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An Audit Report on

Selected Contracts at the Health and Human Services Commission

June 2014

Report No. 14-035

Selected Contracts at the Health and Human Services Commission

Overall Conclusion

The Health and Human Services Commission (Commission) generally complied with state requirements for contract formation and oversight for the two Electronic Benefits Transfer (EBT) system contracts audited. However, for both contracts, the Commission was unable to provide documentation showing that it complied with certain procurement requirements and scored vendors' proposals in accordance with applicable requirements.

The contracts audited were:

- The retailer management services contract, which the Commission executed in March 2007. Initially, that contract had a five-year term and was valued at \$19,776,178. However, that amount did not include certain pass-through fees the Commission was required to pay to the contractor. In addition, the Commission later amended the contract to extend the contract term. Through December 31, 2013, the Commission had made payments totaling \$43,419,389 on that contract.
- The call center services contract, which the Commission executed in December 2006. Initially, that contract had a five-year term and was valued at \$21,685,000. However, that amount did not take into account fluctuations in call volumes and call minutes associated with caseload growth. In addition, the Commission later amended the contract to extend the contract term. Through December 31, 2013, the Commission had made payments totaling \$35,306,704 on that contract.

Both of the contracts audited were with Affiliated Computer Services State and Local Solutions, Inc., which later became Xerox State and Local Solutions, Inc. Both of the contracts end in August 2014. The Commission plans to put both contracts out for bids again in June 2014.

Contract Management Processes

- **Planning** - Identify contracting objectives and contracting strategy.
- **Procurement** - Fairly and objectively select the most qualified contractors.
- **Contract Formation/Rate/Price Establishment** - Ensure that the contract contains provisions that hold the contractor accountable for producing desired results, including all relevant terms and conditions, and establish processes that are cost-effective and aligned with the cost of providing goods and services.
- **Contract Oversight** - Monitor and enforce the terms of the contract.

Source: *State of Texas Contract Management Guide*, Version 1.1.

Background Information on the Electronic Benefits Transfer (EBT) System

The Electronic Benefits Transfer (EBT) system delivers services to the State's Supplemental Nutrition Assistance Program (SNAP) and Temporary Assistance for Needy Family (TANF) program. Specifically, it provides:

- Retailer management services to assist in the delivery of Texas EBT services.
 - Call center services to assist in the delivery of Texas EBT services.
- In fiscal year 2013, the Commission was responsible for administering a total of \$6,025,856,923 in SNAP and TANF benefits. Specifically:
- The Commission was responsible for administering \$5,943,327,741 in SNAP benefits.
 - The Commission was responsible for administering \$82,529,182 in TANF benefits.

Procurement. For both contracts audited, the Commission did not maintain its vendor proposal evaluation summary tool and the related methodology it used to compile the evaluation scoring results. In addition, it was unable to provide documentation showing its compliance with *State of Texas Contract Management Guide* procurement requirements to:

- Include the weights it would use for each evaluation criterion in its solicitation documents.
- Require all employees involved in the development and evaluation of contract solicitations to sign non-disclosure and conflict of interest forms.

Additionally, the Commission did not reject a vendor proposal for the call center services contract that did not include a Historically Underutilized Businesses (HUB) subcontracting plan. (The Commission did not award the contract to the vendor that submitted that proposal.) Texas Government Code, Section 2161.252 (b), and Title 34, Texas Administrative Code, Section 20.14, require agencies to reject from consideration proposals that do not have HUB subcontracting plans.

For both contracts, the Commission also did not comply with Title 1, Texas Administrative Code, Section 391.715, which requires agencies to include proposal evaluation documentation in their procurement records.

Planning. Auditors were unable to review certain Commission planning documentation for both contracts because the Commission was no longer required to retain that documentation according to its records retention schedule. However, auditors confirmed that the Commission complied with *State of Texas Contract Management Guide* planning requirements to:

- Present its solicitation documents to the State's Contract Advisory Team for review.
- Assess contract risks and mitigating actions.
- Develop detailed statements of work.

Contract Oversight. For both contracts, the Commission performed sufficient oversight of contractor operations, made payments to contractors in a timely manner, and retained adequate supporting documentation for contractor payments. However, the Commission made \$49,628 in payments on the retailer management services contract that were not authorized by the contract. Those payments, which were related to enabling clients to use their Supplemental Nutrition Assistance Program (SNAP) benefits in other states, were authorized by a prior contract but were not authorized in the current contract.

