CITY OF HOUSTON

Annise D. Parker
City Controller

Steve Schoonover
City Auditor

HOUSTON AIRPORT SYSTEM
LONG-TERM CONTRACTOR RELATIONSHIPS
PERFORMANCE AUDIT

Report No. 2010-10

OFFICE OF THE CITY CONTROLLER
CITY OF HOUSTON
TEXAS

ANNISE D. PARKER

December 16, 2009

The Honorable Bill White, Mayor
City of Houston, Texas

SUBJECT: Houston Airport System - Long-Term Contractor Relationships
Performance Audit - Report No. 2010-10

Dear Mayor White:

In accordance with the City's contract with MFR, P.C. (MFR), MFR has completed a Performance Audit of the Houston Airport System's (HAS) Long-Term Contractor Relationships. The original objectives of the audit were to:

- Determine to what extent the use of long-term (greater than seven years) contractor relations had benefited the City.
- Determine to what extent such relationships (greater than seven years) were in compliance with the applicable procurement laws.
- Review the cost-benefit of such long-term contractor usage and the appropriateness of their continued selection.

The report, attached for your review, concluded that for specialized construction services HAS demonstrated concerns with the qualifications of the vendor and the vendor's ability to perform the scope of work, which benefited the City. Also, MFR was able to determine that HAS was acquiring services in the most economical manner. However, MFR did note one issue of an operational nature that was brought to the attention of management.

MFR had a limitation in scope pertaining to compliance with the applicable procurement laws as the City maintains the bid documentation for two years in accordance with the Texas State Library & Archives Commission requirements. Therefore, MFR had inadequate information to conclude on whether the City was in compliance with applicable procurement laws and continued vendor selection for long-term contracts.

The observation and recommendation identified during the audit is included in the body of the report. Draft copies of the matters contained in the report were provided to Department officials. The Views of Responsible Officials as to actions being taken are appended to the report as Exhibit C.

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e-mail: controllers@cityofhouston.net

We commend Department management for their timely efforts to take action to remedy the deficiency identified by MFR. We also appreciate the cooperation extended to the MFR engagement team by Department personnel during the course of the audit.

Respectfully submitted,

Annise D. Parker
City Controller

xc: City Council Members
Anthony Hall, Chief Administrative Officer
Michael Moore, Chief of Staff, Mayor's Office
Eric Potts, Interim Director, Houston Airport System
Alfred Moran, Director, Administration and Regulatory Affairs Department
Michelle Mitchell, Director, Finance Department

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December 9, 2009

Controller Annise D. Parker
Office of the City Controller
City of Houston
901 Bagby, 8th Floor
Houston, TX 77002

Re: Houston Airport System Long-Term Contractor Relationships Performance Audit

Dear Controller Parker:

MFR, P.C. (MFR) has completed the City of Houston's (the City) Long-Term Contractor Relationships Performance Audit of the Houston Airport System (HAS). This audit was outlined in our engagement letter dated December 3, 2008 under Contract No. 56546, approved by City Council Ordinance No. 2004-1296.

The original objectives of our audit were to:

- Determine to what extent the use of long-term (greater than seven years) contractor relations had benefited the City.
- Determine to what extent such relationships (greater than seven years) were in compliance with the applicable procurement laws.
- Review the cost-benefit of such long-term contractor usage and the appropriateness of their continued selection.

In accordance with our engagement letter dated December 3, 2008, the scope of our audit includes any currently active long term contracts that are greater than seven years old as of September 30, 2008, either initiated by or on behalf of HAS (sole participant/spending authority).

Our detailed test procedures for the attached performance report were performed through April 30, 2009. We accomplished the objectives except for those related to compliance with applicable procurement laws and the appropriateness of their continued vendor selection. These limitations occurred due to the fact that the City maintains the bid documentation for only two years in accordance with the Texas State Library & Archives Commission requirements.

Because of inherent limitation in controls, errors or fraud may occur and not be detected. Furthermore, the projection of any conclusions, based on our findings, to future periods is subject to the risk that the validity of such conclusions may be altered because of changes made to the system or controls, the failure to make needed changes to the system or controls, or deterioration in the degree of effectiveness of the controls.

