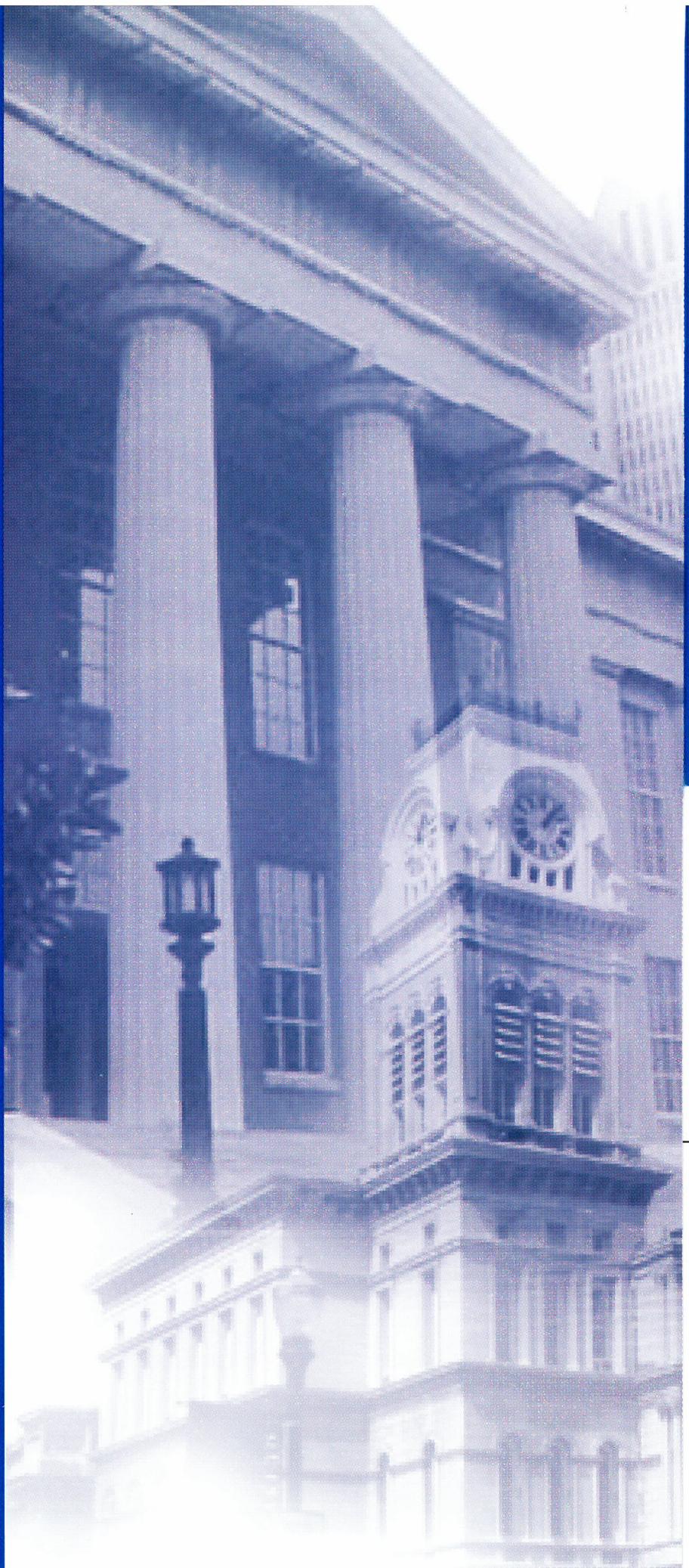




Greg Fischer
Mayor

Louisville Metro Council

The Office of Internal Audit provides independent, objective assurance and consulting services that adds value to and improves Louisville Metro Government.



Office of Internal Audit

Louisville Metro Government

Office Supply Contract

Audit Report

Louisville Metro Government

Office Supply Contract

July 2014



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Executive Summary

PROJECT TITLE

Louisville Metro Government – Office Supply Contract

OBJECTIVE AND SCOPE

The objective was to perform a compliance review of Louisville Metro Government's office supply contract and related expenditure activity. Office supply expenditure activity records and applicable policies and procedures were reviewed. The focus included determining if expenditure activity was in compliance with the terms of Louisville Metro Government's primary office supply contract. The objective of the review was to obtain reasonable assurance that the risks are adequately mitigated through the internal controls in the process.

