

# Arizona Department of Health Services Procurement and Contract Monitoring

Department did not follow some procurement requirements and paid for some services without ensuring they were provided and contract requirements were met

Performance Audit

August 2019  
Report 19-109



A Report to the Arizona Legislature

Lindsey A. Perry  
Auditor General





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August 27, 2019

Members of the Arizona Legislature

The Honorable Doug Ducey, Governor

Dr. Cara Christ, Director  
Arizona Department of Health Services

Transmitted herewith is the Auditor General's report, *A Performance Audit of the Arizona Department of Health Services—Procurement and Contract Monitoring*. This report is in response to a September 14, 2016, resolution of the Joint Legislative Audit Committee. The performance audit was conducted as part of the sunset review process prescribed in Arizona Revised Statutes §41-2951 et seq. I am also transmitting within this report a copy of the Report Highlights to provide a quick summary for your convenience.

As outlined in its response, the Arizona Department of Health Services agrees with 2 of the findings and disagrees with 1 finding, but indicated it plans to implement all of the recommendations.

My staff and I would be pleased to discuss or clarify items in the report.

Sincerely,

Lindsey Perry, CPA, CFE  
Auditor General



## Arizona Department of Health Services Procurement and Contract Monitoring

**CONCLUSION:** The Department's mission is to promote, protect, and improve the health and wellness of individuals and communities in Arizona. The Department reported that it administers over 300 programs, such as the Special Supplemental Nutrition Program for Women, Infants and Children (WIC); the Immunization Program; and the Medical Marijuana Program; and uses contracts and agreements to help fulfill its mission and carry out these programs. For example, in fiscal years 2017 and 2018, the Department spent an estimated \$183 million and \$193 million, respectively, on more than 1,100 contracts and agreements. However, we found that the Department did not follow some State procurement requirements for 22 of the 25 contracts we reviewed. In addition, the Department paid for some services without ensuring they were provided and contract requirements were met, and its payment processing does not consistently provide adequate oversight to ensure the appropriate use of public monies.

### Department did not follow some State procurement requirements for 22 of 25 contracts reviewed

The Department is required to follow statutes and rules that comprise Arizona's Procurement Code and State purchasing requirements established by the State's Procurement Office, which help protect the State's interests by increasing transparency, reducing costs to the State through competition, and helping prevent unethical conduct. Our review of a stratified random sample of 25 contracts for which the Department made payments in fiscal year 2017 identified several discrepancies where the Department incorrectly procured professional services, paid a contractor more than allowed, and did not follow key purchasing requirements. For example, the Department selected a GIS mapping services contractor for its Medical Marijuana Program without first establishing selection criteria, paid this contractor more than \$167,000 allowed by statute for a professional services contract, and inappropriately approved contract amendments that included unallowable tasks and exceeded allowable amounts. In addition, 11 of the 25 contracts we reviewed lacked conflict-of-interest statements for Department program staff involved in the procurement, and 4 of the 25 lacked sufficient justification for limiting competition. Because the Department lacked sufficient procedures to guide procurement staff in complying with these requirements, it is at risk for circumventing Procurement Code and not complying with State purchasing requirements.



Department did not maintain conflict-of-interest statements for **11 of 25** contracts reviewed.

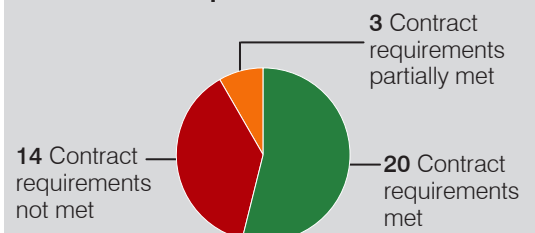
#### Recommendation

The Department should include policies and procedures in its draft procurement manual that help ensure compliance with the Procurement Code and purchasing requirements, complete the manual, and then implement it.

### Department paid for some services without ensuring they were provided and contract requirements were met

We reviewed a sample of 12 Department contracts reflecting nearly \$17.5 million in contract payments made during fiscal year 2017 and found that the Department did not ensure 17 of the 37 contract requirements we reviewed were met. For example, according to the Department, it did not withhold payments for 2 of the 12 contracts even though 1 contractor did not provide all of the specified services and the other provided services

#### Department did not ensure 17 contract requirements were met



without the required staff training to help ensure the expected quality of the services provided. In addition, we found that the Department inadequately monitored 5 of the contracts that received federal funding by not assessing subrecipient risk and inadequately conducting onsite reviews for 2 of these contracts. Finally, the Department did not adequately monitor spending for its GIS mapping services and exceeded the estimated costs for these services by more than \$390,000. By not ensuring that contractors meet all contract requirements, the Department risks paying for services that contractors did not provide or for contract requirements that were not met. The Department has not established policies and procedures to guide program staff's contract monitoring, and although some Department programs had developed their own monitoring practices, these monitoring practices were inadequate when compared to best practices.

## Recommendations

The Department should:

- Develop and implement contract-monitoring policies and procedures that specify and/or require staff roles and responsibilities for monitoring contracts; develop contract administration plans that outline monitoring activities for each contract, including specific and measurable terms in its contracts; and take appropriate action to address noncompliance.
- Develop and implement a centralized process for overseeing its programs' contract-monitoring efforts.
- Develop and implement policy and procedures for working with contractors to recover monies that may have been inappropriately paid and specify in what circumstances it will work with its Assistant Attorney General to recover these monies.

## Department's payment processing does not consistently provide adequate oversight to ensure appropriate use of public monies

To help protect State monies from loss, theft, waste, and abuse, the *State of Arizona Accounting Manual* recommends that State agencies implement various payment-processing practices and procedures. We reviewed a sample of 68 invoice payments totaling nearly \$4.9 million from 12 Department contracts with billing dates or reporting periods from May 2016 through October 2018 and identified concerns with several of the invoices that the Department processed. For example, the Department overpaid a contractor by more than \$12,500 for an invoice that lacked evidence of staff review and, for 5 of the 12 contracts we reviewed, paid more than \$4 million for services without obtaining and reviewing adequate supporting documentation to ensure the services were received. Finally, the Department did not consistently review and approve invoices prior to paying 8 of the 12 contractors. Although the Department has a process for reviewing invoices before paying them, this process does not ensure the Department pays for only authorized services, nor has it ensured that services were received before payment.



More than \$4 million paid without adequate supporting documentation

More than \$862,000 paid with adequate supporting documentation

## Recommendations

The Department should:

- Continue to develop and implement written payment-processing policies and procedures to better safeguard public monies.
- Require appropriate program staff to review supporting documentation before approving invoices for payment and document their review and approval of invoices and supporting documentation.
- Require supervisors to conduct a risk-based review of the invoices program staff approve.



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The Office of the Auditor General has released the second in a series of 4 performance audit reports of the Arizona Department of Health Services (Department). The first report (Report No. 19-107) focused on the Department's administration of the Medical Marijuana Program. This report focuses on the Department's processes for procuring goods and services through contracts, monitoring contracts and agreements to ensure requirements are met, and processing payments for contracts and agreements. The third report will focus on the Department's administration of the Arizona State Hospital (State Hospital), and the final report will focus on additional areas and provide responses to the statutory sunset factors.

## Department uses contracts and agreements to help accomplish major functions

The Department's mission is to promote, protect, and improve the health and wellness of individuals and communities in Arizona. To help fulfill this mission, the Department reported that it administers over 300 programs, such as the Special Supplemental Nutrition Program for Women, Infants and Children (WIC); the Immunization Program; and the Medical Marijuana Program.

State agencies are able to obtain goods and services that help accomplish mission-critical functions by entering into contracts and agreements with private and public entities (see textbox). The Department uses many such contracts and agreements to help accomplish its mission. For example, in fiscal years 2017 and 2018, the Department spent an estimated \$183 million and \$193 million, respectively, on more than 1,100 contracts and agreements (see Figure 1, page 2, which compares fiscal years 2017 and 2018 expenditures). These expenditures represented 40 to 43 percent of the Department's fiscal years 2017 and 2018 expenditures and

**Contract**—Refers to all types of State agreements for the procurement of materials, services, or construction. This includes Arizona State contracts (State-wide contracts), which are contracts established or authorized by the Arizona Department of Administration's (ADOA) State Procurement Office (SPO) for use by State government units such as State agencies.

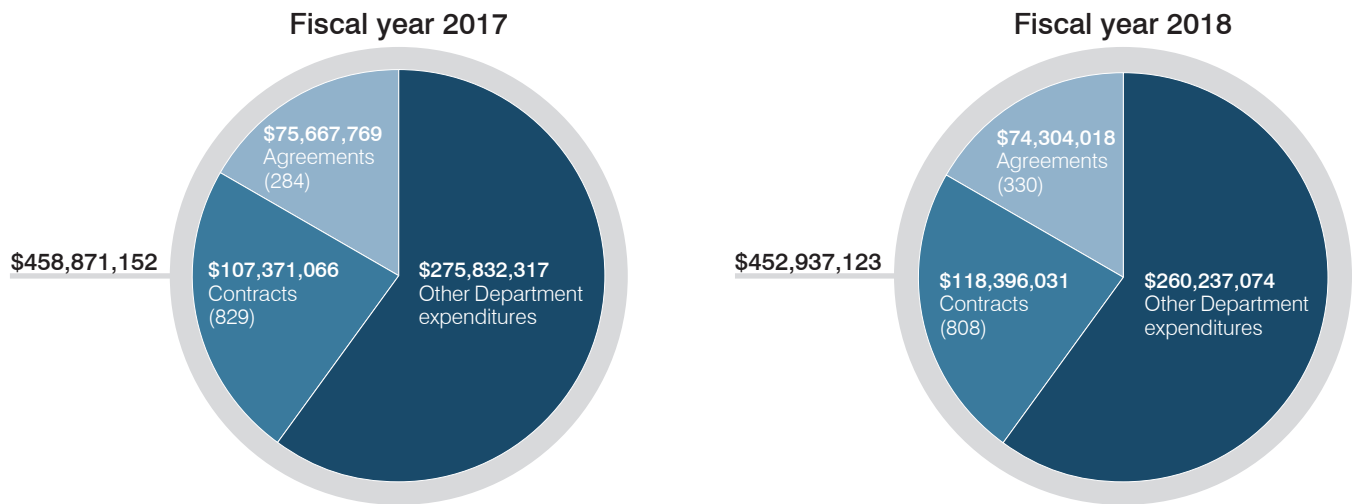
**Agreement**—A contract for services or cooperative action between 2 or more public agencies, such as State agencies, counties, and tribes. According to the Department, its agreements consist of:

- **Intergovernmental agreements (IGAs)**—Agreements for services between the Department and government entities, such as a county or tribe.
- **Interagency service agreements (ISAs)**—Agreements for services between the Department and other State agencies or State universities.

**Subrecipient**—A nonfederal, non-State entity (such as a not-for-profit or county) that receives federal monies through a contract or agreement (such as an IGA or ISA), grant, or donation to carry out part of a federal program or project and is largely responsible for its results.

Source: Auditor General staff summary of Arizona Revised Statutes (A.R.S.) §§11-951, 11-952(A), 41-2503(7), 41-2503(37); Arizona Administrative Code (AAC) R2-7-101(6), (47)&(48); *State of Arizona Accounting Manual (SAAM)*, and interviews with Department procurement staff.

**Figure 1**  
**Department contract and agreement expenditure estimates compared to all other**  
**Department expenditures for fiscal years 2017 and 2018**  
(Unaudited)



Source: Auditor General staff review of Arizona Financial Information System Accounting Event Transaction File for fiscal years 2017 and 2018 and State procurement system contract information.

are paid to contractors and subrecipients with both State monies and federal grant monies.<sup>1,2</sup> Although some of these contracts are for administrative support, such as office supplies and temporary staff, many contracts and agreements support agency functions or provide public services. For example:

- The Department has established agreements with 13 Arizona counties and contracts with 7 private health centers to administer the federal WIC Program, which provides food assistance, nutrition education, and breastfeeding support services to pregnant and post-partum women, infants, and children who are at nutritional risk and whose household income is at or below 185 percent of the federal poverty guidelines. The Department provides these services through contracts and agreements with health centers and counties throughout Arizona. The WIC Program reported that from October 2017 through September 2018, it served an average of more than 133,000 women, infants, and children each month, and during fiscal year 2018, it paid contractors and counties more than \$25 million for WIC services they provided.
- The Department has established agreements with all 15 Arizona counties and 2 cities to provide immunization-related services, such as providing immunization education outreach to schools and childcare facilities and helping pay for and provide immunizations to adults and children. For example, through these agreements, it pays monies for counties and cities to provide various immunizations such as Measles, Mumps, and Rubella (MMR); Diphtheria, Tetanus, and Pertussis (DTaP); and Polio. In fiscal year 2018, the Department paid more than \$3.7 million for immunization services State-wide.
- The Department has established a contract with a private contractor to provide software and support for a trauma registry system to help the Department fulfill its statutory duty to obtain patient data from all trauma centers State-wide to study the sources and causes of trauma and evaluate the cost, quality, efficacy, and appropriateness of trauma programs and services. As of April 2019, the Department's program that oversees

<sup>1</sup> In fiscal year 2017, federal grant funding accounted for more than \$258 million of the Department's total funding of \$453 million. The Department receives its other revenues from the State General Fund, fees, and other tax monies such as tobacco tax monies, which the Department uses to pay for contracts for reducing tobacco usage in the State.