While the Commission monitors contractor performance, it does not have a formal process for reporting information on contractor performance to executive management. In addition, the Commission should strengthen its process for estimating and reviewing contract costs to help ensure that it considers all costs.

Auditors communicated other, less significant issues separately in writing to the Commission.

Summary of Management's Response

The Commission agreed with the recommendations in this report.

Summary of Information Technology Review

Auditors relied on previous State Auditor's Office audit work on the Commission's internal accounting system (the Health and Human Services Administrative System or HHSAS) and on the Uniform Statewide Accounting System (USAS) and performed analysis regarding HHSAS data completeness to determine that HHSAS payment data for both contracts audited was reliable for the purposes of this audit.

Summary of Objectives, Scope, and Methodology

The objectives of the audit were to determine whether the Commission:

- Planned, procured, and established selected contracts for goods and services in accordance with applicable statutes, rules, Office of the Comptroller of Public Accounts (Comptroller's Office) requirements, and Commission policies and procedures to help ensure that the State's interests were protected.
- Managed and monitored selected contracts for goods and services to help ensure that contractors performed according to the terms of the contracts and that contractor billings were valid and supported, in accordance with applicable statutes, rules, Comptroller's Office requirements, and Commission policies and procedures.

The scope of this audit covered the Commission's contracting activities related to the two contracts audited from their inception in fiscal year 2005 through December 2013. The audit concentrated on all phases (planning, procurement, contract formation, and contract oversight) of the contracting process.

The audit methodology consisted of collecting and reviewing procurement documentation and contracts; conducting interviews with Commission staff; reviewing statutes, rules, Comptroller's Office requirements, and Commission policies and procedures; and performing selected tests and other procedures.

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Detailed Results

Chapter 1

For Both Contracts Audited, the Commission Was Unable to Provide Documentation Showing That It Complied with Certain Procurement Requirements and Scored or Screened Vendors' Proposals in Accordance with Applicable Requirements

Electronic Benefits Transfer (EBT) System Contracts Audited

The contracts audited were:

- The **retailer management services contract**, which the Commission executed in March 2007. Initially, that contract had a five-year term and was valued at \$19,776,178. However, that amount did not include certain pass-through fees the Commission was required to pay to the contractor. In addition, the Commission later amended the contract to extend the contract term. Through December 31, 2013, the Commission had made payments totaling \$43,419,389 on that contract.
- The **call center services contract**, which the Commission executed in December 2006. Initially, that contract had a five-year term and was valued at \$21,685,000. However, that amount did not take into account fluctuations in call volumes and call minutes associated with caseload growth. In addition, the Commission later amended the contract to extend the contract term. Through December 31, 2013, the Commission had made payments totaling \$35,306,704 on that contract.

Both of the contracts audited were with Affiliated Computer Services State and Local Solutions, Inc., which later became Xerox State and Local Solution, Inc. Both contracts end in August 2014, and the Commission plans to put both contracts out for bids again in June 2014.

For the two Electronic Benefits Transfer (EBT) system contracts audited (see text box), the Health and Human Services Commission (Commission) was unable to provide documentation demonstrating that it complied with certain procurement requirements and scored or screened vendors' proposals in accordance with applicable requirements. However, it complied with requirements to advertise its solicitations, require vendor conflict of interest disclosures, and require vendor Historically Underutilized Businesses (HUB) subcontracting plans. Auditors were unable to review certain Commission planning documentation because the Commission was no longer required to retain that documentation according to its records retention schedule.

With the exception of an issue involving the clarity of contract payment terms discussed in Chapter 2, the Commission complied with contract formation requirements in the *State of Texas Contract Management Guide*.

The Commission was unable to provide documentation showing that it complied with certain procurement requirements. For both contracts audited, the Commission did not maintain its vendor proposal evaluation summary tool and the related methodology it used to compile the evaluation scoring results. The Commission also did not maintain documentation from the oral presentations the vendors made. According to Commission memos, the oral presentations contained information that the Commission used

in its final contractor selection decisions.

The Commission asserted that it used an evaluation summary tool to consolidate the individual scoring sheets each evaluator completed and apply assigned weights to calculate the final scores for each vendor's proposal. It then summarized the final weighted scores and presented them to the executive commissioner.