This was a compliance review based on the office supply contract with Louisville Metro Government's primary vendor of office supplies, Office Depot. The review included expenditure activity from October 1, 2012 through September 30, 2013. The details of the scope and methodology of the review are addressed in the Observations and Recommendations section of this report.

INTERNAL CONTROL ASSESSMENT

Needs Improvement

RESULTS

Opportunities exist for improving the internal control structure for the office supply contract with Office Depot. Examples include the following.

- **Pricing Structure.** The office supply contract with Office Depot did not include specific details regarding which items were subject to the fixed percentage discount described in the contract.
 - Consequently, the Purchasing Division of the Office of Management and Budget (Purchasing) did not have the information necessary to ensure that purchases from Office Depot were in compliance with the contract. As a result, a substantial amount of the items purchased from Office Depot during the review period were not subject to the favorable discount detailed in the contract.
- **Contractual Compliance.** Issues noted in determining compliance with the contractual terms.
 - Louisville Metro Government was:
 - Overcharged in 492 instances,
 - Undercharged in 1,468 instances.

The net result when taking into account both the undercharges and overcharges, Louisville Metro Government was overcharged \$730.



OFFICE OF INTERNAL AUDIT
LOUISVILLE, KENTUCKY

GREG FISCHER
MAYOR

INGRAM QUICK, CHIEF AUDIT EXECUTIVE

JIM KING
PRESIDENT METRO COUNCIL

Transmittal Letter

July 2, 2014

The Honorable Greg Fischer
Mayor of Louisville Metro
Louisville Metro Hall
Louisville, KY 40202

Subject: Audit of the Louisville Metro Government's Office Supply Contract

Introduction

An audit of Louisville Metro Government's primary office supply contract was performed. The objective was assessing compliance with the terms within the contract with the vendor, Office Depot. The focus included determining if expenditure activity is in compliance with the terms of the contract as well as applicable policies and procedures.

The audit was conducted in accordance with Government Auditing Standards issued by the Comptroller General of the United States and with the International Standards for the Professional Practice of Internal Auditing issued by the Institute of Internal Auditors.

As a part of the review, the internal control structure was evaluated. The objective of internal control is to provide reasonable, but not absolute, assurance regarding the achievement of objectives in the following categories:

- Achievement of business objectives and goals
- Effectiveness and efficiency of operations
- Reliability of financial reporting
- Compliance with applicable laws and regulations
- Safeguarding of assets

There are inherent limitations in any system of internal control. Errors may result from misunderstanding of instructions, mistakes of judgment, carelessness, or other

personnel factors. Some controls may be circumvented by collusion. Similarly, management may circumvent control procedures by administrative oversight.

Scope

A thorough understanding of the office supply contract with Louisville Metro Government's primary vendor of office supplies, Office Depot, and related expenditure activity was gained through the examination of supporting documentation. This was achieved through a thorough review of the contract and an examination of office supply expenditures and supporting documentation.

Expenditure activity and applicable policies and procedures were reviewed. Testing was performed on all transactions with Office Depot that occurred during the second quarter of fiscal year 2013 through the first quarter of fiscal year 2014 (October 2012 through September 2013).

All expenditures for the audit period (October 2012 through September 2013) were reviewed. The activity was examined to assess compliance with the terms of the contract. The details of the scope and methodology of the review are addressed in the Observations and Recommendations section of this report.

Opinion

It is our opinion that the internal control structure for the office supply contract activity needs improvement. The internal control rating is on page 6 of this report. The rating quantifies our opinion regarding the internal controls, and identifies areas requiring corrective action. Opportunities to strengthen the internal control structure were noted. Examples include the following.