The attached report is intended solely for the information and use of the HAS as well as the Office of the City Controller, and is not intended to be used for any other purpose.

MFR is pleased to have been given the opportunity to work on this engagement and we appreciate the cooperation received from your office and HAS.

Very truly yours,

MFR, P.C.

J. David Ahola
Principal, Internal Audit

JDA/ea

HOUSTON AIRPORT SYSTEM
LONG-TERM CONTRACTOR RELATIONSHIPS
PERFORMANCE AUDIT

INDEX

	Page
EXECUTIVE SUMMARY	
Background	1
Objectives and Scope	1
Overall Conclusion and Assessment	2
OBSERVATION AND RECOMMENDATION	
Detailed Background	4
Audit Methodology	4
Observation and Recommendation	
1. Inaccurate SAP Contract Data	5
Exhibit A – Sample of SAP Contracts Greater Than Seven Years Old as of September 30, 2008	7
Exhibit B – Selected Contracts with Inaccurate Dates in SAP	9
Exhibit C – Views of Responsible Officials	11

HOUSTON AIRPORT SYSTEM
LONG-TERM CONTRACTOR RELATIONSHIPS
PERFORMANCE AUDIT

EXECUTIVE SUMMARY

Background

On September 28, 2007 MFR completed the preliminary survey of the City-Wide Long-Term Contractor Relationships Performance Audit Phase One (Phase One).

For Phase Two, the detailed fieldwork stage, MFR selected three City departments for further analysis; the Houston Fire Department (HFD), the Public Works and Engineering Department (PWE), and the Houston Airport System (HAS). This report on HAS is one of three reports issued to the City as a result of the further analysis of the selected departments in Phase Two of the audit.

Objectives and Scope

The original objectives of the audit were as follows:

- Determine to what extent the use of long-term (greater than seven years) contractor relations had benefited the City.
- Determine to what extent such relationships (greater than seven years) were in compliance with the applicable procurement laws.
- Review the cost-benefit of such long-term contractor usage and the appropriateness of their continued selection.

MFR had a limitation in scope pertaining to compliance with the applicable procurement laws as the City maintains the bid documentation for two years in accordance with the Texas State Library & Archives Commission requirements. This also prohibited MFR from determining the appropriateness of the vendors continued selection.

The scope of the audit was any currently active long-term contracts that were greater than seven years old as of September 30, 2008, either initiated by or on behalf of HAS (sole participant/spending authority).

Overall Conclusion and Assessment

For specialized construction services we noted that HAS demonstrated concerns with the qualifications of the vendor and the vendor's ability to perform the scope of work, which benefited the City. For the selected sample of contracts, as noted above, MFR had inadequate information to conclude on whether the City was in compliance with applicable procurement laws and continued vendor selection. Since a formal cost study analysis was not available for review, MFR performed alternative procedures including inquiries and review of contract documentation. As a result of performing these procedures, MFR was able to determine that HAS was acquiring the services in the most economical manner.

MFR noted one issue of an operational nature that was brought to the attention of HAS Management during fieldwork and is as follows:

- For eight of the 45 contracts identified through the reconciliation process, end dates recorded in SAP were prior to September 30, 2008; however, according to the manual list prepared by HAS the contracts were open as of September 30, 2008. MFR selected four of the eight contracts for testing. For three of four contracts tested, HAS made payments after the contract end date recorded in SAP. The City may be at risk of making payments pertaining to contracts that may no longer be valid.

OBSERVATION AND RECOMMENDATION

Detailed Background

During Phase One of the audit, MFR obtained an electronic download of the contract data from the City's Advantage Financial Management System (AFMS). MFR identified in excess of 1,100 contracts for the entire City that were in effect for over seven years. For Phase Two of the audit, MFR obtained electronic downloads of contract data from SAP as well as a manual list of the contracts prepared by HAS. MFR reconciled the AFMS contract data download, SAP electronic contract download and the manual list of contract data provided by HAS. Through the reconciliation process, MFR identified 45 HAS contracts with a total amount of $41,565,756.

MFR judgmentally selected an original sample of 15 long-term contracts totaling $24,447,988 from the population of 45 contracts. See "Exhibit A" for a listing of the contracts in the sample.

