



An Audit Report on

**The Texas Education Agency's  
Procurement and Oversight of Texas  
Virtual School Network Contracts**

September 2016

Report No. 17-002



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## Overall Conclusion

The Texas Education Agency (Agency) should improve its contract formation processes and strengthen its oversight of the contracts audited for the Texas Virtual School Network (TxVSN) to ensure that it complies with statutes, Office of the Comptroller of Public Accounts (**Comptroller's Office**) requirements, Agency policies and procedures, and the contracts' requirements. Specifically, the Agency did not have an executed contract before it allowed the Region 10 Education Service Center in Richardson (Region 10 ESC) to administer the TxVSN. In addition, the Agency did not consistently provide sufficient oversight of certain components of its contracts with the Region 10 ESC.

The Agency executed two contracts and a contract renewal with the Region 10 ESC more than four to six months after the contracts were effective and the Region 10 ESC and its subcontractor had begun performing work covered by those contracts.<sup>1</sup> As a result, the Agency did not have a contract in place for the operation of the TxVSN for more than 15 months during fiscal years 2015 and 2016.

Although Agency staff were in frequent communication with the Region 10 ESC and its subcontractor regarding work related to the TxVSN, the Agency did not require sufficient supporting documentation to allow it to verify that

### Background Information

The Legislature established the Texas Virtual School Network (TxVSN) in 2007 to provide Texas students with equitable access to quality online courses. The Texas Education Agency (Agency) offers state-supported online learning opportunities to students across the state through the TxVSN using a network approach in partnership with school districts.

During fiscal year 2015, the Agency paid the Region 10 Education Service Center in Richardson (Region 10 ESC) \$2,175,531 to administer the TxVSN. Of that amount, invoices that Region 10 ESC submitted to the Agency indicated that \$1,326,162 was passed through to the Harris County Department of Education, which was a **subcontractor**. The Agency's contract with the Region 10 ESC for fiscal years 2016 and 2017 totals \$4,502,848.

Texas Education Code, Section 30A.052, directs the commissioner of education to contract with a regional education service center to operate the network. The Agency prepared and sent a solicitation to all education service centers for a new contract with a term beginning September 1, 2015, which it awarded to the Region 10 ESC.

The TxVSN is made up of two components:

- The TxVSN course catalog provides Texas public school students with expanded access to high school courses. Students may take online high school, advanced placement, and dual credit courses along with courses at their campus to meet their graduation plan.
- The TxVSN online schools program offers full-time virtual instruction through approved schools to eligible Texas public school students in grades 3-12.

Sources: Texas Education Code, Section 30A.052; the Uniform Statewide Accounting System; and the TxVSN Web site at <https://www.txvsn.org/>.

<sup>1</sup> A contract's "execution date" is the date on which a contract has been signed by all the necessary parties. A contract's effective date is the date on which the rights and obligations under the agreement become operational, typically the first day of the contract's term.

services were received prior to payment and expenditures were allowable. In addition, the Agency did not require Region 10 ESC to submit a monthly list of tasks and activities performed with the invoice as required by the contract or provide other documentation allowing the Agency to tie the invoices to work performed related to contract deliverables.

As a result, auditors could not determine whether (1) the Agency verified that services had been received prior to payment, (2) the reimbursements were for allowable expenditures, and (3) payments coincided with the Region 10 ESC and its subcontractor's work on the deliverables. In addition, the Agency did not complete a risk assessment for the fiscal year 2015 TxVSN contract that could have helped ensure that the Agency adequately monitored the performance of the Region 10 ESC and its subcontractor, and it did not complete all required documentation and procedures when renewing and closing out the fiscal year 2015 TxVSN contracts. However, the Agency paid invoices on time and ensured that the total payments did not exceed the budget approved in the contract.

The Agency established and generally followed entitywide contracting policies and procedures that were consistent with the *State of Texas Contract Management Guide* to award the fiscal year 2016 TxVSN contract. However, the Agency did not post certain contracting procedures to its Web site or provide a link to those procedures for inclusion on the Comptroller's Office's Web site, as required. While Agency contract managers met training and certification requirements and applicable personnel completed nondisclosure and conflict of interest statements, the Agency did not ensure that all purchasing personnel completed required disclosure statements prior to awarding the fiscal year 2016 TxVSN contract. The Agency also did not fully define the contract deliverables in its solicitation, which would have helped facilitate the Agency's monitoring of those deliverables. In addition, the Agency's review process did not ensure that the indirect cost rates included in the executed contracts were accurate. That resulted in incorrect indirect cost payments to the Region 10 ESC for fiscal year 2015.

Auditors communicated other, less significant issues related to the planning, procurement, formation, and oversight of the contracts audited to the Agency separately in writing.

Table 1 presents a summary of the findings in this report and the related issue rating. (See Appendix 2 for more information about the issue rating classifications and descriptions.)

Table 1

Summary of Chapters/Subchapters and Related Issue Ratings		
Chapter/ Subchapter	Title	Issue Rating <sup>a</sup>
1-A	The Agency Allowed the Region 10 ESC and Its Subcontractor to Perform Work on the TxVSN Without an Executed Contract	Priority
1-B	The Agency Should Strengthen Its Financial and Performance Monitoring of the TxVSN Contract	High
2	The Agency Generally Complied with Statutes and Requirements for Contract Planning and Procurement; However, It Should Strengthen Controls Over Certain Planning, Procurement, and Formation Processes	Medium
<p><sup>a</sup> A subchapter is rated Priority if the issues identified present risks or effects that if not addressed could critically affect the audited entity's ability to effectively administer the program(s)/function(s) audited. Immediate action is required to address the noted concern and reduce risks to the audited entity.</p> <p>A subchapter is rated High if the issues identified present risks or effects that if not addressed could substantially affect the audited entity's ability to effectively administer the program(s)/function(s) audited. Prompt action is essential to address the noted concern and reduce risks to the audited entity.</p> <p>A subchapter is rated Medium if the issues identified present risks or effects that if not addressed could moderately affect the audited entity's ability to effectively administer program(s)/function(s) audited. Action is needed to address the noted concern and reduce risks to a more desirable level.</p> <p>A subchapter is rated Low if the audit identified strengths that support the audited entity's ability to administer the program(s)/functions(s) audited or the issues identified do not present significant risks or effects that would negatively affect the audited entity's ability to effectively administer the program(s)/function(s) audited.</p>		

## ***Summary of Management's Response***

At the end of each chapter in this report, auditors made recommendations to address the issues identified during this audit. The Agency agreed with the recommendations in this report.