<sup>2</sup> According to the Department, as of April 2018, it had received federal grants from multiple federal agencies, including the United States Department of Agriculture for the WIC Program and several grants from the United States Department of Health and Human Services.

the trauma registry system reported that there were 48 trauma centers throughout the State that participate and report data to its State-wide trauma registry. In fiscal year 2018, the Department paid \$49,500 for the trauma registry services contract.

- The Department has established various contracts for goods and services to assist with patient care at the State Hospital. The State Hospital provides long-term inpatient psychiatric care to Arizonans with mental illnesses who are under court order for treatment. These contracts provide various goods and services, such as clothing for patients and trash collection. In addition, because the State Hospital provides psychiatric care to individuals the courts designate as sexually violent persons, it contracts with psychiatrists to perform psychosexual screening and evaluation services and provide recommendations to courts related to decreasing a patient's restrictions or releasing a patient from the State Hospital. In fiscal year 2018, the Department spent approximately \$16.7 million on 180 contracts to assist with patient care at the State Hospital.
- The Department purchases geographic information system (GIS) mapping services for its Medical Marijuana Program. The Medical Marijuana Program is responsible for certifying nonprofit medical marijuana dispensaries and issuing registry identification cards to qualifying patients, caregivers, and medical marijuana dispensary agents. The GIS mapping contractor provides mapping services to help locate prospective dispensaries, qualifying patients, and operating dispensaries. In fiscal year 2018, the Department paid more than \$310,000 for GIS mapping services for its Medical Marijuana Program.

For more information on our review of the contracts and agreements associated with these programs and services, see Findings 1 through 3, pages 7 through 24.

## State Procurement Code and procurement policies establish purchasing requirements

The State Procurement Code (Code) is a compilation of statutes and rules that govern State agency contracting and purchasing.<sup>3</sup> SPO is responsible for reviewing State agencies' compliance with the Code and developing procurement policies that further govern purchasing in the State. For example, State agencies are required to competitively solicit proposals or bids for contracts unless the agency has legitimate reasons to limit competition. The Code also requires agencies to use existing State-wide contracts to meet the agency's needs for goods and services that may be available through these contracts. In addition, SPO delegates specific authority to conduct procurements and enter into contracts. For example, SPO may delegate unlimited procurement authority to some State agencies while limiting other State agencies' procurement authority. For procurements that will exceed a State agency's delegated procurement authority, SPO must conduct these procurements. As of August 2018, SPO granted the Department's chief procurement officer unlimited procurement authority allowing the Department to establish contracts for any amount without SPO's permission, including contracts for more than \$1 million.

During fiscal year 2017, the Department paid approximately \$107.4 million for all contracted goods and services. This consisted of more than \$37 million for State-wide contracts, more than \$43 million for contracts that it competitively solicited, and approximately \$26 million for limited competition contracts that it procured (see Figure 2, page 4).<sup>4</sup> For each type of contract, the Code requires the Department to comply with the following:

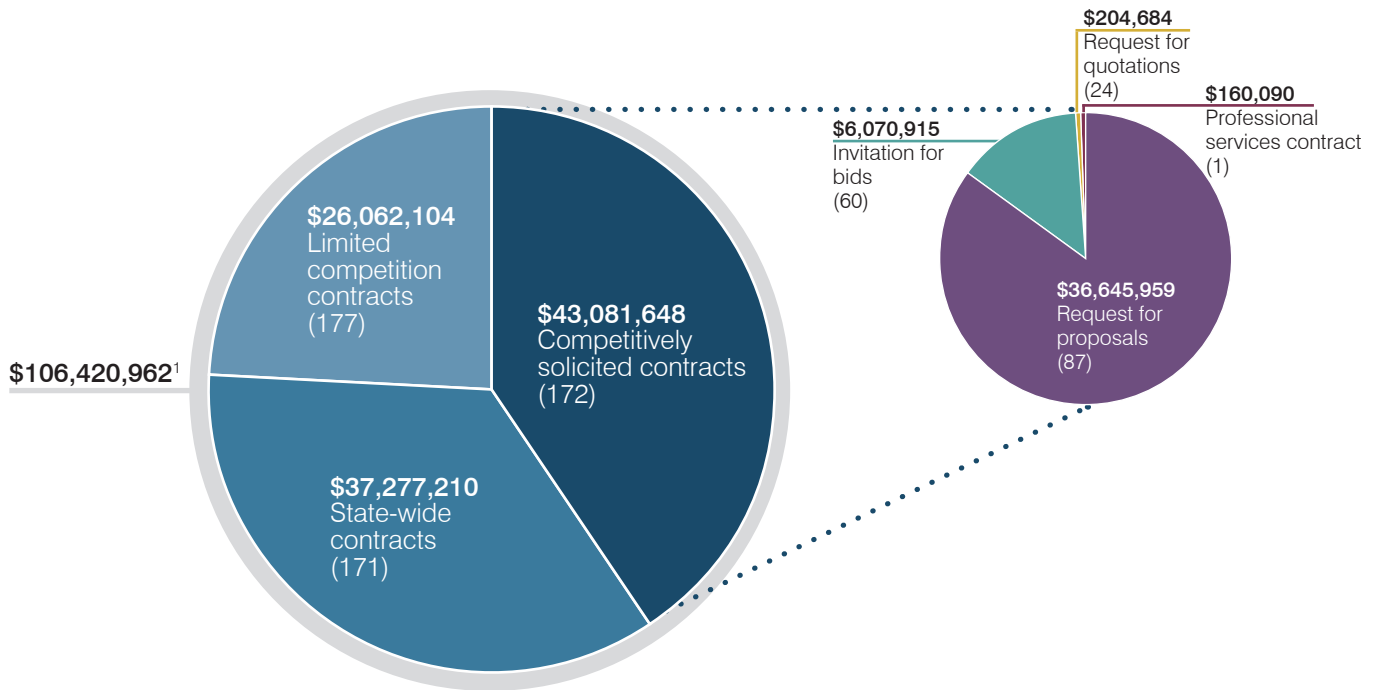
- **Required use of State-wide contracts**—When State-wide contracts are available, the Department is required to use these contracts for purchasing goods and services, such as office supplies and temporary staffing services.<sup>5</sup> According to SPO, State-wide contracts can provide State agencies with a better price or value on frequently purchased goods or services that many State agencies use.

<sup>3</sup> The Code is found in A.R.S. §41-2501 et seq and AAC R2-7-101 et seq. These requirements apply to most state agencies except those agencies that are exempted by A.R.S. §41-2501.

<sup>4</sup> Fiscal year 2018 data was not completed and available at the time of the analysis.

<sup>5</sup> AAC R2-7-607.

**Figure 2**  
**Estimated Department contract payments by contract type**  
**Fiscal year 2017**  
(Unaudited)



<sup>1</sup> This amount does not include \$950,104 in contract spending related to 309 contracts that lacked documentation in the State's procurement system identifying which procurement type was used.

Source: Auditor General staff review and analysis of the Arizona Financial Information System *Accounting Event Transaction File* for fiscal year 2017 and State procurement system contract information.

- **Competitively solicited procurement requirements**—If a State-wide contract is not available to provide the needed goods or services, the Code includes requirements for how contracts may be established to help the State obtain the best value from contracts by fostering competition among contractors.<sup>6</sup> In addition, it includes requirements for handling purchases based on the dollar threshold of the planned purchase. For example, for purchases valued at:
  - \$100,000 or greater—The Department must issue invitations for bids (IFB) or requests for proposals (RFP) to contractors. The Department must award the contract to the lowest bidder of an IFB or to the proposal received in response to an RFP that is determined in writing to be the most advantageous to the State. In addition, if seeking professional services, such as architect or engineer services, the Department may use a modified solicitation process described in the Code.
  - \$10,001 to \$99,999—The Department must issue a request for quotation (RFQ) to a minimum of 3 small businesses and award the contract to the offer the Department determines most advantageous to the State.
  - \$10,000 or less—The Department can make small dollar purchases of \$10,000 or less in a few ways. For example, the Department may award a contract using reasonable judgment and is not required to obtain competitive quotes but may request quotes from potential bidders if it chooses. State agencies may also

<sup>6</sup> A.R.S. §§41-2533 through 41-2535; and AAC R2-7-D301 through R2-7-D304.

use authorized purchasing cards to pay for purchases totaling \$10,000 or less in accordance with the *State of Arizona Accounting Manual (SAAM)*.

- **Limited competition requirements**—The Code describes circumstances under which State agencies may limit competition.<sup>7</sup> Specifically, a State agency may enter into competition impracticable or sole source contracts if competitive bidding is not in the State's best interest (see textbox).<sup>8</sup> For example, the Department has a sole source contract for maintenance services and supplies for the State Laboratory, which the Department oversees. The State Laboratory uses specific equipment and machines to perform its functions, such as identifying and investigating infectious and communicable diseases State-wide. The Department determined it was in the State's best interest to limit competition for the contract when it found only 1 supplier was available for the needed services and supplies.

### Examples of limited competition contracts

**Competition impracticable**—A contract that cannot be competitively bid because competitive bidding is impracticable, unnecessary, or not in the public's best interest.

**Sole source**—A contract that cannot be competitively bid because there is only 1 source or no reasonable alternative exists for the good or service.

Source: Auditor General staff review of AAC R2-7-E301 and R2-7-E303.

## Department's central procurement office helps Department divisions and programs procure contracts and establish agreements

The Department has established a central procurement office that helps Department programs identify and develop contract scopes of work and terms, and comply with procurement requirements, such as appropriately promoting competition for contracts. The procurement office also helps Department programs establish agreements with counties and other government entities to provide various goods and services. Figure 3 (see page 6) illustrates the procurement office's process for working with Department programs to procure contracts and establish agreements.

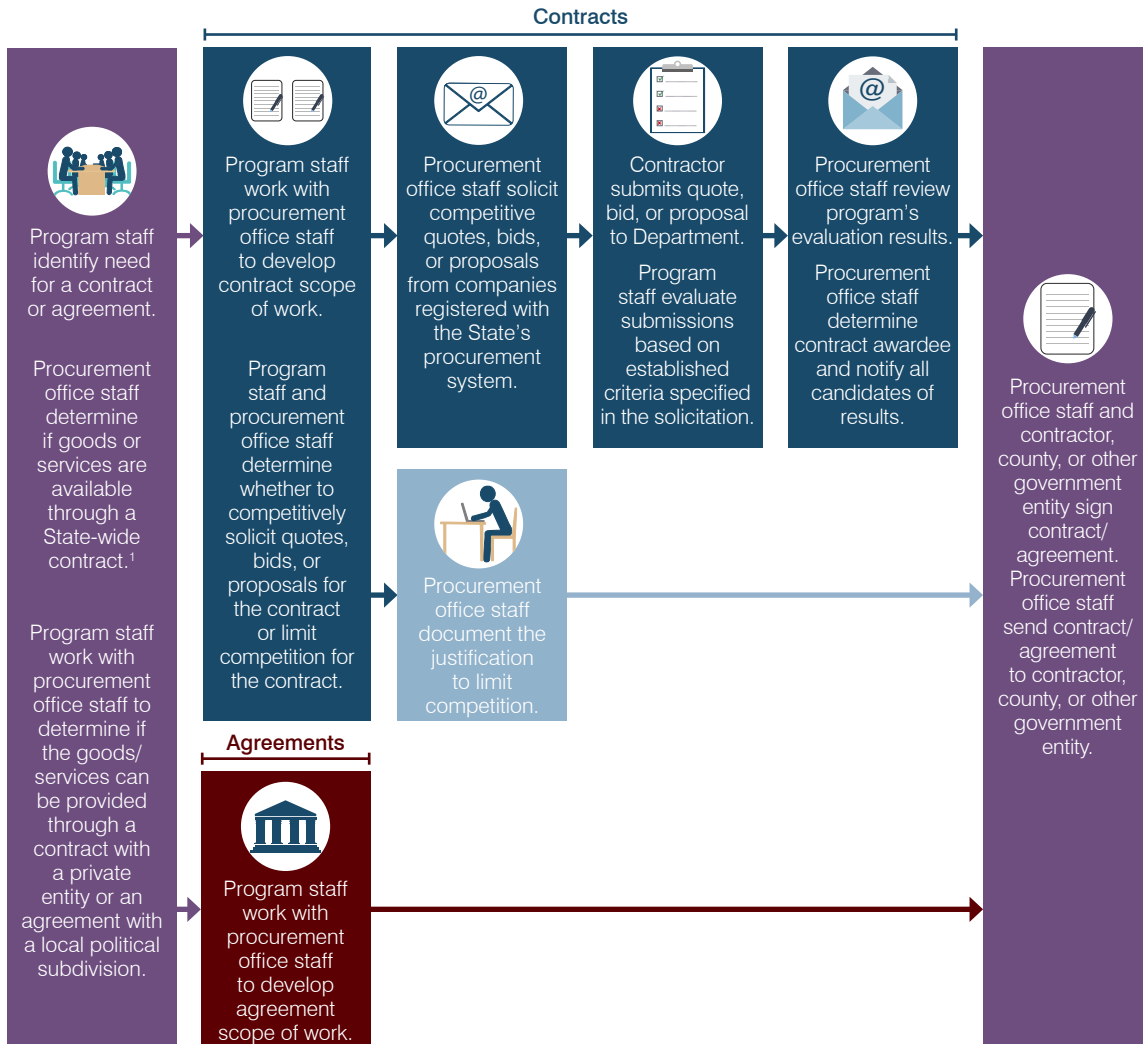
## Department programs responsible for monitoring contracts and agreements and reviewing invoices before contractors receive payment

The Department holds its various programs responsible for monitoring its contracts and agreements (see Finding 2, pages 15 through 19, for more information on the Department's process for monitoring contracts/agreements). In addition, the programs are responsible for reviewing invoices to ensure contractors have provided the required goods and services before approving invoices for payment (see Finding 3, pages 21 through 24, for more information regarding payment processing).

