

Office of Internal Audit

Department Terms and Conditions Audit



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Prepared for Audit Committee Meeting of the Department of Employee Trust Funds, 12.08.22;
prepared by Michelle Hoehne
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Reviewed and approved by Yikchau Sze, Director, Office of Internal Audit
Electronically Signed XX/XX/22

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Executive Summary

We have completed an audit of the Department Terms and Conditions (DTCs) used in Department of Employee Trust Funds (ETF) procurement and contracting for goods and services. These DTCs are managed by the Bureau of Budget, Contract Administration, and Procurement (BCAP), with assistance from the Office of Legal Services (OLS) and other ETF subject matter experts (SMEs). This audit was completed in accordance with the fiscal year (FY) 2022-2023 Biennial Audit Plan to determine whether ETF has processes in place to ensure DTCs are appropriately maintained and applied, including which contracts include which DTCs and the basis of any mandatory DTCs and their application.

During FY 2022 ETF had approximately \$50 million in contract expenditures on administrative supplies and services and for other third-party administration non-benefit disbursements. Our audit focused primarily on higher risk procurements that occurred during the past several years. Our review resulted in no audit findings as we did not identify any significant concerns with the processes to maintain and apply ETF's DTCs. However, we provided two process improvement suggestions for management's consideration.

Background

ETF Procurement

ETF has the need to procure external goods and services to support its many programs and operations. Procurement is managed centrally by BCAP, with collaboration from OLS and other ETF SMEs. During FY 2022, ETF had approximately \$50 million in contract expenditures on administrative supplies and services and for other third-party administration non-benefit disbursements¹.

ETF's procurement falls under two different Wisconsin statutory authorities – Chapter 16 and Chapter 40. Chapter 16 procurements, for which procurement rules are established by Wisconsin's Department of Administration (DOA), are used for general goods and services needed for ETF operations. For contracts established under Chapter 16 authority, DOA has developed various procurement forms and standard terms and conditions that need to be used in contracts. Specific to contract terms and conditions, DOA guidance included in the State Procurement Manual (Section PRO-404) indicates that these required terms and conditions may be incorporated into additional terms established by agencies. However, the guidance also allows a procuring agency's legal counsel to authorize exceptions to those terms during contract negotiations. Chapter 40 of Wisconsin Statutes provides ETF's governing boards independent contractual authority. This authority is for purchasing program-related services and those services directly related to the different boards' fiduciary responsibilities. ETF has an agreement with DOA that for Chapter 40 procurements, ETF will use applicable DOA guidance, but ETF has additional discretion throughout the procurement process.

ETF has developed its own DTCs to be used in the procurement process. These DTCs are used in contracts with vendors to govern the contractual relationship and protect ETF's business interests by mitigating common contract risks. ETF currently has 43 clauses within the DTCs covering a wide variety of topics that can be included in vendor contracts. The standard terms and conditions as established by DOA were used in the development of ETF's DTCs.

DTC Maintenance

In 2017 ETF established a DTC workgroup made up of BCAP and OLS staff, along with other ETF SMEs. The SMEs included in the workgroup are ETF staff from the following areas: information technology, information security management, policy, privacy, and compliance, and program management areas. This workgroup is charged with proposing and reviewing any changes necessary to ETF's DTCs.

¹ Ref. ETF | 9.2.22 | 6D - Administrative Supplies and Services and Non-Benefit Disbursements Charged to Benefit Program Appropriations

DTC Application to Procurements

During the fall of 2021, BCAP, with assistance from OLS, formalized guidance on the DTCs application to procurements. This DTC Guidance on Use document is intended to provide ETF staff with a general decision-making framework to help protect ETF's interests, drive consistency in decision-making, encourage competition in the procurement process, allow for timely contract negotiations and make efficient use of staff time, all while reducing risk in the procurement process. It discusses the roles of BCAP, OLS and other stakeholders and includes purchase risk factors to consider. These risk factors include urgency, cost, the nature of the good/services, if confidential information is involved, the length of the contract, and experience with the market/service. The document provides general guidance of how DTCs are applied based on the type of procurement and overall risk level determined based on the risk factors.