### *Audit Objective and Scope*

The objective of this audit was to determine whether the Agency procures and oversees TxVSN contracts in accordance with Texas statutes and applicable rules and regulations.

The scope of this audit covered:

- The six-month TxVSN contract and a six-month TxVSN contract renewal with the Region 10 ESC for fiscal year 2015 that was effective September 1, 2014, and ended August 31, 2015. Auditors reviewed the contract oversight phase of the contracting process for those two contracts.

- The TxVSN contract with the Region 10 ESC for fiscal year 2016, effective September 1, 2015, and ending August 31, 2017. Auditors reviewed the planning, procurement, and formation phases of the contracting process for that contract.

# Contents

## *Detailed Results*

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Chapter 1 The Agency Did Not Execute Contracts Prior to Allowing Work to Start on the TxVSN and It Did Not Sufficiently Monitor the Contract .....	1
---	---

Chapter 2 The Agency Generally Complied with Statutes and Requirements for Contract Planning and Procurement; However, It Should Strengthen Controls Over Certain Planning, Procurement, and Formation Processes .....	8
--	---

## *Appendices*

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Appendix 1 Objective, Scope, and Methodology .....	13
---	----

Appendix 2 Issue Rating Classifications and Descriptions .....	17
---	----

Appendix 3 Enrollment and Expenditure Information for TxVSN .....	18
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Appendix 4 <b>Related State Auditor's</b> Office Work .....	21
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# Detailed Results

## Chapter 1

### *The Agency Did Not Execute Contracts Prior to Allowing Work to Start on the TxVSN and It Did Not Sufficiently Monitor the Contract*

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The Texas Education Agency (Agency) did not execute the contracts for the Texas Virtual School Network (TxVSN) in a timely manner. The Agency allowed the contractor to perform services on the TxVSN while they were still negotiating contract terms, conditions, and budget. In addition, the Agency did not sufficiently monitor the TxVSN contract.

#### Chapter 1-A

#### The Agency Allowed the Region 10 ESC and Its Subcontractor to Perform Work on the TxVSN Without an Executed Contract

The Agency did not finalize the contract terms, conditions, and budget for the TxVSN prior to allowing the contractor to perform work.

Chapter 1-A  
Rating:  
Priority<sup>2</sup>

Auditors reviewed three TxVSN contracts between the Agency and the Region 10 Education Service Center in Richardson (Region 10 ESC): (1) a six-month contract for fiscal year 2015 that began September 1, 2014; (2) a six-month renewal for fiscal year 2015 that began March 1, 2015; and (3) a two-year contract for fiscal years 2016 and 2017 (referred to in this report as the fiscal year 2016 TxVSN contract) that began September 1, 2015. All three contracts were executed significantly after their effective dates. Specifically:

- The initial six-month contract for fiscal year 2015 (for September 1, 2014, through February 28, 2015) was not executed until January 9, 2015, or more than four months after the effective date of that contract.
- The other six-month contract for fiscal year 2015 (for March 1, 2015, through August 31, 2015) was a renewal of the initial contract; however, it did not include the date on which the commissioner of education signed the executed contract. On August 12, 2015, the chief deputy commissioner signed a contract approval and certification letter stating that staff were authorized to proceed with the procurement. That letter is required prior to the execution of a contract of more than \$1.0 million and serves as a routing form that is sent to the commissioner of

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<sup>2</sup> The risks related to the issues discussed in Chapter 1-A are rated as Priority because they present risks or effects that if not addressed could critically affect the audited entity's ability to effectively administer the program(s)/function(s) audited. Immediate action is required to address the noted concern and reduce risks to the audited entity.

education. The chief deputy commissioner's signature was dated more than five months after the effective date of the contract.

- The fiscal year 2016 TxVSN contract (for September 1, 2015, through August 31, 2017) was not executed until March 14, 2016, after auditors began this audit and more than six months after the effective date of that contract. That delay occurred because the Agency was engaged in negotiations with the Region 10 ESC and its subcontractor, the Harris County Department of Education, to finalize the contract terms, conditions, and budget for the TxVSN.

Because auditors determined that each of the fiscal year 2015 and 2016 contracts was executed after the contract's effective date, auditors also reviewed TxVSN contracts between the Agency and the Region 10 ESC for fiscal years 2011 through 2014. The Agency executed each of those contracts between five and nine months after the contract's effective date.

For all three of the fiscal year 2015 and 2016 contracts tested, the Agency allowed the Region 10 ESC and its subcontractor to perform the work specified in the contracts prior to the execution of those contracts. Although the Agency did not make any payments to the Region 10 ESC for services performed until after the contracts had been executed, the Agency's *Contract Development and Administration Manual* states that contracts should be signed before any services are rendered. Allowing services to be performed prior to having agreed-upon contract terms, conditions, and a budget in place limits the Agency's ability to effectively monitor the program and leaves the Agency, the contractor, and the subcontractor without adequate direction on performance and budget expectations.

#### Recommendation

The Agency should ensure that contracts are executed prior to allowing its contractors to begin work.