Audit Methodology

As part of the planning phase, MFR gained an understanding of the contract data conversion process from AFMS to SAP.

To accomplish the scope and objectives of this performance audit, the MFR team performed the following audit procedures:

- Prepared for and conducted an entrance conference with department management responsible for administering long-term contracts.
- Conducted interviews and performed a walk through to assess operating effectiveness of management controls, and performance of related long-term contracts.
- Identified, documented, and assessed the department's processes to monitor long-term contracts.
- Researched and reviewed applicable procurement laws, policies, and procedures and determined whether the City was in compliance with the regulations.
- Verified the completeness and accuracy of the list of long-term contracts that were identified during Phase I and reconciled the significant differences.
- Reviewed the specific tasks being performed by the contractors and determined through interviews and the review of documentation, the reasons for their continued use by the City rather than utilizing City employees or other contractors.
- Determined if the original scope of contracted work had been expanded.
- Assessed, on a test basis, the level of compliance by the contractor with the scope, objectives, and contract terms by reviewing a sample of contracts and corresponding sample of support invoices.
- Performed cost benefit analysis for the selected contracts to determine whether the City was acquiring goods/services in the most economical manner.
- Obtained available market information of the costs of the services provided by the selected contract.
- Determined whether contractors identified were delinquent in payment of the City's property taxes by reviewing the tax records at the Harris County Appraisal District website.

The following exceptions were noted when MFR performed the procedures above.

OBSERVATION AND RECOMMENDATION

1. INACCURATE SAP CONTRACT DATA

Observation

During our contract population reconciliation process for phase two of the audit, MFR identified eight of the 45 contracts that had end dates before September 30, 2008 in SAP; however, according to the list prepared by HAS the contracts were open as of September 30, 2008. MFR selected four of the eight contracts for testing. For three of the four contracts tested, the payments were made after the contract end date recorded in SAP. See Exhibit "B" for a detail listing of these three contracts. The City may be at risk of making payments pertaining to contracts that may no longer be valid.

Recommendation

MFR recommends that HAS:

- Coordinate with the ERP Group to modify the contract information structure in SAP to ensure that all open purchase orders related to contracts are properly reported and reviewed to reduce the risk of unauthorized payments and extensions of executed contracts.

EXHIBIT A

Sample of SAP Contracts Greater Than Seven Years Old as of September 30, 2008

EXHIBIT A

Sample of SAP Contracts Greater Than Seven Years Old as of September 30, 2008

SAP Outlined Agreement Number	Contractor Name	Contract Start Date[1]	Contract End Date[2]	Contract Amount[3]
4600004560	3/D INTERNATIONAL, INC	03/01/1999	12/31/2007	$ 465,201
4600006288	ADAMS AND REESE LLP	06/26/2001	06/26/2012	842,979
4600004456	M ARTHUR GENSLER JR & ASSOCIATES	08/13/1995	12/30/2006	121,268
4600004558	LOCKWOOD ANDREWS & NEWNAM INC	01/25/1995	12/31/2006	10,180,545
4600006067	MCBRIDE RATCLIFF & ASSOCIATES	04/12/1999	04/12/2008	506,924
4600000510	NEW SOUTH PARKING	12/08/1999	01/28/2010	3,000,000
4600005040	OTHON INC	11/30/1999	11/30/2009	5,393,356
4600000588	ROGER BATES AIRPORT CONSULTANT	10/11/2001	01/31/2010	845,108
4600000413	SOUTHWEST AIRPORT SERVICES INC	12/07/1993	12/06/2011	7,525
4600000547	ZUCKERT SCOUTT & RASENBERGER	01/09/2001	01/09/2010	1,878,040
4600007925	BELLAMY-NORTH & ASSOCIATES	08/01/2000	08/03/2008	24,559
4600004470	CONSTRUCTION LIMITED	01/13/2000	01/13/2009	249,731
4600004468	CHARLES D GOODEN CONSULTING	05/27/1999	05/27/2007	137,146
4600004499	BROWN & ROOT (KBR)	12/30/1998	10/31/2006	777,349
4600004506	RATNALA & BAHL INC	11/20/2000	11/22/2008	18,257
TOTAL				**$24,447,988**