<sup>7</sup> A.R.S. §41-2536, AAC R2-7-E301, and R2-7-E303.

<sup>8</sup> The Code allows limited competition procurements in 3 situations: when only 1 vendor offers the good or service, under unusual or unique procurement situations, or in emergency situations. In addition, SPO must approve limited competition contracts that exceed a State agency's procurement authority. However, the Department's unlimited procurement authority allows it to approve limited competition contracts.

**Figure 3**  
**Department process for procuring contracts and establishing agreements**



<sup>1</sup> If the goods and services are available through a State-wide contract, State agencies do not have to establish a contract and will purchase goods and services through the existing contract.

Source: Auditor General staff review of Department procurement policies and procedures and interviews with Department staff.



## Department did not follow some State procurement requirements for 22 of 25 contracts reviewed

### Procurement requirements help protect the State

As discussed in the Introduction (see pages 3 through 6), the Department is required to follow the Code, a compilation of statutes and rules that govern State purchasing. The Department is also required to follow procurement policies established by SPO when it procures contracts. State purchasing requirements help protect the State's interests by increasing transparency, reducing costs to the State through competition, obtaining the best value for its monies, and preventing unethical conduct. For example, the Code requires competition for most purchases totaling more than \$100,000 and prohibits individuals with conflicts of interest from participating in contractor selection.<sup>9,10</sup>

The Code also requires the Department to purchase goods and services totaling more than \$100,000 using competitive solicitations such as an RFP or an IFB (see textbox on page 8 for more information on these types of solicitations).<sup>11</sup> These types of solicitations can provide for increased competition, generate more options among competing proposals for identifying the best goods and services, the cheapest prices, or most advantageous purchases for the State, and can maximize the purchasing value of State monies. The Code also allows the Department to purchase professional services, such as architect and engineer services, through a professional services contract that requires less competition than an IFB or RFP.<sup>12</sup> Although a professional services contract is solicited competitively, this type of solicitation would allow the Department to select a contractor from a list of contractors prequalified by SPO.

### Department incorrectly procured professional services and paid contractor more than allowed

We reviewed a stratified random sample of 25 of the 349 Department contracts for which the Department made payments in fiscal year 2017, including 13 competitively bid contracts and 12 limited competition contracts (see Appendix B, pages b-1 through b-2, for more information on the sample selection). Although the Department made payments for 1,113 contracts and agreements in fiscal year 2017, we excluded agreements from the sampled population that are not subject to the procurement code, State-wide contracts generally procured by the ADOA, and contracts lacking documentation in the State's procurement system.<sup>13</sup> Our review identified 1 contractor that

<sup>9</sup> A.R.S. §§41-2533, 41-2534, and 38-503(A).

<sup>10</sup> Competition may also be limited for exceptions described in the Introduction on page 5.

<sup>11</sup> A.R.S. §§41-2533 and 41-2534.

<sup>12</sup> A.R.S. §41-2581.

<sup>13</sup> Auditors' stratified random sample was selected from among the 1,113 contracts and agreements for which the Department made payments in fiscal year 2017. Of these, we excluded the 284 agreements that are not subject to procurement code, the 171 State-wide contracts that are generally procured by the ADOA, and 309 contracts that lacked documentation in the State's procurement system identifying which procurement type was used, were for purchases totaling less than \$10,000, and/or involved purchases of goods and services that appeared reasonable for the Department's purposes. We selected our sample from the 349 remaining contracts (see Appendix B, pages b-1 through b-2, for more information on the sample selection).



## Examples of competitive solicitations

**IFB**—An invitation for bid process is used for purchases totaling \$100,000 or greater, when price is the key determining factor. The agency must evaluate the bid to determine whether it conforms to the requirements in the invitation and award the contract to the lowest priced bidder.

**RFP**—A request for proposal process is used for purchases totaling \$100,000 or greater, when best value is considered over lowest price. The agency must evaluate the bid and award the contract to the proposal it determined in writing was most advantageous to the State based on evaluation factors in the proposal. For example, evaluation factors could include the most experience, price, and/or the best overall method of providing the goods or services specified in the RFP.

**RFQ**—A request for quotation may be used for purchases between \$10,000 and \$100,000. The agency is required to solicit these quotes from at least 3 small businesses.

**Professional services**—A professional services contract may be used to obtain professional services, such as architect services for amounts less than \$250,000 and engineer services for amounts less than \$500,000. Agencies may identify potential contractors from a list of prequalified contractors that SPO establishes based on its review of requests for qualifications. To contract with a professional services contractor on SPO's list, the agency must form a selection committee that will identify contractors that provide the desired services. The selection committee must review the contractors' qualifications and select at least 3 to notify of the procurement opportunity. The agency will review offers, interview contractors, and make a selection based on competence and qualifications.

Source: Auditor General staff review of A.R.S. §§41-2533, 41-2534, 41-2535, and 41-2581; AAC R2-7-D302; and SPO technical bulletins.

the Department paid without following some purchasing requirements. Specifically, the Department spent more than \$667,000 as of November 2018 for GIS mapping services without adhering to the following purchasing requirements:

- **Selected contractor without establishing selection criteria**—The Code requires State agencies to evaluate bids and proposals from potential contractors based on various criteria (see textbox above for examples of criteria for competitive solicitations). For example, State agencies must select the offer most advantageous to the State from among proposals received through an RFP or, if the contract is solicited through an IFB, agencies must select the lowest-priced bidder that meets the IFB's qualifications, such as a contractor that provides staff who have professional licenses.<sup>14</sup> In addition, when State agencies procure contracts for professional services, such as architect or engineer services, the Code requires agencies to evaluate offerors based on criteria the agency established and published and select the contractor based on qualifications rather than the contractor's proposed fees or price.<sup>15</sup>

However, the Department did not establish criteria for selecting GIS mapping services or evaluate the proposals based on any established criteria. Specifically, the Department requested services but did not include any criteria in its request that it would use to evaluate proposals and select a contractor. As a result, it did not evaluate the 2 proposals it received to provide GIS mapping services based on any established criteria. Without establishing and publishing written criteria and evaluating the proposals based on that criteria, the Department cannot demonstrate that it selected the contractor best able to provide the services it requested. Absent any criteria, the Department selected the contractor with the lowest-priced proposal.

- **Exceeded the authorized statutory spending limit for this contract type**—The Code limits spending on a professional services contract to \$500,000.<sup>16</sup> To obtain professional services for amounts more than \$500,000, agencies must contract using another type of competitive solicitation, such as an RFP or IFB, that

<sup>14</sup> A.R.S. §§41-2533(G) and 41-2534(G).

<sup>15</sup> A.R.S. §41-2581(B).

<sup>16</sup> A.R.S. §41-2581 (A)(B) limits spending on professional services contracts to no more than \$500,000 and further limits contract spending for professional services by an architect or architect firm to \$250,000.



helps ensure that the State agency has promoted adequate competition as required by the Code. For the GIS mapping services contract, the Department exceeded this statutory spending limit by more than \$167,000 as of November 2018. According to the Department, it was not aware of the \$500,000 limit and did not expect to spend more than that amount (see Finding 2, page 17, for more information). After we brought this issue to the Department's attention during the audit, the Department awarded a new GIS mapping contract in March 2019 to the same contractor using an RFP process.<sup>17</sup>

- **Inappropriately approved contract amendments that included unallowable tasks and exceeded allowable amounts**—The Code allows agencies to amend contracts if the price of the services the amendment authorizes was evaluated in the contractor's original offer.<sup>18</sup> In addition, the Department may amend contracts to include services that were not evaluated in the original contract and exceed more than 25 percent of the original contract amount only if SPO determines in writing that the amendment is advantageous to the State and the price is determined to be fair and reasonable.

However, in February 2018, the Department signed a contract amendment for its GIS mapping services contract that included some services that were not in the contractor's original proposal, such as services to map historical qualifying patient addresses. Program staff could not provide a clear explanation regarding the purpose of these additional services. As of November 2018, the Department had paid the contractor nearly \$50,000 for mapping historical qualifying patient addresses. In addition, the amendment's agreed-upon prices exceeded the amount authorized by the Code. Specifically, this amendment totaled more than \$233,000, which is nearly 480 percent more than the contractor's original contract proposal of \$40,280 and greatly exceeded the 25 percent limit. The Department also failed to notify and obtain a written determination from SPO that the amendment's price was fair and reasonable and that it was advantageous to the State.

In May 2018, the Department signed a second amendment to the contract, which also did not comply with the Code because it included services not in the original contract proposal. Specifically, through this amendment, the Department requested and authorized the contractor to provide more than \$3,000 of mapping services for vital statistics. According to program staff, this amendment was intended to assist the Department's Vital Statistics Program and would not be paid for by the Medical Marijuana Program. As of March 2019, the Department had not paid for any vital statistics mapping services.

- **Lacked a signed contract and unclear if contract terms were established**—According to the National State Auditors Association's (NSAA) best practices for contracting for services, contracts for services should be formal written documents that identify responsibilities of the parties to the contract, clearly state and define the scope or statement of work and contract terms, and contain appropriate signatures or approvals.<sup>19</sup> In addition, SPO has developed a standard procedure for documenting contracts and amendments, which requires the contract file to include important documentation that describes contract terms, such as contract specifications or a statement of work expected from the contractor and an offer and acceptance of the award, which is a document that allows both parties to acknowledge and agree to the contract terms.

However, the Department's documentation for the GIS mapping services did not clearly demonstrate that a contract had been established and that contract terms were developed and agreed upon. For example, the Department had not developed a detailed statement of work or specific terms and conditions, such as each party's responsibilities, a contract termination date, or when and how invoices should be received. Instead, the Department's procurement file for this contract contained a 1-page project summary of the requested GIS mapping services and a copy of the uniform terms and conditions document that the ADOA makes available to all State agencies. In addition, this file contained the contractor's revised cost estimate and project proposal document, which included anticipated time frames for providing services, a description of the proposed methods for some of the tasks, and a cost estimate with hourly contractor staff rates. However,

<sup>17</sup> The Department received and evaluated 6 responses prior to awarding the new contract.

<sup>18</sup> AAC R2-7-101 and R2-7-604.

<sup>19</sup> National State Auditors Association (NSAA). (2003). *Contracting for services: A National State Auditors Association best practices document*. Lexington, KY.

it was unclear if both parties acknowledged and accepted this cost estimate and project proposal because the Department lacked an offer and acceptance of award and signatures from both parties.

The Department's February 2018 amendment to the contract also lacked clear terms and an explanation of the agreed-upon services. Specifically, this amendment added new tasks, such as mapping to update historical qualifying patient and caregiver addresses, and the overall spending anticipated for these tasks, but did not explain what this work would entail, why it was being performed, when it was due, or the price per unit for these services. Without clear terms and an explanation of the agreed-upon services, Department staff lacked the information needed to ensure the contractor provided services for the agreed-upon price. For example, in April 2017, the GIS mapping services contractor charged \$0.56 per address to update caregiver and dispensary addresses, while in May and June 2017, it charged \$0.29 and \$0.38 per address, respectively, for this service. However, we could not determine whether these amounts were correct because the amendment lacked information about the unit prices for mapping caregiver and dispensary addresses. As of November 2018, the Department had paid more than \$26,000 for this service, which was twice the anticipated spending amount indicated in the amendment for this service.

## Department did not follow other key purchasing requirements

Our review of Department contracts also identified other discrepancies in 22 of the 25 contracts we reviewed in which the Department did not follow 1 or more key purchasing requirements (see Appendix B, pages b-1 through b-2, for more information on the sample selection). These discrepancies demonstrate the Department's failure to follow all purchasing requirements, adequately protect the State, and appropriately safeguard State monies. Specifically, the Department:

- **Lacked conflict-of-interest disclosure statements for Department program staff involved in procuring 11 contracts**—

The Code requires agency staff to disclose conflicts of interest and refrain from participating in contract decisions if they have a substantial interest.<sup>20</sup> In addition, SPO policies require procurement personnel to sign an annual conflict-of-interest disclosure statement and maintain these statements in a file (see textbox). These policies also require staff with a significant role in developing or evaluating a contract to sign a conflict-of-interest disclosure statement when a procurement begins. However, for 11 of the 25 contracts we reviewed, the Department lacked conflict-of-interest disclosure statements for all Department program staff who participated in the procurement and assisted in contractor selection. In addition, the Department did not have calendar year 2018 annual conflict-of-interest statements on file for 1 of the 19 procurement office staff we reviewed. Department management could not provide an explanation for why these disclosures were missing.