#### Management's Response

*The Agency agrees with the auditor's recommendation. The following facts help explain the context for the contract and contract negotiations:*

- *This is an inter-local contract with an Education Service Center that had been performing contract services regarding the TxVSN for many years. Ongoing operation of the TxVSN is required for students to complete their TxVSN related classes.*



- *In order to improve the contract, TEA entered into prolonged contract negotiations with the Education Service Center. As a result of these negotiation efforts, execution of the contract was delayed. During contract negotiations, TEA did not tell the Education Service Center to cease TxVSN operations because stopping operations would have been highly disruptive to students, districts, teachers and providers and potentially interfered with student's ability to graduate high school on time.*
- *No invoices were paid to the TxVSN until the contract was executed.*
- *Monthly invoices were reviewed pursuant to the contract terms and were not paid unless the Agency was satisfied contract services were performed.*

*TEA will put controls in place to monitor the timely execution of contracts and conduct training for staff to emphasize the need for contracts to be executed prior to allowing contractors to begin work.*

*Completion date: January 1, 2017*

*Responsible Person: Director, Purchasing and Contracts*

Chapter 1-B

### The Agency Should Strengthen Its Financial and Performance Monitoring of the TxVSN Contract

Chapter 1-B  
Rating:  
High <sup>3</sup>

The Agency did not sufficiently monitor the fiscal year 2015 TxVSN contracts. Specifically, the Agency did not verify that services had been received prior to payment, program expenditures were allowable, and payments were linked to clear and measurable deliverables. It also did not identify high-risk areas for monitoring or complete contract renewal and close-out procedures.

The Agency did not require sufficient supporting documentation to allow it to verify that services were received prior to payment, expenditures were allowable, or payments coincided with deliverables.

The Agency paid a total of \$2,175,531 to the Region 10 ESC for the fiscal year 2015 TxVSN contracts. Based on invoices that the Region 10 ESC submitted to the Agency, \$1,326,162 of that amount was passed through from the Region 10 ESC to its subcontractor, the Harris County Department of Education.

<sup>3</sup> The risks related to the issues discussed in Chapter 1-B are rated as High because they present risks or effects that if not addressed could substantially affect the audited entity's ability to effectively administer the program(s)/function(s) audited. Prompt action is essential to address the noted concern and reduce risks to the audited entity.

The Agency did not require the Region 10 ESC to provide sufficient documentation to support the expenditures submitted for reimbursement, including expenditures related to the Harris County Department of Education. Instead, invoices that the Region 10 ESC submitted generally included a total amount by object code per month and were supported by a spreadsheet that tied back to the approved budget. However, that spreadsheet did not provide detailed information about the expenditures. In addition, the invoices did not include support for the Region 10 ESC's payments to the Harris County Department of Education.

Payments to the Region 10 ESC also were not linked to clear and measurable deliverables. Specifically, the Agency did not require the Region 10 ESC to submit a monthly list of tasks and activities performed with an invoice, as required by the contract, or provide other documentation allowing the Agency to tie the invoices to work performed related to the contract deliverables. As a result, auditors could not determine whether (1) the Agency verified that services had been received prior to payment, (2) expenditures were allowable, and (3) payments coincided with the Region 10 ESC and its subcontractor's work on the deliverables.

By not requiring the Region 10 ESC to submit adequate documentation with its invoices, the Agency limits its ability to identify potentially unallowable or unsupported expenditures. For example, in a September 2015 audit report, the State Auditor's Office identified issues related to the Harris County Department of Education's invoices for its work on the TxVSN, including issues related to allowability and support for certain types of expenditures. During fiscal years 2012 and 2013, the Harris County Department of Education was unable to provide sufficient documentation to support \$223,745 in fiscal year 2012 and \$137,431 in fiscal year 2013 for salary expenses for information technology staff, and an additional \$314,431 in fiscal year 2012 and \$177,100 in fiscal year 2013 for support salaries related to the TxVSN. In addition, the Harris County Department of Education allocated (1) \$86,315 to the TxVSN in fiscal year 2012 for office space renovations that were completed in November 2010 and (2) \$90,000 to the TxVSN in fiscal year 2013 specifically to expand an emergency alert system; however, that expansion was not performed and the Harris County Department of Education fully expended that \$90,000 for other purposes. For more complete information on the issues identified, see *An Audit Report on Selected State Contracts and Grants at the Harris County Department of Education* (State Auditor's Office Report No. 16-004, September 2015).

The Agency's *Contract Development and Administration Manual* states that invoices should detail the services performed and associated costs, and that invoices should be reviewed to ensure all of the following: (1) the

contractor's billing coincides with the contract's progress, (2) the invoice corresponds with the contract terms, and (3) the costs shown are allowable. In addition, the Agency's *Contract Development and Administration Manual* states that costs must be adequately documented<sup>4</sup> to determine whether they are allowable, and that contract payments must be linked to a clear and measurable deliverable.

The Agency reviewed and approved all invoices, made payments to the Region 10 ESC in a timely manner, required the submission of historically underutilized business subcontracting plan progress reports from the Region 10 ESC and the Harris County Department of Education with each invoice, and ensured that total payments did not exceed the budget or amount agreed to in the contracts.

The Agency should strengthen its performance monitoring and perform a risk assessment to identify high-risk areas for focused monitoring activities.

The Agency conducted monthly phone conferences with the Region 10 ESC and the Harris County Department of Education to monitor deliverables related to the fiscal year 2015 TxVSN contracts. As a result, auditors tested 36 elements associated with the 9 deliverables identified in the fiscal year 2015 TxVSN contracts, and determined that the Agency adequately monitored 31 of those elements. However, the Agency did not consistently:

- Provide timely review, approval, and oversight of new systems, updates, or changes to existing systems, services, procedures, or documentation. For example, based on a review of monthly status meeting agendas, the Agency did not approve in a timely manner a proposed Web application development plan submitted by the Region 10 ESC during the initial fiscal year 2015 contract. As a result, the Region 10 ESC was unable to proceed with that Web application development until near the conclusion of the contract period.
- Monitor whether the Region 10 ESC was keeping all software licensures in compliance and up to date. The Region 10 ESC did not report on software licensures, as required by the contract.
- Monitor whether the Region 10 ESC provided required quarterly reports related to the availability of service, downtime, and usage of TxVSN systems.