For higher risk procurements -- as well as some medium risk procurements -- ETF's general position is to include all ETF DTCs in the contract. For other contracts, ETF has identified critical DTCs that should be included, if possible. There are some contracts for which ETF may need to use a vendor's terms as a starting point in negotiation. In those instances, ETF will try to negotiate contract language in for those DTCs identified as critical. Further, for higher risk procurements, ETF OLS will often identify DTCs for which substantial changes will not be allowed for the specific procurement. When submitting proposals or bids, vendors are not typically allowed to include assumptions or exceptions to those terms. However, ETF may negotiate minor issues, as determined acceptable by OLS, with the language in those DTCs to support a vendor-required change. If there are significant deviations from the established DTC Guidance on Use that are necessary to establish a contract, procurement staff work with OLS to determine acceptability, note these in the procurement file and make the ETF signatory aware of the deviations prior to signing the contract.

Audit Objective and Scope

Our audit was conducted in conformance with International Standards for the Professional Practice of Internal Auditing issued by the International Internal Audit Standards Board.

The audit objective was to determine whether ETF has processes in place to ensure DTCs are appropriately maintained and applied, including which contracts include which DTCs and the basis of any mandatory DTCs and their application. The scope included the current DTC process for procurements, including those under both Chapter 16 and Chapter 40 procurement authority.

Results and Recommendations

Positive Results

Overall, we did not identify significant concerns with the maintenance and application of ETF's DTCs. We found that:

- ETF's DTCs have been designed to protect the business needs of ETF.
- A framework has been developed to guide ETF staff in the procurement process as it relates to DTC application. Providing risk-based guidance, this framework still allows for the flexibility needed with the wide variation of services and goods needing to be procured to support ETF programs and operations.
- ETF legal and procurement staff, along with ETF SMEs, collaborate throughout the contract negotiation phase to obtain the best possible terms for ETF contracts.
- ETF DTCs are reviewed and modified, as needed by procurement and legal staff, as well as other ETF SMEs. We found recent DTC modifications to incorporate common industry terms identified by vendors through recent procurements.
- Surveyed ETF management involved in recent procurements did not identify concerns with ETF's DTCs being overly restrictive, which could lead to a decrease in vendor competition.

Process Improvement Considerations

Although we did not identify significant concerns with the maintenance and application of the DTCs, we identified the following process improvement suggestions for management's consideration:

- DOA Terms and Conditions Crosswalk: In our review of ETF's DTCs to DOA's Standard Terms and Conditions, we were not able to identify the incorporation of all DOA's terms and conditions into ETF's DTCs. Additionally, there was not documentation supporting the decision to exclude certain DOA terms and conditions from ETF's DTCs or elsewhere in the contracts that we reviewed. We recommended that ETF staff complete a crosswalk from DOA terms and conditions to ETF's DTCs or other contract documentation, to ensure DOA terms are adequately incorporated or justified as to why they are excluded from ETF's DTCs.

- Transparent Negotiation Language: In our review, we found some ETF procurement solicitations for which vendor assumptions or exceptions were prohibited for certain DTCs. However, the final contracts included negotiated language for those DTCs. While a couple of these procurements that were completed more recently included language that ETF may be willing to negotiate minor issues, similar language was not included in all procurements we reviewed for which this occurred. We recommended that going forward, ETF's willingness to negotiate minor issues on DTCs listed as not allowing assumptions or exceptions, be consistently indicated for vendor transparency and fairness.

Audit Methodology

The Office of Internal Audit conducted this audit by:

- Reviewing ETF's DTCs, including a comparison to DOA's Standard Terms and Conditions.
- Reviewing a selection of procurements to determine if the risk-based framework documented in the DTC Guidance on Use document was being applied, whether adequate DTC review and approvals were involved in the selected procurements, and for overall consistency in DTC usage. Our review focused on those procurements that are considered higher risk.
- Considering whether adequate representation of ETF's business interests is included in the DTC workgroup, as well as in the review of individual procurement DTCs, as necessary.
- Performing inquiries with program management about the procurement process and their opinion on ETF's DTCs. Specifically, we inquired if they had any procurement or contract concerns (i.e., DTCs being too flexible and not protecting ETF's interests) and if they knew of any effects on vendor competition (i.e., DTCs being too restrictive, limiting the number of potential vendors).