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"Providing procurement services through operational leadership, legal compliance, and enhanced value for our customers and the state's procurement community."



Procurement Compliance Annual Report Fiscal Year 2015

**STATE OF ARIZONA
STATE PROCUREMENT OFFICE
PROCUREMENT COMPLIANCE
ANNUAL REPORT
FISCAL YEAR 2015**

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Overview

A division of the Arizona Department of Administration (ADOA), the State Procurement Office (SPO) serves as the central procurement authority for the State of Arizona and is responsible for a variety of procurement services including regulatory services, policy-making, management, direct contracting and purchasing services, ancillary and support services, as well as related technical assistance. The Arizona Procurement Code (APC) is the governing statutes and rules by which procurement is performed in the State of Arizona. Under ARS § 41-2511, amended by HB2599 in Fiscal Year 2013, the Director of ADOA, and by delegation the State Procurement Administrator (SPA) under rule R2-7-201, establishes and maintains programs to ensure compliance with the APC.

The SPO compliance program was developed in Fiscal Year 2014. The SPO compliance program was modeled after Chapter 8 of the 2014 Federal Sentencing Guidelines (FSG) – Sentencing of Organizations. The FSG prescribes the chief mitigating factor of criminal misconduct in organizations in the private, non-profit, and public sectors, is the establishment of an effective compliance program. An effective compliance program is defined by the FSG to include:

1. Written standards of conduct and policies and procedures
2. Designation of a compliance officer and other appropriate bodies
3. Effective education and training
4. Audits and evaluation techniques to monitor compliance
5. Establishment of reporting processes for complaints
6. Appropriate disciplinary mechanisms
7. Investigation and remediation of systemic problems

Prior to the development of the SPO compliance program, SPO has addressed item #1 with the distribution of the APC, Standard Procedures (SPs), and Technical Bulletin's (TBs). In FY14 Q4 the compliance program was piloted in SPO's Shared Services Section. The SPO Compliance Unit recommended during the pilot that formal Procurement Policies and Procedures Manual be established. As of May, 2015 this manual is still under development.

SPO addressed items #2 and #3 of the FSG guidelines in FY14 in accordance with HB2599 through the designation of the Compliance Officer and Chief Learning Officer. Both the compliance

and training programs went “live” on July 1st, 2014. These programs serve to improve consistency in procurement practices across all State agencies. The compliance and training programs also influence one another through identification of new training needs and improved consistency in procurement practice.

The SPO Compliance Unit addresses item #4 of the FSG guidelines through the establishment of two evaluation techniques to monitor procurement compliance. To maximize the compliance program’s effectiveness under limited budget and manpower, the first compliance monitoring technique is the Control Self-Assessment (CSA). In FY15, 11 agencies completed the CSA, provided evidence of completion to the SPO Compliance Unit, and implemented corrective action plans as coordinated with the SPO Compliance Unit. The second compliance monitoring technique is the Procurement Performance Review (PPR). In FY15, five agencies were scheduled for an onsite compliance review performed by the SPO Compliance Officer.

Item #5 of the FSG guidelines was established this year through the SPO Procurement Compliance Hotline. This hotline is hosted on SurveyMonkey.com and is a separate SurveyMonkey.com account from any other owned by SPO. The only party with access to the reports submitted is the SPO Compliance Officer. Submittals through the hotline may include procurement compliance questions, concerns, or complaints, and may be submitted when alternative avenues of communication are not seen as viable to the individual reporter.

The APC provides the SPA with existing adequate authority to address FSG guideline #6 to maintain appropriate disciplinary measures. In addition to these measures, the SPO compliance program also established a recognition program to encourage state agencies to improve procurement compliance.

Lastly, the SPO compliance program addresses FSG guideline #7 through several mediums. Systemic procurement compliance concerns are addressed with the SPA in bi-weekly meetings. System issues are reviewed with the SPO Business Specialist to address changes to TBs and SPs. Observations and adjustments to procurement procedures are communicated at monthly CPO meetings, and through the public posting of PPR findings on the SPO website.