Without signed disclosure statements, the Department is unable to assure the public that it considered potential conflicts of interest and that Department staff did not improperly use their position for their or their relative's benefit. Further, because conflicts of interest can result in issues

**Conflict-of-interest disclosure statement**—Document on which a Department employee who has or whose relative has a substantial interest (i.e., financial) in a contract, sale, purchase, service, or decision discloses this interest. Statute and procurement policy requires employees to disclose conflicts of interest; requires statements to be signed and retained for State agency staff who have a significant role in a procurement, such as evaluating bids for a contract; and requires State agency staff to disclose any substantial interest in a contract at the outset of a procurement (see Appendix A, pages a-1 through a-2, for the SPO-prescribed conflict-of-interest form).

Source: Auditor General staff review of A.R.S. §§41-2503.36 and 38-502(A) and SPO procurements procedures and technical bulletins.



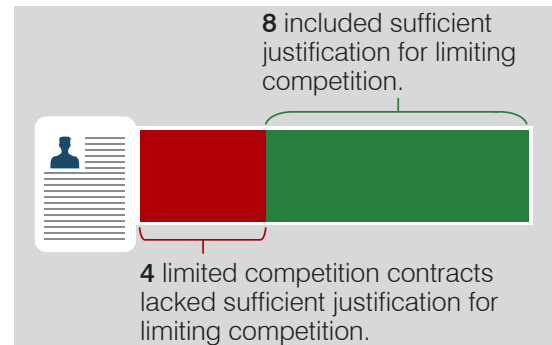
Department did not maintain conflict-of-interest statements for **11 of 25** contracts reviewed.

<sup>20</sup> A.R.S. §38-503(A).

such as inferior goods or services, higher contract costs, significant contract changes, and unnecessary purchases of goods or services, missing disclosure statements can put the Department at risk for these issues.<sup>21</sup>

- **Lacked sufficient justification for limiting competition for 4 contracts**—The Code allows agencies to limit competition if they use a State-prescribed process and can justify limiting competition (see textbox in Introduction, page 5, for descriptions of limited competition contracts). In addition, SPO has delegated authority to the Department’s chief procurement officer to approve the use of limited competition contracts at the Department.<sup>22</sup> When procuring a limited competition contract, an agency must demonstrate it protected the State’s interests by documenting explanations for why limiting competition is necessary, such as evidence that there is only 1 contractor in the State who can provide a good or service, and evidence of its efforts to seek other sources.<sup>23</sup> These requirements can help to ensure agencies do not unnecessarily limit competition and select a contractor that is more costly or less qualified than other available contractors.

However, we reviewed 12 contracts for which the Department limited competition and found that the Department did not provide sufficient justification for limiting competition for 4 of these contracts. Specifically, for these 4 contracts, the Department lacked documentation supporting and/or its documentation lacked explanations for why limiting competition was in the State’s best interest.



- **Did not provide required notification to its staff that it was beginning the solicitation process for 20 contracts**—Statute and purchasing policies require the Department to notify all Department staff in a prescribed manner when it initiates a procurement.<sup>24</sup> However, 20 of the 25 contracts we reviewed lacked evidence that the Department notified all of its staff of these procurements. The Department was unable to provide an explanation for why it did not provide these notifications.

According to SPO management, this requirement helps inform those responsible for a procurement that it has officially begun and helps prevent any Department staff from inadvertently and inappropriately providing information to a potential contractor that would give an unfair advantage during the procurement process. Without this notification, a Department staff person could be contacted by a contractor and inadvertently provide the contractor with information that other potential contractors do not have, which may provide the contractor with an unfair advantage.

- **Used an expired contract**—In addition, the Code allows agencies to procure contracts for goods and services for up to 5 years.<sup>25</sup> The Department authorized a limited competition contract for a trauma registry system for 4 years, and this contract expired in November 2017 with an option to extend it until November 2018 through a contract amendment. Although the Department did not extend this contract beyond November 2017 through such an amendment, it continued to request services from the contractor after the contract expired and paid monies to the contractor through fiscal year 2018. Operating under an expired contract puts the Department at risk because the costs and terms of the services being received are uncertain. In January 2019, during the audit, the Department entered into a new 1-year limited competition contract with this contractor for the trauma registry system.

<sup>21</sup> Association of Government Accountants. (n.d.). *Contract management*. Retrieved 10/5/18 from <https://www.agacgfm.org/Tools-Resources/intergov/Fraud-Prevention/Tools-by-Business-Process/Contract-Management.aspx>.

<sup>22</sup> As discussed in the Introduction (see page 3), as of August 2018, SPO had delegated unlimited procurement authority to the Department.

<sup>23</sup> AAC R2-7-E301 et seq.

<sup>24</sup> A.R.S. §41-753(D), SPO Technical Bulletin No. 10, and SPO standard procedures.

<sup>25</sup> A.R.S. §41-2546.

## Department lacks sufficient procedures to guide procurement staff

Although the Department has developed a draft procurement manual that contains some procedures, it has not consistently followed its procedures for requirements, such as obtaining staff conflict-of-interest statements, informing all Department staff when beginning the solicitation process, and documenting the statement of work and offer and acceptance of the award. In addition, the Department has not finalized this manual because, according to Department staff responsible for updating the manual, they are still adding information about the State's new procurement system, which was introduced in October 2018.

The draft manual also lacks some important guidance that would help ensure staff consistently comply with purchasing requirements, such as procedures for:

- Appropriately procuring professional services, including guidance for how to establish evaluation criteria, under what circumstances it will use a professional services contract, and how to document this procurement, including the statement of work and offer and acceptance of the award.
- Approving only contract amendments that include goods and/or services considered in the original solicitation and amounts allowed by the Code unless otherwise determined in writing by SPO.
- Justifying limited competition contracts, including factors staff may consider when determining to limit competition, how to determine the price is fair and reasonable, and how to document why limiting competition is in the State's best interest to document these efforts and decisions.
- Tracking the completion of each procurement step to ensure all required procurement steps were performed.
- Tracking contract spending and contract expirations to prevent Department staff from spending more than is allowed per the contract type or using expired contracts.
- Conducting a supervisory review to help ensure the completion of key procurement steps, such as obtaining signed conflict-of-interest statements, informing all Department staff that a solicitation is beginning, and ensuring that both parties sign the contract offer and acceptance of award to finalize the contract.

As a result, the Department is at risk of circumventing and not complying with State procurement law.

During the audit, the Department reported that it began taking steps to improve its compliance with purchasing requirements by requiring staff to refer to a list of SPO procurement requirements as a checklist when developing every contract. This list includes purchasing requirements, such as obtaining conflict-of-interest statements and documenting the justification for limiting competition on applicable contracts, and indicates whether a supervisor has reviewed the checklist. However, this checklist does not provide guidance for how to properly comply with all purchasing requirements, such as how to procure professional services or ensuring amendments are approved only if they align with Code requirements.

Finally, the Department's procurement office management reported that the Department lacks a structured procurement training program. The absence of a structured training program has likely contributed to the procurement noncompliance issues we identified. In addition, there have been ongoing changes in the Department's procurement office staffing, which may have further contributed to the noncompliance issues we identified. For example, 3 different chief procurement officers and 1 interim chief procurement officer worked for the Department during the course of our audit.

### Recommendations

The Department should:

1. Include policies and procedures in its draft procurement manual that address issues identified in this finding to help ensure compliance with the Code and purchasing requirements. The Department's procurement manual should provide policies and procedures that require the following:

- a. Appropriately procuring professional services, including guidance for how to establish evaluation criteria, under what circumstances it will use a professional services contract, and how to document this procurement, including the statement of work and offer and acceptance of the award. In doing so, the Department should work with its Assistant Attorney General to determine how these contracts may be used to comply with the Code.
  - b. Approving only contract amendments that include requirements considered in the original solicitation and amounts allowed by the Code unless otherwise determined in writing by SPO.
  - c. Justifying limited competition contracts and documenting these efforts and decisions.
  - d. Tracking the completion of each procurement step to ensure all required procurement steps were performed.
  - e. Tracking contract spending and contract expirations to prevent Department staff from spending more than is allowed per the contract type or using expired contracts.
  - f. Conducting a supervisory review to help ensure the completion of key procurement steps, such as obtaining signed conflict-of-interest statements, informing all Department staff that a solicitation is beginning, and ensuring that both parties sign the contract offer and acceptance of award to finalize the contract.
  - g. Training appropriate staff on State procurement requirements and Department policies and procedures once they have been fully developed.
2. Complete its draft procurement manual and implement it.
  3. Modify the procurement checklist it began using during the audit to include guidance for missing procurement requirements, such as procuring professional services and ensuring contract amendments are approved only if they align with requirements in the Code and implement the use of the checklist, including supervisory review.

**Department response:** As outlined in its [response](#), the Department agrees with the finding, and will implement the recommendations.



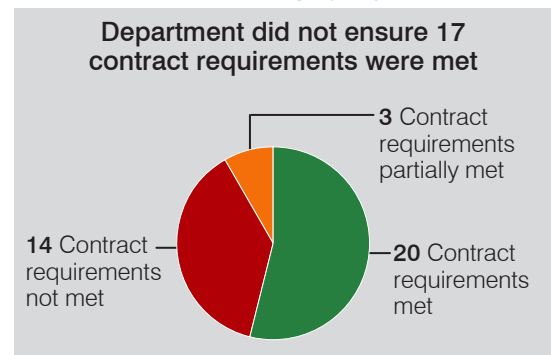


## Department paid for some services without ensuring they were provided and contract requirements were met

### Department did not always ensure requirements were met and inadequately monitored contracts supported by federal funding and contract spending

We reviewed a sample of 12 Department contracts and agreements (referred to as contracts in this finding) reflecting nearly \$17.5 million in contract payments during fiscal year 2017 and the Department's monitoring practices for a sample of 37 requirements within these contracts and determined that the Department had not adequately monitored these contracts and the associated requirements.<sup>26</sup> Specifically, the Department did not ensure some requirements were met, inadequately monitored some of its contracts that are supported by federal funding, and did not adequately monitor spending for 1 contract as follows:

- **Department did not ensure that 17 contract requirements were met and risks paying for services not provided**—Based on our review of the 37 requirements, we found the Department was unable to establish that 14 requirements were met and could establish that 3 requirements were only partially met. By not ensuring that contractors meet all contract requirements, the Department risks paying for services that contractors did not provide or for contract requirements that were not met. For example, according to the Department, it did not withhold payments to 2 of the 12 contracts we reviewed even though 1 contractor did not provide all of the specified services and the other contractor provided services without the required staff training to help ensure the expected quality of the services provided. The Department paid more than \$65,000 to these 2 contractors in fiscal year 2017. Specifically:
  - **Department's Community Health Nurse Program did not ensure nurses completed training/orientation requirements before working within community**—The Department contracts for specially trained community health nurses who provide home visits to high-risk infants, women, and children; health assessments of infants and children; and referrals to community resources. The contract requires the nurses to complete trainings/orientations in 12 required areas to ensure they are qualified to provide services within the community. However, we found that both nurses working for the program



<sup>26</sup> We selected 12 contracts and agreements for review from the 1,113 contracts and agreements for which the Department made payments in fiscal year 2017. This sample consisted of 7 of the 25 contracts from the stratified random sample described in Finding 1 (see page 7) which were selected to ensure we reviewed multiple divisions' contract monitoring practices; 4 of the 284 agreements for which the Department made payments in fiscal year 2017 that we judgmentally selected based on monies spent, the counties involved, and the Department programs responsible for the agreements; and 1 of 171 State-wide contracts the Department used in fiscal year 2017 that we judgmentally selected based on monies spent (see Appendix B, pages b-1 through b-2, for more information on the sample selection).



had not completed 4 of the trainings/orientations the contract required. These trainings/orientations cover areas such as conducting a supervised home visit, conducting an observation of a neonatal intensive care unit, and using specialized screening tools. By not ensuring that the nurses completed the required training, the nurses may not have been fully trained to provide the specified services in the community, and the contractor was in violation of the contract terms.



