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## **A Follow-Up Audit Report on Management Controls at the General Services Commission**

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February 1999

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# Key Points of Report

## A Follow-Up Audit Report on Management Controls at the General Services Commission

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### Overall Conclusion

The General Services Commission (Commission) has made little progress in correcting longstanding problems in critical operations since the issuance of *An Audit Report on Management Controls at the General Services Commission* (SAO Report No. 97-080, August 1997). Problems in the key areas of cost recovery, construction management, and procurement continue despite the fact they have been brought to management's attention repeatedly over the last six years.

Many of the outstanding issues reflect management's inability to improve the quality and cost-effectiveness of the goods, facilities, and services the Commission provides to other state agencies. This is concerning because the Commission's primary role in state government is to provide support services for other state agencies. The Commission received over \$81 million from selling a variety of goods and services to other state agencies in addition to its \$100 million in appropriations during fiscal year 1998.

### Key Facts and Findings

- Problems in the cost recovery, construction management, and procurement functions have been brought to management's attention in 22 different internal and external audit reports between 1992 and 1998. Management committed to fix the problems in its responses to these reports, yet problems continue in these areas.
- The Commission has accumulated a combined fund balance of approximately \$32 million as of August 31, 1998. The Commission's revolving fund accounts include a surplus balance of approximately \$19.2 million, \$8.6 million of which is available after allowing for a \$10.5 million cushion for working capital.
- The Commission continues to have problems managing construction schedules and budgets, following good business practices, and improving client relations because it has not developed basic construction project management processes. Without a project management system, the Commission cannot determine when to take actions to mitigate the effects of time and cost overruns. At the time of our review, the Commission was responsible for managing construction projects valued at \$355 million.
- The Commission may be missing opportunities to save the State money because procurement trends are not formally evaluated to ensure the State takes full advantage of volume buying to obtain lower prices. This type of analysis should be an expected practice for the State's central procurement officer.

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*This audit was conducted in accordance with Government Code, Section 321.0133.*

# Executive Summary

**T**he General Services Commission (Commission) has made little progress in correcting longstanding problems in critical operations since the issuance of *An Audit Report on Management Controls at the General Services Commission* (SAO Report No. 97-080, August 1997). Problems in the cost recovery, construction management, and procurement functions have been brought to management's attention in 22 different internal and external audit reports between 1992 and 1998.

Management has committed to fix the problems each time they have been brought to its attention. However, management's efforts have not resulted in significant changes to agency operations. The fact that the same issues remain today indicates that management is either unable or unwilling to implement the necessary corrective actions. In some instances, management's actions indicate that it does not understand what the real problems are, or what needs to be done to fix them. For example, management is placing heavy reliance on the development of a new \$10.6 million automated system to solve a number of its operational problems. However, because management has not yet corrected fundamental flaws in its business procedures, automating those faulty procedures will not do much to improve operations.

These management issues are especially troubling because they reflect the Commission's inability to improve the quality and cost-effectiveness of the goods, facilities, and services it provides to the State. As external state agencies purchase goods and services from the Commission with funds appropriated by the Legislature, it is important that the Commission provide efficient

services at reasonable prices. The Commission received over \$81 million from selling a variety of goods and services to external state agencies in addition to its \$100 million in appropriations during fiscal year 1998.

Some progress has been made in correcting specific procedural-related issues since the issuance of our fiscal year 1997 audit report. These issues are discussed in Section 1 of this report. However, despite the improvements to individual processes, larger-scale, agencywide weaknesses have not substantially improved.

## **Interagency Overcharges Have Contributed to Accumulated Surpluses in Cost Recovery Funds**

In the cost recovery area, the Commission has accumulated a combined fund balance of approximately \$32 million as of August 31, 1998. The Commission's revolving fund accounts include a surplus balance of approximately \$19.2 million, \$8.6 million of which is available after allowing for a \$10.5 million cushion for working capital. The balances have accumulated through a combination of charging client agencies more than it costs to provide goods and services, transfers of general revenue funds for designated expenses, and transfers of prior general revenue surpluses accumulated by operations. State statute allows the Commission to carry the balances forward each year without obtaining approval through the appropriations process.

The extent and consistent pattern of increases in fund balances suggests that the Commission has not

# Executive Summary

appropriately controlled and accounted for the fund accumulations. For example, the fund balances for the TEX-AN and Capitol Complex Telephone System programs increased 116 percent and 42 percent respectively over the last four years. As a result, the telecommunications revolving account has an available balance of approximately \$7 million as of August 31, 1998, in addition to working capital reserves of almost \$10 million. State statute requires excess balances designated for system upgrades to be transferred to a statewide network applications account. Although the Commission indicated that excess funds will be used for system upgrades, it has not transferred the balances to the statewide account as required by statute.

The accumulated balances are just one indicator that the Commission's rate-setting practices may not be sufficient to ensure that client agencies receive the best price. Management's emphasis on maximizing revenue to cover costs instead of controlling costs and improving the efficiency of services allows the Commission to pass along any operational inefficiencies to agencies that pay for its services.

## **Construction Project Management Is Still a Problem**

In the construction management area, the Commission continues to have problems managing construction schedules and budgets, following good business practices, and improving client relations because it has not developed basic project management

processes. We could not determine the true status of the Commission's ongoing construction projects because of questions regarding the accuracy and completeness of available project data. At the time of our review, the Commission was responsible for managing construction projects valued at \$355 million. The State paid the Commission over \$600,000 in project management fees during fiscal year 1998 to manage these projects.

## **The Commission Does Not Fully Pursue Strategies to Maximize Cost Savings In Its Procurement Practices**

The Commission may have missed opportunities to save the State money because it does not formally and regularly evaluate procurement trends to ensure the State maximizes its use of volume buying to obtain lower prices. This type of analysis should be an expected practice for the State's central procurement officer, responsible for the purchase of over \$556 million in goods and services for other state entities during fiscal year 1998.

Additionally, the Commission has not fully implemented legislation that became effective September 1, 1997, requiring the debarment of poorly performing vendors to prevent them from bidding on state contracts.

## **Summary of Management's Responses**

The Commission does not agree with our finding that it has not made substantial progress in

# Executive Summary

addressing prior audit issues. However, the Commission does concur with most of the recommendations made in the report. The Commission's responses are aimed only at correcting specific examples in audit reports, not on ensuring the Commission provides cost-effective goods and services. Management's responses begin on page 23.

## Summary of Objective

The overall objective of this follow-up audit was to determine whether the Commission had made improvements in critical agency functions since the issuance of *An Audit Report on Management Controls at the General Services Commission* (SAO Report No. 97-080, August 1997). Specific objectives for agency functions, as well as the scope and methodology, are included in Appendix 1.

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## Management Has Not Effectively Addressed Longstanding Problems in Key Operational Areas

The General Services Commission (Commission) has made little progress in improving the quality and cost-effectiveness of its operations in the key areas of cost recovery, construction management, and procurement since the issuance of *An Audit Report on Management Controls at the General Services Commission* (SAO Report No. 97-080, August 1997). These problems include:

- Cost Recovery – Poor rate-setting practices are reflected by the accumulation of a surplus balance of approximately \$19.2 million, \$8.6 million of which is available from operations intended to provide goods and services to other state agencies on a break-even basis. (See Section 2 of this report.)
- Construction Management – Problems managing construction schedules and budgets, following good business practices, and improving client relations continue due to the lack of a construction project management system. (See Section 3 of this report.)
- Procurement – Procurement trends have not been formally evaluated to identify opportunities for cost savings. Legislation that became effective September 1, 1997, requiring the debarment of poorly performing vendors to prevent them from bidding on state contracts has not been fully implemented. (See Section 4 of this report.)

Even more disturbing is the number of times problems in the same areas have been brought to management's attention. Management has been made aware of problems in the three key areas repeatedly over the last six years. (Appendix 2 includes details of the problems identified in 22 different internal and external audit reports issued between 1992 and 1998.)

Although management committed to fixing the problems each time, the fact that the same issues remain today indicates that management is either unable or unwilling to implement the necessary corrective actions. In certain instances, management appears to lack the basic understanding and knowledge of business practices necessary to improve the quality and cost-effectiveness of the goods, facilities, and services the Commission provides to other state agencies. In other instances, executive management's lack of emphasis on taking corrective actions has caused these problems to persist.

Section 1-A:

## **Initiatives Undertaken Since August 1997 Have Not Significantly Improved Commission Operations**

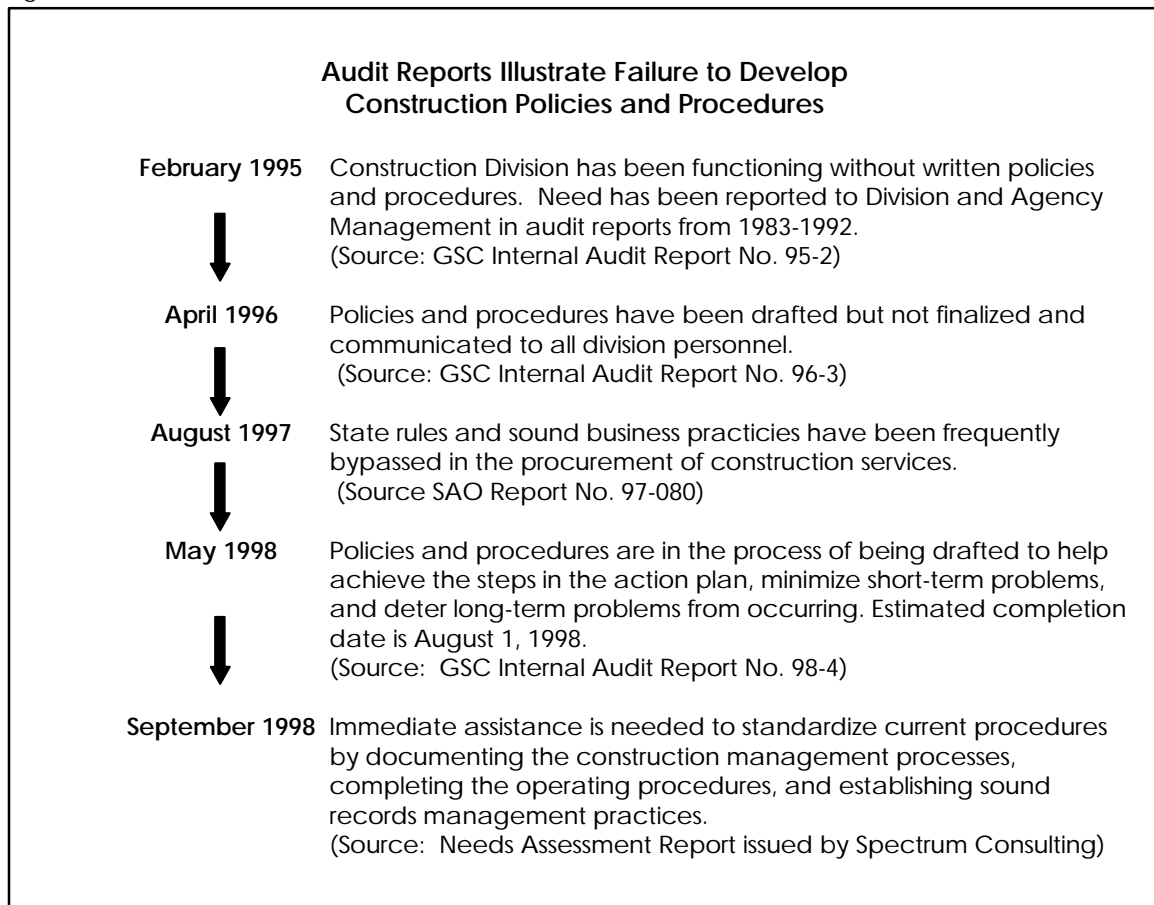
These management issues are evidenced by the fact that initiatives undertaken since the issuance of our prior report have not significantly improved agency operations. Specific examples include:

- Actions taken over the last year have largely focused on correcting the symptoms of the problems instead of addressing the root causes.
  - As a solution to the issues included in our prior report on management's lack of accountability, management developed an "accountability policy" to ensure agency staff would be held accountable for achieving agency goals. Yet a December 1998 Internal Audit report concluded that "the agency does not have a mechanism in place to monitor the achievement of agency goals." The policy does little to improve accountability when management does not adequately monitor the achievement of agency goals.
  - Management is placing heavy reliance on the development of a new \$10.6 million automated information system to solve a number of its operational problems. Improvements to the Commission's information systems are needed and were identified during our last audit. However, because management has not corrected fundamental flaws in its business procedures, automation will not do all that is needed to improve Commission operations. The automation of flawed procedures still results in poor performing operations. Furthermore, the development of this system will take several years even if the Commission receives funding for it. At the time of our audit, management had delayed addressing existing operational weaknesses pending implementation of the new automated system.
  - The Commission's Fiscal Division developed a rate-setting methodology that provides a sound framework for development and analysis of rates in accordance with statutory requirements. The framework represents an improvement since the previous audit, and it provides a mechanism to fix prior problems in the rate-setting area. However, management has not fully implemented this framework. As a result, the Commission continues to have problems developing economical rates because management's philosophy is focused on maximizing revenue to cover its costs, not cost-effectiveness.
- Management has failed to implement actions to which it had previously committed.
  - Management committed to implementing a variety of construction project tracking systems five times since 1995.