Control Self-Assessments (CSA)

Nine agencies were assigned to complete a CSA in FY15, with two additional agencies voluntarily completing a CSA, all of whom coordinated with the SPO Compliance Officer with responses and establish corrective action plans. Agencies assigned to complete a Control Self-Assessment have \$100,000 Procurement Delegation. Agencies followed a prescribed schedule to submit portions of the CSA on a quarterly basis. Scheduled portions of the CSA were submitted to SPO:

September 30th:	Sections 1 – 3
December 31st:	Sections 4 – 5
March 31st:	Section 6.1

Section 1 is a general overview of the purchasing organization, including the individual sub-delegation of authority to personnel and acknowledgement that training was completed commensurate to the position and level of delegated authority. Section 2 is a review of the agency’s procurement policies and procedures manual. This review checks for the manual’s completeness and if it is up-to-date with current rules and statute. The first quarter review is completed with Section 3, which examines the agency’s reporting requirements to SPO, including such items as special purchases, and sub-delegation updates.

The second quarter review begins with Section 4, which examines agency procurement staff training and agency specific sub-delegation procedures. Section 5 of the CSA reviews the agency’s own internal controls to safeguard against conflict of interest, theft, and improper disclosure of trade secrets.

Lastly, \$100,000 delegated agencies complete Section 6.1 as a stand-alone submittal. This is due to a greater degree of detail and time necessary for this review, which covers an office selection of at least five RFQs within the last 12 months. Remaining sections of the CSA, which cover IFBs, RFPs, and special purchases, do not apply to \$100,000 delegated agencies.

<u>Completed CSA’s</u>
AZ Board of Early Childhood Development
AZ Geological Survey
AZ School Deaf & Blind
AZ Dept. of Gaming
AZ State Parks
AZ State Lottery
AZ Dept. of Agriculture
AZ State Fair
AZ Dept. of Revenue
AZ State Land Dept.
AZ School Facilities Board

CSA Findings

The CSA consists of a total of 90 line-items of review. Depicting frequency of non-compliance, the top 12 agency self-observed line-items are reflected in the “FY15 Most Common CSA Findings.”

Section 2 was the most frequent section of non-compliance. Specifically, out of the 11 agencies completed CSAs, seven declared that their office does have a procurement policies and procedures manual. However, two-thirds of the policy and procedures manuals in the agencies are not up-to-date with current rules and statute. Missing, or out of date, sections of agency manuals include: Instructions for Set-Aside purchases; Procedures to add/delete/modify authority in ProcureAZ; Procedures for cooperative purchasing agreements; and, Procedure for dealing with unethical behavior.

Several issues of procurement contract file non-compliance are reflected in the FY15 Most Common CSA Findings. Two-thirds of RFQs reviewed were acknowledged as containing documents uploaded to ProcureAZ that did not adhere to the naming conventions required of SPO SP#006. Of five files reviewed in which a non-small business was awarded a contract, three files did not contain a determination to use a non-small business. Five applicable RFQs did not include a statement that only a small business would be awarded a contract.

Lastly, two areas of the CSA addressing procurement training and ethics present further opportunities for improvement.

Half of the agencies completing the CSA reported that they had not communicated the SPO

FY15 Most Common CSA Findings	
<i>Are documents named in ProcureAZ following SPO SP#006 Naming Conventions?</i>	66.67%
<i>Is the Agency Procurement Policy and Procedure (PPP) Manual Up To Date?</i>	66.67%
<i>If RFQ was not awarded to a small business - is there a determination in file to award to non-small business?</i>	60.00%
<i>Does RFQ include statement that only a small business will be awarded a contract?</i>	55.56%
<i>PPP Manual includes agency procedures to add/delete/modify authority in ProcureAZ</i>	54.55%
<i>Agency has communicated SPO Procurement Compliance Hotline to Employees.</i>	54.55%
<i>Does PPP Manual Include Instructions for Set-Aside</i>	50.00%
<i>Does agency provide in-house procurement training to new personnel?</i>	45.45%
<i>Does agency have a procedure for dealing with unethical behavior?</i>	36.36%
<i>PPP Manual includes instructions to submit procurement reports to SPO</i>	33.33%
<i>PPP Manual includes procedures regarding cooperative purchasing agreements?</i>	33.33%
<i>Did the agency director, or designee, inform employees when the first PDS was signed, and notify the State Procurement Administrator?</i>	33.33%