The Commission also asserted that it obtained clarification during vendors' oral presentations regarding their proposals, which helped to identify vendor strengths and weaknesses that the Commission used in its final contractor selection decisions. One factor the Commission considered in its decision memos was the vendors' ability to meet Texas-specific requirements. However, the Commission was unable to provide auditors with evidence regarding the requirements that were specific to Texas or provide justification for its decisions regarding vendor qualifications related to that factor.

The Commission did not comply with Title 1, Texas Administrative Code, Section 391.715, which requires health and human services agencies to include evaluation documentation in their procurement records. Because the documentation discussed above was not available, auditors were unable to determine whether the Commission selected the proposals that provided the best value.

The Commission did not always score and screen vendor proposals properly. Specifically:

- **Retailer management services contract.** For the retailer management services contract, the Commission provided a list of 12 evaluators but only 10 proposal scoring sheets. The Commission was unable to provide documentation supporting its assertion that two of the evaluators were not present the first day the proposals were evaluated and subsequently removed from the evaluation team. With minor differences, auditors' recalculation of the evaluation scores aligned with the Commission's final evaluation scores.
- **Call center services contract.** For the call center services contract, the Commission was unable to provide documentation supporting why it did not reject one proposal that did not include the required HUB subcontracting plan. Although the Commission determined that proposal did not include a HUB subcontracting plan, it evaluated and scored the proposal for consideration in awarding the contract. Texas Government Code, Section 2161.252 (b), and Title 34, Texas Administrative Code, Section 20.14, require agencies to reject proposals that do not have HUB subcontracting plans. The Commission did not award the contract to the vendor that submitted that proposal.

The decision memo the Commission presented to the executive commissioner for the call center services contract also contained cost calculation errors. However, those errors would not have affected the Commission's final decision about which vendor to select.

- **Both contracts audited.** For both contracts audited, the proposal evaluators did not document their scores for some of the individual scoring elements listed on the score sheets. However, those errors would not have affected the Commission's final decision about which vendor to select.

Not properly scoring and screening proposals increases the risk that the Commission might not select the proposal that provides the best value.

The Commission did not include weights associated with evaluation criteria in its solicitation documents. For both contracts audited, the Commission did not include the weights it would use for each evaluation criterion in its solicitation documents. While the Commission's solicitations identified the four evaluation criteria the Commission would use to evaluate proposals, they did not disclose the scoring weights. The Commission asserts that it did not disclose the scoring weights to avoid providing potential bidders with insight into the Commission's selection methodology. Additionally, the Commission did not document the weights assigned to each criterion prior to advertising the solicitations.

The *State of Texas Contract Management Guide* requires agencies to include in solicitations, at a minimum, the weight assigned to each criterion. Not documenting decisions for not complying with that requirement and not documenting scoring weights prior to advertising solicitations could increase the risk that scoring weights could be altered to favor a specific vendor.

The Commission did not consistently comply with nondisclosure and conflict of interest requirements. For both contracts audited, the Commission was unable to provide certain nondisclosure and conflict of interest forms signed by employees involved in the development of the solicitations and evaluation of the proposals. Specifically:

- For the retailer management services contract, the Commission was unable to provide a nondisclosure form for 1 (8 percent) of 13 employees involved in the proposal evaluation process, and it was unable to provide conflict of interest forms for 3 (18 percent) of 17 employees involved in the contract development and proposal evaluation process.
- For the call center services contract, the Commission was unable to provide nondisclosure forms for 6 (46 percent) of 13 employees involved in the proposal evaluation process, and it was unable to provide conflict of interest forms for 6 (35 percent) of 17 employees involved in the contract development and proposal evaluation process.

The *State of Texas Contract Management Guide* requires each member of an evaluation team to complete a nondisclosure form prior to any involvement with proposal documents. Additionally, Texas Government Code, Section 2262.004, requires employees involved in procurements to disclose any relationship they have with entities that have contracts exceeding \$25,000. Not complying with nondisclosure and conflict of interest requirements increases the risk that employees could inappropriately share information regarding solicitations with vendors or take actions that are not in the Commission's best interests.

Additionally, for both contracts audited, none of the conflict of interest forms contained documentation of approval by the executive commissioner, as those forms required. Not documenting that approval increases the risk that objectivity in the procurement process could be impaired.

The Commission complied with certain requirements regarding advertising and solicitation content when it procured both contracts. Specifically, it:

- Advertised both solicitations on the *Electronic State Business Daily* for more than 21 days, as required by Title 34, Texas Administrative Code, Section 20.214.
- Included in both solicitations a requirement for vendors to disclose any conflicts of interest, as required by the *State of Texas Contract Management Guide*.
- Included in both solicitations a requirement for vendors to include HUB subcontracting plans in their proposals, as required by Texas Government Code, Section 2161.252.

