1. Solicitation #17-207-SS – Forest City LLC</u> We relied upon appropriate documents and signoffs, in making this determination, however, we recognize that the standard "Sole Source Justification Form" was not used.</p> <p><u>2. Solicitation #17-144-SS Environmental Systems Research Institute, Inc.</u> Environmental Systems Research Institute, Inc (ESRI) is a well-established provider of software systems that supports and licenses its own products. While this sole source was appropriate it lacked a letter from ESRI confirming its licensing and support practices. A letter to this effect should have been included in the file.</p>

EXECUTIVE SUMMARY (CONTINUED)

Detailed Observation(s) - continued

<u>Risk Rating</u>	<u>Observation</u>	<u>Recommendation</u>	<u>Management's Action Plan</u>
Moderate	1. Inadequate Documentation to Substantiate Sole Source Determination - continued		
	<p><u>Solicitation #17-017-SS Spike Cavell Analytic Inc.</u></p> <ul style="list-style-type: none"> Solicitation #17-017-SS – contract value of \$36,495 by the Purchasing Office did not have a Sole Source Justification Form as required per the County's <i>Purchasing Manual</i>. There is no documented approval of the sole source procurement, only the signed contract. Per review of a memorandum dated January 14, 2016 from the County's Acting Assistant Purchasing Agent to the Acting Director, DMF and Deputy Director, DMF, although it is documented that the vendor is qualified to provide this service, there is no justification substantiating that this vendor is the only and most qualified to provide this service, as stipulated per Code of Virginia, <i>Virginia Public Procurement Act § 2.2-4300</i>. <p>Without the proper documentation to justify a sole source request, the Purchasing Agent is unable to adequately review and approve the sole source procurement</p>	<p>Additionally, we recommend that the County's <i>Purchasing Manual</i> regarding supporting documentation required for Sole Source Justification Forms be adhered to without exception. Sole Source Justification Forms should be utilized to support all sole source procurements and not be approved unless all required supporting documentation is attached to the form. In instances where documentation is missing, the Purchasing Agent should obtain missing documentation prior to approval.</p> <p>For sole source purchases made by the Purchasing Office, a secondary review and approval should be made by either the Purchasing Agent or an independent person(s) outside of the Purchasing Office with the appropriate level and knowledge.</p> <p>A complete justification for solicitation #17-017-SS – Spike Cavell Analytic Inc should be documented and added to the sole source's supporting documentation.</p>	<p>Response (continued):</p> <p><u>3. #17-017 Spikes Cavell Analytic, Inc</u></p> <p>Spikes Cavell Analytic, Inc is a well-established provider of software systems that supports and licenses its own products. It provides a unique and innovative methodology for analyzing spend across jurisdictions and is utilized by other regional jurisdictions including Fairfax County. It provided the ability to evaluate joint purchasing opportunities and facilitate inter-governmental cooperation. While this sole source was appropriate it lacked a full documentation of the software's capabilities and was not accompanied by a completed Sole Source Justification form. Fuller documentation should have been provided on the appropriate form.</p> <p>Responsible Party: The Purchasing Agent</p> <p>Estimated Completion Date: Complete</p>

EXECUTIVE SUMMARY (CONTINUED)

Improvement Opportunity

<u>Improvement Opportunity</u>	<u>Recommendation</u>
Monitoring of Sole Source Procurements	
<p>Based on walkthroughs, there is no periodic monitoring and/ or review function of active sole source procurements being performed by Purchasing. No active listing of all sole source procurements is maintained, but a report may be generated from the system of record as necessary.</p> <p>Periodic reviews and monitoring of sole source activity allows a reviewer(s) to identify trends and actions utilized to circumvent the purchasing process. These practices help keep sole source use visible to stakeholders and provide a secondary control over the process as a whole. For example, active sole source vendors/ agreements may become obsolete considering new contracts entered into through the standard procurement process which utilizes competitive bidding to secure the optimal provider. Additionally, the ability to identify the need for a new contract/ agreement is increased based on the monitoring of reoccurring sole sourced vendors, services and products.</p>	<p>Periodically (quarterly or semi-annually), the Purchasing Office should generate a listing of all new and active sole source procurements. The listing should be reviewed by appropriate individuals in order to identify trends, such as an increasing number of sole source procurements. Additionally, the review should include sole source procurements with reoccurring purchase orders to determine if any new vendors have been contracted that could provide this same service. Evidence of review should be retained.</p>