Compliance Hotline to their staff. One third of the agencies reported that they did not have a policy which address unethical behavior. Nearly half of agencies report that they do not currently have in-house procurement training for newly hired procurement personnel.

CSA Highlights

Significant Procurement Role was introduced October 2014. As a new requirement of procurement in the State, agencies completing the Control Self-Assessment indicate a strong level of compliance to obtaining signed Annual Procurement Disclosure Statements from employees whose regular job duties include procurement related functions, with only 10% not meeting this requirement. Additionally, just 18.18% of files reviewed did not contain a procurement disclosure statement for state employees, whose regular job duties are not procurement related, yet had a role in the development of the procurement, evaluation tool, participated as an evaluator, or recommended a vendor to provide service.

SPO TB# 002 outlines the required training, experience, education, and certification for each position and level of delegation for procurement personnel. Only 10% of agencies completing the CSA reported that personnel training did not meet these standards, however did indicate a corrective action plan to complete necessary training.

Lastly, only 10% of agencies completing the CSA indicated they did not presently endeavor to purchase 1% of all money spent through designated Set-Aside contracts. Likewise, through coordination with the SPO Compliance Unit, this agency now understands the requirements of ARS 41-2636.

CSA Corrective Actions

Agencies completing the CSA are instructed to develop their own SMART corrective action plans to remedy their findings. Corrective action plans should be Specific, Measurable, Achievable, Realistic, and Time-bound. Agencies are instructed to develop their own corrective action plan with the SPO Compliance Unit's goal that the agencies are more likely to "own" their findings and resolutions. The SPO Compliance Unit calendared follow-up dates to review the agency' progress on their corrective actions on dates appropriate to the agency's action-plan timeline. In the event

the SPO Compliance Unit received a CSA response without a corrective action plan, the unit then devised a corrective action-plan of its own. In the event the SPO corrective action plan prompted questions or comments from the owning agency, this was used as an opportunity for the SPO Compliance Unit to encourage the agency to develop an alternative SMART action plan.

Procurement Performance Review (PPR)

<u>Completed PPRs</u>
AZ Board of Appraisal
AZ Game and Fish Division
AZ Dept. of Health Services
AZ Dept. of Veterans' Services
AZ State Retirement System

Five agencies were assigned to participate in a full onsite-PPR in FY15. Agencies participating in a PPR are either of unlimited delegated procurement authority, by special request, or as assigned by the SPA. Each PPR took approximately three months to complete. The PPR is initiated by a kickoff letter sent to the CPO which advises the agency has been selected for a review, documentation needed by the SPO Compliance Unit, and an approximate timeframe by which the review should follow.

An entrance interview is scheduled, approximately 30 days following the kickoff letter, with the CPO and agency procurement personnel. Prior to the entrance interview, requested documentation is received from the CPO, reviewed, and procurement files are reviewed through ProcureAZ. The entrance interview serves as an opportunity for the SPO Compliance Unit to assess the procurement personnel's knowledge of the APC, identify processes unique to the agency, and to clarify questions formed during the file review prior to the entrance interview. The PPR covers all of the same sections, as described, within the CSA. However, in addition, the PPR includes a review of IFBs, RFPs, Sole Source, Emergency, and Competition Impracticable procurements, and additional reporting requirements applicable to unlimited delegated procurement offices.

