



# **Colorado Statewide Contract Management Practices**

## **Performance Audit**

**Deloitte & Touche LLP**  
**February 2005**

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*Deloitte & Touche LLP*  
**Contract Auditor**

February 11, 2005

Members of the Legislative Audit Committee:

This report contains the results of a performance audit of the State of Colorado's contract management practices, as well as practices for the Departments of Personnel & Administration, Natural Resources, Corrections, Human Services, the University of Colorado, and the Attorney General's Office. The audit was conducted pursuant to Section 2-3-103, C.R.S., which authorizes the State Auditor to conduct audits of all departments, institutions, and agencies of state government. The State Auditor contracted with Deloitte & Touche LLP to conduct this performance audit. The report presents our observations, findings, and recommendations.

Very truly yours,

*Deloitte & Touche LLP*

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# Section I

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## REPORT SUMMARY

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### Authority, Purpose, and Scope

Deloitte & Touche conducted this performance audit under contract with the Office of the State Auditor pursuant to Section 2-3-103, C.R.S. This audit reviewed statewide contract management practices and evaluated practices at the Departments of Personnel & Administration, Natural Resources, Corrections, and Human Services, the University of Colorado, and the Attorney General's Office. The audit work was performed from June through September 2004. We acknowledge the assistance and cooperation extended by management and staff at each of the participating agencies.

### Background

The State of Colorado contracts with private vendors for a range of personal services which are defined in statute as services acquired to directly benefit the State in its operations. [Section 24-50-502, C.R.S.] Statute allows the State to contract for personal services when it will increase the efficiency of service delivery without undermining the quality of the services provided or the principles of the state personnel system. [Section 24-50-501, C.R.S.] According to State Fiscal Rules, state agencies and institutions of higher education have the primary responsibility for overseeing and managing their personal services contracts. This includes identifying a need for service, defining the scope of work, obtaining a qualified vendor, preparing the contract, and submitting the contract for the appropriate levels of review and approval prior to final contract execution. According to statute and State Fiscal Rules, there may be several layers of review before a contract is executed. This may include a review by the Division of Human Resources (within the Department of Personnel & Administration) to ensure that the agency is appropriately contracting out personal services according to statute, a review by the Attorney General's Office to ensure that the contract meets all of the necessary legal requirements, and finally a review by the State Controller's Office to ensure that the contract has received the required approvals, the contract services are an appropriate use of agency funds, and the agency has encumbered sufficient funds to cover the cost of the contract. Agencies receiving delegation authority and waivers from the Department of Personnel & Administration and the Attorney General's Office can conduct one or more of their own reviews internally.

The Department of Personnel & Administration reports that in Fiscal Year 2004 the State spent almost \$3.8 billion on personal services contracts. Medicaid contracts with physicians and nurses through the Department of Health Care Policy and Financing make up about \$2.6 billion, or 68 percent, of this amount. Contracts at several large agencies, such as the Departments of Transportation (\$505.5 million), Higher Education (\$322.9 million), and Human Services (\$132.1 million), make up a majority of the remaining amount. Overall, personal services contracts represent about 25 percent of the \$15 billion expended by the State in Fiscal Year 2004.

# Summary of Audit Findings

## Contract Administration

Contract administration is the initial phase of the contracting process that begins with identifying a need for services and ends with the approval of a contract that meets the needs of the State. We reviewed statewide contract administration practices as well as practices for four state agencies and one institution of higher education and found:

- **Centralized contract management information is limited.** Currently the State's primary centralized, automated system for tracking contract information is COFRS, the State's financial reporting system, which only tracks high-level contract information such as encumbrance amounts, approvals, and start and end dates. In addition, the CLIN system, a module within COFRS, tracks the status of contracts as they move through the personal services certification, State Controller's, and Attorney General's review processes. Neither COFRS nor CLIN track important contract management information such as contract deliverable status, service level agreements, deadlines, or performance recovery amounts and neither has ad hoc reporting capabilities for contracts. To ensure that state agencies collect and track sufficient information to effectively manage their contracts, the Department of Personnel & Administration needs to develop a statewide contract management system or assist state agencies with developing their own internal contract tracking systems that contain baseline information and standardized data elements.
- **Increased delegation to agencies should be evaluated.** At the time of the audit, 53 out of 70 (76 percent) state agencies and institutions of higher education had at least partial delegated State Controller review authority and 33 out of 70 (47 percent) had at least partial delegated Attorney General review authority. Although all state agencies have the option of requesting delegation authority, many do not make this request because they lack the appropriate resources to conduct their own internal contract reviews. Agencies without delegated review authority must continue to have their contracts reviewed by the State Controller's Office and the Attorney General's Office. Currently the State Controller's Office has 1.25 FTE to review about 2,200 contracts per year, while the Attorney General's Office has 1.5 FTE to review about 1,200 contracts per year. We found that agencies are in the best position to review the scope of work, deliverables, deadlines, and remedies set forth in their contracts. Therefore, both offices should continue to evaluate the resources currently allocated to the review function and work with agencies to identify additional agencies that could conduct their own reviews internally. Increasing the number of agencies that receive delegated authority would allow the State Controller's Office to direct additional resources to its oversight responsibility and monitor contract management practices to ensure agency compliance with state contracting requirements.
- **Some agencies do not comply with contract requirements.** We reviewed 31 state contracts and found (1) three University of Colorado contracts did not contain a maximum dollar amount as required by State Fiscal Rules, (2) work commenced on three Department of Human Services contracts and one University of Colorado contract prior to approval by the State Controller or a delegate in violation of statute and State Fiscal Rules, and (3) five University of Colorado contracts and two Department of Human Services contracts did not contain the appropriate signatures. Failure to comply with these requirements can potentially invalidate the contracts and expose the State to unnecessary risk.

- **Personal services certification statutory criteria should be expanded.** In October 2003, the Division of Human Resources implemented a statewide waiver pilot program that allows state agencies to conduct their own personal services certification reviews for contracts meeting established statutory criteria. We identified instances where other statutes authorize an agency to contract out for services, but the type of services authorized fall outside of the statutory criteria and thus, the contracts must still undergo a personal services certification review by the Division. Requiring agencies to submit contracts for review even though statutes authorize outsourcing may unnecessarily lengthen the contract review and approval process.
- **Agencies do not consistently use performance measures in state contracts.** Performance measures in contracts provide information to assess the quality of the product the agency is receiving and set standards and outcome objectives against which the product can be evaluated. We reviewed a sample of 31 state contracts and found that only six of the contracts included some type of performance measures. Performance measures can help improve accountability in the contracting process because they provide an objective standard for staff to use when determining if a contractor has successfully completed its contractual obligations and whether services met quality standards.
- **There is no centralized statewide information on contracts that result in litigation or mediation.** Although the Attorney General's Office is responsible for litigating all state contractual disputes, it does not maintain or track statewide information on contracts that result in litigation or mediation. Currently attorneys are assigned to specific agencies and these attorneys are responsible for handling all contract disputes for their assigned agency. Although the individual attorneys may maintain information on disputes for their agency, information for all state agencies is not consolidated into a centralized database. The lack of statewide information on contract disputes makes it difficult to determine and monitor the total cost of these disputes to the State and to identify trends in the types of issues that lead to disputes.

## Contract Monitoring

Effective contract monitoring occurs throughout the life of a contract and can include developing a clear scope of work, managing and documenting ongoing day-to-day contract issues, monitoring the progress of the work performed by a contractor to ensure the quality of the services provided, and ensuring the State receives value for the money spent. We reviewed statewide contract monitoring practices, as well as practices for four state agencies and one institution of higher education and noted the following issues:

- **Some agencies made advance payments to contractors prior to their receipt of services.** State Fiscal Rules prohibit the use of advance payments without the written approval of the State Controller. We reviewed a sample of 31 state contracts and found that advance payments were made inappropriately for two contracts without the State Controller's approval. One was a University of Colorado contract for \$180,000 in chartered transportation services and the other was a Department of Corrections contract for \$86,000 in computer software maintenance services. When advance payments are made inappropriately, it puts the State at risk of not receiving services equal to the value of the monies paid on the contract.