BACKGROUND, OBJECTIVES AND APPROACH

Background

Overview

Laws relative to the procurement process, in general, are found in the Code of Virginia, *Virginia Public Procurement Act § 2.2-4300*. The County also maintains the *Arlington County Purchasing Manual* (“*Purchasing Manual*”), prepared in accordance with the *Arlington County Purchasing Resolution* (“*Purchasing Resolution*”), in order to provide clear direction to all County employees regarding purchasing policies.

The County has identified their purchasing system as a hybrid known as “*Decentralized Process with Centralized Authority*.” Per the *Purchasing Manual*, the purchasing system,

“.. is designed to avoid the pitfalls of the two traditional approaches by taking advantage of the subject matter expertise that resides in the County Departments, and the procurement expertise of the central Purchasing staff in the Purchasing Office.”

Most of the purchasing process (i.e. preparing specifications, evaluating bids and proposals, and managing contracts) is the responsibility of Departments, who are considered the “subject matter experts” for the goods and services they need. The Purchasing staff reviews Department purchasing-related work to ensure that applicable procurement laws, policies and procedures are followed, and with limited exception has final award authority.

For the system to be effective, managers of the personnel assigned to purchasing-related work in their Department must ensure that their personnel are committed to understanding what is expected of them, and capable of fulfilling their duties. Likewise, the Purchasing Agent must ensure that those staff in the Purchasing office and in the Departments to whom authority is delegated are equally committed and capable.”

Methods of procurement noted in the *Virginia Public Procurement Act § 2.2-4300* are as follows:

- Competitive Sealed Bid
- Competitive Negotiation
- Sole Source
- Emergency
- Small Purchases
- Reverse Auctioning

Sole Source Procurements

In accordance with the *Purchasing Manual*, Exemptions from Competition Section C Sole Source Purchases, and *Purchasing Resolution*, Section 4-104 Sole Source Procurement, “A contract may be awarded without competitive bidding or competitive negotiation when the Purchasing Agent determines in writing, after conducting a good faith review of available sources, that there is only one source practicably available for that which is to be procured. The Purchasing Agent shall conduct negotiations, as appropriate, to obtain the best price, delivery, and terms. A record of sole source procurements shall be maintained that lists each contractor's name, the type of each contract, the item(s) procured and the identification number of each contract file.”

BACKGROUND, OBJECTIVES AND APPROACH (CONTINUED)

Background - continued

Sole Source Procurements (Continued)

The *Purchasing Manual*, Exemptions from Competition Section C Sole Source Purchases, further states:

“In our decentralized system Departments prepare a written justification which must be supported by a Sole Source Justification form, and approved by Purchasing. The explanation must be complete and accurate, and must explain why the specific goods/ services are the only goods/ services that can meet the needs of the Department; why the recommended Contractor is the only practicable source available to provide the specified goods/ services; and the process used by the Department to gather the information used in its determination.

Unless the sole source is a one-time purchase, an agreement must be signed by the County and the Contractor. In such cases, the Department will need to provide detailed specifications and/or a detailed Scope of Work to be included in the agreement. The specifications or SOW must be consistent with the written justification provided (i.e. if it is stated that a firm is the only source that can provide some system because their system performs some unique function, the specifications need to clearly require that the system perform that function). The Department must attach the approved Sole Source Justification form and all related documentation to the PO so there is a complete record of the process.

If the sole source is not a one-time purchase, the Department and Purchasing will work together to establish an appropriate period of time (term) for the sole source to be in effect, depending on the market for the goods or services being procured. This agreed-upon term will become the “Contract Term” in the resulting agreement.”