- **Department’s Trauma System Program did not ensure contractor met requirements for all 7 contract requirements we reviewed**—The Department contracts for a trauma registry system that contains patient data from all designated trauma centers State-wide to facilitate studying the sources and causes of trauma and to evaluate the cost, quality, efficacy, and appropriateness of trauma programs and services. This contractor provides data entry access and storage for each participating healthcare institution in the State and provides the Department with reporting capabilities using the trauma registry system’s data. However, the Department was unable to establish that the contractor met all 7 contract requirements we reviewed. For example, the Department could not demonstrate that the contractor had maintained updated security requirements, such as by performing vulnerability scanning and security assessments for web applications, which helps keep patient data secure by checking for security vulnerabilities in accordance with IT best practices. In addition, the trauma registry contract requires the contractor to establish a communication link that allows trauma registry facilities and hospitals to share patient records electronically. Although the contract required that the contractor complete the communication link by January 2015, as of July 2019, the contractor had yet to complete this communication link (see Finding 3, pages 21 through 22, for more information about this contract requirement being paid without being received). Further, the contractor was required to provide upgraded software at all participating institutions, but program staff could not provide documentation that the contractor completed this requirement for any of the institutions.<sup>27</sup>

- **Department inadequately monitored some of its contracts that federal funding supports**—According to the Code of Federal Regulations (CFR), agencies that receive federal monies and subsequently pass these monies on to subrecipients through contracts must monitor the subrecipients (see Introduction, page 1, for information on subrecipients).<sup>28</sup> The level of monitoring the oversight agency, such as the Department, provides should be based on an assessment of various risk factors, including the subrecipient’s prior experience, whether it has new personnel, and any prior audit findings.<sup>29</sup> Based on its risk assessment, the oversight agency can then determine the type of monitoring needed to provide reasonable assurance that the subrecipient is complying with federal regulations.<sup>30</sup> In addition, the CFR mentions several types of monitoring tools that may be used, such as audits and onsite reviews.<sup>31</sup>

Five of the 12 contracts we reviewed received some federal funding, and the Department paid more than \$13 million for these 5 contracts in fiscal year 2017. However, none of the 5 Department programs assessed subrecipient risk to determine how they would monitor these 5 contracts and the subrecipients associated with these contracts. Although the 5 Department programs had determined that onsite reviews were an important part of their monitoring activities and 1 of these programs was required by the CFR to conduct onsite reviews, some of these programs did not adequately conduct these onsite reviews. Specifically, 1 of

<sup>27</sup> According to program staff, there were 48 participating institutions as of April 2019.

<sup>28</sup> 2 CFR 200.62, 200.74, 200.86, 200.93, 200.303, and 200.331(d).

<sup>29</sup> 2 CFR 200.331(b).

<sup>30</sup> 2 CFR 200.303 and 200.331(e).

<sup>31</sup> 2 CFR 200.331(e)(2)(3).



the Department's 5 programs was not performing onsite reviews, and a second program was not performing all of the onsite reviews the CFR required.<sup>32,33</sup>

Noncompliance with the CFR could result in reduced future federal funding for the Department.<sup>34</sup> In addition, failure to perform adequate risk-based monitoring could prevent the Department from detecting contract noncompliance or from identifying unallowed expenditures.<sup>35</sup> For example, for the 1 program that was not performing onsite reviews, we identified issues with inadequate controls for expenditures for 1 of its subrecipients. Specifically, in fiscal year 2017, our Office reviewed expenditures for a Department Public Health Emergency Preparedness agreement with 1 county and found that \$19,364 of the subrecipient's purchases were not supported, not necessary, and/or not allowed.<sup>36</sup> As of July 2019, our Office is conducting a financial investigation of the county that is a subrecipient of this program to determine the amount of public monies misused, if any, and the extent to which those monies were misused. By not ensuring an appropriate level of monitoring, such as by assessing risk to determine the frequency and location of its onsite reviews, the Department could be at risk of further potential misuse of public funds.

- Department inadequately monitored spending for GIS mapping services**—As shown in Table 1, the Department exceeded the estimated costs for its GIS mapping services by more than \$390,000. Specifically, in March 2016, the GIS mapping contractor provided the Department with a \$40,280 cost estimate for its services, but as of February 2018, the Department had paid this contractor more than \$355,000, nearly 9 times the original estimated amount for these services. In addition, the Department's 2 contract amendments signed in February and May 2018 proposed spending an additional \$236,000 for other specified services, and similarly, as of November 2018, the Department had exceeded this amount by more than \$75,000. Our review found that the Department had not monitored its spending for these services to ensure that it stayed within the authorized spending amounts. The Department was also unable to explain why it did not seek a formal, competitive procurement for the GIS mapping services and, as discussed in Finding 1 (see pages 7 through 10), did not seek a formal, competitive procurement until we brought concerns with this contract to the Department's attention during the audit.

**Table 1**  
**Department Medical Marijuana GIS mapping services contractor payments exceeded anticipated spending as of November 2018**  
 (Unaudited)

Description	Proposed costs	Amount spent	Excess	Percentage of actual spending compared to proposed costs
Contract costs	\$ 40,280	\$ 355,218	\$ 314,938	882%
Tasks added in amendments	236,455	312,214	75,759	132%
<b>Total</b>	<b>\$276,735</b>	<b>\$667,432</b>	<b>\$390,697</b>	<b>241%</b>

Source: Auditor analysis of Medical Marijuana GIS mapping services contract, amendments, and payments to contractor.

<sup>32</sup> During the audit, in September 2018, the Public Health Emergency Preparedness Program began to conduct onsite reviews.  
<sup>33</sup> The Department's WIC Program is required to perform onsite reviews once every 2 years of at least 20 percent of the clinics in each local agency or 1 clinic, whichever is greater.  
<sup>34</sup> 2 CFR 200.338.  
<sup>35</sup> 2 CFR 200.62(c), 200.331(b), 200.331(2).  
<sup>36</sup> In September 2018, the county submitted documentation to the Department that it had reimbursed these monies.

## Department lacks policies and procedures for programs' contract-monitoring practices

Program staff are responsible for monitoring their respective contracts to ensure that all contract requirements are received and meet quality expectations. However, the Department had not established any policies and procedures to guide program staff's monitoring of contracts, and it had not required its programs to do so. In addition, the Department has not provided any oversight of its programs' contract-monitoring practices. Although some Department programs have developed monitoring practices, we found that these monitoring practices were inadequate when compared to contract-monitoring best practices. For example, the Department and its programs:

- **Have not developed written contract administration plans that outline monitoring activities**—Best practices for administering and monitoring contracts state that effective contract monitoring involves proper oversight throughout the term of the contract and recommends developing a written contract administration plan for each contract (see textbox).<sup>37</sup> A contract administration plan helps ensure that a contract is properly monitored throughout its term and that the contractor or subrecipient satisfied the contract's requirements. Monitoring with a contract administration plan also helps ensure that public monies are used for their intended purposes.

However, program staff did not develop a contract administration plan for any of the 12 contracts we reviewed. Additionally, although 2 Department programs had developed written contract-monitoring procedures, these procedures lacked various components of a well-developed contract administration plan, such as defined monitoring roles and responsibilities and the specific documentation needed to support compliance with all contract requirements.

**Contract administration plan (CAP)**—A tool for helping agencies monitor a contract that may specify critical information such as:

- Personnel responsible for monitoring the contract.
- Expected contract requirements.
- How to measure contractor performance.
- When contract requirements are due.
- Methods and time frames for reporting.
- Documentation required of contractor for contract requirements and payments.
- Key contract terms and conditions.
- Contract-monitoring methods.

Source: Auditor General staff review of NASPO, n.d.

- **Did not include specific, measurable terms and reporting requirements in the contracts**—The NSAA recommends contracts contain specific, measurable terms and reporting requirements as part of an effective monitoring system and that the contractors and subrecipients meet all contract requirements.<sup>38</sup> However, contract terms for 3 of the 12 contracts we reviewed lacked specific, measurable terms that would help program staff effectively monitor the contracts. For example, the GIS mapping contractor maps qualifying patients and revises locations of qualifying patients and dispensaries because of address changes and releases data as needed. The Department uses information obtained from the contractor to make decisions regarding issuing dispensary registration certificates. However, the Department lacks contract terms that specify how often to report the data, what types of data or reports the contractor should provide to the Department, or how the contractor should bill for these services.
- **Did not take action when contract requirements were not met**—NSAA best practices indicate that for effective contract monitoring, agencies should document that they received goods and services and that contractors met requirements, and should take action when contractors do not perform, such as withholding payment. However, Department programs did not have a method to determine whether contractors met contract requirements or a mechanism to track when contract requirements were due, and whether they took action to address noncompliance for 8 of the 12 contracts we reviewed. In addition, for 14 of the 37

<sup>37</sup> National Association of State Procurement Officials (NASPO). (n.d.) *Contract administration best practices guide*. Lexington, KY. Retrieved 6/15/18 from [https://www.naspo.org/Portals/16/CMGuide/NASPO-Contract\\_Administration\\_Best\\_Practices\\_Guide-f.pdf](https://www.naspo.org/Portals/16/CMGuide/NASPO-Contract_Administration_Best_Practices_Guide-f.pdf).

<sup>38</sup> NSAA, 2003.

requirements we identified that were not met, program staff did not take action to address the noncompliance such as withholding payment.

- **Had not tracked spending limits**—NASPO and the NSAA recommend monitoring spending patterns and comparing contractors' charges to contract terms.<sup>39</sup> However, some Department programs had not developed tools to track spending against contract-spending limits. Specifically, Department programs responsible for 6 of the 12 contracts we reviewed did not have a method to track contract-spending limits.

During the audit, the Department established policies and procedures for monitoring contracts that receive federal funding to help ensure its programs comply with CFR monitoring requirements. Specifically, in April 2019, the Department developed a policy for monitoring these contracts that requires its programs to incorporate a risk assessment to determine the level of monitoring the programs should provide to contractors and subrecipients. The Department reported that it began implementing this policy in May 2019.

## Recommendations

The Department should:

4. Develop and implement written policies and procedures to direct and guide its contract monitoring. Consistent with best practices, these policies and procedures should specify and/or require:
  - a. Program requirements and staff roles and responsibilities for monitoring contracts.
  - b. Developing a written contract administration plan outlining monitoring activities for each contract.
  - c. Including specific and measurable contract terms, and reporting requirements in the contracts.
  - d. Taking appropriate action to address noncompliance, such as withholding payment.
  - e. Developing and using tools and/or methods to effectively track completion of contract requirements, including spending.
5. Develop and implement a centralized process, including written policies and procedures, for overseeing its programs' monitoring efforts to ensure compliance with the contract policies and procedures it developed.
6. Develop and implement policy and procedures for working with contractors that will provide guidance on recovering any monies that may have been inappropriately paid, including specifying in what circumstances it will work with its Assistant Attorney General to recover these monies.
7. Continue to implement its newly developed policy for monitoring contracts that receive federal funding to ensure that its programs conduct risk assessments to determine the appropriate level of monitoring to perform for contractors or subrecipients.

**Department response:** As outlined in its [response](#), the Department agrees with the finding, and will implement the recommendations.

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<sup>39</sup> NSAA, 2003; NASPO, n.d.





## Department's payment processing does not consistently provide adequate oversight to ensure appropriate use of public monies

### Payment-processing requirements help protect public monies

To help protect State monies from loss, theft, waste, and abuse, the SAAM recommends that State agencies implement various payment-processing practices and procedures. For example, State agencies should review appropriate documentation for reasonable assurance that contracted vendors have provided required goods and services before paying for the invoiced goods and services. If a State agency's resources do not permit a review of all documentation that has been submitted to support billed costs, State agency management should consider a risk-based review approach. In addition, a person with approval authority and with the operational, procedural, and financial expertise to conduct the review should review and approve invoices and supporting documentation.

Further, statute requires the Department to comply with federal law and authorized regulations for any contracts involving federal monies and requires that payments not be made without a fully approved written contract.<sup>40</sup> Because federal monies support several of the Department's contracts, it must also adhere to applicable provisions of the CFR.<sup>41</sup> These regulations require the Department to have a process that provides reasonable assurance that payments are properly accounted for and in compliance with federal terms and conditions.<sup>42</sup>

### Department paid for unauthorized services, overcharges, and services without ensuring they were received

We reviewed a sample of 68 invoice payments totaling nearly \$4.9 million from 12 Department contracts and agreements (referred to as contracts in this finding) with billing dates or reporting periods from May 2016 through October 2018 and identified concerns with several of the invoices that the Department processed.<sup>43</sup> The following examples of unauthorized costs, overcharges, and paying for services without adequate documentation demonstrate that the Department has not always adequately safeguarded public monies. Specifically, the Department:

- **Paid for unauthorized services**—In January 2018, the Department paid \$10,000 for unauthorized services related to its Trauma System Program's trauma registry contract, which had expired (see Finding 2, page

<sup>40</sup> A.R.S. §§41-2637, 41-2513(E).

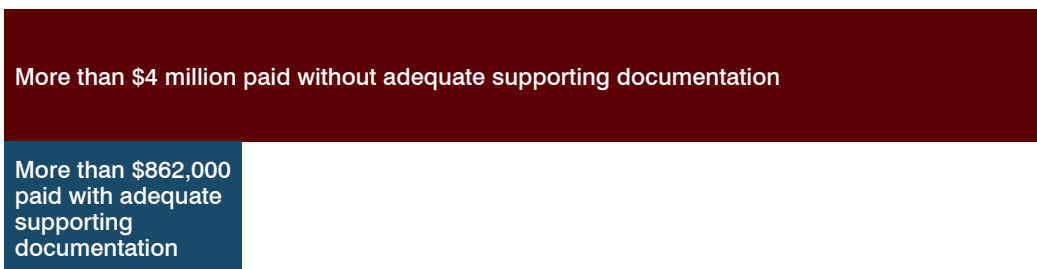
<sup>41</sup> 2 CFR 200.69, 200.74, 200.86, 200.93, 303, 200.331.