The PPR concludes with a draft report to the SPA for review. A final PPR, both edited and signed by the SPA and Compliance Officer, is presented to the agency CPO via an exit interview. Findings and recommendations are discussed with the CPO, and the CPO is instructed to draft a response with a corrective action-plan to SPO within 21 days. The final PPR, including agency response once received, is posted to the SPO website as a public record.

PPR Findings

The PPR consists of a total of 230 line-items of review.

Depicting frequency of non-compliance, the top 12 observed line-items are reflected in the “FY15 Most Common PPR Findings.”

Several line items in the PPR for FY15 stand out as trends of procurement non-compliance. One area of concern is that of vendor certificates of insurance. All offices reviewed did not possess uniform procedures for ensuring vendor insurance was up to date. Consequently, this is evidenced by the more poignant issue that 75% of contract files reviewed in FY15 either contained out-of-date vendor insurance, or did not contain vendor insurance at all.

Similar to the results found in the CSAs, this year’s unlimited delegated agencies did not possess a current and up-to-date procurement policies and procedures manual in 75% of offices reviewed. While most offices possessed a manual, either the manuals were 5-10 years out of date, or lacked specific sections of procurement procedures*. Arizona Department of Veterans’ Services (ADVS) is highly recognized for the agency’s very thorough and up-to-date manual.

Another frequent theme in the FY15 PPR reviews is that of missing documentation in the official state procurement file of record: ProcureAZ. This includes, as referenced above, missing vendor certificates of insurance. Additionally, special procurements lacked documentation as required by the APC. For instance, 80% of sole-source procurements lacked documentation that the price was fair and reasonable.

FY15 Most Common PPR Findings	
<i>Does agency have procedures to ensure vendor insurance is up to date?</i>	100.00%
<i>Documentation sole-source price is fair & reasonable.</i>	80.00%
<i>Is vendor insurance in file up-to-date?</i>	75.00%
<i>Is the Agency Procurement Policy and Procedure (PPP) Manual Up To Date?*</i>	75.00%
<i>Are all agency procurement staff certified by public procurement organization?</i>	60.00%
<i>Do all agency procurement staff undergo training to enhance professional status?</i>	60.00%
<i>Are contract files complete and available for inspection within 10(3) days of award?</i>	58.33%
<i>Are PDS in file for all state-employees involved in preparation/selection?</i>	57.14%
<i>Is there a written procurement request, or linked to a requisition in ProcureAZ, in file?</i>	51.61%
<i>Emergency – given circumstances, evidence maximum competition employed?</i>	50.00%
<i>Are documents named in ProcureAZ following SPO SP#006 Naming Conventions?</i>	50.00%
<i>Does the agency provide in-house procurement training and mentoring programs for newly-hired procurement personnel?</i>	50.00%
<i>*Note: Ten additional line items ranked within 50.00 – 75.00% were contributing factors to an incomplete agency procurement policy and procedure manual</i>	

50% of emergency procurements lacked evidence that maximum competition was employed given the circumstances. Also, over half of files reviewed this year did not contain a procurement request, either in writing, or linked in ProcureAZ to a requisition. Through entrance interviews with procurement personnel, instances were addressed in which personnel were not familiar with the requirements, addressed above, for emergency and sole-source documentation. Additionally, personnel reflected mixed responses regarding the agency's official procurement file. In some circumstances, the file was a combination of ProcureAZ and hard-copy, and not all hard-copy procurement records were necessarily uploaded to ProcureAZ as prescribed by SPO SP#006.

PPR Highlights

The FY15 PPRs resulted in several highlights of good compliance processes and controls in state procurement. It is noteworthy to address, although procurement policies and procedure manuals in most cases were not up to date, it was a SPA initiative to update these manuals only within this past fiscal year. Several manuals reviewed this year, while not up to date, were either in process of being updated, or had an outlined schedule by which the agency was already planning to update the manual. Moreover, ADVS represented one agency with a complete and up-to-date manual.

