

**Montgomery County, Maryland
Offices of the County Executive
Office of Internal Audit**



**Contract and Grant Monitoring by
The Montgomery County Department of Housing and Community
Affairs**

November 18, 2014

Highlights

Why MCIA Did this Audit

As part of the County Wide risk assessment completed by Montgomery County's Office of Internal Audit (MCIA), contract and grant monitoring by departments was identified as a high risk area. In FY13, the County's total value of purchase orders issued under contracts totaled approximately \$733 million. This audit of the Department of Housing and Community Affairs (DHCA) is part of a continuing review of contract and grant monitoring; DHCA is the ninth department we are reporting on. DHCA FY13 contractual purchase orders totaled approximately \$5.9 million, or roughly 2% of the total \$733 million.

What MCIA Recommends

MCIA is making 2 recommendations to DHCA to improve the performance and enhance the existing internal controls pertaining to contract monitoring and invoice review and approval. DHCA concurred with the recommendations.

November 2014

Contract and Grant Monitoring by the Montgomery County Department of Housing and Community Affairs

What MCIA Found

Based upon the procedures performed, the Montgomery County Department of Housing and Community Affairs has adequately designed and implemented procedures and internal controls for contract monitoring and invoice review and approval. However, there is an opportunity for improvement regarding contract performance monitoring. Our testing of seven DHCA contracts identified one instance where contract monitoring was insufficient. In addition, there is one opportunity to strengthen controls design regarding invoice review and approval.

We found internal controls over contract monitoring and invoice review and approval could be improved to ensure that: 1) deviations to the contract are appropriately amended on a timely basis and 2) DHCA's required invoice review and approval procedures are formally documented in writing.

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Objectives

This report summarizes the work performed by Cherry Bekaert LLP on behalf of Montgomery County Office of Internal Audit (MCIA) in an internal audit of the Montgomery County contract and grant monitoring process. The scope of this engagement included reviewing the contract and grant monitoring policies and procedures of the Montgomery County Department of Housing and Community Affairs (DHCA). The objective of the audit was to:

Review and test the effectiveness of contract and grant monitoring policies and procedures followed by the DHCA. The audit will seek to determine whether contractor performance is contractually compliant and being effectively tracked, that contract changes and extensions are being properly managed, and that applicable invoices are properly reviewed, maintained, and are accurate. This audit will include reviewing monitoring by departments by both program performance and financial accountability.

This internal audit report was performed in accordance with consulting standards established by the American Institute of Certified Public Accountants (AICPA) and generally accepted government auditing standards (GAGAS) established by the Government Accountability Office (GAO), as appropriate. Our proposed procedures, developed to meet the objectives stated above, were reviewed and approved in advance by MCIA. Interviews, documentation review, and field work were conducted from June to August 2014.

Background

Contracting Activity in Fiscal Year 2013

In FY13, DHCA was the ninth highest department in purchase order spending under contracts. DHCA had approximately 0.81% (\$5.9 million) of the total FY13 expenditure for purchase orders issued. A total of 75 contracts were in effect during FY13 ranging from \$1,046 to \$831,921. DHCA is also unique in that the department is responsible for the funding of contracts that are actually awarded and monitored by other departments such as Health and Human Services¹. DHCA contracts tended to consist of the purchase of services dedicated to increasing the supply and availability of affordable housing and outreach programs used to build a strong, vibrant community.

Contract Monitoring

Contract administrators have the responsibility of monitoring their respective contracts to ensure that vendor performance is in conformity with contract specifications. In the DHCA, contract administrators are typically assigned to contracts within their area of expertise. For example, a department member working with construction would handle contracts related to building and residential rehabilitation. Contracts in DHCA are generally service related. Contract administrators monitor performance on service-related contracts by visiting vendors on site to observe performance, scheduling meetings or conference calls to review performance, reviewing periodic monitoring

¹ Included in the contracting dollars for DHCA are contracts while funded by DHCA are managed by other departments such as HHS.

reports, and through communication with other DHCA staff who are on-site when services are provided.

Invoice Review and Approval

Contract administrators receive invoices directly from vendors and review the invoice for compliance with contract terms and accuracy of fees charged. Informal department guidance requires contract administrators to either sign or initial the invoice cover sheet to evidence their approval of the invoice. Once approved, the invoice is forwarded to a DHCA Accounts Payable Clerk for processing in the County's financial system (Oracle). The AP Clerk forwards the payment package to the applicable manager for initial approval by the section/division. In the case of absence of an approver, there are individuals assigned as secondary approvers. The initially approved payment package is submitted to the Budget and Financial Manager, who performs a second approval of department invoices in Oracle. In the event the Budget and Financial Manager is unable to review invoices, the Division Chief and/or Division Manager will perform the duties. Once approved, copies are given to the originating contract administrator. Per County policy, any invoice over \$10,000 must also be submitted for approval to Accounts Payable personnel within the Department of Finance.