- **Some agencies do not maintain complete contract administration files.** Our review of 31 state contracts found that contract administration files contain very little documentation to support the monitoring activities that occur. For example, we found that the contract administration files for four University of Colorado contracts and one Department of Corrections contract contained no documentation related to contract monitoring activities. The absence of contract administration files limits the State's ability to defend its position if a dispute arises with respect to a contract.
- **Some agencies are not consistently completing contractor performance evaluations.** The *State Contract Procedures and Management Manual* recommends that state agencies complete performance evaluations at the end of each project, but they are not required to do so. We found performance evaluations were not completed for 2 of the 7 University of Colorado contracts we reviewed. Without performance evaluations, it can be difficult to determine if contractors meet the performance expectations and standards included in the contract and ensure the State receives full value for the funds it expends. Evaluations can also be useful when determining if a contractor should be used on future projects.
- **Contract management guidance needs improvement.** We reviewed the guidance currently provided by the Department of Personnel & Administration, as well as guidance provided by the individual state agencies and institution of higher education reviewed and found that (1) the Department of Personnel & Administration needs to update the *State Contract Procedures and Management Manual* to reflect current contracting requirements and practices, (2) the Department of Personnel & Administration should provide contract management training to agency and institution personnel, and (3) state agencies and institutions of higher education should provide training to their contract management staff.
- **Contract monitors are not consistently evaluated on their contract monitoring skills.** We found that although contract administrators are evaluated on their contracting skills, agency staff reported that contract monitors are not. In addition, according to staff at the state agencies and institution of higher education we reviewed, contract monitors are not consistently provided with the performance expectations surrounding their contracting responsibilities. This can lead to a lack of staff accountability for effective contract performance.

Our recommendations and the responses of the Departments of Personnel & Administration, Human Services, and Corrections, the University of Colorado, and the Attorney General's Office can be found in the Recommendation Locator.



## RECOMMENDATION LOCATOR

Rec. No.	Page No.	Recommendation Summary	Agency Addressed	Agency Response	Implementation Date
1	12	Evaluate the cost-benefit of implementing an integrated, statewide contract management system. If this system is not feasible, work with agencies to identify critical contract management information and develop their own internal contract tracking systems that include standardized data elements.	Personnel & Administration	Agree	August 2005
2	14	Continue to evaluate the resources currently allocated to the contract review process and determine if changes are needed, work with agencies to identify those with the expertise to conduct their own reviews, and improve oversight of agencies with delegated authority.	Personnel & Administration  Attorney General's Office	Agree  Agree	June 2006  July 2005
3	16	Ensure that work does not commence on a project prior to final contract approval, develop procedures for ensuring that contracts contain the appropriate signatures, and verify that contracts contain a maximum dollar amount.	University of Colorado  Human Services	Partially Agree  Partially Agree	December 2005  January 1, 2006
4	18	Revise the standard contract signature page to ensure it contains all necessary information and develop guidelines for identifying and documenting the legal status of the contractor and the authority of the person signing the contract.	Personnel & Administration	Partially Agree	September 2005
5	19	Consider proposing statutory change to include additional criteria outlining situations where personal services contracts are permissible.	Personnel & Administration	Partially Agree	July 2005
6	21	Develop a methodology for determining what performance measures should be used in personal services contracts and the information needed to evaluate contractor performance.	Personnel & Administration	Agree	December 2005
7	21	Maintain and track information for all agencies on contracts that result in litigation or mediation and report the information to the Department of Personnel & Administration.	Attorney General's Office	Agree	March 2005
8	23	Ensure that advance contract payments are not made without the written approval of the State Controller and include payment procedures in each agency's training curriculum.	University of Colorado  Corrections	Agree  Agree	July 2005  July 2004