[1] Contract Start Date recorded in SAP as of May, 2009
[2] Contract End Date recorded in SAP as of May, 2009
[3] Contract Amount recorded in SAP as of May, 2009

EXHIBIT B

Selected Contracts with Inaccurate Dates in SAP

EXHIBIT B

Selected Contracts with Inaccurate Dates in SAP

SAP Outlined Agreement Number	Contractor Name	Contract End Date[4]	Last Payment Date
4600004560	3/D INTERNATIONAL, INC	12/31/2007	02/06/2009
4600004456	M ARTHUR GENSLER JR & ASSOCIATES	12/30/2006	03/07/2008
4600004558	LOCKWOOD ANDREWS & NEWNAM INC	12/31/2006	02/18/2009

[4] Contract End Date recorded in SAP as of May, 2009

VIEWS OF RESPONSIBLE OFFICIALS

EXHIBIT C

CITY OF HOUSTON

INTEROFFICE CORRESPONDENCE

TO: Ms. Annise D. Parker
City Controller

FROM: Eric R. Potts
Interim Airport Director
Houston Airport System

DATE: December 7, 2009

SUBJECT: Long-Term Contractor Relationships Performance Audit

We received a request from MFR, P.C. dated November 20, 2009 to provide a written response to the performance audit of the Houston Airport System ("HAS") Long-Term Contractor Relationships audit. As a result of the audit, MFR had the following Observation and Recommendation:

INACCURATE SAP CONTRACT DATA

Observation:

During our contract population reconciliation process for phase two of the audit, MFR identified eight of the 45 contracts that had end dates before September 30, 2008 in SAP; however, according to the list prepared by HAS the contracts were open as of September 30, 2009. MFR selected four of the eight contracts for testing. For three of the four contracts tested, the payments were made after the contract end date recorded in SAP. See Exhibit "B" for a detail listing of the three contracts tested. The City may be at risk of making payments pertaining to contracts that may no longer be valid.

Recommendation:

MFR recommends that HAS:

- Coordinate with the ERP Group to modify the contract information structure in SAP to ensure that all open purchase orders ("P.O.") related to contracts are properly reported and reviewed to reduce the risk of unauthorized payments and extensions of executed contracts.

Views of Responsible Officials

In response to this observation and recommendation, we would like to make the following observations:

2009 DEC -8 AM 11:

- While the control pertaining to the contract end date in SAP is not functional, HAS believes that all payments have been made against valid contracts.

- We also are concerned that payments can be made against a P.O. that may have expired.

- It is our understanding that a start and an end date must be entered when setting up the initial Outline Agreement prior to the contract being approved by City Council. Many of the contracts on the list provided are design or construction contracts which

EXHIBIT C

may not have a stated end date and may continue beyond the end date put on the Outline Agreement as it is the project and the funding that guides this. The end date on construction contracts is initially set up as 3 – 5 years from the date it is processed.

- HAS can review dates and make adjustments as we know the project is extending beyond that date. We do not know at this time whether that will require actions between HAS and the Controller's Office or whether that can be done from here. Concerns: Where is the control if it is done alone by HAS? How do we prove to Controller's that it is still valid as an on-going contract?
- Even with an end date, we need to make sure that the system will allow payment even after the date for work completed before the end date. All contracts may have a few months before the payment is made for work completed, but the final payment for a construction contract may be years after the project has been completed and requires City Council action to authorize the final retainage release.

- Even though the Outline Agreement requires an end date, the payments are made against the Purchase Order which does not have an end date requirement. This may need to be set up by the ERP team. Except for Tech. Services, HAS sections that monitor and/or pay against the P.O. can print only a screen shot of the P.O, not the entire P.O.

Some things that we are doing to monitor contracts that have no end date are:

- Monitor contracts monthly. Contracts with no payments for several months are referred back to the Planning, Design and Construction division ("PDC") to determine if they are still active.

- After Substantial Completion letters are sent from PDC, review associated design, construction management, testing contracts for final payment and closing of the P.O.

We would be happy to work with the ERP Team to effectuate changes to provide better controls on this process.

Views of Responsible Officials

Eric R. Potts

Eric R. Potts

ERP:ee

cc: Ian Wadsworth
Ellen Erenbaum
J. David Ahola, MFR, P.C.