Scope and Methodology

We reviewed contract and grant monitoring in two phases. Phase 1, conducted in FY12, consisted of interviewing responsible individuals from Department of General Services (DGS) and eight other County departments to gain an understanding of the policies and procedures followed in monitoring vendor performance under contracts and grants. In addition, Phase 1 included detailed testing of contract and grants monitoring procedures of one contract from each of the eight County departments with the highest purchase order spending for calendar year 2011. Results of the procedures performed in Phase 1 were used as a basis for developing the approach to Phase 2 testing.

Between FY13 and FY14, six departments were audited as part of Phase 2; the results of those audits are detailed in reports posted on the MCIA web site². That part of Phase 2 involves detailed testing of the monitoring and invoice review and approval procedures for County departments over contracts and grants in effect for FY12, while the continuation of Phase 2 utilized fiscal year 2013 contracts and grants. Using the Office of Procurement's 2013 purchase order data, we initially selected 13 contracts for discussion with DHCA staff, using the following criteria:

- Dollar amount of purchase orders issued under the contract
- Description of services being procured on purchase orders issued
- Length of time contract was in place during FY13
- Contract monitored by DHCA³

We met with DHCA staff to gain an understanding of the goods or services procured under each contract, the length and tenure of the contract, or contractor, and how much

² Departments previously audited during Phase 2 include the Department of Environmental Protection, the Police Department, the Department of Transportation, the Department of General Services, Fire and Rescue Services, Department of Economic Development, and Department of Recreation.

³ Contracts funded by DHCA but are monitored by other departments were excluded from population.

activity the department had with the contractor in FY13 and FY14⁴. Based upon information shared by department staff, we selected 7 contracts, totaling \$695,712 or approximately 5.1% of the total purchase orders issued for the department, for review as follows:

Table 1 – Contract Sample Selection for Phase 2

Vendor	Contract #	Description of Goods or Services	PO Amounts for FY13
E & R Services	102115	Fenton Village common area revitalization	\$360,965.57
City of Rockville	1024538	Community Development	\$177,346.46
Rebuilding Together	1763000121AA	Tenant Counseling and Housing Initiatives	\$56,424.41
Baruch & Pagan Associates	9761000086AB	Residential Weatherization Services	\$36,076.57
Casa De Maryland	1019554	Pine Ridge Community Center	\$33,760.43
Rummel, Klepper, & Kahl LLP	7761000070AB	Architectural and Engineering Services	\$22,638.34
Housing & Community	1013055	Homebuyer Education & MPDU orientation classes	\$8,500.00
Total			\$695,711.78

Our testing for Phase 2 focused on the following

- Reviewing procedures performed by department staff to ensure contractor performance was in accordance with contract terms.
- Reviewing procedures performed by department staff to ensure payments made to contractors were for services or goods provided in accordance with contract terms.

The attributes we tested are listed below:

Table 2 – Attributes Tested for Contract Administration/Monitoring

Attribute	Description
A	Monitoring of contractor performance milestones delivery, submission of status reports, and/or submission of invoices and other data related to payment
B	Reviewing of contractor status and performance reports
C	Pre approving, receiving, inspecting, and/or accepting of contractor work
D	Certifying costs incurred for payment under time and material or labor hour contracts
E	Performing site visits or visual observations of contractor work performance, if applicable
F	Monitoring procedures performed in accordance with contract terms continually and on a timely basis
G	Identification and reporting of contract problems and violations to appropriate managers on a timely basis

⁴ Scope used for testing over invoicing and monitoring for the Department of Housing and Community Affairs was 7/1/2012 through 5/31/2014

Table 3 – Attributes Tested for Invoice Review and Approval

Attribute	Description
A	Invoice calculations are reasonable and accurate (foot and cross-foot)
B	Supporting documentation required by the contract was submitted with the invoice
C	Unallowable costs do not appear to be included in invoice submission
D	Invoice signed by Contract Administrator/Monitor
E	Invoice approved by department designated individual
F	Voucher approved by A/P
G	Amount per invoice agrees to amount paid
H	Invoice approved by Auditor/Project Manager/Chief
I	Appropriate retainage fees (of 10%) were withheld from the invoice
J	Agreed course dates per monthly invoice to calendar of publicized courses

Results

Overall, the results of our testing found that contract and grant monitoring and invoice review and approval were generally performed in accordance with applicable County policies and procedures, department practices and contract or grant terms and conditions. For all contracts tested, opportunities for improvement in contract monitoring were noted as evidence by the two exceptions related to two attributes tested for contract monitoring, yielding a 2.04% error rate.⁵ With regard to the attributes tested for invoice review and approval, we noted no exceptions.