However, as of November 1998, the Commission still has not developed an effective process to set, monitor, and control construction project deadlines. Similarly, the Construction Division continues to operate without finalized policies and procedures, despite the fact that the need for guidelines has been brought to management's attention since 1983. (See Figure 1.) The impact of management's failure to follow through on these corrective actions is included in Section 3.

- In response to the State Auditor's Office fiscal year 1997 management control audit, Commission management concurred that its procurement practices needed strengthening in order to obtain lower prices through maximizing the use of volume buying. Management's response to the prior audit report indicated that effective March 1997, purchasers were required to perform routine evaluations, including cost-analyses, to ensure the State took full advantage of volume-buying opportunities. However, as of November 1998, the Commission does not formally and regularly evaluate the advantages of volume buying.

Figure 1



These management issues are especially troubling because the Commission's primary role in state government is to provide support services for other state agencies. Because agencies purchase the goods and services from the Commission with funds appropriated by the Legislature, it is important that the agency provide efficient services at reasonable prices. The Commission received over \$100 million in appropriations during fiscal year 1998. In addition, the Commission collected over \$81 million from selling a variety of goods and services to other state agencies.

Section 1-B:

### **Some Prior Audit Findings Have Been Addressed**

Some progress has been made in correcting specific, procedural-related issues since the fiscal year 1997 management control audit. We recognize and appreciate the individual efforts agency employees have taken to make these improvements. However, it is important to keep in mind that despite the improvements to individual processes, larger-scale, agencywide weaknesses have not substantially improved.

We noted improvements in the following areas:

- Enhanced communication with staff through all-staff seminars and other initiatives
- Development of a rate-setting methodology for cost recovery functions
- Development of a buy-build-lease methodology
- Development and compliance with policies for the procurement of raw land
- Development and compliance with policies for merit awards and reclassifications
- Compliance with state space requirements

#### Recommendation:

As we stated in our prior report, to make comprehensive changes to its operations, the Commissioners and executive management must implement corrective actions that will not only address existing problems, but will also provide some assurance that the same mistakes are not repeated in the future. To bring about major improvements in performance, management should refocus its efforts to identify and address the root causes of the problems outlined in this and past reports. These reports contain good recommendations that can serve as a starting point.

Both Internal Audit and the State Auditor's Office could assist with this process to ensure that initiatives focus on the real problems. Additionally, management must commit to give priority to any initiatives developed to address the problems and to see those initiatives through until completion.

In addressing the root causes of problems, management should:

- Focus on its mission and the need to satisfy its customers in order to fulfill that mission. Identifying what customer needs must be met and served is critical to meeting the Commission's mission. Management should ensure its products and services are aligned with customer needs and business goals.
- Assess internal processes to ensure that they are designed and operated to meet those customer needs. Management must then prioritize its efforts by determining which processes are in greatest need of improvement in terms of cost, quality, and timeliness. It must then analyze the gap between where it is and where it needs to be to achieve desired outcomes and target those processes that are in most need of improvement.
- Finally, management should determine if staff members possess the skills, knowledge, and abilities to effectively operate those critical internal processes so that customer needs are met and the Commission's mission is fulfilled.

## Interagency Overcharges Have Contributed to Accumulated Surpluses in Cost Recovery Funds

**Fiscal Year 1997  
State Auditor's Office Findings  
Cost Recovery**

The lack of consistent and validated fee-setting methodologies results in each division interpreting costs and setting rates without considering the efficiency of its operations.

The Commission should be more aggressive and proactive in improving the economy and efficiency of the services it provides.

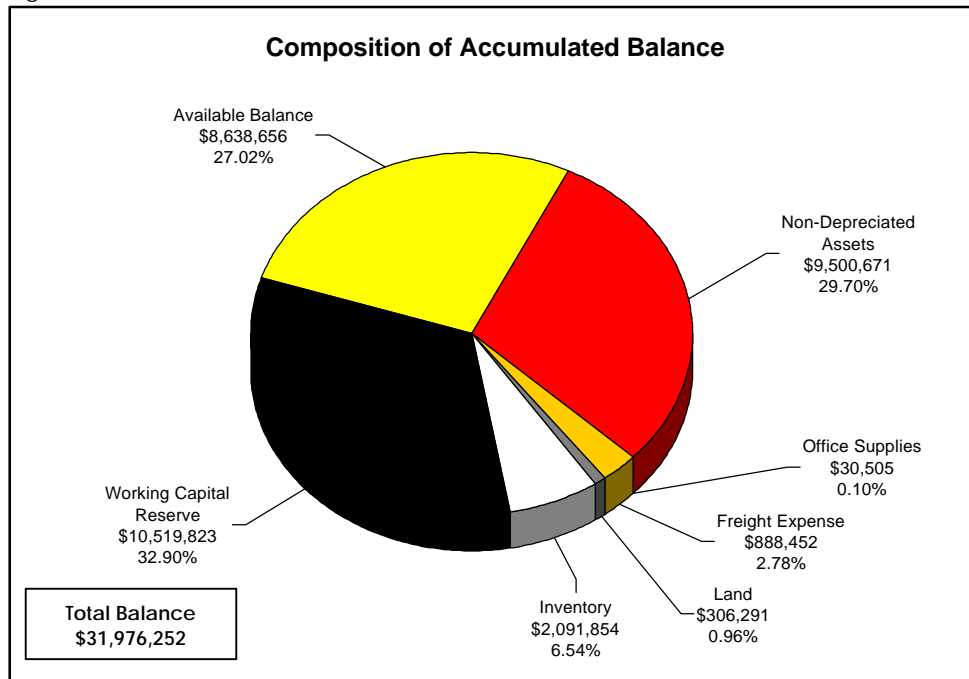
Source: SAO Report No. 97-080, August 1997

The Commission has accumulated a combined fund balance of approximately \$32 million as of August 31, 1998. The revolving fund accounts include a surplus balance of approximately \$19.2 million, \$8.6 million of which is available after allowing a \$10.5 million cushion for working capital. Figure 2 illustrates the components of the \$32 million fund balance. The balances have accumulated through a combination of charging client agencies more than it costs to provide goods and services, transferring general revenue for designated expenses, and transferring prior general revenue surpluses accumulated by operations.

State statute allows the Commission to carry the fund balances forward each year. This means that the

Commission can spend the funds as it chooses (within each specific program area) without obtaining approval through the appropriations process. Consequently, it is important that any accumulations are appropriately controlled and accounted for through the rate-setting process. We identified problems in two different components of the rate-setting process: (1) planning for and management of the accumulated balances and (2) a lack of emphasis on the economy and efficiency of services provided to client agencies.

Figure 2



Source: Commission Financial Statements

## Balance Accumulations Have Not Been Appropriately Planned for or Managed

### Cost Recovery Facts

Cost recovery functions are operations required to recover the cost of providing services. Although full cost recovery functions are intended to break even, it is likely that operations will suffer a profit or loss in any one year.

The Commission operates a variety of cost recovery programs, including 11 full cost recovery functions (see Table 1) and a number of partial cost recovery functions.

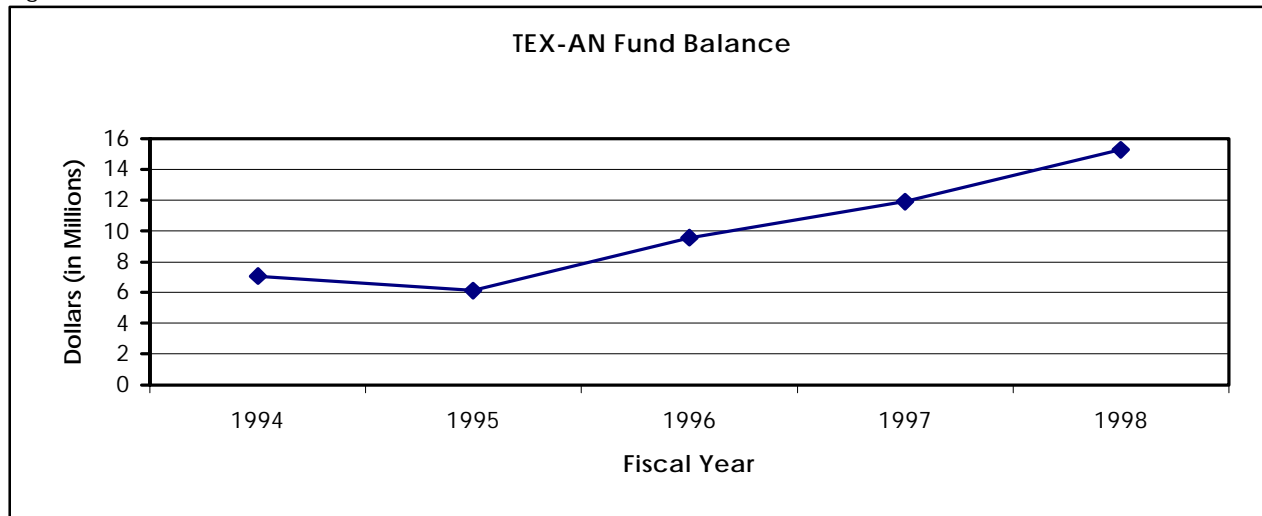
The Commission collected over \$81 million in operating revenues from the 11 full cost recovery functions during fiscal year 1998.

Accumulations of funds may occasionally be necessary to upgrade or replace equipment. However, the extent and consistent pattern of increases in fund balances suggests that the Commission has not appropriately planned for or controlled the balance accumulations.

The majority of the combined accumulated balance is attributable to the TEX-AN (Texas agency long distance service) and the Capitol Complex Telephone System (CCTS) programs. The fund balances for these programs increased 116 percent and 42 percent respectively over the last four years (see Figures 3 and 4 for trends), despite several rate decreases over the last three years. While the Commission has plans to use the fund balances,

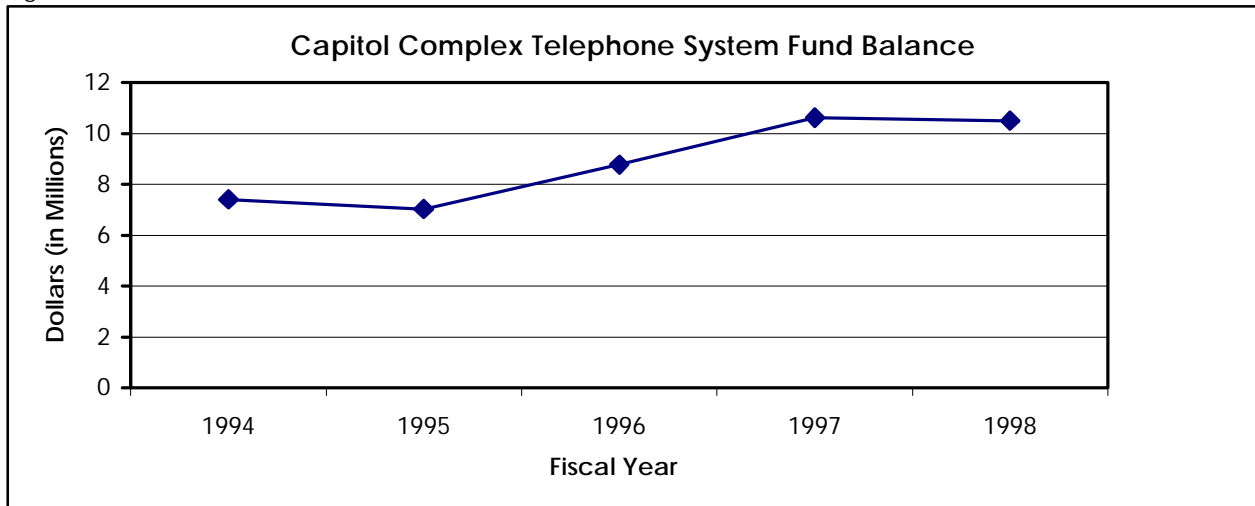
accumulations over the last four years have not been based on formal projections of the funding needed to finance system upgrades.

Figure 3



Source: Commission Financial Statements

Figure 4



Source: Commission Financial Statements

For example, the Commission states that the TEX-AN account balance accumulated because it is deliberately overcollecting for services in order to pay for implementation of the TEX-AN 2000 upgrade. The Commission began formal planning for the TEX-AN upgrade in early 1998, and has formulated plans that provide details on the technical upgrades needed, along with estimates of the total funding needed. However, the plans do not include calculations of the impact of the current accumulated balance on either the cost of the upgrade or future rates. Furthermore, fund accumulations over the last four years have not been based on formal projections of the funding needed to finance the TEX-AN 2000 upgrade.

Additionally, problems with excess accumulations in the TEX-AN and CCTS programs were previously brought to the Commission's attention. The Comptroller transferred \$5 million in excess funds from the telecommunications revolving account to the General Revenue Fund during fiscal year 1994. Legislation effective September 1, 1995, subsequently addressed the issue of accumulated balances in these programs by mandating transfer of excess funds to a statewide network applications account. Balances in the statewide network applications account are to be appropriated only for the purchase, improvement, or maintenance of information resources, technologies, or applications.