Auditors were unable to review certain Commission planning documentation for both contracts audited because the Commission was no longer required to retain that documentation according to its records retention schedule. The Commission's record retention schedule requires the Commission to maintain planning documentation for three years after it makes its procurement decisions, and the Commission procured the two contracts audited during fiscal year 2007. However, auditors confirmed that the Commission complied with *State of Texas Contract Management Guide* planning requirements to:

- Present its solicitation documents to the State's Contract Advisory Team for review. The Commission considered all comments that team provided. It chose to incorporate 2 (20 percent) of 10 comments into the retailer management contract solicitation and 2 (33 percent) of 6 comments into the call center services contract solicitation.
- Assess contract risks and mitigating actions. (The Commission also presented its risk assessment to the State's Contract Advisory Team for review.)
- Develop detailed statements of work. The Commission included a detailed scope of work in its solicitations for both contracts audited that described vendor responsibilities, reporting requirements, and operational requirements for both contracts.

Recommendations

The Commission should:

- Comply with Texas Administrative Code requirements to maintain all evaluation documentation, including scoring methodology and scoring documents, in its procurement records.
- Comply with Texas Government Code and Texas Administrative Code requirements to include documentation of accepting and rejecting proposals in its procurement records.
- Develop and implement procedures to review the information it will use for contracting decisions to help ensure that information is accurate and complete.
- Comply with *State of Texas Contract Management Guide* requirements to include the weight assigned to each evaluation criterion in its solicitation documents.
- Require all personnel involved in the development and evaluation of the vendor proposals to sign nondisclosure and conflict of interest forms, obtain required approval of those forms, and maintain all of those forms.

Management's Response

HHSC Procurement and Contracting Service (PCS) has strengthened its policies, procedures, and review processes to ensure all procurement documents, including but not limited to (a) scoring methodologies, (b) evaluation documents, (c) the acceptance and rejection of proposals, and (d) nondisclosure and conflict of interest forms, are accurate, complete, and maintained in the procurement file.

In addition, a Contract Management Workgroup was formed in July 2013 to develop an enterprise-wide Contract Management and Risk Assessment Manual. The manual will formalize and contain comprehensive contract management policies and procedures, universal guidelines, best practices, and standards that will apply to all enterprise agencies in accordance with H.B. 3648 and S.B. 1681, 83rd Legislature, Regular Session, 2013.

While the current State of Texas Contract Management Guide requires that weights be assigned to each evaluation criterion in solicitation documents, efforts are underway within the Contract Advisory Team (CAT) to revisit this requirement to allow state agencies the flexibility not to disclose evaluation weights. PCS supports this potential change, but will take appropriate steps to ensure compliance with current Contract Management Guide requirements.

Estimated Completion Date:

September 2014 Issue Contract Management and Risk Assessment Manual

Title of Responsible Person:

Deputy Executive Commissioner for Procurement and Contracting Services

The Commission Made Payments on Both Contracts Audited in a Timely Manner, But It Made Certain Payments on the Retailer Management Services Contract That Were Not Authorized

Except for the interoperability payments discussed below, the Commission processed contract payments for both contracts audited in accordance with the *State of Texas Contract Management Guide*. Auditors tested 91 payments totaling \$10,870,589 and determined that they were properly supported and authorized, reflected the amounts documented in the contract pricing tables, and paid in a timely manner.

For the time period audited, the Commission segregated processes for verifying contractor performance, approving invoices, and processing and recording payments; it also required multiple approvals for expenditures that exceed certain dollar thresholds. The Commission established separate divisions to segregate processes for (1) verifying that contractors provide deliverables and (2) approving contractors' invoices. The Accounting Operations Division processed payments in the Commission's internal accounting system (the Health and Human Services Administrative System). The Lone Star Business Services Division and the Operations and Support Division segregated responsibilities to help ensure that (1) contractors provided deliverables and invoices agreed with the deliverables received and (2) invoice amounts were calculated correctly using the contract pricing terms in each contract's pricing tables. Additionally, the Commission had policies requiring multiple payment approvals based on dollar thresholds.

From August 2008 through December 2009, the Commission made a total of \$49,628 in interoperability fee payments on the retailer management services contract that were not authorized by the contract (see text box for additional details on interoperability).