Any department within Arlington County has the ability to request that a procurement be sole sourced, but ultimately, the request must be approved by Purchasing prior to notifying the selected vendor. Foregoing the competitive bidding process, and awarding a sole sourced contract carries a number of risks if not monitored consistently. Specifically, these risks include:

- Legal action, such as lawsuits and fines, due to violations of state or federal procurement laws;
- Corruption between the buyer and seller;
- Poor public perception if Sole Sourced contractor caused a reportable event;
- Overpaying for goods or services due to non-competitive bidding;
- Vendors leveraging sole source contract to take advantage of the County (i.e. inflating prices, unsatisfactory performance of contract, etc.); and
- Less than optimal quality of service or goods due to non-competitive bidding.

BACKGROUND, OBJECTIVES AND APPROACH (CONTINUED)

Objectives and Approach

Objectives

The objectives of this internal audit were designed to assess whether the system of internal controls surrounding sole source procurements are adequate and appropriate for effective purchasing in compliance with County policies and the *Virginia Public Procurement Act*. This included validating:

- Sole source declarations are warranted, no reasonable alternatives exist, and conditions supporting sole source declarations are present;
- An appropriate level of management, following County policies, is making sole source declarations;
- Sole source procurements are not being made without prior approval; and
- The requirements of sole source procurements occur as prescribed in County policies and the *Virginia Public Procurement Act*.

The scope for this internal audit included all identifiable sole source procurements entered into between July 1, 2016 and June 30, 2017. The County entered into 36 sole source contracts during this timeframe, which was the basis for our sample selection.

Approach

Our approach to the audit execution consisted of the following phases:

Understanding and Documentation of the Process

During the first phase, we performed the following:

- Conducted interviews with the appropriate representatives to discuss the scope and objectives of the project, obtain preliminary data, and establish working arrangements;
- Obtained copies of copies of relevant purchasing records;
- Reviewed the applicable State and County policies related to this internal audit;
- Conducted interviews with responsible personnel within Purchasing to obtain an understanding of the unique aspects in order to perform our testing; and
- Developed process maps, which are included in this report.

Evaluation of the Process and Controls Design and Testing of Operating Effectiveness

The purpose of this phase was to test compliance and internal controls. The audit period for transactional testing included all identifiable sole source procurements entered into between July 1, 2016 and June 30, 2017.

This phase also consisted of an evaluation of the design and testing of operating effectiveness. We performed walkthroughs and detailed testing, on a sample of 15 sole source procurements, which occurred during the testing period.

Specific procedures performed included:

- Gathered background information on the County's sole source procurement procedures and any required controls or documentation, including the *Arlington County Purchasing Resolution* and *Arlington County Purchasing Manual*;
- Determined how procurement procedures are followed in accordance with the *Virginia Public Procurement Act*;

BACKGROUND, OBJECTIVES AND APPROACH (CONTINUED)

Objectives and Approach - continued

Evaluation of the Process and Controls Design and Testing of Operating Effectiveness (Continued)