Surplus balances in the telecommunications revolving account have not been transferred to the statewide network applications account as required by the 1995 statute. The telecommunications revolving account has a surplus balance of approximately \$7 million as of August 31, 1998, in addition to working capital reserves of almost \$10 million. Balances intended to be used for TEX-AN and CCTS upgrades should have been specifically identified and transferred to the statewide network applications account periodically over the last four years in order to comply with statutory requirements.



Although the amounts are relatively smaller, similar trends exist in other full cost recovery programs. The combined fund balance for the Commission's full cost recovery functions increased \$7.6 million, or almost 31 percent, between August 31, 1996, and August 31, 1998. Of the nine remaining full cost recovery programs, only one, the Central Print Shop, had documented plans that included projected expenditures for future equipment upgrades in its rate-setting calculations. (See Table 1.)

Table 1

Fund Balances by Program				
Revolving Fund Account	Program	Total Fund Equity	Surplus Balance	
			Working Capital <sup>a</sup>	Available Balance
Telecommunications	TEX-AN	\$ 15,284,461	\$ 9,140,237	\$ 4,151,685
	Capitol Complex Telephone System	10,493,250	799,876	3,062,280
	DIR Project	(440,134)	(1,141,497) <sup>b</sup>	0
General Revolving Account	Central Store	1,126,247	546,053	86,719
	Central Print Shop	1,174,801	377,750	315,036
	Business Machine Repair	602,367	222,734	170,984
	North Print Shop	497,718	186,482	0
	Construction Inspections	221,363	72,386	148,477
	Minor Construction	64,313	36,996	0
	Project Management	(145,476)	(147,443) <sup>b</sup>	0
Federal Surplus Property Account	Federal Surplus	3,097,342	426,249	703,475
<b>Total – All Revolving Accounts</b>		<b>\$ 31,976,252</b>	<b>\$ 10,519,823</b>	<b>\$ 8,638,656</b>

<sup>a</sup> Working capital calculation is based on maximum allowed per federal regulations.

<sup>b</sup> Negative balances indicate a negative cash flow absorbed (or funded) by other programs within the revolving account.

Source: Commission Financial Statements

Section 2-B:

### Rate-Setting Practices May Not Ensure Client Agencies Receive the Best Prices

The accumulated fund balances are just one indicator that the Commission's rate-setting practices may not be sufficient to ensure that client agencies receive the best prices. Additional indicators of management's emphasis on maximizing revenue to cover costs instead of controlling costs and improving efficiency of services include:

- If a cost recovery function suffers a loss, rates are sometimes raised to recover the loss without analysis of the associated costs. We noted cases where the only action considered by management was to increase the rates charged to client agencies. This approach allows the Commission to pass along any operational inefficiencies to agencies that pay for its services.

For example, the project management function plans to increase its fiscal year 1999 rate to cover a loss of approximately \$320,000 incurred during fiscal year 1998. Analysis of revenue and expenditure trends over the last two years indicate that while revenues have decreased approximately 10 percent, expenditures have increased 144 percent.

- Instead of decreasing its costs to reflect the decline in business, management has requested additional general revenue appropriations to make up for the shortfall in fees collected from external vendors. The Commission is authorized to charge vendors a fee to register on the Centralized Master Bidders List (CMBL), which is a partial cost recovery function. According to the agency, registration renewals are only averaging 64 percent of the fiscal year 1996 and 1997 registrations. Management is requesting \$1,052,000 in general revenue for fiscal years 2000 and 2001 to maintain operations of the CMBL at its current level although the workload has declined by 36 percent.

We saw no evidence of analysis of the appropriateness of expenditures in these cases.

Recommendation:

To improve its rate-setting practices, management should fully implement the requirements of the rate-setting policy developed by the Fiscal Division. To do so, management must change its emphasis from “have we covered all of our costs?” to “are we providing the best services at the best price?” Specifically:

- Management should comply with the policy’s requirement to benchmark the rates it charges with similar services in the private sector.
- To ensure proper accounting and control of profits and losses generated from cost recovery functions, management should routinely evaluate the reasons for the profits and losses, including analysis of both revenue and expenditure trends. Based on the results of the analysis, either the rates or expenses should be adjusted accordingly.

Accumulations of funds may occasionally be necessary to upgrade or replace equipment. However, accumulations should be planned, including projection of needed changes to the rates, and formally approved by the appropriate authorities.

- Funds accumulated for the purposes of upgrading TEX-AN and CCTS should be transferred to the statewide network applications account in accordance with statutory requirements.
- To ensure that the Commission has the necessary expertise to complete these tasks, management should hire a cost accountant with experience in services similar to those provided by the Commission. This position (or positions) should be solely devoted to the cost recovery functions.

Section 3:

## Construction Project Management Is Still a Problem

**Fiscal Year 1997  
State Auditor's Office Findings  
Construction Management**

Inadequate management of construction and architect/engineer service contracts has resulted in project delays, price escalations, and strained relations between the Commission and the entities it serves.

State rules and sound business practices have been frequently bypassed in the procurement of construction services.

Source: SAO Report No. 97-080, August 1997

The Commission continues to have problems managing construction schedules and budgets, following good business practices, and improving client relations. These weaknesses can lead to project delays and cost overruns, which can ultimately translate to increased costs for the taxpayers. These problems persist because the Commission has not developed basic construction project management processes to effectively plan, monitor, and control construction schedules and budgets. As mentioned in Section 1, problems in this area have been brought to management's attention a number of times over the last six years.

At the time of our review, the Commission was responsible for managing construction projects valued at \$355 million. The State paid the Commission over

\$600,000 in project management fees during fiscal year 1998 to manage these projects. The need to effectively monitor construction budgets and schedules will become even more crucial over the next biennium as the Commission proceeds with the development of the Robert Mueller Airport. The Commission currently estimates the design and construction costs of this single project to be almost \$300 million.

Indicators of the Commission's lack of a project management system include:

- We could not determine the true status of ongoing construction projects because of questions regarding the accuracy and completeness of project data available at the Commission. The processes the Commission uses to manage project time lines and budgets are so poor it has difficulty accurately tracking and reporting basic information such as "The Number of Construction Projects Managed." Without timely and accurate information, the Commission cannot take actions to mitigate the effects of cost and time overruns. The State Auditor's Office fiscal year 1997 management control audit found that delays in completing or getting projects started were caused by the Commission's failure to develop, monitor, and effectively manage project schedules.

We found a number of discrepancies in the Commission's monthly *Project Status Report*, which was developed after the fiscal year 1997 SAO audit to provide the Commission with a tool to monitor the status of ongoing construction projects. Discrepancies included:

- Information in the report varies from project schedules provided to clients. The *Project Status Report* for the month ended October 31, 1998 (presented to the Commissioners in November 1998), indicated that the construction of the Robert E. Johnson Building, valued at over \$30 million, was on schedule for an estimated completion date of January 5, 1999. However, the estimated final completion date was May 21, 1999, according to a project schedule dated October 13, 1998.
- Deviations from original time lines are not included and explained. The original project files indicate that the Capitol Visitors Parking Garage, valued at \$8.6 million, and the Lot 2E parking garage, valued at \$6.4 million, were scheduled for occupancy in December 1998. However, the project status report presented to the Commissioners in November 1998 indicated that the construction of the parking garages was on schedule with estimated completion dates of March 20, 1999, and February 17, 1999, respectively. The report does not include an explanation of the differences in the occupancy dates.
- Not all scheduled projects are included in the status report. According to a schedule agreed upon by the Commission and the Department of Public Safety, the architect/engineer selection process for six projects valued at over \$2.6 million was set to begin in July 1998. However, the initial process did not begin until November 1998, approximately four months behind schedule. An accurate status report should have included these projects, along with the reasons for the delays.

Additionally, a report issued by the Commission's Internal Auditor in December 1998 noted that 13 projects included in a performance measure count as of May 31, 1998, were not included in the *Project Status Report* prepared for the Commissioners.

- Two contracts totaling over \$1.5 million were verbally awarded to prevent funds from lapsing at the end of the fiscal year. Sound business practices dictate that fully executed contracts should be in writing to protect the State's interests. However, the Commission's legal counsel subsequently justified the transaction by issuing a ruling that Commission statutes do not specifically require contract awards to be in writing. Instead of establishing appropriate safeguards in the project management process to prevent the problems that created the need to verbally award the contracts from reoccurring, management focused on justifying the transaction after the fact. Subsequently, we found another instance in June 1998 where the dates were

changed on invoices totaling over \$70,000 apparently to cover the fact that work began before a contract was executed.

- Customers continue to express dissatisfaction with project management services provided by the Commission. Representatives from four different state agencies indicated to the State Auditor's Office that the Commission was not effective in planning and managing construction projects. One customer indicated that the project management process was worse than it was at the time of our prior audit.

However, during fiscal year 1998, the Commission received satisfactory or excellent service ratings on 90 percent of the customer response cards it provided to its clients.

These examples illustrate how the lack of a basic project management framework creates an environment where management is forced to react to events as they occur, often deviating from good business practices in the process, because safeguards to protect the State's interests have not been implemented.

Recommendation:

To implement an effective project management system which ensures that projects are completed on time, to specifications, and within budget, the Commission must:

- Identify critical information needed to ensure projects are completed on time, to specifications, and within budget.

**What Is the Construction Industry Institute?**

The Construction Industry Institute is a non-profit research organization whose mission is "improving the total quality and cost effectiveness of the U.S. construction industry, thereby improving the competitive position of U.S. business in world markets." It is a " unique consortium of owners, designers, constructors, and the academic community who are committed to working together toward a common goal: the improvement of the U.S. construction industry from project conception to start-up and maintenance."

Members of the Construction Industry Institute include Aramco Services, Chevron Corporation, DuPont, Exxon Research, General Motors, The University of Texas System, Bechtel, Brown & Root, Fluor Daniel, and The M.W. Kellogg Company.

- Implement a system to track and use the data to ensure that the process is meeting the expectations of agency management, the Commissioners, and the customers.
- Finalize project management policies to provide project managers with a foundation to manage the projects. Provide training and tools to assist in implementing the finalized procedures.

Because of the history of failed attempts, the Commission should consider using local expertise to enhance its project management function. An outstanding resource for making a powerful impact on project management effectiveness is the Construction Industry

Institute (CII), which is located next to The University of Texas at Austin campus. A cross-section of the world's leading owners, contractors, and design professionals

research all areas of the construction, design, and project management processes. Based on this research, CII offers the following products to the public:

- Research summaries
- Software
- Research reports
- Implementation resources
- Videotapes
- Education modules
- FasTrack education resources
- Training courses
- Consulting services

The Commission could greatly benefit from CII's comprehensive research by using it to identify, develop, and communicate the best practices of the construction industry.

Training courses offered locally include the following:

- Development and Alignment of Project Objectives
- Pre-Project Planning
- Scope Definition and Control
- Performance Management
- Optimizing Project Schedules
- Work Packaging for Project Control
- Construction Planning for Start-Up
- Managing the Small (Special) Project

Section 4:

## The Commission Does Not Fully Pursue Strategies to Maximize Cost Savings in Its Procurement Practices

<p style="text-align: center;"><b>Fiscal Year 1997 State Auditor's Office Findings Procurement</b></p> <ul style="list-style-type: none"><li>• The Commission continues to do business with poorly performing vendors because information on past vendor performance is not consistently used in the procurement process.</li><li>• The advantages of volume buying have not been calculated in the past. Without this type of evaluation, the Commission has no assurances that the State is taking full advantage of volume buying to obtain lower prices.</li></ul>
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Section 4-A:

### Efforts to Maximize the State's Volume Buying Power Should Be Improved

The Commission may be missing opportunities to save the State money because procurement trends are not formally and regularly evaluated to ensure the State takes full advantage of volume buying to lower prices. Formal analysis and evaluation of procurement data should be an expected practice for the State's central procurement officer. The Commission was directly responsible for the purchase of over \$558 million in goods and services for other state entities during fiscal year 1998.

In its responses to the State Auditor's Office fiscal year 1997 management control audit, management concurred that the agency's volume buying practices needed strengthening. Management indicated that a policy requiring purchasers to consistently evaluate products and services procured by the Commission, including a cost-savings analysis, had been implemented in March 1997.

However, the Commission could not provide documentation that formal evaluations had been performed in the year since our last audit. In fact, the Central Procurement Division reversed its policy in July 1998 and deleted the requirement for a cost analysis. Some purchasers use an informal process to evaluate procurement trends. Essentially, identification of potential term contracts is left up to purchasers' and procurement managers' judgement. The managers primarily rely on a normal review of purchase orders to identify procurement trends. When a trend is noticed, it then triggers an analysis of the feasibility of using a term contract to obtain a lower price. If these trends are not noticed through the purchase order approval process, no other process is in place to ensure volume buying advantages are maximized.

Management maintains that its informal evaluation is sufficient to ensure that the State is maximizing cost savings. However, with the risk that heavy workloads could hinder a manager's ability to accurately identify buying trends, reliance only on this informal process is not sufficient to ensure that the Commission identifies and takes advantages of all cost-savings opportunities. Additionally, purchases made by state agencies under delegated purchasing authority are not considered in the informal evaluation. Delegated purchases totaled approximately \$468 million in fiscal year 1998. Without consideration of trends in delegated purchases, the Commission may be missing additional opportunities to maximize cost savings.