EBT Interoperability

The Electronic Benefit Transfer Interoperability and Portability Act of 2000 mandated nationwide interoperability of Supplemental Nutrition Assistance Program (SNAP) EBT systems and portability of electronically issued benefits. The Texas EBT system supports interoperable EBT transactions for Texas clients who shop out of state and for out-of-state clients who shop in Texas.

Source: *Health and Human Services Commission Request for Offers for Texas Electronic Benefits Transfer (EBT) Retailer Management Services*, Request for Offers No. 529-06-0095.

The Commission stopped making those interoperability payments in 2009, when the contractor stopped invoicing for those services. According to the Commission, the contractor asserted that it stopped invoicing for those services because of the administrative burden associated with invoicing for those services.

Although the retailer management services contract audited did not contain language that directly obligates the Commission to pay for interoperability fees, it required the contractor to perform interoperability activities and maintain a contract with a third party (called a switch processor) to process interoperability transactions. The switch processor contract required by the retailer management services contract defined the services to be performed and the payment structure, but the Commission was not a party to the switch processor contract.

While the \$49,628 in interoperability payments the Commission made are related to the retailer management services contract, that contract did not contain specific language authorizing or obligating the Commission to make

those payments. (The Commission had amended a prior retailer management services contract to include specific language that authorized such payments.) The Commission asserts that the interoperability payments were authorized in the section of its request for offers that describes the contractor's responsibilities related to interoperability processes.

The *State of Texas Contract Management Guide* states that, when developing a contract, clarity of contract terms and completeness of the issues are primary importance to prevent misunderstanding and conflict. It also notes that a contract is legally binding only if its terms are sufficiently defined.

The Commission did not consistently record corresponding purchase order or contract numbers when it processed payments on both contracts audited. From the inception of both contracts audited through December 31, 2013, the Commission made payments on both contracts totaling approximately \$78.7 million. For \$6.5 million (8 percent) of those payments, the Commission did not record a corresponding purchase order or contract number in the Health and Human Services Administrative System. Not recording a purchase order or contract number increases the risk that the Commission could make an unauthorized payment or pay more than the authorized amount.

For both contracts audited, the Commission's expenditures for 3 (12 percent) of 26 purchase orders tested exceeded the amounts on the approved purchase orders by an insignificant amount (less than 2 percent of the purchase order amount).

Recommendations

The Commission should:

- Comply with *State of Texas Contract Management Guide* requirements to ensure that contracts contain clear and complete terms by defining all costs.
- Consistently record purchase order or contract numbers in the Health and Human Services Administrative System when it processes payments to contractors.

Management's Response

While there were instances of related purchase orders or contract numbers not being associated with the EBT contracts in the Health and Human Services Administrative System (HHSAS), the auditors found no instances of unauthorized payments or amounts associated with this issue. Accounting Operations has reviewed the transactions cited in the audit and taken steps to strengthen staff training to ensure all payment requests are associated with a valid purchase order or contract. In addition, managers who approve

vouchers have been reminded to verify and ensure that payment requests are appropriately completed.

A Contract Management Workgroup was formed in July 2013 to develop an enterprise-wide Contract Management and Risk Assessment Manual. The manual will formalize and contain comprehensive contract management policies and procedures, universal guidelines, best practices, and standards that will apply to all enterprise agencies in accordance with H.B. 3648 and S.B. 1681, 83rd Legislature, Regular Session, 2013.

This manual will provide specific guidance to HHSC and enterprise agency contract managers and staff who process and approve requisitions and payment requests to clarify:

- *The types of purchases that require (a) a requisition to be submitted and approved and (b) a purchase order or contract to be in place, before an associated payment may be processed.*
- *That business area managers are, by approving the request for payment, providing assurance that the amount requested for payment does not cause total payments against the purchase order or contract to exceed the authorized amount.*

Estimated Completion Date:

September 2014 Issue Contract Management and Risk Assessment Manual

Title of Responsible Person:

Deputy Executive Commissioner for Procurement and Contracting Services Deputy Executive Commissioner for Financial Services

The Commission Complied with Contract Monitoring Requirements for Both Contracts Audited, But It Should Ensure That Contractors Comply with Contract Requirements in a Timely Manner and Improve Its Estimation of Contract Costs

Contract Monitoring

For both contracts audited, the Commission complied with *State of Texas Contract Management Guide* requirements to monitor contract compliance by monitoring deliverables and performance and following up on contractor noncompliance. However, the Commission should strengthen its monitoring processes to help ensure that contractors comply with contract requirements in a timely manner.