Rec. No.	Page No.	Recommendation Summary	Agency Addressed	Agency Response	Implementation Date
9	24	Establish standards for monitoring and maintaining contract administration files, revise the <i>Contract Procedures and Management Manual</i> checklist to indicate which items are essential and should be included in files, and communicate the standards and importance of contract administration files through training.	Personnel & Administration	Agree	December 2005
10	24	Provide training to staff on contract monitoring responsibilities and periodically review contract administration files.	University of Colorado Corrections	Agree Agree	December 2005 July 2005
11	26	Require contractor performance evaluations be completed at the end of every state contract and included in contract administration files and contract tracking systems.	Personnel & Administration	Partially Agree	December 2005
12	26	Require staff within the central contract office to periodically review contract administration files to ensure contract monitors complete performance evaluations.	University of Colorado	Agree	December 2005
13	28	Update the <i>State Contract Procedures and Management Manual</i> , provide contract administration and monitoring training to agency staff, and ensure that agencies and institutions have established adequate controls and standards regarding training for contract management staff.	Personnel & Administration	Partially Agree	December 2005
14	30	Assist state agencies and institutions of higher education with performance planning and evaluations for contract monitor staff.	Personnel & Administration	Agree	December 2005

## Section II

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# OVERVIEW

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## Background

The State of Colorado contracts with private vendors for a range of personal services. According to statute, personal services are defined as services acquired to directly benefit the State in its operations. [Section 24-50-502, C.R.S.] Statute allows the State to contract for personal services when it will increase the efficiency of service delivery without undermining the quality of the services provided or the principles of the state personnel system. [Section 24-50-501, C.R.S.] According to State Fiscal Rules, a contract is required for all personal services costing more than \$50,000.

According to State Fiscal Rules, state agencies and institutions of higher education have the primary responsibility for overseeing and managing their personal services contracts. However, the Department of Personnel & Administration (DPA) and the Department of Law handle portions of the contract approval process. These departments have the following responsibilities:

- **DPA – Division of Human Resources.** The State Personnel Director is statutorily required to review and approve almost all personal services contracts. The purpose of the personal services certification review is to ensure that contracts conform with statutory and constitutional requirements related to contracting out services that have historically been performed by state employees. The Director has delegated this responsibility to staff of the Division of Human Resources. Division staff review contracts to determine if contracting for personal services historically performed by state employees is cost-effective and if the contracted services will be of at least the same quality as those offered by state employees. [Section 24-50-503(1), C.R.S.] The Division has also implemented a waiver program which allows state agencies and institutions of higher education to conduct their own personal services certification review for certain services.
- **DPA – State Controller’s Office.** The State Controller’s Office is statutorily required to review and approve all state contracts. The State Controller’s Office also establishes rules and policies governing contracts. The purpose of the State Controller’s review is to ensure that the contract has been reviewed and approved by all appropriate parties, the contract services are an appropriate use of state funds, and the agency has encumbered sufficient funds to cover the cost of the contract. Statute allows the State Controller to delegate this review authority to state agencies and institutions of higher education upon request. [Section 24-30-202, C.R.S.] When an agency or institution receives delegated authority, that organization enters into a delegation agreement with the State Controller and is responsible for conducting the reviews and ensuring that contracts comply with statutory and constitutional requirements. The State Controller’s Office also publishes the State Contract Procedures and Management Manual which provides guidance for all phases of the contracting process, from planning through contract close-out.

- **Department of Law – Attorney General’s Office.** State Fiscal Rules require the Attorney General’s Office to review all personal services contracts to ensure that contracts comply with constitutional and statutory requirements, regulations, and executive orders. The review also ensures the authority of the agency or institution to enter into the agreement and the legal sufficiency of the contract. According to State Fiscal Rules, both the State Controller and the Attorney General’s Office must approve delegating the requirement for legal review to qualified legal staff at an agency or institution.

This performance audit reviewed the State’s contract management practices and evaluated practices at four state agencies and one institution of higher education, including the Departments of Personnel & Administration, Natural Resources, Corrections, Human Services, and the University of Colorado. The following table shows each of the agencies reviewed and their review authority.

<b>AGENCIES REVIEWED</b>			
<b>Agency</b>	<b>Personal Services Certification Waiver Program</b>	<b>State Controller Delegation Authority</b>	<b>Attorney General Delegation Authority</b>
Personnel & Administration	Yes	No	No
Natural Resources	Yes	Partial <sup>1</sup>	Partial <sup>1</sup>
Corrections	Yes	Partial <sup>2</sup>	No
Human Services	No	Partial <sup>1</sup>	Partial <sup>1</sup>
University of Colorado	No	Yes	Yes
<b>Source:</b> Department of Personnel & Administration data.			
<sup>1</sup> The Departments of Natural Resources and Human Services have delegated authority to review and approve standard contracts that have previously been approved by the State Controller’s and the Attorney General’s Offices.			
<sup>2</sup> The Department of Corrections has delegated authority to review and approve contracts up to \$50,000.			