- **Pricing Structure.** The office supply contract with Office Depot did not include specific details regarding which items were subject to the fixed percentage discount described in the contract. Consequently, the Purchasing Division of the Office of Management and Budget (Purchasing) did not obtain the information necessary from Office Depot to ensure that purchases were in compliance with the contract. As a result, a substantial amount of items purchased from Office Depot were not subject to the favorable discount detailed in the contract.
 - During the review period, 5,371 of 13,994 transactions (38%) with Office Depot did not receive the discount described in the contract. The transactions included multiple items, all of which were not under contract and were not subject to the discount rate detailed within the contract. The total dollar amount for these transactions was \$276,887 which was 51% of the total funds (\$541,314) expended with Office Depot during the review period.
- **Contractual.** Issues noted in determining the expenditures' compliance with the contractual terms.
 - There were a number of transactions in which Louisville Metro Government was charged a price that was not in compliance with the price or pricing parameters noted within the office supply contract. Louisville Metro Government was:
 - Overcharged in 492 instances
 - Undercharged in 1,468 instances

The net result when taking into account both the undercharges and overcharges, Louisville Metro Government was overcharged \$730.

Corrective Action Plan

Representatives from Office of Management and Budget have reviewed the results and are committed to addressing the issues noted. Corrective action plans are included in this report in the Observations and Recommendations section. We will continue to work with Office of Management and Budget to ensure the actions taken are effective to address the issues noted.