<sup>42</sup> 2 CFR 200.62.

<sup>43</sup> We selected 12 contracts and agreements for review from the 1,113 contracts and agreements for which the Department made payments in fiscal year 2017. This sample consisted of 7 of the 25 contracts from the stratified random sample described in Finding 1 (see page 7) which were selected to ensure we reviewed multiple divisions' contract monitoring practices; 4 of the 284 agreements for which the Department made payments in fiscal year 2017 that we judgmentally selected based on monies spent, the counties involved, and the Department programs responsible for the agreements; and 1 of 171 State-wide contracts the Department used in fiscal year 2017 that we judgmentally selected based on monies spent (see Appendix B, pages b-1 through b-2, for more information on the sample selection).

16, for more information). Specifically, the Department paid for a communication link so that emergency management system records and trauma registry system records could be interchanged. However, the Department's \$10,000 payment was a full prepayment to the contractor for the communication link, and as of July 2019, the communication link was yet to be established.<sup>44</sup> Program management reported that the contractor would not provide the communication link until it was paid in full but promised it would perform the work at an unknown later date. According to the SAAM, prepayments to nonpublic entities such as contractors are permitted only with the written consent of the State Comptroller.<sup>45</sup> However, the Department did not obtain this permission before paying the contractor, nor had the contractor established the communication link 1½ years after the Department prepaid the contractor.

- **Overpaid 1 contractor**—During the audit and as a result of our inquiries, the GIS mapping contractor reported it accidentally overcharged the Department by more than \$12,500 in October 2018, which represented more than one-third of the total invoice amount for that month. The Department had not required the contractor to submit supporting documentation with its invoice, and there was no evidence that program staff reviewed and approved the invoice for accuracy prior to payment. In November 2018, the contractor credited the full amount back to the Department. As mentioned in Finding 1, the Department exceeded the allowed limit on the contract by more than \$167,000 (see pages 8 through 9).
- **Paid contractors without ensuring services were received and costs were appropriate**—For some of the invoices we reviewed, the Department did not obtain adequate documentation to support receiving the indicated services before payment. Specifically:
  - **Department did not review adequate supporting documentation for invoices**—We found that for 5 of the 12 contracts we reviewed, the Department did not obtain and review adequate supporting documentation for invoices we reviewed totaling more than \$4 million.<sup>46</sup> For example, the Department paid Pima County more than \$785,000 for its Healthy People, Healthy Communities agreement for implementing “evidence based preventative health strategies” that Pima County provided for the period of January through June 2017. We reviewed 2 invoices from this time period and found that although Pima County provided the Department with a summary of charges on its invoices, the Department did not obtain supporting documentation to support the charges listed. According to the Department, it required Pima County to submit quarterly reports prior to approving invoices, but our review of these quarterly reports found they did not include specific documentation to support the charges. For example, 1 invoice we reviewed included charges for more than \$40,000 related to family planning services. Pima County's quarterly report narratively described providing various family planning services, including 8 Pima County staff attending a conference on adolescent issues such as drug abuse and violence, providing reproductive health education to 29 teens, and treating chlamydia in students at 4 sites where family planning services are offered. However, the Department did not obtain any supporting documentation to conduct a risk-based review of these activities, such as receipts for conference attendance, training attendance records for the reproductive health education, or the number and costs of treating the teens for chlamydia. Further, the staff person who was overseeing the program and authorizing the invoices



<sup>44</sup> Program staff reported they have requested a due date of December 31, 2019, from the contractor.

<sup>45</sup> The State Comptroller's written approval is not needed provided the payment meets multiple conditions, such as receiving the services within 1 year from providing payment.

<sup>46</sup> We determined that 1 contract did not require supporting documentation for its invoices because of the nature of its services—trash removal.

reported that he did not use the quarterly report contents to determine if he should authorize payment for the invoices.

Additionally, the Department paid Maricopa County more than \$2.5 million for WIC Program services from April through June 2017, but did not obtain and review supporting documentation for invoices paid during the period. Because the WIC program receives federal funding, this lack of review puts the Department at risk for paying costs that are not allowed by federal regulations, which could result in reduced future federal funding for the Department.<sup>47</sup>

Further, the Department paid the GIS mapping contractor more than \$667,000 for services billed from May 2016 through October 2018. The contractor provided monthly invoices to the Department averaging more than \$22,000 for its services, such as charges for mapping historical patient, caregiver, and dispensary addresses and developing unique address identifications. However, the Department did not obtain and review documentation, such as data and reports, to support that the invoiced services were provided before authorizing payment.

- **Department did not consistently review and approve invoices**—Invoices for 8 of the 12 contracts reviewed lacked consistent and documented program staff review and approval of the invoices. For example, the Medical Marijuana Program approved payments for 30 invoices with billing periods between May 2016 and October 2018, and 19 of the invoices totaling more than \$500,000 did not show program staff’s documented review and approval of invoices before payment. Typically, the Department’s program staff use signatures or initials to demonstrate the review and approval of invoice charges for appropriateness.

## Department lacks comprehensive payment-processing policies and procedures

Although the Department has a process for reviewing invoices before paying them, this process has not adequately ensured that the Department pays for only authorized services, nor has it ensured that services were received before payment. Specifically, the Department reported that its payment process requires program staff to review invoices, sign or initial the invoices to indicate review and approval, and submit invoices to a secondary reviewer who ensures monies are available for that payment. However, this process does not ensure supporting documentation is obtained or reviewed for invoices, or that each invoice is adequately reviewed and approved before payment. In addition, the Department has not documented this process in written policies and procedures.

Also, some program staff reported that they had not received training to guide their review of invoices. In the absence of policies and training, each Department program has developed varied, informal practices for reviewing and approving invoices. For example, although program staff signed or initialed all invoices for 4 of the 12 contracts we reviewed, for the remaining contracts, staff either did not sign or initial an associated invoice on at least 1 occasion or reported they sent an email to indicate they approved an invoice. In addition, only 3 of the 12 programs had developed written procedures for reviewing or obtaining supporting documentation.

During the audit, in April 2019, the Department developed a policy for reviewing invoices from contractors or subrecipients that receive federal funding. Specifically, the Department’s policy requires staff to monitor these contractors or subrecipients by reviewing and approving invoices and requiring all contractors or subrecipients to submit activity reports. According to Department management, it began implementing the new policy in May 2019. The Department reported that it has not developed a similar policy for reviewing invoices for contracts that do not involve federal funding.

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<sup>47</sup> 2 CFR 200.338 and 7 CFR 246.19(a)(2).



## Recommendations

The Department should:

8. Continue to develop and implement written payment-processing policies and procedures to better safeguard public monies and prevent payments for unauthorized services, overcharges, and paying for services without ensuring they were received by:
  - a. Requiring program staff with the expertise and knowledge about the contract requirements to obtain and review adequate supporting documentation prior to approving invoices for payment. In instances when resources do not permit a review of all supporting documentation, the Department should use a risk-based approach to review the supporting documentation.
  - b. Conducting a risk-based supervisory review of the invoices and supporting documentation that program staff approved.
  - c. Documenting program staff's invoice review and approval with a consistent approval method, such as initials, signatures, or another method, to show that they reviewed and approved the invoice and supporting documentation.
9. Train all appropriate staff on its payment-processing policies and procedures once they are developed.
10. Ensure that its various programs and program staff adhere to its payment-processing policies and procedures as part of overseeing its programs for compliance with its contract-monitoring policies and procedures as recommended in Finding 2.

**Department response:** As outlined in its [response](#), the Department disagrees with the finding, but will implement the recommendations.





# SUMMARY OF RECOMMENDATIONS

## Auditor General makes 10 recommendations to the Department

The Department should:

1. Include policies and procedures in its draft procurement manual that address issues identified in this finding to help ensure compliance with the Code and purchasing requirements. The Department's procurement manual should provide policies and procedures that require the following:
  - a. Appropriately procuring professional services, including guidance for how to establish evaluation criteria, under what circumstances it will use a professional services contract, and how to document this procurement including the statement of work and offer and acceptance of the award. In doing so, the Department should work with its Assistant Attorney General to determine how these contracts may be used to comply with the Code.
  - b. Approving only contract amendments that include requirements considered in the original solicitation and amounts allowed by the Code unless otherwise determined in writing by SPO.
  - c. Justifying limited competition contracts and documenting these efforts and decisions.
  - d. Tracking the completion of each procurement step to ensure all required procurement steps were performed.
  - e. Tracking contract spending and contract expirations to prevent Department staff from spending more than is allowed per the contract type or using expired contracts.
  - f. Conducting a supervisory review to help ensure the completion of key procurement steps, such as obtaining signed conflict-of-interest statements, informing all Department staff that a solicitation is beginning, and ensuring that both parties sign the contract offer and acceptance of award to finalize the contract.
  - g. Training appropriate staff on State procurement requirements and Department policies and procedures once they have been fully developed (see Finding 1, pages 7 through 13, for more information).
2. Complete its draft procurement manual and implement it (see Finding 1, pages 7 through 13, for more information).
3. Modify the procurement checklist it began using during the audit to include guidance for missing procurement requirements, such as procuring professional services and ensuring contract amendments are approved only if they align with requirements in the Code and implement the use of the checklist, including supervisory review (see Finding 1, pages 7 through 13, for more information).
4. Develop and implement written policies and procedures to direct and guide its contract monitoring. Consistent with best practices, these policies and procedures should specify and/or require:
  - a. Program requirements and staff roles and responsibilities for monitoring contracts.
  - b. Developing a written contract administration plan outlining monitoring activities for each contract.
  - c. Including specific and measurable contract terms, and reporting requirements in the contracts.

- d. Taking appropriate action to address noncompliance, such as withholding payment.
  - e. Developing and using tools and/or methods to effectively track completion of contract requirements, including spending (see Finding 2, pages 15 through 19, for more information).
5. Develop and implement a centralized process, including written policies and procedures, for overseeing its programs' monitoring efforts to ensure compliance with the contract policies and procedures it developed (see Finding 2, pages 15 through 19, for more information).
  6. Develop and implement policy and procedures for working with contractors that will provide guidance on recovering any monies that may have been inappropriately paid, including specifying in what circumstances it will work with its Assistant Attorney General to recover these monies (see Finding 2, pages 15 through 19, for more information).
  7. Continue to implement its newly developed policy for monitoring contracts that receive federal funding to ensure that its programs conduct risk assessments to determine the appropriate level of monitoring to perform for contractors or subrecipients (see Finding 2, pages 15 through 19, for more information).
  8. Continue to develop and implement written payment-processing policies and procedures to better safeguard public monies and prevent payments for unauthorized services, overcharges, and paying for services without ensuring they were received by:
    - a. Requiring program staff with the expertise and knowledge about the contract requirements to obtain and review adequate supporting documentation prior to approving invoices for payment. In instances when resources do not permit a review of all supporting documentation, the Department should use a risk-based approach to review the supporting documentation.
    - b. Conducting a risk-based supervisory review of the invoices and supporting documentation that program staff approved.
    - c. Documenting program staff's invoice review and approval with a consistent approval method, such as initials, signatures, or another method, to show that they reviewed and approved the invoice and supporting documentation (see Finding 3, pages 21 through 24, for more information).
  9. Train all appropriate staff on its payment-processing policies and procedures once they are developed (see Finding 3, pages 21 through 24, for more information).
  10. Ensure that its various programs and program staff adhere to its payment-processing policies and procedures as part of overseeing its programs for compliance with its contract-monitoring policies and procedures as recommended in Finding 2 (see Finding 3, pages 21 through 24, for more information).



## Arizona Department of Administration's procurement disclosure statement for personnel with a significant procurement role



ARIZONA DEPARTMENT OF ADMINISTRATION  
STATE PROCUREMENT OFFICE

### PROCUREMENT DISCLOSURE STATEMENT

*(Insert Solicitation # Here)*

*(Insert Solicitation Title Here)*

Dear Employee:

You have been selected to participate in the particular procurement activity as referenced above. Your selection was based on your technical knowledge and expertise in this area. Your regular job duties may not include procurement activities but for the purpose of this process you may play a significant procurement role in one or more of the following: participating in the development of a procurement as defined in ARS § 41-2503; participating in the development of an evaluation tool; approving a procurement as defined in ARS § 41-2503 or an evaluation tool; serving as a technical advisor or an evaluator who evaluates a procurement as defined in ARS § 41-2503; or recommending or selecting a vendor that will provide materials, services or construction to this state.

It is essential that the integrity of the procurement process be maintained to ensure that each Offeror is given fair and equal consideration. Your familiarity with particular brands, types of equipment, material, services, individuals or firms may tend to influence your evaluation; however, you are required in this specific instance to be particularly objective and guard against any tendency that might slant your evaluation in favor of a personal preference.