## Personal Services Contracting Dollars

The Department of Personnel & Administration reports that in Fiscal Year 2004 the State spent almost \$3.8 billion on personal services contracts. Medicaid contracts with physicians and nurses through the Department of Health Care Policy and Financing make up about \$2.6 billion, or 68 percent, of this amount. Contracts at several large agencies, such as the Departments of Transportation (\$505.5 million), Higher Education (\$322.9 million), and Human Services (\$132.1 million), make up a majority of the remaining amount. Overall, personal services contracts represent about 25 percent of the \$15 billion expended by the State in Fiscal Year 2004. The following table shows the total number of contracts outstanding during Fiscal Year 2004 and the total dollar amount of those contracts for the five agencies we reviewed during the audit.

<b>PERSONAL SERVICES CONTRACTS FOR AGENCIES REVIEWED FISCAL YEAR 2004</b>		
<b>Agency</b>	<b>Number of Contracts</b>	<b>Total Contract Amount</b>
Personnel & Administration	251	\$20,206,000
Natural Resources	285	\$32,622,900
Corrections	288	\$51,752,700
Human Services	994	\$132,088,100
University of Colorado	561	\$183,594,500
<b>TOTAL</b>	<b>2,379</b>	<b>\$420,264,200</b>
<b>Source:</b> Fiscal Year 2004 Personnel Services Annual Report, Financial Data Warehouse, and agency data.		

## **Audit Scope**

Our audit reviewed statewide contract management practices and followed up on prior recommendations made in the 1995 Contract Management Oversight performance audit. During the audit, we reviewed contract files and data and interviewed staff at the Departments of Personnel & Administration, Natural Resources, Corrections, and Human Services, the University of Colorado, and the Attorney General's Office. In addition, we reviewed contract management practices for three states, including Arizona, Florida, and Washington. Audit work was conducted from June through September 2004. We acknowledge the management and staff at the Departments of Personnel & Administration, Natural Resources, Corrections, and Human Services, the University of Colorado, and the Attorney General's Office for their efforts and cooperation during the audit.

## Section III

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# CHAPTER 1 – CONTRACT ADMINISTRATION

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## Background

Contract administration is the initial phase of the contracting process that begins with identifying a need for services and ends with the approval of a contract that meets the needs of the State. Effective contract administration is critical to ensuring that the scope of work included in the contract appropriately defines the services required by the State and outlines the vendor's responsibilities regarding meeting project milestones and deliverables. Each state agency is responsible for administering its own contracts. This includes identifying a need for service, defining the scope of work, obtaining a qualified vendor, preparing the contract, and submitting the contract for the appropriate levels of review and approval prior to final contract execution. As mentioned previously, there may be several layers of review before a contract is executed. This may include a review by the Division of Human Resources to ensure that the agency is appropriately contracting out personal services according to statute, a review by the Attorney General's Office to ensure that the contract meets all of the necessary legal requirements, and finally a review by the State Controller's Office to ensure that the contract has received the required approvals, the contract services are an appropriate use of agency funds, and the agency has encumbered sufficient funds to cover the cost of the contract. As discussed below, agencies receiving delegation authority and waivers from the Department of Personnel & Administration and the Attorney General's Office can conduct their own reviews internally.

This chapter evaluates state practices for reviewing and approving personal services contracts and maintaining contract management data. The contract administration issues we discuss throughout this chapter can potentially expose the State to significant risks. Therefore, we present findings and recommendations for improving the contract administration process and reducing the State's risk exposure.

## Contract Management System

During the audit we compared Colorado's practices for administering and managing contracts with practices in place in Arizona, Florida, and Washington. We found that overall, Colorado has made improvements since the Office of the State Auditor's 1995 Contract Management Oversight audit and its practices are relatively comparable with those in Arizona and Florida; while Washington's practices appear to be more progressive. We show a comparison of these practices in the following table.