Contract files, with very high frequency, contained the most up-to-date SPO template forms, including Uniform Terms and Conditions, Instructions, and special purchase determinations. All unlimited delegated agencies also had signed Annual Procurement Disclosure Statements for all procurement personnel in each respective office. Agencies are familiar with the use, and goals of state set-aside contracts. Finally, offices also routinely complete and submit quarterly limited competition reports and random e-verify Arizona Legal Worker's Act verifications as required.

PPR Corrective Actions

Each PPR, after identification of a trend of non-compliance, is followed by a recommendation for remediation. However, like the CSA, ownership of the corrective action plan belongs to the respective agency CPO. The SPO Compliance Unit followed up with agency CPOs on the corresponding dates associated with each corrective action item provided by the agency CPO. Through this process, SPO assisted agency CPO's by providing guidance and resources to help accomplish the CPO's goals.

Procurement Compliance Hotline

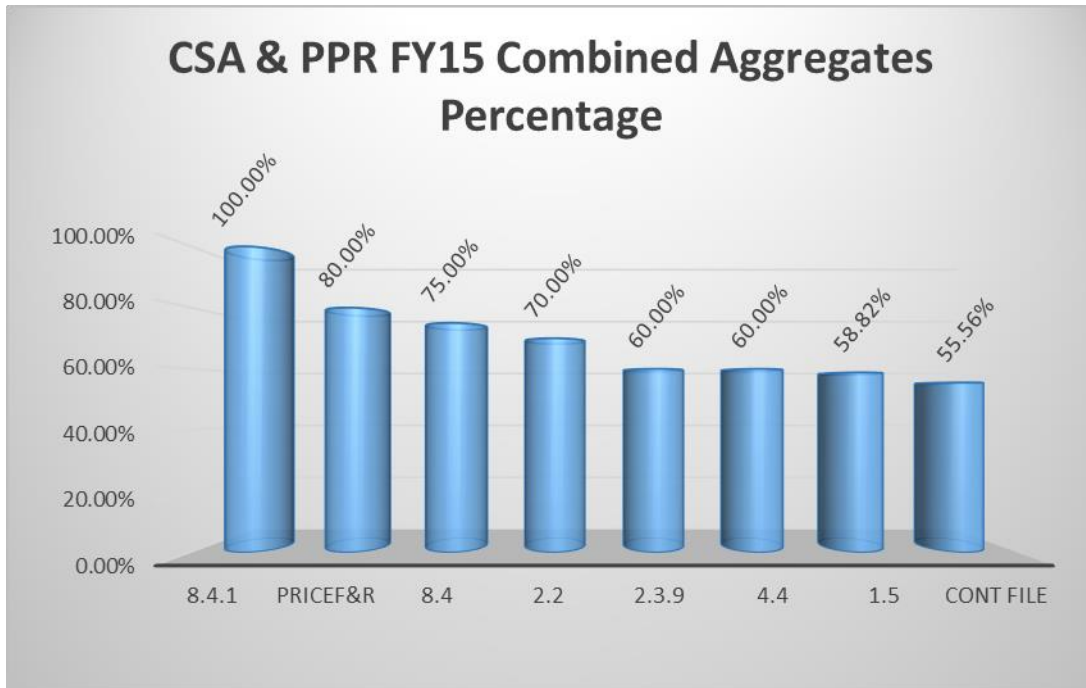
SPO provides a Procurement Compliance Hotline to State procurement personnel as a means of addressing procurement questions or concerns which, by the employee's assessment, cannot be addressed through their supervisor. This hotline is provided via the SPO Website and hosted by SurveyMonkey.com. Potential inquirers are instructed to first direct their questions and concerns to their direct supervisor or upper management. Non-State employees are instructed to contact the responsible employee, CPO, or agency ombudsman. If the reporter feels that these options are not viable, then the reporter may submit their question or concern to the SPO Compliance Officer. Reports may be submitted either anonymously or confidentially. Confidential reports are protected to the extent possible depending on the nature of the report and necessity of investigation. Only the SPO Compliance Officer has login rights to the data collected on the specific SurveyMonkey.com account dedicated to the hotline.