The Commission has developed a formal risk assessment process to identify the contractor deliverables it will review during the year. Based on that risk assessment, during fiscal year 2013 the Commission reviewed 79 (47 percent) of the 167 retailer management services contract deliverables and 27 (25 percent) of the 109 call center services contract deliverables. The Commission also uses a spreadsheet to track contractor performance and document the contract standards for measuring compliance with contract terms. It uses the vendor performance results each year in its risk assessment.

In addition, the Commission has a formal process to follow up on contractor noncompliance with contract requirements, which includes a requirement for the Commission to approve a contractor's corrective action plan. From 2009 to 2013, the average rate of contractor noncompliance (determined through the Commission's review of contractor deliverables) was 5 percent for the retailer management services contract and 13 percent for the call center services contract (noncompliance for the call center services contract improved to 7 percent in fiscal year 2013).

The Commission generally followed its monitoring processes for both contracts audited. However, auditors identified certain aspects of monitoring that the Commission should improve. Specifically:

- For the retailer management services contract, the Commission did not have documentation showing its acceptance of the contractor's plans for corrective action for 1 (8 percent) of 12 instances in which the contractor was required to submit a corrective action plan due to noncompliance. Not consistently maintaining the corrective plan acceptance documentation increases the risk that contractors may not implement corrections.
- For the call center services contract, the Commission did not charge the contractor liquidated damages or pursue other remedies to correct repeated

noncompliance. From July 2009 through January 2013, the contractor repeatedly did not comply with a contract requirement to provide six audio tapes each quarter for the Commission’s review. While the Commission followed up with quarterly requests for corrective action plans for almost four years, it did not pursue imposing liquidated damages or other remedies.

The Commission’s uniform contract terms and conditions incorporated into both contracts audited authorize the Commission to pursue liquidated damages or other remedies for repeated contractual deficiencies. Additionally, the Commission has documented procedures that require management to review instances of contractor performance for which liquidated damages may be recommended to the Procurement and Contracting Services Division.

The Commission’s contract managers perform periodic reviews of the monitoring files to help ensure that staff perform assigned monitoring activities in a timely manner. However, that process did not fully resolve the issues discussed above. The Commission also does not have a formal process to report information about a contractor’s performance to executive management. Without formal reporting of contractor performance to executive management, the Commission increases the risk that noncompliance issues may not be escalated in a timely manner.

Contract Cost Estimates

The Commission has a formal process to develop and approve contract amendments. However, the Commission’s amendments to the two contracts audited highlighted an issue regarding its estimation of initial contract costs. The Commission did not capture all costs when it initially estimated costs associated with both contracts audited. That increases the risk that incorrect information could be reported to and used by oversight agencies and executive management for budgeting and contracting decisions. Specifically:

Pass-through Fees for the Retailer Management Services Contract

- Temporary Assistance for Needy Family (TANF) cash-back fees: \$0.50 for each of the first two cash-only transactions of \$50 or more.
 - Third-part processor fees: \$0.02 for each cash and Supplemental Nutrition Assistance Program (SNAP) EBT program transaction effected via a point-of-sale terminal.
 - Supply credits: A credit per transaction for supplies and telephone line usage necessary in connection with the use of that equipment.
- Source: Commission *Lone Star Operating Rules*.

- The Commission’s initial five-year cost estimate for the retailer management services contract was \$19,776,178. Auditors verified that amount was supported by the contract’s cost tables. However, the total actual costs for the initial five-year period were \$34,362,806, or 74 percent more than the initial cost estimate.¹ The Commission did not include pass-through fees (Temporary Assistance for Needy Family [TANF] cash back fees, third party processor fees, and supply credits, see text box for additional details) that are authorized by the Commission’s *Lone Star Operating Rules* in its initial cost estimate. The *Lone Star Operating Rules* are referenced in the retailer management services

¹ Payments on the retailer management services contract through December 31, 2013, have totaled \$43,419,389.

contract. When the Commission amended that contract to extend it for an additional 19 months, it included those pass-through fees in the contract cost estimate.

The Commission has developed a cost model to capture all actual contract costs and project future contract costs, including the pass-through fees. However, it has not formalized its methodology for that cost model and it did not review the preparation of that cost model to ensure that it contained consistent, accurate information.