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<sup>4</sup> According to the Agency's *Contract Development and Administration Manual*, required documentation may include, but is not limited to, travel records, time sheets (time and effort), actual invoices to support costs, contracts and subcontracts, mileage and travel records, billing records, telephone bills, and any other documentation that verifies the expenditure amount and the appropriateness of submitted invoices.

- Verify the accuracy of self-reported data and reports that the Region 10 ESC submits to the Agency.
- Approve a TxVSN guide for verbal and written communication that was developed by the Region 10 ESC. That guide was submitted to the Agency in April 2014, but it had not been approved as of April 2016.

The Agency did not complete a monitoring risk assessment for the fiscal year 2015 TxVSN contracts. According to the *State of Texas Contract Management Guide*, a preliminary risk assessment should be conducted to make an initial determination about the level, type, and amount of management, oversight, and resources required to plan and implement a contract from beginning to end. Completing a risk assessment would help the Agency identify high-risk areas on which to focus its monitoring efforts and help ensure that it adequately monitors key deliverables of the TxVSN contract.

The Agency did not complete all required contract renewal and close-out procedures for its fiscal year 2015 TxVSN contracts.

During the contract renewal and close-out processes for the TxVSN contracts in fiscal year 2015, the Agency did not complete all procedures and documentation required by its *Contract Development and Administration Manual*. Specifically, the Agency did not complete a cost-benefit analysis, contractor performance evaluation, and contract renewal form. In addition, the Agency did not ensure that the purchase order for the fiscal year 2015 TxVSN contract had been closed until more than five months after it made the last payment.

Without completing the documentation and procedures required for contract renewal and close-out, the Agency may not have all the necessary information to (1) determine whether a contract should be renewed or (2) close out a contract in a timely manner. In addition, having documentation related to a contractor's performance can help the Agency when preparing new solicitations.

#### Recommendations

##### The Agency should:

- Require the contractor to provide sufficient supporting documentation, including tasks and activities performed, with the submission of an invoice to allow the Agency to determine whether services had been received and whether the expenditures were allowable.

- Perform a monitoring risk assessment for all contracts to determine the high-risk areas of the contracts on which the Agency should concentrate its monitoring activities, and conduct performance monitoring of key deliverables consistent with the results of the risk assessment.
- Ensure that all documentation and procedures that are required to renew or close out a contract have been completed.

### **Management's Response**

*The Agency agrees with the auditor's recommendations. Although the Agency adequately monitored 31 of the 36 elements associated with nine deliverables, the Agency lacked documentation to support services were received for 5 of the 36 elements audited. The following facts explain the context for the contract:*

- *TEA was in continuous contact with ESC Region 10 regarding the contract budget, contract milestones and contract completion. Much of the TEA monitoring communication was over the phone and was not logged in written documents. Therefore while the contract was being monitored, TEA cannot substantiate all communications and monitoring activities with written documentation.*
- *Monthly invoices were reviewed pursuant to the contract terms and were not paid unless the Agency was satisfied contract services were performed.*
- *The contract was fulfilled on time and within budget.*

*TEA will require all Agency contractors to provide sufficient supporting documentation, including tasks and activities performed, with the submission of an invoice to allow the Agency to determine whether services had been received and whether the expenditures were allowable. The Agency will perform a monitoring risk assessment for all contracts to determine the higher risk areas of the contracts on which the Agency should concentrate its monitoring activities, and conduct performance monitoring of key deliverables consistent with the results of the risk assessment. Also, the Agency will put controls in place to ensure that all documentation and procedures required to renew or closeout a contract have been completed.*

*Completion date: January 1, 2017*

*Responsible Person: Director, Purchasing and Contracts*

## The Agency Generally Complied with Statutes and Requirements for Contract Planning and Procurement; However, It Should Strengthen Controls Over Certain Planning, Procurement, and Formation Processes

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Chapter 2  
Rating:  
Medium <sup>5</sup>

The Agency generally planned and procured the fiscal year 2016 TxVSN contract that it awarded to the Region 10 ESC in accordance with applicable statutes, rules, Office of the Comptroller of Public Accounts (Comptroller's Office) requirements, and Agency policies and procedures. However, the Agency should ensure that statutorily required Web site postings have been added, that appropriate personnel complete required disclosure statements, and that the deliverables contained in the solicitation are completely defined to aid in monitoring the Region 10 ESC's performance. In addition, it should verify that all contract terms are accurate.

The Agency did not ensure that it had added required procedure postings to its Web site and that it had provided a link to those procedures on the **Comptroller's Office's Web site**.

The Agency established contracting policies and procedures in its *Contract Development and Administration Manual* that provide a standard entity-wide contracting process and are consistent with the *State of Texas Contract Management Guide*. As required by Texas Government Code, Section 2261.256(a), the Agency developed contracting procedures that (1) assess the risk of fraud, abuse, or waste in the contractor selection process, contract provisions, and payment and reimbursement rates and methods for the goods and services for which the Agency contracts; (2) identify contracts that require enhanced contract monitoring or the immediate attention of contract management staff; and (3) establish clear levels of purchasing accountability and staff responsibilities related to purchasing.