The SPO Compliance Unit was in receipt of four inquiries during FY15. Two of the inquiries addressed concerns regarding vendor performance. One vendor inquiry was submitted confidentially. This report resulted in an investigation of one vendor's contract performance and licensure to perform work in the State of Arizona. The second inquiry was submitted anonymously. This report resulted in an investigation of man-hours billed versus actual hours worked on specific dates in question. Findings from each investigation were submitted to the SPA for further consideration and action.

The remaining two inquiries were submitted by State employees. The first inquiry was submitted confidentially, but insufficient information was provided to conduct an investigation. This individual was contacted and assured, if additional information were provided, the investigation would maintain the reporter's confidentiality to the best of the SPO Compliance Unit's ability, depending on the nature of the report and investigation. No additional information was provided. The second State employee report was submitted confidentially and, based on the nature of the inquiry, was referred to the respective agency's human resources liaison for further investigation.

Key Findings of FY15

Sixteen agencies, from both PPRs and CSAs, contributed to the aggregate procurement compliance results of FY15. The top eight findings in the figure below represent the greatest frequency of non-compliance across these 16 agencies. Opportunities for State procurement to make greatest improvements to compliance efforts in FY16 are addressed below.



8.4.1 – This line item addresses whether the agency has mechanisms in place to ensure vendor insurance is up to date. 100% of agencies reviewed did not have any such uniform procedure. This was only measured against unlimited delegated agencies.

Price F&R – This line item addresses if the contract file for an emergency procurement contains documentation by the agency which verifies that the price submitted was fair and reasonable pursuant to R2-7-702. Of all emergency procurements reviewed in FY15, 80% did not contain such documentation.

8.4 – This line item reflects the total occurrences in which contractor insurance was either not in the contract file, or insurance in file was not up-to-date. Of all contract files reviewed in FY15 from both CSAs and PPRs, 75% of the files did not have a current and valid vendor certificate of insurance.

2.2 – This line item addresses the frequency of occurrence in which agencies had a procurement policies and procedures manual, however the manual was not up to date with current statutes, rules, technical bulletins, and/or standard procedures. 70% of procurement policies and procedures manuals, from both CSAs and PPRs, were not up to date in FY15.

2.3.9 – This line item addresses, where an agency did have a procurement policy and procedure manual, if the policy and procedure manual contained instructions to purchase from State approved set-aside programs. Just over half of the policy and procedure manuals reviewed, 60%, did not contain such instructions.

4.4 – This line item addresses whether agencies with unlimited delegated procurement authority have 100% of their eligible staff certified by a public procurement organization, such as NIGP, as required by the delegated authority. Of unlimited delegated procurement agencies reviewed, 60% did not yet have all eligible staff certified by a public procurement organization.

1.5 – This line item discusses whether the agency's procurement policies and procedures manual, contained in-house instructions to ensure procurement personnel delegation is added/deleted/modified in ProcureAZ. 58.82% of all offices did not contain such instructions in their procurement policy and procedure manual.

Cont. File – This final line item addresses the frequency in which contract files are fully uploaded to ProcureAZ within 10 days of contract award (after 02/2015 – 3 days). 55.56% of all contract files reviewed, between both CSA and PPRs, were not fully uploaded, including all contract documents, within 10 days of contract award.

Adjustments to Compliance Program for FY16

The SPO compliance program was developed to anticipate regular change. Over the course of each year of the compliance program in practice certain areas of non-compliance will no longer be areas of concern. It is anticipated that communication of top areas of non-compliance and best practices will help all agencies, actively engaged in maintaining compliance to the APC, will remedy areas of concern without direct interaction with the SPO Compliance Unit through a CSA or PPR. Similarly, new areas of non-compliance will emerge and will gain added attention from the SPO Compliance Unit. To provide attention to the SPO compliance program where most important, the following adjustments to the program will be implemented in FY16.