- The Commission's initial five-year cost estimate for the call center services contract was \$21,685,000. However, the total actual costs for the initial five-year period were \$27,243,834, or 26 percent more than the initial cost estimate.² The Commission asserted that the initial cost estimate did not take into account fluctuations in call volumes and call minutes associated with caseload growth, which drive actual costs.

Recommendations

The Commission should:

- Consistently retain documentation showing its acceptance of contractors' corrective action plans.
- Develop and implement a formal process to periodically report information on contractor performance to management to ensure vendor performance in a timely manner.
- Strengthen its policies and procedures related to repeated contractor noncompliance, and develop criteria for addressing repeated noncompliance by imposing liquidated damages or other remedies.
- Develop and implement a formal process for estimating and reviewing contract costs to help ensure that it considers all costs.

Management's Response

HHSC formed a Contract Management Workgroup in July 2013 to develop an enterprise-wide Contract Management and Risk Assessment Manual. The manual will formalize and contain comprehensive contract management policies and procedures, universal guidelines, best practices, and standards that will apply to all enterprise agencies in accordance with H.B. 3648 and S.B. 1681, 83rd Legislature, Regular Session, 2013. While HHSC already utilizes the Comptroller's Vendor Performance Tracking System to report contractor performance, it will, in conjunction with implementation of the

² Payments on the call center services contract through December 31, 2013, have totaled \$35,306,704.

Contract Management and Risk Assessment Manual, revise and strengthen policies and procedures to (a) maintain appropriate documentation to support monitoring efforts and (b) formalize management reporting, including use of the Vendor Performance Tracking System to report contractor performance and instances of repeated noncompliance.

For EBT contracts, Lone Star Business Services currently notifies executive management of instances of contractor performance for which liquidated damages or other remedies may be assessed prior to taking action.

Lone Star Business Services will strengthen processes for retention of documentation and contractor corrective action plans by conducting random documentation reviews at least once per contract year quarter. In addition, the Office of Social Services Business Operations and Support will develop and implement a formal process for estimating and reviewing EBT contract costs to help ensure that all relevant costs are considered. Current contract cost estimates and models include fixed, variable, pass-through, and caseload-sensitive costs, with processes in place to update and maintain the models. Formal processes and procedures for estimating and reviewing contract costs will be documented and completed by June 30, 2014.

Estimated Completion Date:

June 2014 Formalize process of estimating and reviewing contract costs

August 2014 Implement Lone Star Business Services process improvements

September 2014 Issue Contract Management and Risk Assessment Manual

Title of Responsible Person:

Deputy Executive Commissioner for Procurement and Contracting Services

Director for Lone Star Business Services

Director for Program Financial Management and Budget

Appendix

Objectives, Scope, and Methodology

Objectives

The objectives of the audit were to determine whether the Health and Human Services Commission (Commission):

- Planned, procured, and established selected contracts for goods and services in accordance with applicable statutes, rules, Office of the Comptroller of Public Accounts (Comptroller's Office) requirements, and Commission policies and procedures to help ensure that the State's interests were protected.
- Managed and monitored selected contracts for goods and services to help ensure that contractors performed according to the terms of the contracts and that contractor billings were valid and supported, in accordance with applicable statutes, rules, Comptroller's Office requirements, and state entity policies and procedures.

Scope

The scope of this audit covered the Commission's contracting activities related to the following two contracts from their inception in fiscal year 2005 through December 2013:

- The Texas Electronic Benefits Transfer (EBT) Call Center Services contract, which the Commission awarded on December 20, 2006, to Affiliated Computer Services State and Local Solutions, Inc.
- The Texas Electronic Benefits Transfer (EBT) Retailer Management Services contract, which the Commission awarded on March 27, 2007, to Affiliated Computer Services State and Local Solutions, Inc.

Affiliated Computer Services State and Local Solutions, Inc. later became Xerox State and Local Solutions, Inc.

The audit concentrated on all phases (planning, procurement, contract formation, and contract oversight) of the contracting process.

Methodology

The audit methodology consisted of collecting and reviewing procurement documentation and contracts; conducting interviews with Commission staff; reviewing statutes, rules, Comptroller's Office requirements, and Commission policies and procedures; and performing selected tests and other procedures.

The selection methodology for the contracts audited was based on contract dollar amount, type of contract, recent audit coverage, length of contract, number of vendors that bid, and the effect of the contracts on the Commission's major programs.