Section 4-B:

## Legislation to Limit Business With Vendors Who Perform Poorly Has Not Been Fully Implemented

Commission purchasers do not routinely consider information on vendors' past performance when purchasing goods and services for other state agencies. Statutory changes made during the 75th Legislative Session placed an even greater responsibility on the Commission to consider vendor performance during the procurement process. However, the Commission has not yet fully implemented the vendor debarment program required by Senate Bill 1752.

In the fiscal year 1997 audit, we found that vendors who performed poorly continued to receive contract awards as long as they were the lowest bidders meeting specifications. Purchasing goods from poorly performing vendors can be costly to the State both in terms of actual dollar costs as well as lost efficiencies. When agencies do not receive goods ordered in a timely manner or do not receive quality goods, they may not be able to provide services efficiently and effectively.

Senate Bill 1752, passed during the 75th Legislative Session (effective September 1, 1997), provided the Commission with a clear means for managing vendors who performed poorly through a debarment program. The Commission passed rules in December 1997 establishing a framework for the implementation of the debarment system. However, the Commission was just beginning to implement the system as we were concluding our audit work in November 1998.

Over the last year, the Commission has developed procedures that require agencies to report vendor performance information for certain transactions. However, these policies are insufficient to address previously identified problems because the Commission still has not developed a reliable system to accumulate, track, and evaluate vendor performance data submitted by the agencies. The Commission must have a reliable method to track and assess vendor performance to provide a basis for decisions regarding vendor debarment.

### Recommendation:

- As the State's procurement officer, the Commission should take a formal, proactive approach to ensure that the State maximizes the benefits of volume buying. To do so, the Commission should:
  - Develop specific criteria to use in evaluating procurement trends. The criteria should include (1) basic factors such as benchmarks to measure when increases in volume indicate development of a term contract would be beneficial and (2) calculation of the average cost savings obtained using term contracts.



- Identify the information needed to perform the evaluations and develop a system to track it. Information on delegated purchases made by external agencies should also be included in the evaluations.
- Formally evaluate the procurement data on a regular basis (quarterly, semi-annually) and document the evaluations using a consistent approach.
- Fully implement the vendor debarment program required by Senate Bill 1752 (75th Legislative Session). In order to successfully implement the vendor debarment program, the Commission must develop and implement a system to track and report complete and accurate data on vendors' past performance from both the General Services Commission and external agencies.

## Solutions to Improve Self-Sufficiency of the LoanSTAR Revolving Loan Program Have Been Identified but Not Implemented

**Fiscal Year 1998  
State Auditor's Office Finding  
LoanSTAR Program**

Energy Office management needs to improve its ability to track, forecast, and analyze the financial operations of the LoanSTAR Revolving Loan Program. The loans are not generating enough interest income to cover administrative costs of the LoanSTAR Program as required by statute.

Source: SAO Report No. 98-014, January 1998

The State Energy Conservation Office (Energy Office) of the General Services Commission has identified potential improvements to move administration of the LoanSTAR revolving loan program towards self-sufficiency. Energy Office management prepared position papers in November 1998 outlining two potential solutions to address fiscal management concerns identified in *An Audit Report on Contract Administration at the State Energy Conservation Office of the General Services Commission (Petroleum Violation Escrow Funds)* (SAO Report No. 98-014, January 1998). The solutions proposed by the Energy Office include:

- Generate LoanSTAR administrative revenues through expediting project time lines and imposing payment penalties for contract time extensions.

- Adjust program interest rates for state agencies and institutions of higher education. The Energy Office's analysis of this option indicates that the administrative self-sufficiency (revenue generated by loan interest will cover administrative costs) might be reached during fiscal year 1999.

The proposed solutions had not been implemented at the time we concluded fieldwork in November 1998; therefore, the appropriateness of the proposed solutions could not be evaluated.

Recommendation:

We recommend that the Commission continue its efforts to improve fiscal management of the LoanSTAR revolving loan program to ensure it meets its statutory requirements.

## Auditor's Follow-Up Comments

### General Comments

Throughout its responses, the Commission states it has partially or fully implemented several recommendations from previous State Auditor and Internal Audit reviews. These assertions are self-reported. Our follow-up review found that significant problems in mission-critical operations have not been corrected.

Our follow-up work at the Commission focused on determining if operational problems identified in our prior audit report had been corrected. The number of recommendations Commission management has implemented is irrelevant if problems still exist that prevent the Commission from fulfilling its mission. Once problems have been identified, it is management's responsibility to ensure that the underlying causes of the problems have been addressed, regardless of the audit recommendation.

The Commission incorrectly states that "because the major areas of concern in the 1997 audit have been addressed, the 1999 follow-up audit is focused on other matters." There are no new issues. The matrix below sets forth the direct correlation between the issues included in the fiscal year 1997 audit report and the fiscal year 1999 follow-up audit report. Management's inability to make the connection between the fiscal year 1997 audit findings and the follow-up audit findings highlights the fact that management does not appear to understand what the real problems are or how to fix them.

Area	Fiscal Year 1997 Audit Findings	Fiscal Year 1999 Follow-Up Audit Findings
Cost-Recovery	<p>The lack of consistent and valid fee-setting methodologies results in each division interpreting costs and setting rates <i>without considering the efficiency of its operations</i>.</p> <p>The Commission should be more aggressive and proactive in improving the economy and efficiency of the services it provides.</p>	<p>Accumulated fund balances of almost \$32 million and management's emphasis on maximizing revenue instead of controlling costs and improving efficiency of services indicate that the Commission's rate setting practices may not be sufficient to ensure that client agencies receive the best prices.</p>
Construction Management	<p>Inadequate management of construction and architect/engineer service contracts has resulted in project delays, price escalations, and strained relations between the Commission and the entities it serves.</p> <p>State rules and sound business practices have been frequently bypassed in the procurement of construction services.</p>	<p>The Commission has not developed basic construction project management processes to effectively plan, monitor, and control construction schedules and budgets.</p> <p>The lack of a basic project management framework creates an environment where management is forced to react to events as they occur, often deviating from good business practices in the process, because safeguards to protect the State's interests have not been implemented.</p>

Area	Fiscal Year 1997 Audit Findings	Fiscal Year 1999 Follow-Up Audit Findings
Procurement	<p>The advantages of volume buying have not been calculated in the past. Without this type of evaluation, GSC has no assurances that the State is taking full advantage of volume buying to obtain lower prices.</p> <p>The Commission continues to do business with poor performing vendors because information on past vendor performance is not consistently used in the procurement process.</p>	<p>The Commission may be missing opportunities to save the State money because procurement trends are not formally and regularly evaluated to ensure the State takes full advantage of volume buying to lower prices.</p> <p>Commission purchasers do not routinely consider information on vendor's past performance when purchasing goods and services for other state agencies.</p>

### Issue Areas Raised by the Follow-up Audit:

Our specific follow-up comments generally address management's responses in the three key areas of cost recovery, construction management, and procurement.

#### Cost Recovery

The Commission's response questions the fact that the cost recovery area was not identified in the 1997 audit as a "key area." Various problems in cost recovery functions were included in three of four sections of the fiscal year 1997 audit report. Management's failure to recognize the cost recovery function as a key operational area when over 40 percent of its funding is provided by the cost recovery programs is another indicator of management's lack of understanding of the real problems in these areas.

The Commission's response cites a long list of actions taken in the rate-setting areas. We reviewed these processes and actions during the course of our fieldwork. The issues cited in Section 2 of this report indicate that management's efforts in this area have not been sufficient to ensure the Commission provides the best services at the best prices. The steps taken by the Commission since the last audit have not been effective in correcting all prior problems. The framework provided by the Commission's rate-setting methodology is effective as a tool only if it is used appropriately.

For example, management asserts that because external agencies decide to use some of its services, it must mean the rates are cost-effective. The Commission's mission is to provide the State with the best possible services at the lowest possible costs. Management's response appears to indicate that as long as its rate is lower than a competitor's, there is no need for additional analysis of cost-effectiveness.

The Commission's response indicates that two reports were issued from the Telecommunications Planning Group highlighting plans for use of the TEX-AN

program balances. The approximately \$25 million fund balance in the telecommunications revolving account cited in our report had already accumulated by the time the plans cited by the Commission were developed in October 1998.

The Commission's response asserts that rates for the CCTS and TEX-AN programs are adjusted appropriately as evidenced by the fact that rates have been reduced several times in the last few years. Our follow-up audit notes the rate decreases, but asserts that despite these rate decreases, the accumulated fund balances have steadily increased over the last four years. If the rates for these programs had not been decreased, the accumulated balances would be even greater than those currently cited in the report.

The Commission's response indicates that federal guidelines provide for 60 days of working capital being retained. The federal guidelines cited by the Commission allow a maximum of 60 days working capital. However, these guidelines do not officially apply to the balances accumulated in the Commission's cost recovery accounts. If, through analysis of cash flows and aged accounts receivable, it is determined that operations do not dictate the need for 60 days of working capital, it is not prudent for the Commission to maintain the maximum amount solely because it is allowable at the federal level. We allowed for the maximum 60-day requirement in our calculation. However, the Legislature may wish to specifically address if the full 60-day requirement is necessary.

The Commission's response lists a number of factors associated with legislative oversight of the fund balances. The final report provided to management on February 9, 1999, contains no reference to a legislative oversight issue. Therefore, we do not understand the nature of Management's response.

The Commission's response indicates that the SAO used the example regarding the CMBL with full knowledge of the circumstances involved. Our point is that the analysis was not done before the Legislative Appropriations Request was submitted in the first place. The analysis was only done after the issue was brought to management's attention during the audit. We left the example in the report to support our point that the analysis should have been done before additional funds were requested in the Legislative Appropriations Request.

### **Construction Management**

The Commission's response asserts that it has construction management processes in place to plan and monitor construction projects. A project management system is not the same as a reporting tool. The Commission's current approach to project management is to react as events occur and let circumstances run the jobs. A project management system is important to ensure that the Commission takes actions to meet established goals despite circumstances imposed by factors such as weather and customers.

An effective project management system should provide the Commission with (1) a mechanism to anticipate potential delays so that contingency plans could be developed and (2) the means to determine the causes of delays and cost overruns so appropriate corrective action could be taken to bring the job back on track.

As the Commission states in its response, we found that budgets and schedules for the Commission's projects are often established by others, such as the contractors. Without an independent assessment of project time lines and budgets, the Commission is not in a good position to make decisions for efficiently using resources, coordinating personnel on the job, and planning and controlling the work.

### Procurement

The Commission's response states that the Central Procurement Division routinely assesses money-saving opportunities in its purchasing program. During our fieldwork, the Commission could not provide documentation that formal evaluations had been performed in the year since our prior audit. The internal policy referred to in the Commission's response (Procurement Policy Section 21.3) is vague, and only identifies potential types of information which could be considered in the development of new term contracts. In fact, the policy is less defined than the Commission policy which existed at the conclusion of the fiscal year 1997 audit. The revised policy does not include benchmarks or guidelines to assist in determining when a term contract would be in the best interests of the State as recommended in both the fiscal year 1997 and follow-up audits.

The Commission's response indicates that 16 new term contracts were developed during fiscal year 1998. Our test of procurement files indicated that as of September 1998, only three new term contracts had gone into effect since September 1, 1997. The rest of the contracts provided as "new" term contracts were actually renewals of existing contracts for standard purchases such as food services.

The Commission's response asserts that that legislation may be required to clearly authorize the Commission's analysis of delegated purchasing authority. We disagree with management's assertion. Per the Commission's own rules (Texas Administrative Code, Section 113.11[c][3]), items purchased under delegated authority may not include items available under a term contract in most cases. Therefore, the Commission not only has the authority, but the obligation to ensure that the use of term contracts is maximized. The Commission's primary argument appears to be that it would be too difficult to obtain the procurement data from the agencies. We maintain that the collection of this type of data should be a routine function for the State's central procurement officer.

The Commission's response indicates that management has "partially implemented" an automated system to track vendors' past performance. However, further examination of the Commission's response indicates that the Commission is no further along than it was at the time of our fiscal year 1997 audit. Management states that the system requires extensive modification, it is up to the agencies to assess

vendor performance, and training on the revised system will take time. We fail to understand how this could be considered as “partially implemented” when, as we found in our follow-up work, the Commission has not yet developed a reliable system to track and report complete and accurate data on vendors’ past performance.

### Conclusion

Overall, the Commission’s response to our audit indicates its efforts have been superficial and aimed only at correcting specific examples in audit reports, not ensuring the Commission provides cost-effective goods and services. This further supports the conclusion in our Management Issue finding that management does not understand what the real problems are, or what needs to be done to fix them. A further example of this can be seen in the Commission’s response relating to the Comprehensive Needs Analysis.

The Commission’s response indicates that it has adopted the recommendation from the consultant’s needs analysis to improve and integrate agency work processes prior to applying technology solutions. The Commission’s response is referring to the Final Report of the Comprehensive Needs Analysis dated September 4, 1998, which recommends that the Commission “align and apply technology only after improving and integrating agency work processes.” Specifically, the consultant’s report states that:

- Technology is not always the answer or even required to improve business operations. Some of the processing problems within the organization come from the lack of standard management processes, not a lack of automation.
- Immediate assistance is needed to standardize current procedures by documenting the construction management processes, completing the operating procedures, and establishing sound records management practices.