- **Changes to CSA & PPR Templates:** In FY15 the CSA & PPR templates had individual line-items which checked to confirm that solicitations included specific language found in Uniform Instructions and Uniform Terms and Conditions as required by the APC. This was a time-consuming process and resulted in no significant areas of non-compliance. In FY16 the CSA & PPR templates will, in lieu of separate line-items of required language from the APC, instead validate that the reviewed solicitation used the most up-to-date Uniform Instructions and Uniform Terms and Conditions issued by SPO as required by the agency signed delegated procurement authority.
- **Additional Changes to CSA Template:** The CSA template, in FY16, will provide assigned agencies additional explanation, definitions, and examples on how to properly complete the self-assessment process.
- **Risk Based Quarterly Review:** Beginning FY16 the SPO Compliance Unit will randomly sample contract files from all agencies to monitor for statewide procurement compliance and progress to areas previously identified as potentially systemic procurement compliance concerns, special procurements, and piggyback purchasing. This random sample will select from agencies not already scheduled for PPR/CSA review. The random sampling will take place at the end of each fiscal quarter, beginning FY16Q1, reviewing of identified areas of risk from 10% of files from the preceding 12 months.
- **Annual PPR Follow-up:** Beginning FY16, each agency that participated in a PPR the preceding year will have a one year follow-up by teleconference with the SPO Compliance

Officer. This follow-up will be scheduled in the corresponding fiscal quarter to the preceding year's review. This follow-up will discuss previous findings and the office's efforts to remedy the findings. A memo will be drafted by the SPO Compliance Officer which summarizes the call and will be distributed to the agency CPO and SPA.

FY15 Compliance Recognition

The SPO Compliance Unit set forth the goal to not only measure areas of non-compliance, but also incentivize particularly strong compliance to the APC. This is accomplished through the establishment of three levels of the SPO Platinum Compliance Award. This award results in an image file which, upon the awarded agency's management approval, may be placed on the procurement office's website as demonstration of the office's commitment to compliant procurement in the State. The SPO Compliance Unit anticipates this award will motivate offices to maintain strong compliance to earn the award again in the future. It is further anticipated this award will motivate other agencies, not yet reviewed by the SPO Compliance Unit, to establish strong procurement compliance controls to earn future recognition.



Procurement compliance was scored by total line items in the PPR found as "in compliance." Due to the validation involved by the SPO Compliance Unit in assessing procurement compliance controls, the award is exclusive to unlimited procurement delegated agencies undergoing a full PPR.

In recognition of the Arizona Department of Veterans' Affairs (ADVS) noteworthy efforts to maintain and advance its procurement compliance controls, SPO recognizes ADVS with the FY15 Platinum Compliance Award.

FY16 Schedule

Every agency with unlimited delegated procurement authority shall be reviewed via PPR at least once every four years. Agencies with \$100,000 delegated procurement authority will complete a

CSA at least once every four years. The SPO Compliance Unit shall notify all agencies of their annually scheduled review at the beginning of each fiscal year. When deemed necessary, or by special request, the SPA may assign additional agencies for compliance review, under either a CSA or PPR. \$10,000 delegated procurement authority agencies, and any other agency not already scheduled for review, are highly encouraged, though not required, to conduct CSAs to proactively identify opportunities to improve compliance controls.

The selected offices for FY16 were randomly chosen, through a lottery selection, by the unlimited delegated procurement authority agency CPO's at a staff meeting at the close of FY14.

<u>Procurement Performance Reviews</u>
Dept. of Economic Security
Dept. of Environmental Quality
Dept. of Public Safety
Dept. of Education

<u>Control Self-Assessments</u>
Commission on the Arts
State Treasurer
Registrar of Contractors
State Forestry Division
Governor's Office Highway Safety
Corporation Commission
AZ Medical Board
Board of Appraisal
Office of Tourism