You are required to report to the Procurement Officer, or person facilitating the above referenced procurement process, any actual or potential conflict of interest as defined in A.R.S. § 38-503, § 41-2616C, § 41-753 and § 41-2517. You are also subject to the Code of Ethics set forth in Section R2-5A-501 of the Arizona Department of Administration, Personnel Division, Administrative Rules and Regulations.

An additional consideration is the legal mandate to maintain strict security and confidentiality regarding the content of any proposal, as well as the proceedings of the Evaluation Committee meetings during the evaluation process. Once the evaluation process has started, it is essential that any contact with Offerors, other than that disclosed, be through, and by, the Procurement Officer or person facilitating the above referenced procurement.

In addition, the Employee shall not have any communication related in any way to the particular procurement, except during formal Committee meetings, with any Offeror or potential subcontractor to that Offeror prior to award, nor shall that Member discuss the proposal or their evaluation with anyone other than the Procurement Officer, or person facilitating the above referenced procurement and Evaluation Committee Members. This is mandatory.

A person who holds a Significant Procurement Role as defined by ARS § 41-741 and § 41-2503 for a particular procurement shall sign a statement before starting any participation that the person has no financial interest in the procurement other than that disclosed and will have no contact with any representative of a competing Offeror related to the particular procurement during the course of evaluation of proposals, except those contacts specifically authorized by sections ARS § 41-2534, § 41-2537, § 41-2538 and § 41-2578. The person shall disclose on this statement any contact unrelated to the pending procurement that the person may need to have with a representative of a competing offeror and any contact with a representative of a competing offeror during evaluation of proposals except those contacts specifically authorized by sections ARS § 41-2534, § 41-2537, § 41-2538 and § 41-2578. A person who has been identified as having a significant procurement role for this procurement and fails to disclose contact with a representative of a competing offeror or who fails to provide accurate information on this statement is subject to civil penalty of at least one thousand dollars but not more than ten thousand dollars.

cc: Agency File

SPO Form 120 – Procurement Nondisclosure Disclosure Statement (rev 08/14)

**PROCUREMENT DISCLOSURE STATEMENT**

As mandated by A.R.S. § 38-503, I, \_\_\_\_\_, have listed on this form all ownerships, employments, public and private affiliations and relationships held by me and/or a relative<sup>1</sup> which may have a substantial (pecuniary<sup>2</sup> and proprietary<sup>3</sup>) interest as defined in A.R.S. § 38-502 (11) in any contract, sale, purchase or service involving the agency. I understand that as my interests or those of my relatives change, I may need to modify this statement.

The substantial interests, both pecuniary and proprietary, held by me and/or a relative which may involve the State include (attach additional sheets as necessary):

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During the course of my regular business, I may have contact, unrelated to this procurement, with the Offerors listed below, who have submitted proposals in response to this solicitation (attach additional sheets as necessary):

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<sup>1</sup>"Relative" means my spouse, child, child's child, parent, grandparent, brother or sister (of the whole or half-blood) and their spouses and the parent, brother, sister or child of my spouse.

<sup>2</sup>"Pecuniary" means money or economic or other benefits that can be valued in monetary terms

<sup>3</sup>"Proprietary" means ownership or rights by virtue of ownership, whether public or private.

Citations listed above are available on the SPO website, [www.spo.az.gov](http://www.spo.az.gov).

**Statements**

The Undersigned attests to and agrees to abide by the following statements:

I have read and understand the above and agree to be bound by the rules and principles represented. If applicable, I have also received, read and understand the Evaluation Committee Instructions for this procurement. I know of no conflict of interest on my part nor have I committed any indiscretion or accepted any gratuities or favors that would compromise my impartiality. Further, I will not accept an offer of employment from or have employment discussions with any person or entity lobbying for or potentially responding to a solicitation during the defined time frame stated in ARS § 41-753. I will maintain all deliberations of the Evaluation Committee in strict confidence during the evaluation process. My recommendations shall be based upon an objective/subjective review of the Offeror's response and the appropriate award criteria from the solicitation in accordance with the Arizona Procurement Code. I have read and understand ARS § 41-753, § 41-2517 and § 41-2616C and will fully comply with the requirements.

I have not and will not communicate with any potential Offeror or vendor in preparation of specifications/scopes of work, evaluation tool or other confidential information related to the above referenced Solicitation which would provide an unfair advantage or to prepare specifications/scopes of work which favor particular vendor(s).

I have not and will not provide insight, confidential information or assistance to any potential Offeror or vendor that might give an unfair advantage or inhibit fair competition for the above referenced Solicitation. My input regarding the development of the Solicitation documents, if any, has been and will be based solely on the State's requirements. I have not and will not communicate those requirements or confidential information to any potential Offeror or vendor.



## Objectives, scope, and methodology

The Office of the Auditor General conducted this performance audit pursuant to a September 14, 2016, resolution of the Joint Legislative Audit Committee. This audit was conducted as part of the sunset review process prescribed in Arizona Revised Statutes (A.R.S.) §41-2951 et seq. This audit focuses on the Department's processes for procuring contracts to obtain goods and services and monitoring its contracts and agreements, including paying contractors' and subrecipients' invoices for goods and services.

We used various methods to study the issues in this performance audit. These methods included reviewing applicable statutes, rules, and the Arizona Department of Administration's (ADOA) *State of Arizona Accounting Manual*; contracting best practices published by the National State Auditors Association; Department-provided documents, including policies, procedures, and contract documentation; information on the Department's website; and interviewing Department staff.<sup>48</sup> In addition, we used the following specific methods to meet the audit objectives:

- To evaluate whether the Department appropriately procured contracts, we:
  - Reviewed data from the Arizona Financial Information System (AFIS) *Accounting Event Transaction File* for fiscal year 2017 and State procurement system contract information to determine the Department's contract expenditure amounts and the types of contracts for which the Department made payments for fiscal year 2017.
  - Reviewed a stratified random sample of 25 contracts selected from among the 1,113 contracts and agreements for which the Department made payments in fiscal year 2017. Of the 1,113 contracts and agreements, we excluded 284 agreements that were not subject to procurement code; the 171 State-wide contracts that were generally procured by the ADOA; and 309 contracts that lacked documentation in the State's procurement system identifying which procurement type was used, were mostly for purchases totaling less than \$10,000, and/or involved purchases of goods and services that appeared reasonable for the Department's purposes. Our sample was randomly selected from the 349 remaining contracts and included 13 competitively solicited contracts—including 6 contracts procured through RFP, 4 contracts procured through an IFB, 2 contracts procured through an RFQ, and 1 professional services contract—and 12 limited competition contracts—including 5 contracts procured as sole source contracts and 7 contracts procured as competition impracticable contracts. This review included contract documentation provided through the State's procurement system and from the Department's files, such as conflict-of-interest disclosure statements, solicitations, and statements of work.
  - Interviewed SPO staff and reviewed SPO policies, guidance, and forms.
  - Reviewed information from the Association of Government Accountants regarding procurement practices.<sup>49</sup>

<sup>48</sup> National State Auditors Association (NSAA). (2003). *Contracting for services: A National State Auditors Association best practices document*. Lexington, KY.

<sup>49</sup> Association of Government Accountants. (n.d.). *Contract management*. Retrieved 10/5/18 from <https://www.agacgfm.org/Tools-Resources/intergov/Fraud-Prevention/Tools-by-Business-Process/Contract-Management.aspx>.

- To evaluate the Department's contract-monitoring practices for contracts and agreements, we:
  - Reviewed applicable CFR requirements for monitoring subrecipients and best practices from NASPO.<sup>50</sup>
  - Reviewed a sample of 12 contracts and agreements that the Department made payments for in fiscal year 2017 to determine whether the Department's programs had adequately monitored the contracts and agreements. This sample consisted of 7 of the 25 contracts from the stratified random sample discussed previously (see page b-1) which were selected to ensure we reviewed multiple divisions' contract monitoring practices; 4 of the 284 agreements for which the Department made payments in fiscal year 2017 that we judgmentally selected based on monies spent, the counties involved, and the Department programs responsible for the agreements; and 1 of 171 State-wide contracts the Department used in fiscal year 2017 that we judgmentally selected based on monies spent. In addition, we reviewed a total of 37 contract/agreement requirements by judgmentally selecting at least 1 requirement from each contract or agreement.<sup>51</sup> This review included requesting and reviewing various documentation that would support contract requirements were met and monitored.
- To evaluate the Department's practices for reviewing and paying invoices for contracts and agreements, we:
  - Reviewed a judgmental sample of 33 invoices from the sample of 12 contracts and agreements previously mentioned that had billing dates or reporting periods between April and June 2017. We also reviewed a judgmental sample of 35 additional invoices with alternative billing dates or reporting periods between May 2016 and October 2018 based on factors such as risks identified during the audit or insufficient invoices available during the April through June 2017 sample period. This review included requesting and reviewing supporting documentation associated with these invoices.
  - Reviewed applicable CFR requirements for monitoring contractors and subrecipients.
- To obtain additional information for the Introduction, we compared data from the *AFIS Accounting Event Transaction File* for fiscal years 2017 and 2018 and State procurement system contract information to determine the Department's contract expenditure amounts and the types of solicitations used to procure contracts.
- Our work on internal controls included reviewing the Code; SPO policies, procedures, and technical bulletins; and Department policies for contract procurement; and testing the Department's compliance with these requirements. We also reviewed requirements listed in the contracts and agreements and tested whether the Department had monitored the contractors for compliance with these requirements. In addition, when available, we reviewed contract-monitoring policies and procedures developed by the Department programs responsible for monitoring the 12 contracts and agreements we sampled for review, and reviewed Department-prepared reports and analyses. Finally, we reviewed the Department's newly created policy for subrecipient monitoring. We reported our conclusions on applicable internal controls and the Department's need to improve these internal controls in Findings 1 through 3.

We conducted this performance audit of the Department in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

We express our appreciation to the Department's Director and staff for their cooperation and assistance throughout the audit.

<sup>50</sup> National Association of State Procurement Officials (NASPO). (n.d.). *Contract administration best practices guide*. Lexington, KY. Retrieved 6/15/18 from [https://www.naspo.org/Portals/16/CMGuide/NASPO-Contract\\_Administration\\_Best\\_Practices\\_Guide-f.pdf](https://www.naspo.org/Portals/16/CMGuide/NASPO-Contract_Administration_Best_Practices_Guide-f.pdf).

<sup>51</sup> We were unable to evaluate 9 requirements for various reasons, such as the contractors did not provide the specified services during the time frame reviewed or were not performing unsatisfactorily.

# AGENCY RESPONSE





# ARIZONA DEPARTMENT OF HEALTH SERVICES

August 22, 2019

Ms. Lindsey Perry, Auditor General  
Arizona office of the Auditor General  
2910 North 44<sup>th</sup> Street, Suite 410  
Phoenix, Arizona 85018

Re: Procurement and Contract Monitoring Performance Audit

Dear Ms. Perry:

Attached please find our response to your audit on our procurement and contract monitoring. We appreciate the critical role that the Auditor General plays in ensuring state agencies are performing at the highest level and in accordance with statutory requirements and generally accepted standards.

At the Arizona Department of Health Services (Department), as part of our mission of supporting *Health and Wellness for all Arizonans*, we are committed to continuous quality improvement and updating processes and procedures to ensure we are appropriate fiduciaries of limited taxpayer resources, follow statutory and regulatory guidelines, and deliver high-quality services to our customers.

Indeed, this commitment is evident in the fact that as you note, as of August 2018, the Arizona State Procurement Office (SPO), the central procurement authority for the State of Arizona, which is responsible for overall oversight and procurement policies for the State, has granted the Department's chief procurement officer unlimited procurement authority. This is the highest tier of responsibility and recognition of compliance. This determination was based on the SPO experts' evaluation of our procurement staff's experience, performance and capacity, and a demonstrated ability to follow appropriate procurement and contracting policies and procedures.

In our response to your findings, we make clear we will undertake activities that will enhance our processes and ensure appropriate oversight. We also appreciate your staff working with us on how the findings are presented and we are able to agree with two out of your three findings. However, we remain concerned with how your findings are conveyed, as we believe they are presented without appropriate context, do not give proper perspective of the work conducted and lack clarity regarding the limits of the conclusions of your findings. As a result, the presentation has the potential to leave the readers with an inaccurate understanding of our

Douglas A. Ducey | Governor    Cara M. Christ, MD, MS | Director



Ms. Lindsey Perry, Auditor General  
August 22, 2019  
Page 2

performance. Specifically, we are concerned with a lack of clear statement that, due to the small sample size and overall sampling methodology, the results are not generalizable across all our activities. We appreciate you adding detail about your sampling approach. However, readers without familiarity with sampling methodology might not understand the context and limits of your findings, which could cause readers to believe the findings represent a comprehensive assessment of our performance.

**(See Appendix C: Auditor General reply to agency response, items #1a and #1b)**

In addition, we would also note that, although we are agreeing with several of your findings, and will implement all the recommendations, there are examples throughout the document with which we do not agree. For brevity, we will not note each instance of disagreement. However, we do wish to highlight one example, on the GIS mapping services contract. While the audit notes the Department exceeded the \$500,000 limit on a professional services contract, the Department had received guidance from SPO that this contract was not under the Professional Services of the Code and therefore not subject to the limit. Because Auditor General reports are now being cited in litigation over the Medical Marijuana program, we want to ensure we are on the record with disagreeing with this example.