The tables presented below provide a summary of the exceptions noted during our testing.

Table 4 – Summary of Exceptions from Phase 2 Contract Administration/Monitoring Testing

Attribute Tested	Total Exceptions Per Attribute	Sample Tested Per Attribute	% Exceptions Per Attribute
A - Monitoring of contractor performance milestones delivery	0	7	0%
B - Reviewing of contractor status and performance reports	0	7	0%
C - Receiving, inspecting, and/or accepting of contractor work	0	7	0%
D - Certifying costs incurred for payment	0	7	0%
E - Performing visual observations of contractor work	0	7	0%
F - Monitoring procedures performed in accordance with contract terms	1	7	14%
G - Identification and reporting of contract problems timely	-	7	0%

⁵ Contract Monitoring Error rate : Total number of exceptions noted (1)/ Total number of attributes tested (49)= 2.04%

Attribute Tested	Total Exceptions Per Attribute	Sample Tested Per Attribute	% Exceptions Per Attribute
Total Exceptions	1		
Total Samples Tested	7		
# of Samples with Exceptions	1		

Below is a summary of our findings on specific contracts reviewed.

Contract #1013055 Housing & Community - Home buying education seminars for low income individuals

1. Contract Administration and Monitoring (Attribute F):

- We found the two instances in which DHCA and the contractor agreed to changes in contract requirements. However, the modifications were not documented in a formal amendment to the contract. Per County Procurement Regulations Section 11B.04.01.11, *Item 11.1.1 Authorization*, A contract modification is not effective and a contract must not proceed with performance under the modification, until and unless the contract modification is executed by the contracting officer⁶. While the agreed upon changes were not expanding but reducing the contractors scope of work, the changes should have been formally documented and approved by the contracting officer in a contract amendment.
 - i. Per Section C, Scope of Service, *Reports*, the vendor is to provide three reports on a monthly basis: 1) Number of First-Time Homebuyer Class (FTHB) attendees for the preceding month must be submitted by the 15th of the following month; 2) Report detailing the number of Moderately Priced Housing Unit (MPDU) attendees at each First-Time Homebuyer Class, with a racial/ethnic breakdown for the preceding month must be submitted by the 15th of the following month; and 3) Rating/Comment sheets from attendees at the MPDU Orientation Seminars must be submitted to the Department after each session. Due to a racial discrimination complaint received by the County (regarding report #2 – racial/ethnic breakdown), the County deemed the vendor to be no longer required to request and submit the report. The contract terms were never amended to remove the requirement.
 - ii. Per Section C, Scope of Services, *Work Statement, #4*, the contractor must provide a semi-annual Post Purchase Education/Counseling Class to new MPDU owners. Per the Contract Administrator, the County and the contractor agreed not to hold this class and instead to replace the class with FTHB and MPDU classes. The contract terms

⁶ County Procurement Regulations Section, 11B.00.01.02, *Item 2.4.24 Contracting Officer*. The CAO, Director, others delegated by these officials to act within their authority, and other officials specifically authorized by these regulations to enter into a contract on behalf of the County. Only contracting officers may execute contracts or contract modifications on behalf of the County.

were not amended to reflect the discontinuation of the semi-annual class and the increase number of FTHB and MPDU classes.

Other Matters

Invoice Review and Approval

In discussions and in response to request for written department procedures DHCA staff stated that there were no formal written guidelines within the department detailing required invoice review and approval procedures. Having formal written procedures is a best practice and a fundamental internal control. Among other things, it allows employees to know precisely what is expected of them. While we noted no exceptions in our testing of invoice review and approval there is a need for written procedures. For example, there is a risk that employees newly assigned to contract administration duties would not have readily assessable information regarding department procedures to follow. This could lead to improper review and approval as well as procedures being missed altogether.

Recommendations

We recommend that the Department of Housing and Community Affairs Director:

1. Reinforce with contract administrators the responsibility of ensuring that vendors comply with all contract requirements and that any agreed changes or removal of contract terms be documented in a contract amendment.
2. Formalize and document existing department invoice review and approval procedures as a reference for current and future department personnel.