However, the Agency did not post on its Web site procedures related to (1) identifying contracts requiring enhanced contract monitoring or the immediate attention of contract management staff and (2) the establishment of clear levels of purchasing accountability and staff responsibilities related to purchasing, or provide a link to those procedures for inclusion on the Comptroller's Office's Web site as required by Texas Government Code, Section 2261.256(c). As a result, those Web sites do not contain the Agency's procedures to identify contracts requiring additional oversight or

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<sup>5</sup> The risks related to the issues discussed in Chapter 2 are rated as Medium because they present risks or effects that if not addressed could moderately affect the audited entity's ability to effectively administer program(s)/function(s) audited. Action is needed to address the noted concern and reduce risks to a more desirable level.

clarify accountability for purchasing, both of which would increase transparency for the Agency's contracting process.

The Agency ensured that contract managers met training and certification requirements, but it should ensure that all appropriate personnel complete the required disclosure statements.

Agency contract managers associated with the fiscal year 2016 TxVSN contract met training and certification requirements for managing the contract, and the Agency assigned program staff with knowledge of the TxVSN to provide oversight of the TxVSN. In addition, all Agency employees involved in the contracting process completed nondisclosure and conflict of interest statements.

However, three Agency employees involved in the contracting process did not complete a required disclosure statement for purchasing personnel. Those three employees were involved in the development of the solicitation, served on the proposal evaluation team, or serve as the point of contact for the contract.

The *State of Texas Contract Management Guide* and the *Agency's Contract Development and Administration Manual* require purchasing personnel<sup>6</sup> to submit a completed disclosure statement for purchasing personnel prior to the award of any major contract.<sup>7</sup>

Auditors did not identify any conflicts of interest among the Agency's purchasing personnel. However, if the Agency does not ensure that employees who meet the definition of purchasing personnel have completed the required disclosure form, there is an increased risk that those employees may have an undisclosed conflict of interest.

The Agency generally planned and procured the fiscal year 2016 TxVSN contract **according to applicable requirements; however, the Agency's solicitation** did not include some elements that would have facilitated the monitoring of deliverables.

To help ensure compliance with applicable state laws, rules, requirements, and Agency policies and procedures, the Agency performed the following contract planning and procurement activities for the fiscal year 2016 TxVSN contract:

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<sup>6</sup> Texas Government Code, Section 2262.004, defines purchasing personnel as an employee of a state agency who makes decisions on behalf of the state agency or recommendations regarding (1) contract terms or conditions on a major contract; (2) who is to be awarded a major contract; (3) preparation of a solicitation for a major contract; or (4) evaluation of a bid or proposal.

<sup>7</sup> Texas Government Code, Section 2262.001, defines a major contract as a contract having a value of at least \$1 million.

- Performed a preliminary contract risk assessment.
- Selected the appropriate procurement method.
- Adopted historically underutilized business rules equivalent to the rules adopted by the Comptroller's Office and determined that there would be subcontracting opportunities prior to the solicitation.
- Ensured that evaluation criteria for selecting the winning bidder reflected the essential qualities and performance requirements to achieve the contract objectives.
- Approved the solicitation prior to advertisement.
- Sent the solicitation to each of the regional education service centers.

In addition, the Agency ensured that the solicitation included required components, including the project description, proposal requirements, request for contractor qualifications, best value considerations, and proposal evaluation criteria. However, the *State of Texas Contract Management Guide* provides a list of elements that should be included in a solicitation so that each deliverable is clearly defined, which helps set the conditions for monitoring. While the Agency included a description of the work to be performed and a standard of performance for each deliverable in the solicitation, it did not ensure that the solicitation included sufficient procedures for verifying, monitoring the quality of, and accepting each deliverable. In addition, it did not specify for each deliverable a compensation structure consistent with the type and value of work performed, or a contractual remedy for deliverables that do not meet standards specified in its contract.

Not fully defining the elements of each deliverable increases the risk that the Agency may not receive the quality of deliverables it expects from the contractor.

The Agency did not ensure that the indirect cost rates stated in its TxVSN contracts were accurate.

The Agency's contract review and approval process did not ensure that all terms in its contracts with the Region 10 ESC for the TxVSN were accurate. Specifically, the indirect cost rates approved in all three of the fiscal year 2015 and 2016 TxVSN contracts tested did not match the Agency-approved indirect cost rates for the Region 10 ESC during the relevant time periods. As a result, the amounts the Agency reimbursed the Region 10 ESC for indirect costs related to the TxVSN during fiscal year 2015 were incorrect. Due to the incorrect indirect cost rates, the payment for the initial six-month fiscal year



2015 contract was overstated by \$247, while the payment for the six-month fiscal year 2015 contract renewal was understated by \$4,436.<sup>8</sup> Although those amounts are a small portion of the total expenditures, not ensuring that indirect cost rates are accurate increases the risk that the Agency may pay more than it should for those expenditures.

#### Recommendations

The Agency should:

- Ensure that the required Agency procedures are posted on its Web site and provide the Comptroller's Office a link to those procedures as required by Texas Government Code, Section 2261.256.
- When applicable, ensure that all employees involved in the contracting process have completed a disclosure statement for purchasing personnel prior to their involvement with the contract, as required by the *State of Texas Contract Management Guide* and Agency contracting policy.
- Ensure that all elements recommended in the *State of Texas Contract Management Guide* to clearly define contract deliverables are included in a solicitation document prior to release.
- Strengthen its review process for contracts to ensure that all terms in contracts are accurate.

#### Management's Response

*The Agency agrees with the auditor's recommendations.*

*The Agency will ensure that the required Agency policies and procedures are posted on its Web site and provide the Comptroller's Office a link to those policies and procedures as required by Texas Government Code, Section 2261.256.*

*Completion date: By September 30, 2016*

*The Agency will ensure all staff are aware of the applicable Disclosure Statement for Purchasing Personnel form documents required for each contract.*

*Completion date: September 30, 2016*

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<sup>8</sup> As of April 2016, the Agency had not made any indirect cost payments for the fiscal year 2016 contract audited.