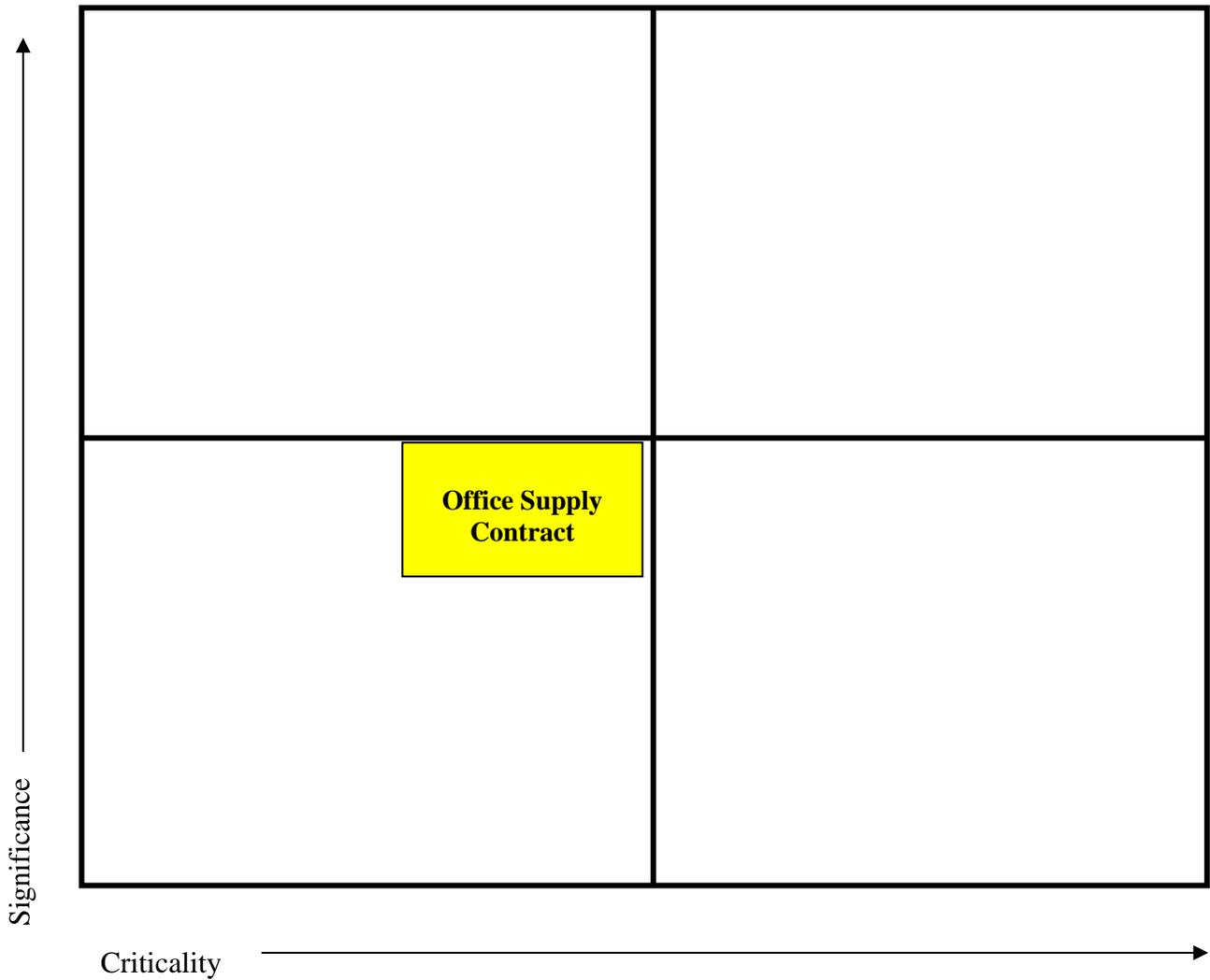
Sincerely,



Ingram Quick, CIA, CFE
Chief Audit Executive

cc: Louisville Metro Council Government Accountability and Ethics Committee
Director of Office of Management and Budget
Louisville Metro External Auditors
Louisville Metro Council President

Internal Control Rating



<u>Legend</u>			
<u>Criteria Issues</u>	<u>Satisfactory</u> Not likely to impact operations.	<u>Needs Improvement</u> Impact on operations likely contained.	<u>Inadequate</u> Impact on operations likely widespread or compounding.
Controls	Effective.	Opportunity exists to improve effectiveness.	Do not exist or are not reliable.
Policy Compliance	Non-compliance issues are minor.	Non-compliance issues may be systemic.	Non-compliance issues are pervasive, significant, or have severe consequences.
Image	No, or low, level of risk.	Potential for damage.	Severe risk of damage.
Corrective Action	May be necessary.	Prompt.	Immediate.

Background

Louisville Metro Government's contract with Office Depot was effective as of September 2011. The initial term of the contract is a period of one year, and it is renewable for up to four additional one year terms. The contract was bid jointly with multiple local governmental entities including, Louisville Metro Government. Although, Louisville Metro Government is a participant in the contract, the required procurement process, including the issuance and administration of the Request for Proposal (RFP), was performed by another local governmental entity, acting as the Lead Agency. Louisville Metro Government purchased \$541,314 in supplies and other goods from Office Depot during the audit period (October 2012 through September 2013).

This was a scheduled audit.

Summary of Audit Results

I. Current Audit Results

See Observations and Recommendations section of this report.

II. Prior Audit Issues

The Office of Internal Audit has not performed any previous reviews of Louisville Metro Government's office supply contract.

III. Statement of Auditing Standards

The audit was performed in accordance with Government Auditing Standards issued by the Comptroller General of the United States and with the International Standards for the Professional Practice of Internal Auditing issued by the Institute of Internal Auditors.

IV. Statement of Internal Control

An understanding of the internal control structure was obtained in order to support the final opinion.

V. Statement of Irregularities, Illegal Acts, and Other Noncompliance

The review did not disclose any instances of irregularities, any indications of illegal acts, and nothing was detected during the review that would indicate evidence of such. Any significant instances of noncompliance with laws and regulations are reported in the Observations and Recommendations section of this report.

VI. Views of Responsible Officials / Action Plan

A draft report was issued to the Office of Management and Budget on May 30, 2014. It was determined that a formal exit conference was not necessary.

The views of Office of Management and Budget officials are included as corrective action plans in the Observations and Recommendations section of the report. The plans indicate a commitment to addressing the issues noted.

LMCO §30.36(B) requires Louisville Metro Agencies to respond to draft audit reports in a timely manner. It specifically states that

“The response must be forwarded to the Office of Internal Audit within 15 days of the exit conference, or no longer than 30 days of receipt of the draft report.”

The Office of Management and Budget’s response was provided within this required timeframe.

Observations and Recommendations

Scope

A review of Louisville Metro Government's office supplies contract and related expenditure activity was performed. Applicable policies and procedures and office supply expenditure activity records were reviewed. The focus included determining if expenditure activity was in compliance with the terms of Louisville Metro Government's contract with its primary vendor for office supplies, Office Depot. The objective of the review was to obtain reasonable assurance that the risks are adequately mitigated through the internal controls in the process.