Department Comments and MCIA Evaluation

We provided DHCA with a draft of this report for formal review and comment on October 20, 2014 and DHCA responded on November 4, 2014. DHCA stated said it concurred with the report's recommendations and had implemented corrective actions. (See Appendix A for DHCA response.)

Appendix A



DEPARTMENT OF HOUSING AND COMMUNITY AFFAIRS

Isiah Leggett
County Executive

Richard Y. Nelson, Jr.
Director

MEMORANDUM

November 4, 2014

TO: Larry Dyckman, Manager
Office of Internal Audit
Offices of the County Executive

FROM: Richard Y. Nelson, Jr., Director
Department of Housing and Community Affairs

SUBJECT: Response to the Office of Internal Audit's Report on Contract and Grant Monitoring

The purpose of this memorandum is to respond to the Office of Internal Audit's report on Contract and Grant Monitoring for the Department of Housing and Community Affairs.

At the Department of Housing and Community Affairs (DHCA), we are dedicated to increasing the supply and availability of affordable housing and developing and maintaining healthy, vibrant and strong communities. We offer programs and services that prevent and correct problems that contribute to the physical decline of residential and commercial areas, work with landlords and tenants to ensure fair and equitable relations between the parties, and enforce the local housing code to ensure existing housing is maintained in a safe and sanitary condition.

The audit review resulted in two recommendations to improve contract monitoring practices in DHCA. Our responses are as follows:

Recommendation 1: Reinforce with contract administrators the responsibility of ensuring that vendors comply with all contract requirements and that any agreed changes or removal of contract terms be documented in a contract amendment.

DHCA agrees with the recommendation and provides the following clarification.

The two requirements in the contract with Housing and Community Initiatives, Inc. (HCI) that were modified relate to the implementation and operation of the Moderately Priced Dwelling Unit (MPDU) program. In order to effectively implement this complex housing program, the Director of DHCA requires flexibility to make re-adjustments among approved classes provided by the Contractor in order to respond to changing programmatic conditions and demand among participants, so long as those

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adjustments do not materially or substantially change the scope of the contract, the implementation of the program, or increase the monetary value of the contract.

In the case of the demographic data collection and reporting, the Director of DHCA modified this requirement based upon a public complaint made to the County's Office of Inspector General (OIG) and upon advice from the County Attorney's office. To be accurate, DHCA did not deem "the vendor to be no longer required to request and submit the report", but only to make a change to the demographic data reporting section on the class registration form to explicitly inform registrants that providing the data on race, sex, disability status, etc. was voluntary and would be confidential. After this change was made, the number of registrants self reporting this information was greatly reduced and therefore of no statistically useful value to DHCA. The requirement for demographic data reporting was a minor requirement associated with the more useful number of attendees of the First-Time Homebuyers' class and was required by DHCA for internal informational purposes only (that is, not for any other Federal, State or County reporting purposes); the lack of this data does not materially affect the implementation of the MPDU program or departmental operations.

In regards to the re-allocation among approved classes, when the contract with HCI was drafted, DHCA staff attempted to estimate the number and type of classes that would be needed to meet programmatic demand over the next 12 month period. The re-allocation of the number and type of classes offered under the contract, from one type of approved class (Post Purchase Education) for another type of approved class(es) (First Time Homebuyer or MPDU Orientation) was made due to a lack of demand for the Post Purchase Education classes among new MPDU owners (as reflected in the lack of online registrants for the class), and the increasing demand for the First-Time Homebuyers' and MPDU Orientation classes among prospective applicants to the MPDU program. This change did not materially or substantially affect the implementation of the program. It also did not result in an increased cost to the County or a savings to the contractor as the number of class sessions did not change.

In the future DHCA will draft service contracts of this nature to explicitly state that the Department reserves the right to re-allocate approved classes as necessary based on demand among program participants so long as the number of classes is not increased or reduced, and there is no change in the value of the overall contract.

Recommendation 2: Formalize and document existing department invoice review and approval procedures as a reference for current and future department personnel.

DHCA agrees with the recommendation and reiterates that no exceptions were found in the department's Invoice Review and Approval procedure. The audit confirms that the procedure works and is well-implemented. DHCA has taken appropriate measures to ensure that staff is aware of the procedure. Prior to the finalization of this audit report, DHCA formalized the procedure and sent a department-wide email to staff reinforcing the procedure. This procedure is posted to a file directory to which all staff has access. The procedure will be reinforced for new staff and existing staff as appropriate.

Thank you for the opportunity to respond. If you have any questions related to the above, please contact Tim Goetzinger, Budget and Finance Manager, at 240.777.3728.

RYN:tjg

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