The issues cited in our follow-up report indicate that the Commission has not made the necessary and appropriate improvements to agency work processes, yet it continues to view the new information system as vital to fixing its problems.

## Management's Responses

### GENERAL SERVICES COMMISSION MANAGEMENT RESPONSE TO "A FOLLOW UP AUDIT REPORT ON MANAGEMENT CONTROLS AT THE GENERAL SERVICES COMMISSION"

#### EXECUTIVE SUMMARY

- ◆ In less than eighteen months, GSC has made significant progress in correcting longstanding problems critical to its operations since SAO Report #97-080 was issued in August 1997. Of the 22 internal and external audits cited by the State Auditors Office, 17 are GSC's Internal Audits. Of the 17 Internal Audits, the recommendations from 16 reports have been fully implemented, and 60% of the recommendations have been fully implemented on the other.
- ◆ Processes, policies and management oversight are now in place to prevent violations of statutes, policies and sound business practices, to promote decision-making with appropriate data, and to continue to develop and comply with practices which are effective and efficient in delivering GSC's services to its customers.
- ◆ The Follow-up Audit acknowledges GSC's progress in areas of significant concern in the 1997 audit , such as:
  - ✓ Enhanced communication with staff through all staff seminars and other initiatives
  - ✓ Development of a rate-setting methodology for cost-recovery functions
  - ✓ Development of a buy-versus-build-versus-lease methodology
  - ✓ Development and compliance with policies for the procurement of raw land
  - ✓ Development and compliance with policies for merit awards and reclassifications
  - ✓ Compliance with state space requirements.
- ◆ Because the major areas of concern in the 1997 audit have been addressed, the 1999 follow up audit is focused on other matters, for which GSC can demonstrate substantial progress or a fundamental difference in business philosophy from that of the SAO.
- ◆ GSC Commissioners and Executive Management remain vigilant in the continuing improvement of the agency, through development and compliance with statutes, policies and procedures, appropriate training of its personnel, and commitment to quality customer service.



## Section 1: Management Resonse to Section 1 of Follow-up Audit Report

### Progress on the 1997 Audit Recommendations

- ◆ The General Services Commission (GSC) has made significant progress across the broad range of recommendations contained in the 1997 Audit Report. As of December 31, 1998, GSC had fully implemented six of 11 recommendations. All others are partially implemented for a variety of reasons, but all are well underway to being addressed.
- ◆ Specifically, the 1997 Audit was structured around six findings. From those six findings, the SAO made 11 recommendations for GSC action. The findings, recommendations and current status are set forth below:

**FINDING NO. 1:** Failure to correct long standing problems indicates ineffective oversight and a lack of accountability.

**Recommendation No. 1:** Develop a clear chain of agency wide accountability for improvements.

**STATUS: FULLY IMPLEMENTED:** By 10/16/97, an agency wide accountability policy was developed, approved and in place.

- ✓ The policy requires each employee's job description and list of job responsibilities to be on file, with the exception of vacancies and recently reorganized divisions. All appropriate documentation has been modified for each employee.
- ✓ The Agency's Operating Policies and Procedures have been reviewed and promulgated as of 9/1/98. The Policies and Procedures are closely related to the Accountability Policy and assist in ensuring compliance with applicable law, rules and regulations in fulfillment of the agency's responsibilities.

**Recommendation No. 2:** Assign responsibility for implementing changes.

**STATUS: PARTIALLY IMPLEMENTED:** By 12/31/98, this task was partially complete only, in part, because change and improvement are inherently continuous processes. The aspects of this recommendation that are in existence include:

- ✓ the standardized job description form
- ✓ up to date performance evaluations.

These steps are the building blocks for accurately assigning and monitoring accountability within the agency.

**Recommendation No. 3:** Hold responsible individuals accountable.

**STATUS: FULLY IMPLEMENTED:** As of 12/31/98, each employee had a tailor-made job description and list of job responsibilities that had been negotiated and agreed to.

- ✓ The new Accountability Policy mandates appropriate action be taken when employees do not perform their assigned duties or violate policies or procedures. The policy mandates Managers to take disciplinary action for any violation of statute, rule, policy, or procedure.

**FINDING NO. 2:** Operations routinely violate statute, policy and sound business practice.

**Recommendation No. 4:** Emphasize to all employees the importance of adhering to statutory requirements and policies.

**STATUS: FULLY IMPLEMENTED:** The Accountability Policy and the quarterly "All Staff Seminar" meetings are but a few of the devices used to continually emphasize adherence to statutory requirements and policies and procedures to GSC employees and the vendors with whom GSC does business.

**Recommendation No. 5:** Establish monitoring and enforcement procedures that would detect or prevent noncompliance.

**STATUS: FULLY IMPLEMENTED:** Each division has identified critical compliance items for their respective areas of responsibility. Monitoring systems to ensure compliance for critical items have been developed.

- ✓ The Accountability Policy mandates actions in the event of noncompliance.
- ✓ Bi-weekly activity reports are generated at the division level to executive management.
- ✓ Ad-hoc reporting of important situations to executive management ensures timely analysis, decision-making and resolution.

**Recommendation No. 6:** Address specific issues related to procurement of goods and services.

**STATUS: FULLY IMPLEMENTED:** As of 6/30/98

**Recommendation No. 7:** Address specific issues related to purchases of raw land, evaluation of rates and fees, disposal of surplus property, and merit raises.

**STATUS: PARTIALLY IMPLEMENTED:** Target date for full implementation is May 31, 1999.

- ✓ Purchase of raw land: Policy was implemented 11/1/97. The policy has been adhered to and is the basis for several successful land acquisitions since implementation.
- ✓ Evaluation of Rates and Fees: GSC developed and implemented a policy related to calculation and evaluation of rates and fee on 9/1/97. See Section 2 of this Management Response for more details about the application of this policy since its implementation.
- ✓ Disposal of Surplus Property: GSC surveyed the other 49 states to determine best disposal methods and is recommending a change in statute to authorize the use of a “Central Store” concept for the disposal of state surplus property. The 76<sup>th</sup> Legislature will determine the merits of this proposal.
- ✓ Merit Raises: GSC operating procedure number HRD – 46.8 details management’s responsibility in this area and employee eligibility criteria.

**FINDING NO. 3:** Management has not established a consistent methodology for some procurement and pricing decisions.

**Recommendation No. 8:** Enhance expertise in crucial methodologies (like rate setting and cost benefit analysis) by acquiring expertise in house or contracting out for services.

**STATUS: FULLY IMPLEMENTED:** By 6/1/98, GSC had developed a valid buy v. build v. lease methodology, which received the favorable peer review from the City of Austin’s Real Estate Services Division. This methodology has been used to provide information regarding the proposed redevelopment of the Robert Mueller Municipal Airport to the Legislature Budget Board and the Governor’s Budget Office. Response to the rate setting concern may be found under Status of Recommendation No. 7, above.

**FINDING NO. 4:** Information Systems do not provide adequate and timely information needed to monitor agency performance.

**STATUS: PARTIALLY IMPLEMENTED:** GSC contracted with Spectrum Consulting to conduct a Comprehensive Needs Analysis. The report has been analyzed and an exceptional item in GSC’s LAR has been developed to seek funding for \$4.9 million for FY 99-00, as a first step in addressing the technology needs of the agency.

**Recommendation No. 9:** Perform a comprehensive needs analysis to identify what information is currently available and the level of redundancies that exist in the current information system.

**STATUS: FULLY IMPLEMENTED:** Study complete. The final report from Spectrum Consulting Group, Inc. was delivered 9/4/98. Seven areas were

identified. Applicable recommendations have been developed into portions of GSC's Information Resources Strategic Plan, Biennial Operation Plan and Legislative Appropriations Request.

**FINDING NO. 5:** Recent efforts to improve project management of construction with Architect/Engineer services should be enhanced.

**Recommendation No. 10:** Ensure all prior Internal Audit recommendations are implemented.

**STATUS:** PARTIALLY IMPLEMENTED: The GSC Office of Internal Audit completed follow up audits on programs previously audited back to 1995. As of 12/31/98, all divisions but one have fully implemented all prior recommendations contained in 17 Internal Audits. Of a total of 60 recommendations made by the Internal Auditor, 56 have been fully implemented.

**FINDING 6:** Lack of vendor performance guidelines has allowed the agency to continue doing business with poorly performing vendors.

**Recommendation No. 11:** Develop/Implement an automated system on vendor's past performance for GSC external agencies.

**STATUS:** PARTIALLY IMPLEMENTED: Target date for fully implementation is 12/31/99.

- ✓ GSC has an automated system to track vendor performance, which requires extensive modification to include relevant vendor performance details for assessment.
- ✓ Revisions will be made to ensure objectivity, relevance and uniformity.
- ✓ State agencies and cooperative purchasing members are currently responsible for the determination to award a contract based on prior performance information. It is essential state agencies remain active in sharing information about vendor performance.
- ✓ Training on the revised automated system will take time to reach all users of the system.

- ◆ The General Services Commission Commissioners and Executive Management, since receipt of the 1997 audit, have aggressively lead the employees of the agency to address all problem areas.
- ◆ The GSC Commissioners and Management understand that some topics addressed in the 1997 audit have appeared in audit reports prior to the current Executive Director's administration. The Commissioners and the current Executive Director are responsible for addressing the issues brought to their attention and they have made progress on many. Of the 22 prior audits cited by the SAO (page 1, Follow-up Audit), 17 are GSC Internal Audits. All recommendations from 16 of the 17 Internal Audits have been fully implemented.

- ◆ Some of the issues cited by the 1997 Audit, issued after the conclusion of the last legislative session, may only be addressed with further legislative action, such as:
  - ✓ Amendments to the State Surplus Property statute to effect a more efficient disposal system
  - ✓ Appropriations to support the automation initiative recommended in the needs analysis
  - ✓ Alterations to the delegated purchasing authority for state agencies to provide GSC term contract analysis, as suggested in the Follow –up Audit

### **The Follow-up Audit**

The Follow-up Audit presents three areas where "problems" remain: cost recovery program rate setting methodology; construction project management issues and use of term contracts and the status of the vendor debarment program authorized in the 75th legislature.

- ◆ The Follow-up Audit report faults the new Accountability Policy because a monitoring mechanism is not in place.
  - ✓ GSC agrees that:
    - ✓ An enhanced monitoring mechanism to measure the progress toward GSC goals is the necessary next step and will begin a process to implement this suggestion.
    - ✓ GSC targets full implementation of a formal monitoring process for June 1, 1999.
- ◆ The Follow-up Audit report states that GSC management believes that a \$10.6 million enhanced information system "will solve the majority of its operational problems."
  - ✓ GSC respectfully disagrees and offers the following points:
    - ✓ GSC management does not hold such a belief. The Commission has adopted the recommendation from the needs analysis to improve and integrate agency work processes prior to applying technology solutions. GSC management believes that an enhanced information system is an important component, or tool, to be added to other initiatives to address identified operational deficiencies.
    - ✓ GSC has requested \$4.9 million for hardware and software for FY 00-01.
    - ✓ GSC management disagrees that it has not developed a contingency plan should funding not occur. Depending on the level of funding provided, mission critical deployment of the new system will occur.
- ◆ The Follow-up Audit faults GSC management for not "fully implementing" the rate-setting methodology created in response to the 1997 audit.
  - ✓ GSC respectfully disagrees. GSC Management has lead the agency to accomplish the following since August 1997:

- ✓ GSC has expended significant agency resources to respond to the cost recovery recommendations contained in the 1997 audit.
  - ✓ At the specific direction of the GSC Executive Staff, staff attended SAO sponsored cost recovery training.
  - ✓ Staff established agency-wide policies for consistently calculating cost recovery rates.
  - ✓ Agency-wide policies require an annual review of all cost recovery rates, both full-cost and non-full cost recovery programs.
  - ✓ GSC continues its established policy of preparing modified accrual financial statements for all full cost recovery programs quarterly, thus facilitating the quarterly rate review for the larger programs.
  - ✓ Staff collected cost recovery rate documentation for over thirty (30) programs during 1998.
  - ✓ Staff conducted a review of all agency-wide rates as set forth in the agency wide policy. Reported the rate review results to the Executive Staff.
  - ✓ Staff went beyond the initial SAO recommendations requesting GSC's Internal Audit Staff review the modified accrual financial statements to ensure the fiscal information was accurate.
  - ✓ Internal Audit made recommendations for improvement. Staff has incorporated the majority of those recommendations.
- ◆ The Follow-up Audit faults GSC management for not implementing a "process to set, monitor, and control construction project deadlines."
  - ✓ GSC respectfully disagrees that it has no effective process in place and addresses this issue in detail in Section 3 hereof.
    - ✓ GSC suggests that effective reporting systems related to construction status do not drive the events that occur on a construction project - reports recite what happens.
    - ✓ Weather and soil conditions, schedules and budgets are all elements that have direct impact on successful construction project outcomes.
    - ✓ Entities other than GSC are in control of the process as it relates to a particular construction project.
    - ✓ GSC has lead responsibility for a project and works closely with the using agency to represent the best interests of the State.
  - ◆ Finally, the Follow-up Audit faults Central Procurement for not "formally and regularly" evaluating opportunities for the creation of term contracts for volume buying.
  - ✓ GSC respectfully disagrees with this conclusion and offers the following for consideration:
    - ✓ GSC procurement staff is trained to conduct these evaluations and do apply appropriate methodologies to purchasing opportunities routinely.
    - ✓ GSC has a written internal policy specifying the factors to be used.
    - ✓ GSC features the "number of new term contracts developed" as a performance measure in the budget process.
    - ✓ GSC will continue to work with SAO to improve this process.