**(See Appendix C: Auditor General reply to agency response, item #2)**

As we note throughout the response, we are committed to ongoing improvement opportunities and will implement your recommendations through strategies that will strengthen our activities.

We appreciate your partnership and the opportunity to respond, and we are moving forward to implement recommendations to enhance oversight of our procurement and contracting activities.

Sincerely,

Cara M. Christ, MD  
Director

Attachment

Douglas A. Ducey | Governor    Cara M. Christ, MD, MS | Director

**Finding 1:** Department did not follow some State procurement requirements for 22 of 25 contracts reviewed

**Recommendation 1:** The Department should include policies and procedures in its draft procurement manual that address issues identified in this finding to help ensure compliance with the Code and purchasing requirements. The Department's procurement manual should provide policies and procedures that require the following:

**Recommendation 1a:** Appropriately procuring professional services, including guidance for how to establish evaluation criteria, under what circumstances it will use a professional services contract, and how to document this procurement, including the statement of work and offer and acceptance of the award. In doing so, the Department should work with its Assistant Attorney General to determine how these contracts may be used to comply with the Code.

Department Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: As outlined in our cover letter, the Department does not believe that the wording of the finding accurately reflects the results of the overall audit and feels those who may not fully read the audit could misinterpret the finding. However, the Department is committed to undertaking activities that will enhance our processes and plans to implement the recommendation in 1a by February 1, 2020.

(See Appendix C: Auditor General reply to agency response, item #1a)

**Recommendation 1b:** Approving only contract amendments that include requirements considered in the original solicitation and amounts allowed by the Code unless otherwise determined in writing by SPO.

Department Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: While the Department understands that the auditors have identified one of the contracts as being a Professional Services contract that has contract limits, the Department had worked with the State Procurement Office (SPO) under the belief that the contract was not used under the Professional Services provision of the Code. However, the Department will continue to implement the recommendation in 1b by September 1, 2019.

(See Appendix C: Auditor General reply to agency response, item #2)

**Recommendation 1c:** Justifying limited competition contracts and documenting these efforts and decisions.

Department Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: As outlined in our cover letter, the Department feels those who may not fully read the audit could misinterpret the finding. However, the Department will implement the recommendation specified in 1c to better document and justify contract decisions. Procedures will be developed and implemented by November 1, 2019.

(See Appendix C: Auditor General reply to agency response, item #1a)

**Recommendation 1d:** Tracking the completion of each procurement step to ensure all required procurement steps were performed.

Department Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: The recommendation specified in 1d will be developed and implemented, by February 1, 2020.

**Recommendation 1e:** Tracking contract spending and contract expirations to prevent Department staff from spending more than is allowed per the contract type or using expired contracts.

Department Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: The Department had worked with SPO under the belief that this was a contract that could be extended and was not subject to the Personnel Services limit provision of \$500,000. However, the Department will develop and implement the recommendation specified in 1 e for tracking contract spending and contract expirations, by February 1, 2020.

(See Appendix C: Auditor General reply to agency response, item #2)

**Recommendation 1f:** Conducting a supervisory review to help ensure the completion of key procurement steps, such as obtaining signed conflict-of-interest statements, informing all Department staff that a solicitation is beginning, and ensuring that both parties sign the contract offer and acceptance of award to finalize the contract.

Department Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: The Department will implement the recommendation specified in 1f by September 1, 2019.

**Recommendation 1g:** Training appropriate staff on State procurement requirements and Department policies and procedures once they have been fully developed.

Department Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: The Department will begin training as policies and procedures are developed as specified by February 1, 2020.

**Recommendation 2:** The Department should complete its draft procurement manual and implement it.

Department Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: The Department will complete the draft procurement manual and implement it by February 1, 2020.

**Recommendation 3:** The Department should modify the procurement checklist it began using during the audit to include guidance for missing procurement requirements, such as procuring professional services and ensuring contract amendments are approved only if they align with requirements in the Code and implement the use of the checklist including supervisory review.

Department Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: This recommendation will be implemented, by February 1, 2020.

**Finding 2:** Department paid for some services without ensuring they were provided and contract requirements were met

**Recommendation 4:** The Department should develop and implement written policies and procedures to direct and guide its contract monitoring. Consistent with best practices, these policies and procedures should specify and/or require:

**Recommendation 4a:** Program requirements and staff roles and responsibilities for monitoring contracts.

Department Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: Program requirements and staff roles and responsibilities for monitoring contracts will be developed and implemented as specified in recommendation 4a, by February 1, 2020.

**Recommendation 4b:** Developing a written contract administration plan outlining monitoring activities for each contract.

Department Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: ADHS will develop a written contract administration plan outlining monitoring activities for all contracts as specified in recommendation 4b.

**Recommendation 4c:** Including specific and measurable contract terms, and reporting requirements in the contracts.

Department Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: The Department will include specific and measurable contract terms, and reporting requirements in its contracts as specified in recommendation 4c, beginning immediately.

**Recommendation 4d:** Taking appropriate action to address noncompliance, such as withholding payment.

Department Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: The Department will develop and implement a policy as specified in recommendation 4d by February 1, 2020.

**Recommendation 4e:** Developing and using tools and/or methods to effectively track completion of contract requirements, including spending.

Department Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: The Department will continue to make efforts to enhance our practices to implement the recommendation in 4e. For example, the program has updated the Community Health Nursing Policy and Procedure manual and made revisions to Orientation and Training program requirements to ensure improved monitoring and tracking. The new manuals went into effect 7/1/2019.

**Recommendation 5:** The Department should develop and implement a centralized process, including written policies and procedures, for overseeing its programs' monitoring efforts to ensure compliance with the contract policies and procedures it developed.

Department Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: This recommendation will be implemented by February 1, 2020.

**Recommendation 6:** The Department should develop and implement policy and procedures for working with contractors that will provide guidance on recovering any monies that may have been inappropriately paid, including specifying in what circumstances it will work with its Assistant Attorney General to recover these monies.

Department Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: The Department will develop and implement a payment recovery process, including identifying when to consult the Attorney General, by February 1, 2020.

**Recommendation 7:** The Department should continue to implement its newly developed policy for monitoring contracts that receive federal funding to ensure that its programs conduct risk assessments to determine the appropriate level of monitoring to perform for contractors or subrecipients.

Department Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Response explanation: The Department will continue to implement the Sub-recipient monitoring policy that was recently developed. The policy fully meets the use of risk assessments to determine the appropriate level of monitoring to perform for contractors or sub-recipients as specified in recommendation 7.

**Finding 3:** Department's payment processing does not consistently provide adequate oversight to ensure appropriate use of public monies

**Recommendation 8:** The Department should continue to develop and implement written payment-processing policies and procedures to better safeguard public monies and prevent payments for unauthorized services, overcharges, and paying for services without ensuring they were received by:

**Recommendation 8a:** Requiring program staff with the expertise and knowledge about the contract requirements to obtain and review adequate supporting documentation prior to approving invoices for payment. In instances when resources do not permit a review of all supporting documentation, the Department should use a risk-based approach to review the supporting documentation.

Department Response: The finding of the Auditor General is not agreed to, but the recommendation will be implemented.

Response explanation: As outlined in our cover letter, the Department does not believe that the wording of the finding accurately reflects the results of the overall audit and feels those who may not fully read the audit could misinterpret the finding. The Department is strongly committed to safeguarding public money. However, the recommendation will be implemented Department-wide by February 1, 2020. The Department's recent implementation of the Sub-recipient Monitoring Policy when fully deployed, will fully meet recommendation 8a.

(See Appendix C: Auditor General reply to agency response, item #3)

**Recommendation 8b:** Conducting a risk-based supervisory review of the invoices and supporting documentation that program staff approved.

Department Response: The finding of the Auditor General is not agreed to, but the recommendation will be implemented.

Response explanation: The Department will continue to implement the Sub-recipient monitoring policy that was recently developed. The policy fully meets the risk-based supervisory review of the invoices and supporting documentation specified in recommendation 8b. The Department will incorporate the risk-based approach to all invoices and supporting documentation by February 1, 2020.

**Recommendation 8c:** Documenting program staff's invoice review and approval with a consistent approval method, such as initials, signatures, or another method, to show that they reviewed and approved the invoice and supporting documentation.

Department Response: The finding of the Auditor General is not agreed to, but the recommendation will be implemented.

Response explanation: The recommendation will be implemented by February 1, 2020.

**Recommendation 9:** The Department should train all appropriate staff on its payment-processing policies and procedures once they are developed.

Department Response: The finding of the Auditor General is not agreed to, but the recommendation will be implemented.

Response explanation: The Department will develop payment-processing policies and procedures and, once they are developed, will train all appropriate staff by February 1, 2020.

**Recommendation 10:** The Department should ensure that its various programs and program staff adhere to its payment-processing policies and procedures as part of overseeing its programs for compliance with its contract-monitoring policies and procedures as recommended in Finding 2.

Department Response: The finding of the Auditor General is not agreed to, but the recommendation will be implemented.

Response explanation: The recommendation will be implemented by February 1, 2020.





## Auditor General reply to agency response

We appreciate the Arizona Department of Health Services' (Department) response. However, the Department has included certain statements in its response to the audit findings that necessitate the following comments and clarifications.

1. The Department states that it does not believe our report findings convey appropriate context, give proper perspective of the work conducted, or include a clear statement that the sample size and methodology are not generalizable across all Department activities. We disagree with these assertions. As can be observed in the report, we do not generalize our findings beyond the sample we reviewed. However, the results of our review sufficiently demonstrate the impact of the Department's inadequate procurement, contract monitoring, and payment processing practices. Specifically:
  - a. For Finding 1, our finding heading clearly states that our finding is specific to the 25 Department contracts that we reviewed. This sample of 25 contracts was stratified by contract type to ensure that our review included different types of procurements. Further, within each contract type grouping, the sample was randomly selected, ensuring that each of the Department contracts of that contract type had an equal likelihood of being included in our sample. Although we did not generalize the results of our review to the population, our sample size was sufficient, in the context of other evidence we provided, to conclude that the Department did not always follow all procurement code requirements and may continue to be at risk of doing so. Further, our report clearly states the results of our review and provides necessary context to understand our findings. For example, we reported that 1 of the 25 contracts was inappropriately procured, 11 of the 25 contracts lacked conflict of interest statements, and 20 of the 25 contracts lacked evidence that the Department provided the required notification to its staff. For more information about our sampling methodology, see Appendix B, pages b-1 through b-2, and a detailed footnote on page 7.
  - b. For Findings 2 and 3, we judgmentally selected a sample of 12 contracts and agreements to ensure we reviewed the Department's contract monitoring practices and payment processing for a cross-section of Department programs (please see Appendix B, pages b-1 through b-2, for more information on our sampling methodology). From these 12 contracts, we judgmentally selected a total of 37 contract requirements and 68 invoice payments for further review (see point 3 below for more information about our review of invoice payments). Again, we did not generalize the results of our review, which found that the Department did not ensure 17 of the 37 requirements we reviewed were met, and we limited our findings to our review of these 37 requirements. Similar to Finding 1, our sample size was sufficient, in the context of other evidence we provided, to conclude that the Department did not ensure that all contract requirements were met and may continue to be at risk of doing so.
2. The Department's response indicates, specific to Finding 1, that it received guidance from the State Procurement Office (SPO) that its GIS mapping services contract was not under the Professional Services provisions of the Code and not subject to the \$500,000 limit. First, as indicated in the Department's response, SPO has granted the Department unlimited procurement authority based on SPO's evaluation of Department procurement staff's experience, performance and capacity, and demonstrated ability to follow appropriate procurement and contracting policies and procedures. As such, the Department should understand and adhere to all procurement requirements, regardless of the type of procurement it conducts. Second, although the Department indicates it received guidance from SPO that its GIS mapping services

contract was not under the professional services procurement provisions, Department documentation shows that the Department procured these services under professional services procurement provisions. The Department did not provide documentation or other evidence that its GIS mapping services were contracted through another type of procurement or contract, such as a Request for Proposal or Invitation for Bid.

3. Finally, specific to Finding 3, the Department's response indicates that it does not believe the wording in the finding accurately reflects the overall audit and the finding could be misinterpreted. We disagree with this statement and the evidence we present in Finding 3 supports our findings in this area. Specifically, to assess the Department's payment processing practices, we selected and reviewed 68 invoice payments totaling nearly \$4.9 million from among the 12 Department contracts previously described. This work identified \$10,000 paid for unauthorized services, \$12,500 overpaid to 1 contractor, and more than \$4 million paid without Department staff reviewing adequate supporting documentation to ensure the appropriateness of the amounts billed on the invoices. In fact, we found and reported that the Department reviewed adequate supporting documentation for more than \$862,000 of the \$4.9 million. However, the practices employed to review this supporting documentation did not exist Department-wide. Based on this work and the evidence gathered, we appropriately concluded that the Department's payment processing practices did not consistently provide adequate oversight to ensure the appropriate use of public monies.