*The Agency will ensure that all elements of the State of Texas Contract Management Guide that define contract deliverables are included in the solicitations document prior to release.*

*Completion date: January 1, 2017*

*The Agency will strengthen its review process and controls to ensure that all terms in the contract are accurate.*

*Completion date: September 30, 2016*

*Responsible Person: Director, Purchasing and Contracts*

# Appendices

## Appendix 1

### *Objective, Scope, and Methodology*

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#### Objective

The objective of this audit was to determine whether the Texas Education Agency (Agency) procures and oversees Texas Virtual School Network (TxVSN) contracts in accordance with Texas statutes and applicable rules and regulations.

#### Scope

The scope of this audit covered:

- The six month TxVSN contract and a six month TxVSN contract renewal with the Region 10 Education Service Center in Richardson (Region 10 ESC) for fiscal year 2015 that was effective September 1, 2014, and ended August 31, 2015. Auditors reviewed the contract oversight phase of the contracting process for those two contracts.
- The TxVSN contract with the Region 10 ESC for fiscal year 2016, effective September 1, 2015, and ending August 31, 2017. Auditors reviewed the planning, procurement, and formation phases of the contracting process for that contract.

#### Methodology

The audit methodology consisted of collecting and reviewing contract planning, procurement, formation, and oversight documentation, including the TxVSN contracts; conducting interviews with Agency staff; reviewing statutes and rules, Office of the Comptroller of Public Accounts (Comptroller's Office) requirements, and Agency policies and procedures; and performing selected tests and other procedures.

#### **Data Reliability and Completeness**

Auditors used expenditure information in the Uniform Statewide Accounting System (USAS) and relied on previous State Auditor's Office audit work to determine that data was sufficiently reliable for the purposes of this audit. Additionally, auditors relied on prior State Auditor's Office audit work that tested general and application controls for the Agency's Centralized Accounting and Payroll/Personnel System (CAPPS). Auditors did not perform any additional information technology work at the Agency.

## Sampling Methodology

Auditors tested all TxVSN contract expenditures and reviewed all monthly monitoring activities for all deliverables identified in the two fiscal year 2015 TxVSN contracts.

Information collected and reviewed included the following:

- TxVSN contracts between the Agency and the Region 10 ESC.
- Agency policies and procedures, manuals, and monitoring tools.
- Agency solicitation and bid documentation, evaluation criteria and documentation, and related supporting documentation.
- Agency contract procurement documentation, including planning documentation, approvals, and other supporting documentation.
- Agency personnel training and certification records, financial disclosure statements, disclosure statements for purchasing personnel, and nondisclosure and conflict of interest statements.
- Agency expenditure data from USAS.
- Agency payment documentation, including contractor invoices, approvals, and other supporting documentation.
- Legislative Budget Board contract database.
- Agency internal audit reports.
- A prior State Auditor's Office report and prior information technology work.

Procedures and tests conducted included the following:

- Interviewed Agency staff about contract management.
- Reviewed the Agency's contracting policies and procedures to determine whether they aligned with the *State of Texas Contract Management Guide*.
- Reviewed whether the Agency had posted to its Web site its procedures for identifying contracts that require enhanced contract monitoring and procedures to establish clear levels of purchasing accountability and responsibility, and whether a link to those procedures was provided on the Comptroller's Office's Web site, as required by Texas Government Code, Section 2261.256(c).

- Tested whether Agency’s purchasing staff and contract managers met the training and certification requirements outlined in the *State of Texas Procurement Manual*; Texas Government Code, Sections 2155.078 and 2262.053; and the Agency’s *Contract Development and Administration Manual*.
- Tested whether the Agency adopted historically underutilized business rules equivalent to the rules adopted by the Comptroller’s Office.
- Reviewed planning documentation to determine whether the Agency (1) performed a needs assessment that identified risks, constraints, and objectives; (2) performed a preliminary risk assessment; (3) involved the appropriate sponsors and staff in planning the procurement; (4) selected the appropriate procurement method; and (5) included all elements required by the *State of Texas Contract Management Guide* in its solicitation.
- Reviewed applicable (1) financial disclosure statements, (2) disclosure statements for purchasing personnel, and (3) nondisclosure and conflict of interest statements.
- Tested whether the Agency properly documented bid evaluation criteria and used that criteria when selecting the contractor.
- Reviewed the selected contracts and related supporting documentation to determine whether they contained timely approvals, payment methodology, and applicable essential terms from the *State of Texas Contract Management Guide*, and whether they complied with other requirements.
- Tested contract expenditures for accuracy; proper approvals; and compliance with contract terms, the *State of Texas Contract Management Guide*, the Agency’s *Contract Development and Administration Manual*, and Texas Government Code, Chapter 2251.
- Tested contract expenditures to determine whether payments were for services received and were linked to deliverables.
- Tested the Agency’s monitoring activities for compliance with contract terms, including contract deliverables.

Criteria used included the following:

- Texas Education Code, Chapter 30A.
- Texas Government Code, Chapters 322, 572, 791, 2155, 2156, 2161, 2251, 2252, 2254, 2261, and 2262.
- Title 19, Texas Administrative Code, Chapter 70.
- *State of Texas Contract Management Guide*, versions 1.13 and 1.14.
- *The Agency's Contract Development and Administration Manual*, revised February 2015.
- Contract terms in the selected contracts.

#### Project Information

Audit fieldwork was conducted from January 2016 through June 2016. 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:

- Tony White, CFE (Project Manager)
- Naima Hafeez, MBA (Assistant Project Manager)
- Frances Mikus Barker, MSA
- Jennifer Grant
- Norman G. Holz II, CPA
- Joseph A. Kozak, CPA, CISA
- Jacqueline M. Thompson, CFE
- Dana Musgrave, MBA (Quality Control Reviewer)
- Audrey O'Neill, CIA, CFE, CGAP (Audit Manager)

## Issue Rating Classifications and Descriptions

Auditors used professional judgement and rated the audit findings identified in this report. Those issue ratings are summarized in the report chapters/sub-chapters. The issue ratings were determined based on the degree of risk or effect of the findings in relation to the audit objective.