Testing was performed by analyzing the entire population of 13,994 transactions between Louisville Metro Government and Office Depot, to assess compliance with the pricing terms described in the contract.

Testing of items purchased during the review period included comparing the relevant detailed transaction history to the applicable product price lists, which were included in the contract. Additions and changes to the price lists were obtained from the Purchasing Division of the Office of Management and Budget and verified to the terms of the contract. Due to the vagueness of the contract regarding which items are subject to the fixed percentage discount, pricing compliance of those items could not be assessed using a source independent of Office Depot, such as a catalog or web-site. As an alternative, the catalog list price for those items was obtained directly from Office Depot. A judgmental sample of 36 transactions was tested to provide additional assurance about the completeness, accuracy, and reliability of the detailed transaction history, which was provided by Office Depot.

Physical examination / ocular inspection was performed on a sample of items purchased during the review period to verify that the items were received and were being used as intended.

The review period was for October 1, 2012 to September 30, 2013 (second quarter of FY13 through the first quarter of FY14).

Observations

Issues were noted with office supply contract activity. As a result, the effectiveness of the internal control structure needs improvement. Opportunities to strengthen the controls include the following.

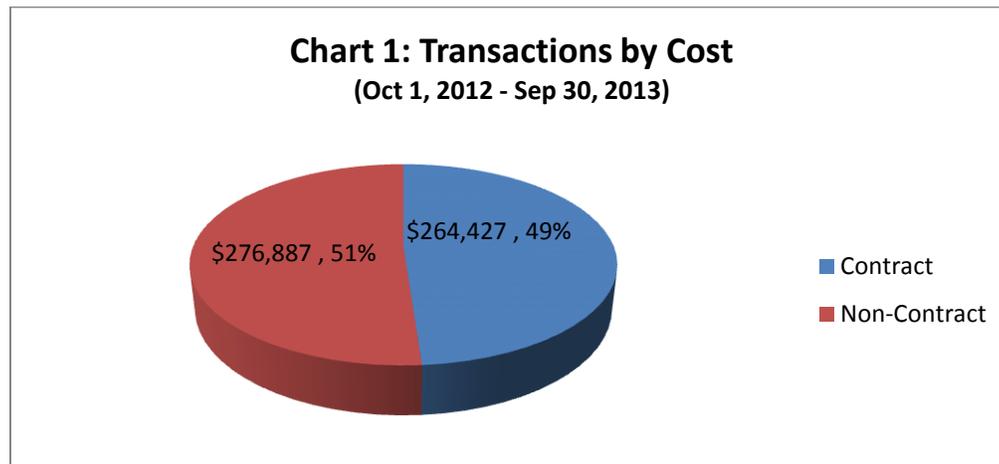
1) Office Supply Contract

Details of these begin on the following page.

1) Office Supply Contract

- **Pricing Structure.** The office supply contract with Office Depot did not include specific details regarding which items were subject to the pricing structure described in the contract. Consequently, the Purchasing Division of the Office of Management and Budget (Purchasing) did not obtain the information necessary from Office Depot to ensure that purchases were in compliance with the contract. As a result, a substantial amount of items purchased from Office Depot were not subject to the favorable pricing detailed in the contract.
 - During the review period, there were 5,371 transactions (38%) with Office Depot that did not receive the discount described in the contract. The transactions included multiple items, all of which were not under contract and were not subject to the favorable discount detailed within the contract. The total dollar amount for these transactions was \$276,887 which was 51% of the total funds (\$541,314) expended with Office Depot during the review period.

Expenditures by category are depicted graphically in Chart 1 shown below.



- **Contractual Compliance.** There were transactions in which Louisville Metro Government was charged a price that was not in compliance with the price or pricing parameters noted within the office supply contract.
 - In 492 of the 13,994 transactions, Louisville Metro Government purchased items at a price that was more than the price guaranteed by the contract. This resulted in Louisville Metro Government being overcharged \$5,566.
 - In 1,468 of the 13,994 transactions, Louisville Metro Government purchased items at a price that was less than the price guaranteed by the contract. This resulted in Louisville Metro Government being undercharged \$4,836.

The net result when taking into account the undercharges and overcharges, Louisville Metro Government was overcharged \$730.