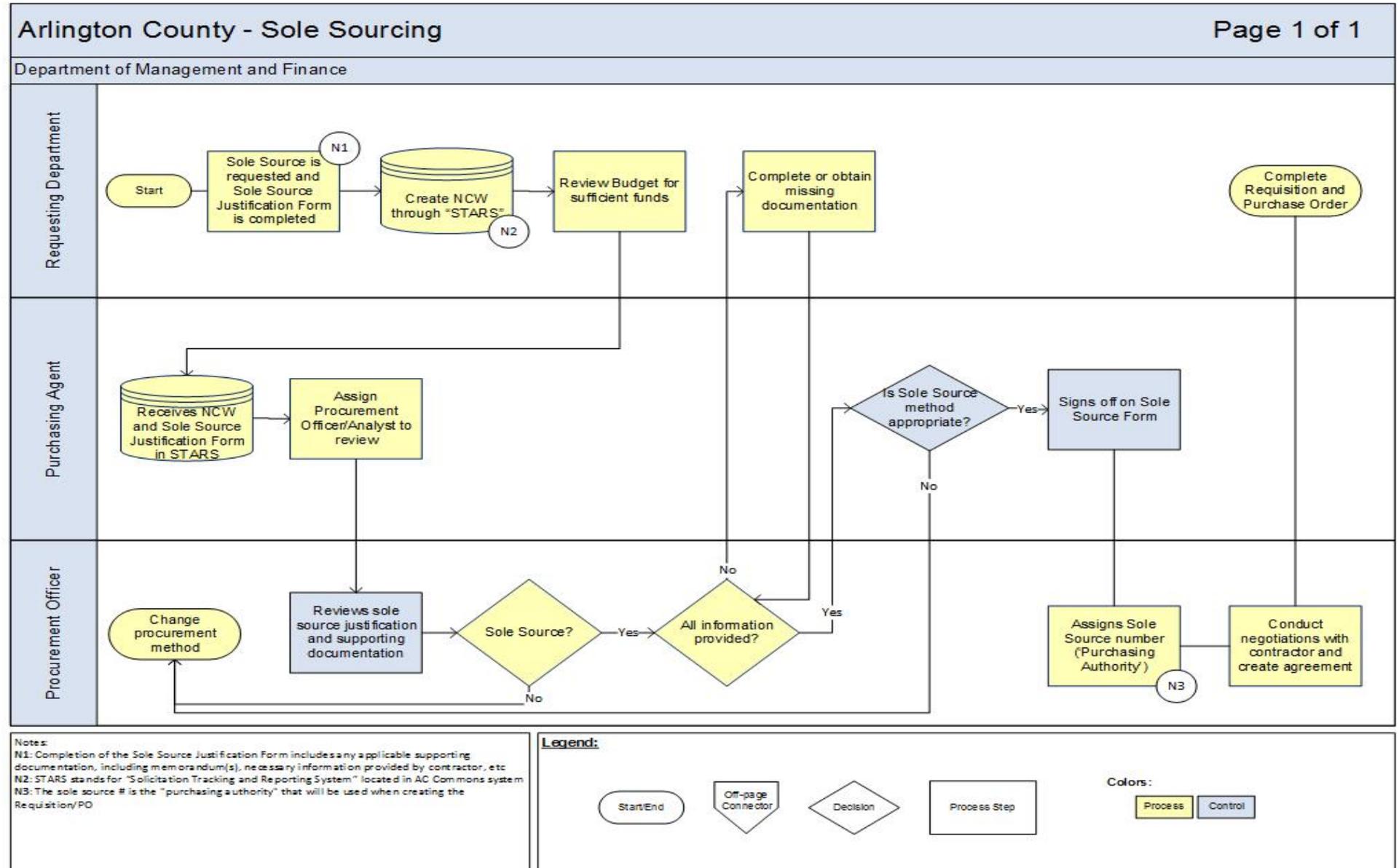
- Determined how sole source contracts are issued and reviewed to ensure there is clearly no other competitive option for the goods/services needed for that department;
- Verified that a New Contract Worksheet (“NCW”) was completed and submitted, that each NCW contained a sole source designation, and that all NCWs were approved by appropriate individuals in accordance with the *Purchasing Manual*;
- Verified that a Sole Source Justification Form was completed, included all required supporting documentation (i.e. memorandum detailing justification for sole source, letter from the Contractor confirming reason for sole source, etc.) and was approved by a Purchasing Agent; and
- Assessed the overall sole source process and controls to determine effectiveness.

Reporting

At the conclusion of this audit, we vetted the facts of this internal audit with Purchasing. The draft report was submitted to Purchasing and DMF for review. An exit meeting was held with Purchasing and DMF to formally review and discuss the draft report and modify accordingly. Management’s corrective action plan with estimated completion dates has been provided and included in the report.

Observation Risk Rating Definitions	
Rating	Explanation
Low	Observation presents a low risk (i.e., impact on financial statements, internal control environment, public perception / brand, or business operations) to the organization for the topic reviewed and / or is of low importance to business success / achievement of goals and internal control structure.
Moderate	Observation presents a moderate risk (i.e., impact on financial statements, internal control environment, public perception / brand, or business operations) to the organization for the topic reviewed and / or is of moderate importance to business success / achievement of goals and improve its internal control structure. Action should be in the near term.
High	Observation presents a high risk (i.e., impact on financial statements, internal control environment, public perception / brand, or business operations) to the organization for the topic reviewed and / or is of high importance to business success / achievement of goals and improve its internal control structure. Action should be taken immediately.

PROCESS MAP





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