In determining the ratings of audit findings, auditors considered factors such as financial impact; potential failure to meet program/function objectives; noncompliance with state statute(s), rules, regulations, and other requirements or criteria; and the inadequacy of the design and/or operating effectiveness of internal controls. In addition, evidence of potential fraud, waste, or abuse; significant control environment issues; and little to no corrective action for issues previously identified could increase the ratings for audit findings. Auditors also identified and considered other factors when appropriate.

Table 2 provides a description of the issue ratings presented in this report.

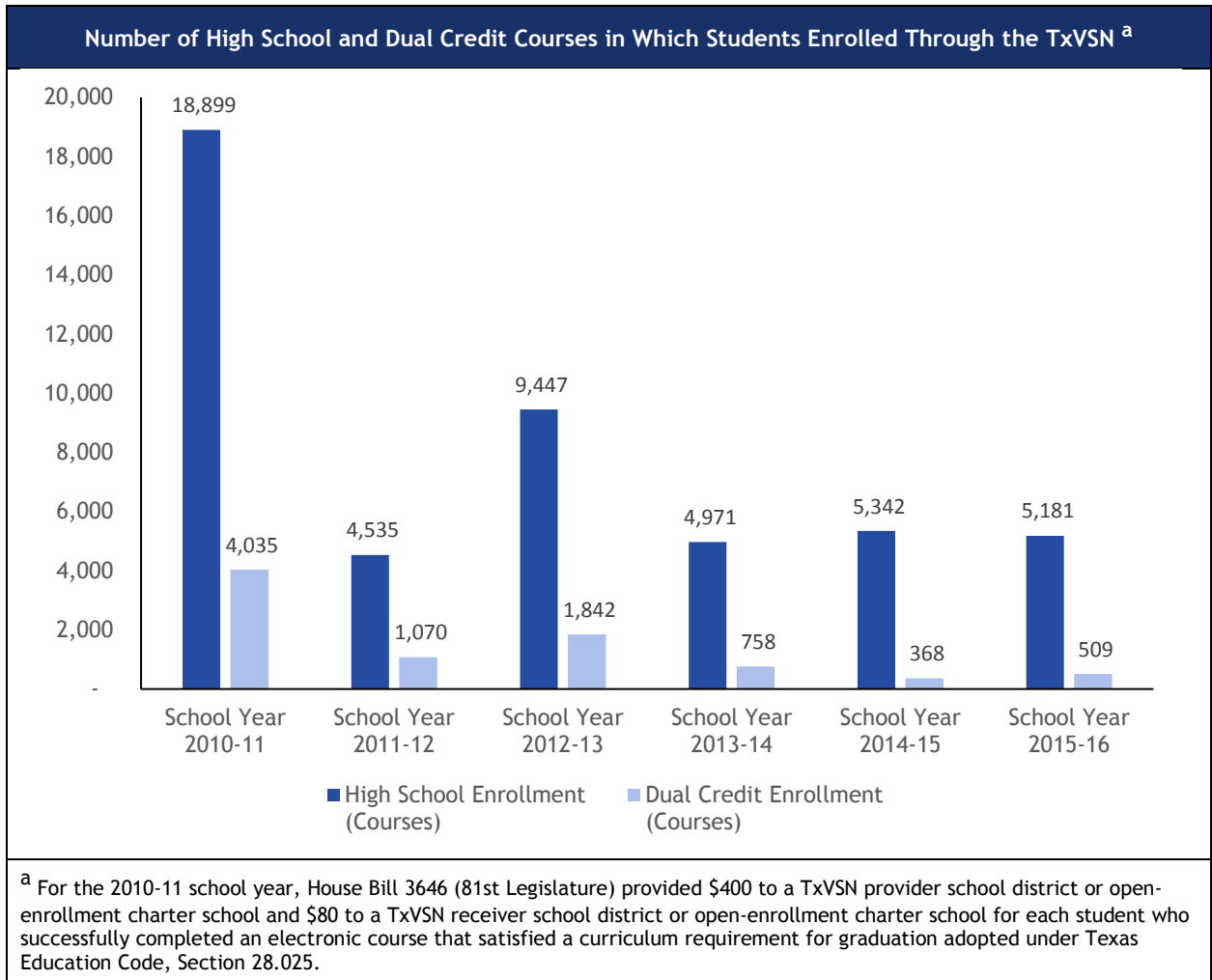
Table 2

Summary of Issue Ratings	
Issue Rating	Description of Rating
Low	The audit identified strengths that support the audited entity's ability to administer the program(s)/functions(s) audited or the issues identified do not present significant risks or effects that would negatively affect the audited entity's ability to effectively administer the program(s)/function(s) audited.
Medium	Issues identified present risks or effects that if not addressed could moderately affect the audited entity's ability to effectively administer program(s)/function(s) audited. Action is needed to address the noted concern(s) and reduce risks to a more desirable level.
High	Issues identified present risks or effects that if not addressed could substantially affect the audited entity's ability to effectively administer the program(s)/function(s) audited. Prompt action is essential to address the noted concern(s) and reduce risks to the audited entity.
Priority	Issues identified present risks or effects that if not addressed could critically affect the audited entity's ability to effectively administer the program(s)/function(s) audited. Immediate action is required to address the noted concern(s) and reduce risks to the audited entity.

## Enrollment and Expenditure Information for TxVSN

Figure 1 shows the number of high school and dual credit courses in which students enrolled through the Texas Virtual School Network (TxVSN) for school years 2010-11 through 2015-16.