Data Reliability and Completeness

Auditors relied on previous State Auditor's Office audit work on the Commission's internal accounting system (the Health and Human Services Administrative System or HHSAS) and on the Uniform Statewide Accounting System (USAS) and performed analysis regarding HHSAS data completeness to determine that HHSAS payment data for both contracts audited was reliable for the purposes of this audit.

Auditors verified the completeness of information in the Commission's risk assessment tool (a spreadsheet) by comparing deliverables listed in that tool with the deliverables listed in the scope of work sections of the audited contracts.

Sampling Methodology

To test the Commission's payment of contractor invoices, auditors selected samples through random selection and results may be extrapolated to the population, but accuracy of the extrapolation cannot be measured.

To test contractor deliverables, auditors used professional judgment to select a sample of deliverables for testing. The sampled deliverables were not representative of the population and, therefore, it would not be appropriate to extrapolate those test results to the population.

Information collected and reviewed included the following:

- EBT contracts and associated amendments between the Commission and Affiliated Computer Services State and Local Solutions, Inc. (which later became Xerox State and Local Solutions, Inc.).
- Commission policies and procedures, manuals, and applicable rules and regulations.
- Commission solicitation and bid documentation, evaluation criteria and documentation, major contract questionnaires, and related supporting documentation.
- Commission procurement files, including planning documentation, purchase requisition forms, purchase orders, approvals, invoices, and other supporting documentation.
- Commission past and present organizational charts for applicable divisions, and Commission personnel training and certification records and nondisclosure forms.

- Commission reports, workbooks, and spreadsheets used to monitor contracts and contract costs, including supporting documentation.
- Commission contract expenditure data from HHSAS and USAS.
- Emails and other documentation that supported information provided by Commission employees during interviews.

Procedures and tests conducted included the following:

- Interviewed employees at the Commission.
- Tested whether the Commission followed applicable guidelines in the *State of Texas Contract Management Guide* and the *State of Texas Procurement Manual* when planning for the contracts audited.
- Reviewed applicable conflict of interest statements and nondisclosure agreements.
- Tested whether the Commission properly documented bid evaluation criteria and evaluation scores.
- Reviewed contracts to determine whether the Commission included essential contract terms listed in the *State of Texas Contract Management Guide*.
- Reviewed contracts and amendments for appropriate authorizations.
- Tested criteria the Commission used to evaluate vendor proposals to determine whether it followed applicable requirements in the Texas Government Code.
- Tested scoring of Commission evaluations to determine whether all evaluators completed the same scoring matrix and to test mathematical accuracy.
- Tested samples of payments on invoices for appropriate documentation, required approvals, and timely payment.
- Tested samples of deliverables to review the Commission's monitoring process.
- Reviewed the Commission's report on the American Institute of Certified Public Accountants' Statements on Standards for Attestation Engagements No. 16 to verify whether automated controls were appropriately designed and operating effectively.

Criteria used included the following:

- Texas Government Code, Chapters 322, 572, 2054, 2151, 2155-2158, 2161, 2251, 2252, 2261, and 2262.
- Title 34, Texas Administrative Code, Chapter 20.
- Title 1, Texas Administrative Code, Chapter 391.
- *State of Texas Contract Management Guide*, Versions 1.1 and 1.9.
- *State of Texas Procurement Manual* (version released in 2012 and version in effect prior to 2012).
- Commission policies and procedures.
- *State of Texas and Health and Human Services Commission Records Retention Schedule*.

Project Information

Audit fieldwork was conducted from December 2013 through June 2014. We conducted this performance audit 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.

The following members of the State Auditor's staff performed the audit:

- Anca Pinchas, CPA, CISA, CIDA (Project Manager)
- Robert G. Kiker, CGAP (Assistant Project Manager)
- Derek J. Felderhoff, MBA
- Michael Gieringer, CFE
- Jerod Heine, MBA
- Tony White, CFE
- Becky Beachy, CIA, CGAP (Quality Control Reviewer)
- Cesar Saldivar, CGAP (Audit Manager)

Copies of this report have been distributed to the following:

Legislative Audit Committee

The Honorable David Dewhurst, Lieutenant Governor, Joint Chair

The Honorable Joe Straus III, Speaker of the House, Joint Chair

The Honorable Jim Pitts, House Appropriations Committee

The Honorable Harvey Hilderbran, House Ways and Means Committee

Office of the Governor

The Honorable Rick Perry, Governor

Health and Human Services Commission

Dr. Kyle L. Janek, Executive Commissioner



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