## **Management Response to Section 1 Recommendations**

The General Services Commission embraces the three recommendations the SAO offers on page 7 of Section 1 of the Follow-up Audit.

- ✓ GSC is a service agency and its focus, mission and goal are customer satisfaction. GSC will continue to strive to listen to its customers and to respond to their evolving needs and expectations. Management is committed to maintaining the alignment between its goods and services and the customers' expectations.
  
- ✓ GSC is focused on the assessment of its internal processes to ensure they are designed to operate in support of the customer's needs. Because this is an ongoing effort, management is constantly reviewing priorities among competing needs to realistically improve processes most critical to delivering customer satisfaction. Part of this assessment process is charting and monitoring processes, their outcomes and measuring the importance to customer service that improvements in a program area would achieve.
  
- ✓ GSC is committed to continuously improving its employee's skills. GSC continues to develop evaluation tools, utilizing an agency-wide Evaluation Committee. In addition, the agency-wide Training Committee is tasked to provide relevant and effective career enhancement and specific training opportunities to meet the customers' needs and the agency's goals.

## **Section 2: Management Response to Section 2 of Follow-up Audit Report**

### **Rate Setting Methodology**

- ◆ In the 1997 Audit, the SAO noted several times that GSC should:
  - formalize its rate and fee setting methodology
  - consistently apply the methodology
  - train personnel to use the methodology
  
- ✓ The GSC expended significant agency resources to respond to the cost recovery recommendations. At the specific direction of the GSC Commissioners and Executive Staff, staff established and completed the following objectives to meet the recommendations:
  - ✓ Staff attended SAO sponsored cost recovery training.
  - ✓ GSC established agency-wide policies for consistently calculating cost recovery rates.
  - ✓ GSC established agency-wide policies for an annual review of all cost recovery rates, both full-cost and non-full cost recovery programs.
  - ✓ The GSC continued the established policy of preparing modified accrual financial statements for all full cost-recovery programs quarterly, thus facilitating the quarterly rate review for the larger programs.

- ✓ Staff collected cost recovery rate documentation for over thirty (30) programs.
- ✓ Staff conducted a review of all agency-wide rates as set forth in the agency wide policy.
- ✓ Staff reported the rate review results to Executive Management.
- ✓ Staff went beyond the initial SAO recommendations by requesting GSC's own Internal Audit Staff to review and provide an independent assessment of the modified accrual financial statements to ensure the fiscal information was accurate.
- ✓ Internal Audit made recommendations for improvement. Staff has incorporated the majority of those recommendations.

### **Cost Recovery**

- ◆ The cost recovery area was not identified in the 1997 audit as a "key area". However, in the Follow-up Audit the cost-recovery area was highlighted as a "key area", see SAO's "Overall Conclusion", page 1.
- ◆ While the Follow-up Audit recommendations provide excellent goals, in many cases the recommendations would occur as a direct result from the continued strict adherence to the policies and procedures placed in existence as a result of the 1997 audit.
  - ✓ In short, the cost recovery process must be provided sufficient time to mature.
- ◆ The SAO's new findings can be condensed into the following assertions:
  - The GSC overcharges for goods and services resulting in accumulated surpluses, without a documented plan to upgrade operations, and not subject to legislative oversight.
  - The GSC practices poor rate setting policies and/or does not comply with established rate setting policies.
  - GSC management's emphasis is on maximizing revenue to recover costs instead of controlling and/or evaluating costs.
- ◆ The SAO asserts the GSC overcharges for goods and services. The SAO implies a surplus of \$19.2M exists. Moreover, the SAO asserts of the \$19.2M surplus, \$8.6 million represents an unencumbered balance after allowing for a working capital account. However, the SAO fails to identify the following relevant factors that apply to these balances:
  - ✓ 84% of the balance resides in two programs, the Capitol Complex Telephone System and TEX-AN programs. The implication that material accumulated balances exist in all programs is misleading. Plans are in place to reduce the CCTS and TEX-AN balances:
    - ✓ The CCTS initiated two programmed rate reductions specifically to reduce balances. Both rate reductions were announced in FY95. The reductions amounted to 25% in FY95 and 9.2% in FY99. Neither could have been programmed without sufficient planning.



- ✓ Two reports were issued from the Telecommunications Planning Group highlighting plans for use of the TEX-AN program balances. The reports entitled "Texas Government Strategic Plan for Telecommunications Services" and "Status of the Plan for a State Telecommunications Network", are both dated October 1, 1998, and were distributed to the legislature. The reports identify the strategic level view for use of TEX-AN accumulated balances.
  - ✓ Specifically, one report highlights that GSC will provide up to \$12.5M to support the new TEX-AN network.
- ✓ The SAO characterization of the working capital balance as a cushion implies that the balance is an unnecessary reserve.
  - ✓ Working capital is a necessity to fund on-going full-cost recovery operations; failure to so retain funds would decrease the efficiency of GSC's operations. Federal guidelines provide for sixty (60) days of working capital being retained.
- ✓ With respect to the lack of legislative oversight, the SAO failed to note or highlight:
  - ✓ All non-industry full-cost recovery balances identified as "Unobligated Balances, 'UB', " must be highlighted in every agency's Legislative Appropriation Request. In compliance with LAR instructions, the GSC identified the estimated UB for these funds.
  - ✓ Numerous ad-hoc reports are provided to external entities to assist in the legislative oversight process. For example, the Legislative Budget Board conducted it's own full-cost recovery program review. The program evaluation was highlighted in the Legislative Budget Board's "Summary of Legislative Budget Estimates".
  - ✓ The GSC must obtain capital budget authority approval through the legislative appropriations process to utilize funds for capital procurements, regardless of the source of funds.
  - ✓ The GSC is required by rider to document industry related capital purchases to the LBB, specifically because the purchases are not highlighted in the LAR.
  - ✓ The Governor's Office agent for preparing the Statewide Cost Allocation plan is provided copies of full-cost recovery modified accrual financial statements on an annual basis.
- ◆ The SAO asserts the GSC possesses poor rate setting policies and/or non-compliance with established rate-setting policies.
- ✓ In response, GSC has accomplished the following:
  - ✓ The GSC conducted thirty (30) rate reviews in FY98.
  - ✓ The GSC prepares modified accrual financial statements for all eleven (11) full-cost recovery programs on a quarterly basis. The financial statements provide immediate feedback on rate setting.
- ◆ The SAO states, "the Commission is not monitoring and adjusting its rates

- appropriately when profits are generated by cost recovery operations."
- ✓ One of the major cost recovery programs, the CCTS program, has reduced rates twice in the past five (5) years. The Tex-An program has also reduced rates several times in the past three years.
  - ◆ SAO noted "project management function plans to increase its FY 1999 rate to cover a loss....".
  - ✓ SAO failed to note it was a specific staff decision to reduce rates. The decision to reduce rates was predicated on the accumulated balance and the conscious decision to reduce the balance.
  - ◆ The SAO states "the Commission pass (es) along its operational inefficiencies to agencies that pay for its services". (Executive Summary, 1<sup>st</sup> full paragraph, pg. 2) The SAO asserts management's emphasis is on maximizing revenue to recover costs instead of controlling costs.
  - ✓ GSC respectfully disagrees and offers the following items for consideration:
    - ✓ 5 of the 11 full-cost recovery programs operated by the Commission compete directly with private-industry counterparts.
    - ✓ State agencies are not required to procure goods or services from the Central Store, the Business Machine Repair program, the two Print Shops and the Minor Construction program. Direct competition with private industry can and does require programs to manage costs or result in loss of business.
    - ✓ The GSC suggests state agencies intent on maximizing appropriations will not procure more expensive goods and service when provided the option to procure elsewhere.
    - ✓ The GSC has benchmarked TEX-AN rates for the last three biennia against private industry for both inter-state and intra-state rates.
    - ✓ Even though state agencies are required to use the TEX-AN network, GSC provides benchmarking data.
    - ✓ The GSC committed to reducing CCTS rates by 5% for the FY00/01 time period in GSC's strategic plan.
    - ✓ Approximately, 58% of TEX-AN customers represent political subdivisions. Political subdivisions are not required to utilize TEX-AN and are free to use any voice and data network service provider.
    - ✓ If the TEX-AN services were over-priced, the GSC suggests political subdivisions would procure services elsewhere.
  - ◆ Finally, the SAO uses an example of an exceptional item request submitted by the GSC involving CMBL fees. (See Section 2, 2<sup>nd</sup> bullet, pg. 10)
  - ✓ GSC notes the following regarding the CMBL exceptional item:
    - ✓ During the audit, GSC staff made clear the CMBL exceptional item was identified as a potential shortfall late in the LAR process.
    - ✓ A management decision was made to submit the request with the full knowledge that additional research was required to fully document the need.

- ✓ The exceptional item was submitted only to highlight a potential requirement. After additional research was completed, the GSC has withdrawn its request.
- ✓ The SAO utilized this example of "not controlling costs" with full knowledge of the circumstances involved.

### **Management Response to Section 2 Recommendations**

- ◆ From the aforementioned assertions, the SAO recommends that:

Recommendation No. 1: GSC comply with the policy's requirement to benchmark the rates it charges with similar services in the private sector.

- ✓ **Management concurs with the recommendation.** The SAO correctly indicates that GSC possesses a policy to monitor benchmarking. The SAO fails to identify:
  - ✓ The TEX-AN program benchmarks rates and reports results through the Automated Budgeting and Evaluation System of Texas (ABEST) performance measure reporting process.
  - ✓ The Central Store program, the Business Machine Repair program, the Print Shop and the Minor Construction program also benchmark rates.
  - ✓ As the process of evaluating rates matures, the GSC will focus on better documenting the on-going benchmarking process.

Recommendation No. 2: To ensure proper accounting and control of profits and losses generated from cost recovery functions, management should routinely evaluate the reasons for the profits and losses, including analysis of both revenue and expenditure trends. Based on the results of the analysis, either the rates or expenses should be adjusted accordingly.

- ✓ **Management concurs to continue the following:**
  - ✓ Prepare quarterly modified accrual financial statements which greatly facilitate this process.
  - ✓ Evaluate all cost recovery rates on an annual basis, at a minimum.
  - ✓ To adjust rates accordingly.

Recommendation No. 3: Funds accumulated for the purposes of upgrading the TEX-AN and CCTS systems should be transferred to the Statewide Network Applications account in accordance with statutory requirements.

- ✓ **Management concurs with the recommendation.**
  - ✓ When balances maintained in the revolving fund account are sufficient to pay the bills of the consolidated telecommunications system and the CCTS, the Commission shall certify those amounts to the comptroller.

Recommendation No. 4: Accumulations of funds may occasionally be necessary to upgrade or replace equipment. However, accumulations should be planned, including projection of needed changes to the rates and formally approved by the appropriate authorities.

✓ **Management concurs with the recommendation.**

- ✓ To complete this task the GSC will strengthen the existing agency policy to add a requirement for full-cost recovery operations that document uses of material cash balances exceeding those funds required to cash flow on-going operations.
- ✓ The target implementation date for this strategy is June 1, 1999.

- ◆ The SAO concludes Section Two of the follow-up audit by recommending "to ensure that the Commission has the necessary expertise to complete these tasks, management should hire a cost accountant with experience in services similar to those provided by the Commission. This position (or positions) should be solely devoted to the cost recovery function."

✓ **Management does not concur with this proposal:**

- ✓ The function could not be justified as a full-time position.
- ✓ The GSC operates 30 unique cost-recovery functions, to obtain a cost accountant(s) with the experience necessary in the varied functions would be very expensive.
- ✓ The GSC may procure outside services as necessary to assist staff with evaluations.
- ✓ Additionally, GSC's Internal Audit Staff may continue to assist with the requirement.
- ✓ As owner of the largest cost recovery programs, TEX-AN and CCTS, the Telecommunications Service Division already possesses in-house staff that conduct the tasks noted.