Recommendations

Appropriate personnel should take corrective actions to address the issues noted. Specifics include the following.

- ✓ Consider seeking an office supply contract that is more aligned with Louisville Metro Government's office supply needs. This could include amending the current contract or rebidding the contract in favor of a more advantageous contract.
- ✓ Establish policies and procedures for instances where Louisville Metro Government uses a contract that is not subject to their bidding process such as instances of where another entity solicits bids for Louisville Metro Government's use. These policies and procedures should include:
 - Consider having the County Attorney review the contract to address uncertainties or vagueness within the contract.
 - Evaluate the contract based on predetermined consistent standards (i.e. checklist).
 - Appropriate personnel should obtain sufficient pricing information to support prices for goods/services under the contract.
 - The decision to use a contract that did not go through Louisville Metro Government's bidding process should go through the appropriate approval process.
 - Consider establishing a process to verify the purchase price (or website price) is in compliance with the contractual pricing for that item. This could include regularly conducting sample tests to ensure that the purchase price is in compliance with the terms of the contract.
- ✓ Purchases are made through the Office Depot website where there is the ability to limit what can be purchased. Consider having Office Depot to limit what can be purchased to only items which are under contract.
- ✓ Ensure that any price changes made by Office Depot are in accordance with the contract and that appropriate notice is provided. Ensure that the contract explicitly states the terms for allowable price changes, if any, for each of the negotiated discount sections. This includes price change frequency, escalation methods, notification, and approval requirements.
- ✓ Require vendors to clearly identify and disclose any price lists they reference for the bidding process and for any subsequent revisions to the contract. This documentation should be available to those persons who make office supplies purchases through the vendor.
- ✓ Require vendors to provide periodic reports on spending trends, compliance with key contract terms, and authorized price lists.
- ✓ Appropriate personnel should review all supporting documentation to ensure the expenditure is in compliance with contractual terms prior to the approval of payment.

Office of Management and Budget's Corrective Action Plan

Metro Government has made the decision to not rebid the office supplies contract at this time. We have worked with the current vendor to put controls in place to address the recommendations made in this audit review.

Metro Government currently has policies and procedures in place to review a contract that we are using as part of a cooperative purchasing agreement. All contracts are reviewed in order to ensure that they meet the statutory procurement requirements in place and that the pricing is adequate for Metro Government's needs. All contracts are reviewed by appropriate Procurement personnel prior to implementation of the contract. All contracts contain pricing information that is to be reviewed by appropriate personnel prior to purchases being made against the contract.

Metro Government has worked with Office Depot to restrict access on the Office Depot website to only items that are included in the contract. Metro Government has received a list of all items that are included on the website and reviewed the list for compliance with the contract. Metro Government will conduct a quarterly review of the items on the Office Depot website to ensure the items are on the contract and at contract pricing.

All contracts contain pricing information that is to be reviewed by appropriate personnel prior to purchases being made against the contract. Contracts are maintained electronically and are available for all Metro Government users to review. Any approved purchase order request that is submitted to OMB for processing should be reviewed and approved prior to submission and compared against the contract to ensure that the price charged is correct.

Office Depot is now sending a monthly spend report for Metro Government to review that includes the details of all orders placed during the prior month. Metro Government will conduct a quarterly review of the items purchased to ensure that only contract items are being purchased on the Office Depot website to ensure the items are on the contract and at contract pricing.

Any approved purchase order request that is submitted to OMB for processing will be reviewed, compared against the contract and approved prior to submission to confirm the purchase that the price charged is correct and agrees with the contract price.



Office of Internal Audit
Reader Survey

Please help us serve you better by taking a few minutes to complete this survey and returning it by mail, facsimile, or email. Contact information is as follows. For your convenience, this form is available on the Office of Internal Audit website.

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Website: www.louisvilleky.gov/InternalAudit/Reports/

Name of Report: Louisville Metro Government – Office Supply Contract

How do you rate this report?			
	Beneficial	Somewhat Helpful	Needs Improvement
Background Information	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Details	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Length of Report	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Clarity of Writing	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Potential Impact	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Suggestions, comments, ideas, thoughts: _____

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