Figure 1

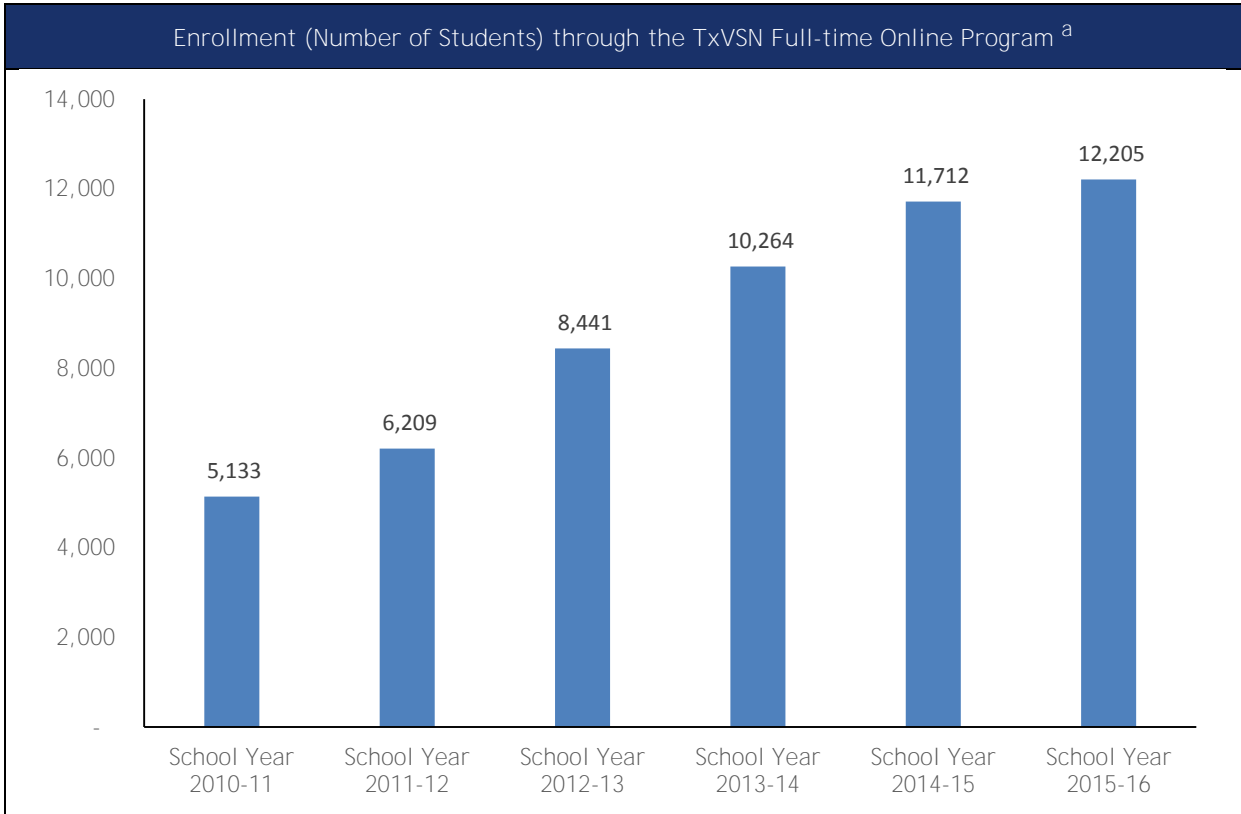


Source: Unaudited data provided by the Texas Education Agency.



Figure 2 shows the number of students enrolled in the TxVSN’s full-time online program for school years 2010-11 through 2015-16.

Figure 2



<sup>a</sup> The Texas Education Agency counts enrollment of fewer than five **students in a provider’s grade level as one student**. There were six instances in which a provider had fewer than five students in a grade level during the 2013-14 school year, three instances in which a provider had fewer than five students in a grade level during the 2014-15 school year, and one instance in which a provider had fewer than five students in a grade level during the 2015-16 school year.

Source: Unaudited data provided by the Texas Education Agency.

The Texas Education Agency receives an appropriation through a rider in the General Appropriations Act for the operation of the TxVSN. Table 3 shows the expenditures for the TxVSN for appropriation years 2010 through 2015.

Table 3

Expenditures for the TxVSN from Appropriated Funds	
Appropriation Year	Expenditures
2010	\$4,436,577
2011	\$17,842,386 <sup>a</sup>
2012	\$3,963,838
2013	\$3,464,028
2014	\$2,294,964
2015	\$2,178,031

<sup>a</sup> For the 2010-11 school year, House Bill 3646 (81st Legislature) provided \$400 to a TxVSN provider school district or open-enrollment charter school and \$80 to a TxVSN receiver school district or open-enrollment charter school for each student who successfully completed an electronic course that satisfied a curriculum requirement for graduation adopted under Texas Education Code, Section 28.025.

Source: Uniform Statewide Accounting System.

For the TxVSN course catalog, in addition to appropriated funding, a student’s school district or open-enrollment charter school pays the TxVSN for courses. The TxVSN collects payment from the student’s school district or open-enrollment charter school and then pays the selected course provider. If the student successfully completes the TxVSN course, then TxVSN operations invoices the school district or open-enrollment charter school for 100 percent of the course cost; however, if the student is not successful or drops the course after the designated drop period, then TxVSN operations invoices the school district or open-enrollment charter school for only 70 percent of the course cost.

For the TxVSN full-time online schools program, eligible school districts and open-enrollment charter schools earn funding for a student enrolled in courses in the same manner they earn funding for a student who is enrolled in a traditional classroom setting, provided that the student successfully completes the courses.

## **Related State Auditor's Office Work**

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<b>Related State Auditor's Office Work</b>		
Number	Product Name	Release Date
16-004	An Audit Report on Selected State Contracts and Grants at the Harris County Department of Education	September 2015
15-042	An Audit Report on Selected Major Agreements Under the Texas Economic Development Act	August 2015
15-009	An Audit Report on Selected Major Agreements Under the Texas Economic Development Act	November 2014
13-042	An Audit Report on Selected State Contracts at the Texas Education Agency	July 2013

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