### **Section 3: Management Response to Section 3 of Follow-up Audit Report**

#### **Construction Project Management System**

- ◆ The Follow-up Audit asserts that the Facilities Construction and Space Management (FCSM) Program has no effective project management processes to manage the construction activities for which it is responsible.
- ✓ GSC respectfully disagrees and offers the following observations:
  - ✓ FCSM has construction management processes in place to plan and monitor construction projects. Budgets and schedules for GSC's projects are often established by others.
  - ✓ GSC, along with other agencies that are responsible for construction, knows that the weather, design professional, contractor, quality and using agency needs directly influence the outcome of a project. GSC respectfully disagrees that a particular type or level of construction management process is the sole direct influence on the on-budget and on-time performance of a construction project.
  - ✓ The construction management tools currently used to plan and monitor projects include:

- The project budget and schedule
  - Contracts binding the various parties to achievement of the project, including the Architectural/Engineering Agreement and the Construction Contract.
  - Many specific-purpose reports developed for monitoring and communicating project status, such as the monthly status reports to the Commission and by-weekly status reports used by Executive Management.
- ✓ FCSM acknowledges that its paper driven process and its multiple reports are not the most user friendly or efficient. GSC is pursuing the implementation of an electronic project management system, that will automate this data and generate improved reports to meet Owner and/or Client needs.
- ✓ FCSM also acknowledges that the different levels of detail available from the various reports at times may lead to confusion. The status reports are one mechanism for communications between FCSM and the Commissioners. In an ongoing effort to improve reporting, FCSM has designed and is implementing a new project report. This report will provide a high level, snap shot of each project schedule and budget. The report is being used for all new projects, as they begin. All projects in progress will be phased into the new report format by June 1, 1999.

### **Procedures & Policies**

- ◆ In accordance with recommendations of the 1997 audit, GSC continues to draft a comprehensive set of policies and procedures for the FCSM's project management, designed to comply with law, policy and best business practices.
- ✓ The appropriate policies are designed to prevent the problems experienced in the past. Should problems occur again, the Commission's Accountability Policy provides a basis for immediate disciplinary correction.
- ✓ The complete set of policies will be finalized by June, 1999.

### **Customer Service**

- ◆ At the suggestion of the 1997 audit report, FCSM created a "Customer Service Card" program which seeks written comments from contracted professionals, including Architect/Engineers and general contractors, and using agencies about their assessment of FCSM's team member performance.
- ✓ The Program commenced in December 1997. For 1998, the Project Management Program achieved an 84.4% satisfaction rating.
- ✓ FCSM acknowledges that it received five (5) less-than-satisfactory responses, for which follow up intervention by management of FCSM were required. FCSM continues to attempt to improve the level of satisfaction with each and every customer, in accordance with each customer's needs and desires.

### **Management Response to Section 3 Recommendations**

- ◆ The SAO recommends the following in Section 3 of the Follow-up Audit:

Recommendation No.1: Identify critical information needed to ensure projects are completed on time, to specifications, and within budget.

- ✓ **GSC concurs with this recommendation.** FCSM continues to work on the identification of critical information needed to ensure projects are completed on time, to specifications, and within budget; or, at least, that deviations from these goals are clearly documented. Management is confident that its new project reporting mechanism will provide greatly improved monitoring and oversight for all projects.

Recommendation No. 2: Implement a system to track and use the data to ensure that the process is meeting the expectations of agency management, the Commissioners and the customers.

- ✓ **GSC concurs with this recommendation.** The current paper driven process is subject to continuous improvement and streamlining to ensure accurate, accessible data of importance to GSC and its customers.
- ✓ GSC is seeking funding in the 76<sup>th</sup> Legislature Session for an advanced computer hardware and software solution, which includes a construction project management component.

Recommendation No. 3: Finalize project management policies to provide project managers with a foundation to manage the project. Provide training and tools to assist in implementing the finalized procedures.

- ✓ **GSC concurs with this recommendation.** Additionally, FCSM is committed to finalizing the project management policies by June 1, 1999. Training and the tools necessary to successfully implement the policies and procedures will be provided to project management staff.
- ◆ The SAO concludes Section 3 of the Follow-up Audit with the suggestion that GSC FCSM rely on the Construction Industry Institute (CII) as a resource on construction design and project management issues.
- ✓ **Management concurs with this suggestion.** GSC understands the need to benchmark practices and provide accurate training for its personnel – it does so through networking with the University of Texas System Office of Facilities Planning and Construction (OFPC) and CII.
  - ✓ The University of Texas System OFPC is much more similar to GSC's Construction Program than CII's. However, CII is a good resource for training and publications. GSC has personnel that have attended

many of the CII offerings. To the extent GSC can use the CII resources and materials, GSC will.

#### **Section 4: Management Response to Section 4 of the Follow-up Audit Report**

##### **Central Procurement Services Volume Buying Practices**

- ◆ The SAO concluded that “the agency may have missed opportunities to save the state money because it does not formally and regularly evaluate procurement trends to ensure the state maximizes its use of volume buying to obtain lower prices.”
- ✓ GSC respectfully disagrees and would offer the following points for consideration:
  - ✓ GSC's Central Procurement Services Division (CPSD) routinely assess money-saving opportunities in its purchasing program, thereby saving the state money through volume buying.
  - ✓ CPSD has an internal policy that lists specific criteria and guidelines for purchasers to consider when making an assessment on whether or not a new term contract should be developed.
  - ✓ One of GSC's assigned legislative performance measures is “number of new term contracts developed”. The agency reports and updates, on a biennial basis, the progress it is making in the creation of new term contracts which are designed to maximize the use of volume buying.
  - ✓ In fiscal year 1997, CPSD developed a total of 18 new term contracts. This was a new performance measure developed on GSC's initiative.
  - ✓ In fiscal year 1998, CPSD developed a total of 16 new term contracts.
  - ✓ CPSD adds repetitively purchased items to existing contracts in order to be more efficient.
  - ✓ Cost benefit analyses are utilized to evaluate the time, cost, and efforts needed to develop a new term contract in comparison with the limited staff resources and potential usage of the contract.
  - ✓ GSC is also responsible for administering the Historically Underutilized Business (HUB) Program, which program goals need to be balanced with the efficiency goals of maximizing the state's buying power.
- ◆ The Follow-up Audit notes that delegated purchases should be examined for term contract potential.
- ✓ GSC will explore this suggestion but would highlight some limitations with the current system:
  - ✓ Delegated purchasing authority is granted to client agencies by the legislature.
  - ✓ Client agencies with delegated authority do not have mechanisms in place to track purchases in a way that it lends itself to analysis by GSC.
  - ✓ The purchasing function within many state agencies is further decentralized making it difficult to analyze purchasing trends.

- ✓ Legislation may be required to clearly authorize GSC's oversight of delegated purchasing authority in this manner, in light of the initiatives contained in SB 1752.
- ◆ GSC does not dispute the SAO's conclusion that the term contract analysis process used by its staff could be done in a more formalized manner.
  - ✓ The CPSD has before requested and would welcome assistance from the SAO to develop and promulgate a policy which satisfies the concern.

### **Vendor Debarment Program**

- ◆ The Follow-up Audit asserts that the GSC has failed to comply with legislation to limit business with poorly performing vendors.
- ✓ GSC respectfully disagrees and would offer the following for consideration:
  - ✓ The Commission's philosophy on vendor management is that GSC would like to help vendors succeed in their business with the state. GSC considers its suppliers to be trading partners, who, when they enter into a contract with the state, should reasonably expect to be engaged in a win-win situation, where both their business goals as well as the state's goals are met.
  - ✓ The Commission's philosophy on sanctions is that debarment is the equivalent of the death penalty and should only be used in the clearest cases of non-performance or flawed performance, established by appropriate evidence.
  - ✓ To these ends, GSC has constructed a program that both recognizes outstanding performing vendors, as well as sanctioning poorly performing vendors.
  - ✓ GSC takes action against non-performing vendors on an escalating level of vendor performance review, from vendor counseling, when it is evident to GSC that a supplier is getting sloppy, or otherwise not meeting the stated needs of a contract, to surveillance, to suspension and, finally, to debarment. Since November 1998, 12 vendors have been suspended from the CMBL and from awards; three have subsequently been reinstated.
  - ✓ The debarment process carries with it an absolute requirement for appropriate due process, meaning that it must be based in fact and be administered fairly and evenhandedly.
  - ✓ The design of GSC's vendor debarment program includes:
    - ✓ Fair administration of any vendor debarments.
    - ✓ Recognition of excellent vendors.
    - ✓ Struggling vendors are counseled and rehabilitated.
  - ✓ The vendor management program, which is the tool for gathering the necessary data related to vendor performance, has to be well planned, and training has to be offered to state agencies to support the system. The target date for full implementation of the automated system is December, 1999.



## **Management Response to Section 4 Recommendations**

- ◆ The SAO recommends the following in Section 4 of the Follow-up Audit:

Recommendation No. 1: The SAO recommends GSC take a formal, proactive approach to ensure the State maximizes the benefit of volume buying by:

- Developing specific criteria to use in evaluating procurement trends. The criteria should include basic factors such as benchmarks to measure when increases in volume indicate development of a term contract would be beneficial and calculation of the average cost savings obtained using term contracts.
  - Identifying the information needed to perform the evaluation and develop a system to track information needed to perform the evaluations. Information on delegated purchases made by external agencies should also be included in the evaluations.
  - Formally evaluating the procurement data on a regular bases (quarterly, semi-annually) and document the evaluations using a consistent approach.
- ✓ **GSC concurs with the recommendation.** The professional purchasers on staff will continue to apply Procurement Policy Section 21.3 appropriately in order to maximize the state's buying power. GSC welcomes the SAO's suggestions about how to translate these recommendations into policies and procedures that will produce intended results.

Recommendation No. 2: SAO recommends GSC fully implement the vendor debarment program required by SB1752. "In order to successfully implement the vendor debarment program, the Commission must develop and implement a system to track and report complete and accurate data on vendor's past performance from both the General Services Commission and external agencies." (Section 4, 2<sup>nd</sup> bullet, pg. 6)

- ✓ **GSC concurs with this recommendation.** GSC has promulgated a vendor tracking system, but it requires changes.
- ✓ GSC must train state agencies in the proper use of this vendor management tool.
  - ✓ The automated tracking system will be modified to align it with the SB 1752 program and is targeted to be in place by December 1999.

## **Section 5: Management Response to Section 5 of the Follow-up Audit Report**

### **State Energy Conservation Office**

- ◆ The SAO notes that the State Energy Conservation Office of GSC was working on potential improvements for the self sufficiency of the LoanSTAR revolving loan program during the November 1998 field work for the Follow-up Audit.

### **Management Response to Section 5 Recommendation**

Recommendation No. 1: SAO recommended GSC continue its efforts to improve fiscal management of the LoanSTAR revolving loan program to ensure it meets its statutory requirements.

- ✓ **GSC concurs with this recommendation.** GSC has accomplished the following:
  - ✓ To achieve administrative self sufficiency for the LoanSTAR Program and to stimulate the program's revolving loan mechanism, the General Services Commission State Energy Conservation Office (GSC/SECO) implemented the following program policy, effective January 1, 1999:
    - Loan interest rates were established which will maintain the revolving fund with a balance in excess of \$95 million, which is sufficient to ensure a solvent program

### **SUMMARY OF GENERAL SERVICES COMMISSION MANAGEMENT RESPONSES TO THE FOLLOW UP AUDIT**

- ◆ The General Services Commission has proven its commitment to resolving long outstanding management problems within the agency. The agency remains committed to fulfilling all recommendations contained in the 1997 Audit and the new ones mentioned in the Follow-up Audit and concurred with in this Management Response.
- ◆ The General Services Commission welcomes the input and assistance of the State Auditor's Office to design policies and processes that will meet the intent of the 1997 and Follow-up Audit recommendations, while supporting the agency's business philosophy.

## Objective, Scope, and Methodology

### Objective

The primary objective of this follow-up audit was to determine whether the Commission had made improvements in critical functions since the issuance of *An Audit Report on Management Controls at the General Services Commission* (SAO Report No. 97-080, August 1997). Our overall, crosscutting objective was to determine if the Commission had improved accountability and oversight of agency operations by:

- Taking sufficient and timely action to address weaknesses cited in previous internal and external reports
- Implementing corrective actions that address the root causes of agencywide problems
- Developing a clear chain of accountability to ensure that appropriate improvements are made to operations
- Establishing monitoring and enforcement procedures to ensure all potential instances of noncompliance are prevented or detected
- Improving intra-agency coordination and communication

### Scope

The scope of this audit was primarily limited to following up on the actions taken to address the issues from *An Audit Report on Management Controls at the General Services Commission* (SAO Report No. 97-080, August 1997). It included assessing the Commission's progress in correcting previously identified weaknesses in the following areas:

- Accountability and oversight of agency operations
- Procurement and management of construction projects
- Development and implementation of methodology for buy-versus-lease decisions
- Compliance with state statutes governing square footage requirements
- Evaluation of procurement trends to maximize advantages of volume buying
- Tracking and use of vendor past performance information in the procurement process

- Compliance with state statutes and agency procedures governing merit raises and reclassifications
- Development of an agencywide career ladder program
- Development of information systems that provide adequate (accurate, user-appropriate, sufficient) and timely information needed to monitor agency performance
- Implementation and evaluation of consistent and accurate rate-setting methodologies for full cost recovery programs
- Compliance with statutory requirements of the Loan STAR Revolving Loan Program

## Methodology

The methodology used on this audit consisted of collecting information performing audit tests and procedures, and analyzing and evaluating the information against established criteria.

Key information collected to accomplish our objectives included the following:

- Interviews with Commission management and staff
- Documentary evidence including review of:
  - All documentation related to the Commission's *Team Excellence 2000* initiative and other information related to the status of Commission initiatives to improve operations
  - Agency policies and procedures (revised and draft versions)
  - Internal Audit reports issued subsequent to August 1997
  - Commission meeting minutes
  - Personnel files, job descriptions, and performance evaluations
  - Results of needs assessment including results of employee focus groups and report issued by Spectrum Consulting in September 1998
  - Review of position papers related to self-sufficiency of LoanSTAR Revolving Loan Program

Procedures and tests conducted:

- Review of processes used to develop, document, communicate, review, and enforce policies and procedures
- Compliance testing of personnel files
- Review and tests of processes used to establish rates and fees for cost recovery services, including review and verification of rate-setting information maintained by both the program areas and the fiscal division

- Compliance testing of processes used to procure architect/engineer and construction services
- Compliance testing of processes used to manage construction projects
- Compliance testing of square footage calculations for Commission office space
- Review of processes used to plan for construction projects
- Review of methodology used to analyze project costs associated with buy-build-lease decisions.
- Review of processes used to track and monitor vendor performance, including consideration of past performance in the vendor selection process
- Review of processes used to evaluate procurement trends
- Review of processes used to procure raw land
- Attendance at Commission “all-staff meetings”

Analysis techniques used:

- Control reviews
- Process reviews
- Data comparison
- Selection and testing of random samples

Criteria used:

- Texas Government Code
- Texas Administrative Code
- General Services Commission’s policies and procedures
- Fund accounting principles from *Fund Accounting: Theory and Practice*
- Project management principles from *Project Planning and Control for Construction*
- The State Auditor’s Office Accountability Project Methodology (general and specific)

**Other Information**

Fieldwork was conducted between July and November 1998. The audit was performed in accordance with applicable professional standards, including:

- Generally Accepted Government Auditing Standards
- Generally Accepted Auditing Standards

The audit work was performed by the following members of the State Auditor's staff:

- Cynthia L. Reed, CPA (Project Manager)
- Hugh T. Ohn, CPA
- Barbette Mays
- Thomas J. Byrnes, MBA
- Susan Van Hoozer, MBA
- Kimberly Heaver
- Anthony Patrick, MBA
- Fred Bednarski III
- Dennis O'Neal, CIA, CGFM (Quality Control Reviewer)
- Frank N. Vito, CPA (Audit Manager)
- Deborah L. Kerr, Ph.D. (Audit Director)

## Summary of Previous Audit Findings

Table 2 summarizes previous audit findings in the Commission's key operations of cost recovery, construction management, and procurement. This summary provides a context for the repetitive nature of the weaknesses identified in this report.

Table 2

Date	Report Name and Reporting Organization	Key Audit Findings
<b>Cost Recovery Issues</b>		
March 1992	<i>Review of Management Controls at the General Services Commission</i> SAO Report No. 92-079	The culture does not promote a skilled work force which is able to react quickly and decisively to customer service issues because of insufficient training, limited communications, and limited delegation of decision making authority.
October 1992	<i>General Services Commission Performance Review</i> Comptroller of Public Accounts	Of immediate concern to TPR is the balance in the Telecommunications revolving account. While this account was created to address the delay in billing and receipt of funds, it has accumulated a balance of almost \$6 million in excess of that needed to pay the phone bills.  GSC's billing procedures for the state's Capitol Complex Telephone Service and long-distance services (TEX-AN) are complicated and result in a 60-to-90 day delay from the time GSC is billed by the telephone companies until the time GSC is reimbursed by state agencies and pays the phone companies.
December 1994	<i>Review of the Building Maintenance Division</i> GSC Internal Audit Report No. 95-1	The Division continues to operate in a crisis management mode due to inadequate planning of scheduled maintenance.
July 1995	<i>Management Control Audit of the Telecommunications Program</i> GSC Internal Audit Report No. 95-3	The cost analysis of the Capitol Complex Telephone System (CCTS) performed by the division in 1994 showed that the program billed more than its cost of operations.  TPR recommended that five million dollars from the TEX-AN and CCTS revolving accounts be transferred to the General Revenue Fund. The transfer was completed in March 1995.
January 1996	<i>Program Control Assessment-Support Services Program</i> GSC Internal Audit Report No. 96-1	Weaknesses in print shop billing process results in over and under billings.

Table 2, continued

Date	Report Name and Reporting Organization	Key Audit Findings
July 1996	<p><i>Environmental Programs Section – Program Control Assessment</i></p> <p>GSC Internal Audit Report No. 96-5</p>	<p>Discrepancies in billing processes occurred because the billing system lacks checks and balances to ensure its accuracy.</p> <p>The Section does not have a system to monitor customer service satisfaction with projects.</p> <p>The Section should develop operational plans to improve efficiency.</p>
March 1997	<p><i>Inspections Section Program Control Assessment</i></p> <p>GSC Internal Audit Report No. 97-2</p>	<p>The billing system for the Division cannot efficiently provide information on the source of unbilled services totaling \$127,399. There is no policy for reviewing or writing off unbillable services.</p>
April 1997	<p><i>Program Control Assessment of the Facilities Planning and Space Management Program</i></p> <p>GSC Internal Audit Report No. 97-1</p>	<p>The program should reduce its operating costs to ensure expenses do not exceed revenues.</p> <p>Program management should evaluate services offered to determine if the services could be provided in a more cost-effective manner.</p> <p>Program management should identify and communicate services offered and the cost of providing those services.</p> <p>Print shop personnel are not being held accountable for justifying cost overruns.</p>
July 1997	<p><i>Program Control Assessment of the Minor Construction Program</i></p> <p>GSC Internal Audit Report No. 97-7</p>	<p>The Program has not fully recovered all costs for the past two years. Since the Program became a full cost recovery operation, the rates have not changed, nor have they been periodically monitored or evaluated.</p>
August 1997	<p><i>An Audit Report on Management Controls at the General Services Commission</i></p> <p>SAO Report No. 97-080</p>	<p>The lack of consistent and validated fee-setting methodologies results in each division interpreting costs and setting rates without considering the efficiency of its operations.</p> <p>GSC should be more aggressive and proactive in improving the economy and efficiency of the services it provides.</p>
January 1998	<p><i>Follow-Up Audit on the Program Control Assessment of the Inspections Program</i></p> <p>GSC Internal Audit No. 98-3</p>	<p>The Division has not developed a policy regarding the aging and removal of unbilled services. Since the original audit, the dollar value and number of unbilled services have increased.</p>



Table 2, continued

Date	Report Name and Reporting Organization	Key Audit Findings
April 1998	<p><i>Follow-Up Audit On The Program Control Assessment of the Facilities Planning Sections</i></p> <p>GSC Internal Audit No. 98-5</p>	<p>The process used to establish rates for planning services is not documented and the approval process for providing those services has not been established.</p> <p>Controls over the billing process should be strengthened.</p> <p>Section management has not evaluated, prioritized, or budgeted the essential cost recovery projects/functions of the Section and the associated costs to be recovered. A list of the projects in progress, anticipated projects, budgeted costs, and related expenditures to date has not been developed.</p>
May 1998	<p><i>Follow-Up Audit on the Program Control Assessment of the Environmental Hazards Section</i></p> <p>GSC Internal Audit No. 98-10</p>	<p>The current billing system has few controls. Controls over data entry have not been developed. The Section does not reconcile the information in the project files to the information entered into the system.</p>
<b>Construction Management Issues</b>		
March 1992	<p><i>Review of the Management Controls at the General Services Commission</i></p> <p>SAO Report No. 92-079</p>	<p>Statewide policies and standards are needed in managing building space. The approach to space management is fragmented. The lack of a consistent standard in allocating space places the State at risk of being inefficient in the management and allocation of office and other building space.</p>
October 1992	<p><i>General Services Commission Performance Review</i></p> <p>Comptroller of Public Accounts</p>	<p>GSC should consider using construction managers from other state agencies and institutions to perform construction project management and inspection on GSC projects.</p> <p>GSC has failed to take an active role in developing standards for buildings and the construction process.</p> <p>GSC should develop and implement a plan for the use of independent expert advisors during the programming and design phases of their projects to ensure cost-efficient construction.</p>
February 1995	<p><i>Management Control Audit of the Design, Construction and Leasing Division</i></p> <p>GSC Internal Audit Report No. 95-2</p>	<p>The Construction Division has been functioning without written policies and procedures. The Division should develop written policies and procedures for project scheduling, monitoring, accounting and reporting to executive management. The need has been reported to Division and Agency Management in previous audit reports dated from 1983-1992.</p>

Table 2, continued

Date	Report Name and Reporting Organization	Key Audit Findings
April 1996	<p><i>Special Audit of Design and Construction Division</i></p> <p>GSC Internal Audit Report No. 96-3</p>	<p>The Division continues to operate in a crisis management mode because former Division management failed to implement fundamental controls needed to manage operations efficiently and effectively.</p> <p>This review identified ongoing concerns for needed improvements, many of which have been previously identified. Failure to address these concerns indicates a material weakness in management controls at GSC.</p> <p>A project tracking system has not been developed. As a result, the risk of experiencing delays is unacceptably high. (Repeat finding from 1995 Internal Audit Report)</p> <p>Review noted written complaints regarding project timelines and qualifications of selected design professionals. There is no formal system to document and analyze customer comments regarding services provided by the Design and Construction Division.</p>
March 1997	<p><i>Inspections Section Program Control Assessment</i></p> <p>GSC Internal Audit Report No. 97-2</p>	<p>The section has not consistently performed warranty inspections as required by statute during the last five years. In addition, an internal policy relating to the disposal of warranty documents and a statute regarding notification of final inspections was also not followed.</p> <p>Section management needs to reemphasize to all personnel the importance of complying with statutes and internal policies.</p>
August 1997	<p><i>An Audit Report on Management Controls at the General Services Commission</i></p> <p>SAO Report No. 97-080</p>	<p>Inadequate management of construction and architect/ engineer service contracts has resulted in project delays, price escalations, and strained relations between GSC and the entities it serves.</p> <p>State rules and sound business practices have been frequently bypassed in the procurement of construction services.</p>
January 1998	<p><i>Follow-Up Audit On The Program Control Assessment of the Inspections Program</i></p> <p>GSC Internal Audit No. 98-3</p>	<p>During the past six years, the Program has not consistently performed warranty inspections as required by statute.</p> <p>The automated database used to track project is not being maintained and is currently incomplete and inaccurate.</p>

Table 2, continued

Date	Report Name and Reporting Organization	Key Audit Findings
May 1998	<p><i>Follow-Up Audit on the Program Control Assessment of the Design and Construction Division</i></p> <p>GSC Internal Audit Report No. 98-4</p>	<p>Management has not developed and implemented an automated tracking system to assign and schedule construction projects. However, the program has analyzed an off-the-shelf automated program to assist in assigning and scheduling projects.</p> <p>Agency procedures were not followed in the recent selection of design professionals for the construction of three parking garages.</p> <p>Division management should review and rewrite the internal procedures related to HUB compliance so that the procedures clearly communicate the areas of responsibility.</p>
September 1998	Needs Assessment Report issued by Spectrum Consulting	Immediate assistance is needed to standardize current procedures by documenting the construction management processes, completing the operating procedures, and establishing sound records management practices.
<b>Procurement</b>		
December 1994	<p><i>1994 Review of Statewide Procurement Practices</i></p> <p>Comptroller of Public Accounts</p>	The Commission should develop and maintain standard protest procedure policies.
February 1996	<p><i>Program Control Assessment for the Central Purchasing Program and Bid Services Section</i></p> <p>GSC Internal Audit Report No. 96-2</p>	<p>Controls over the data entry into the vendor tracking system can be enhanced to ensure the accuracy and completeness of information in the system.</p> <p>Controls to ensure compliance with the Historically Underutilized Business (HUB) Good Faith Effort Program should be strengthened.</p>
May 1996	<p><i>Leasing Division Program Control Assessment</i></p> <p>GSC Internal Audit Report No. 96-4</p>	<p>The current bidders list application does not satisfy all of the criteria outlined in the agency rules.</p> <p>Controls to ensure compliance with the Historically Underutilized Business Good Faith Effort Program should be strengthened.</p> <p>Bid forms have not been updated to reflect changes in law. If the forms are not revised to reflect the current law, a bidder could be incorrectly disqualified.</p>
May 1997	<p><i>Follow-Up to Fiscal Management Division Internal Audit Report</i></p> <p>GSC Internal Audit Report No. 97-3</p>	Payments are not always timed to obtain vendor discounts in compliance with statutory requirements.

Table 2, concluded

Date	Report Name and Reporting Organization	Key Audit Findings
August 1997	<p><i>An Audit Report on Management Controls at the General Services Commission</i> SAO Report No. 97-080</p>	<p>GSC continues to do business with poorly performing vendors because information on past vendor performance is not consistently used in the procurement process.</p> <p>The advantages of volume buying have not been calculated in the past. Without this type of evaluation, GSC has no assurances that the State is taking full advantage of volume buying to obtain lower prices.</p>
February 1998	<p><i>Follow-Up Audit on the Program Control Assessment of the Central Procurement Services Division and Bid Services Section</i> GSC Internal Audit Report No. 98-2</p>	<p>Controls over data entry into the vendor tracking system should be enhanced to ensure that accuracy and completeness of the information in the system.</p> <p>The Central Procurement Services Division is not in full compliance with the HUB Good Faith Effort requirements.</p>