LEADING CONTRACT MANAGEMENT PRACTICES				
LEADING PRACTICE	COLORADO	ARIZONA	FLORIDA	WASHINGTON
Contract approval process delegated to agency	○	●	○	●
Contract management training	○*	●	●	●
Mandatory contract management training				●
Training on assessing risk	○*		○	
Training on performance measures			○	●
Contract management training for field staff responsible for contract monitoring	○*	○	○	●
Certification for contract management			○	
Contract management training for vendors		●	○	
Provide job aides, tool kits, and checklists for contract management	●	○		●
Employ performance measures in contracts as mandatory				○
Employ performance measures in contracts as suggested best practice	○	○	○	●
Performance-based contracting	○			●
Automated contract management system	○	○	○	
Master contracts tailored to agencies	●		○	●
<b>Legend:</b> ● = Fully employed ○ = Partially employed				
<b>Source:</b> Information obtained from the States of Arizona, Florida, Washington, and the Colorado Department of Personnel & Administration. Our review did not include collecting data on the resources allocated to contract management functions in these states. * At the time of the audit, Colorado was not consistently providing contract management training to agency staff. Since work concluded on the audit, the Department of Personnel & Administration has reestablished its contract management training program.				

Although Colorado has made improvements in its contract management practices, we have identified areas where further changes are needed, as discussed throughout this report.

We also reviewed the centralized information available on contract management at both the statewide and agency levels and found that the information is limited. At the statewide level, centralized information is not available on total active contracts in the State and their dollar amount or performance recoveries collected from contractors that fail to meet contract requirements. At the agency level, basic information, such as the number of active and inactive contracts, the number of closed contracts, or the total contracted dollar amount for a specific fiscal year, was also not available at some agencies. Overall, we found that the State needs to take a more systematic and comprehensive approach to contract administration and management to ensure the State maximizes the value received for the \$3.8 billion spent on personal services contracts each year.

Throughout this report we discuss specific areas for improvement and recommend changes to Colorado's contract management process. One key mechanism that is critical to ensuring the State and its agencies have centralized, useful information for managing contracts is an automated contract management system. Currently the State's primary centralized automated system for tracking contract information is COFRS, the State's financial reporting system which tracks high-level contract information, such as encumbrance

amounts, approvals, and start and end dates. In addition, the CLIN system, a module within COFRS, tracks the status of contracts as they move through the personal services certification, State Controller's, and Attorney General's review processes. We found that neither COFRS nor CLIN tracks important contract management information such as contract deliverable status, service level agreements, deadlines, or performance recovery amounts. In addition, COFRS does not have ad hoc querying and reporting capabilities for contracts. Due to the limited contract management capabilities of COFRS and CLIN, some state agencies have developed their own internal contract tracking systems to help them more effectively manage their contracts. For example, three of the five agencies we reviewed (the Departments of Personnel & Administration, Human Services, and Corrections) have each developed their own systems to manage and track the contracting process for their agency. These systems contain information on the vendor, an online version of the contract, tickler dates, and a comment section to track information on deliverables and service level agreements. The University of Colorado uses its financial system and the Department of Natural Resources uses COFRS to track high-level contract information.

To ensure that state agencies collect and track sufficient information to effectively manage their contracts, the Department of Personnel & Administration needs to develop a statewide contract management system. A similar recommendation was made in the Office of the State Auditor's 1995 Contract Management Oversight Audit, but has not been implemented. Ideally, the system would be able to track contracts through all stages of the contracting process, allow contract managers to query contract information and create ad hoc reports, permit users to view labor costs of detailed expenditure items, track performance recovery amounts, include standardized contract templates, and perform various other tasks. An integrated contract management system could also reduce costs, improve the integrity of contract data, and provide consistent statewide contract information for centralized reporting. Individuals at two of the other states we contacted (Arizona and Florida) indicated that with the increased decentralization of the contract management function in their states, it is important that centralized information be available to help them maintain the appropriate level of oversight over this function.

If the Department determines that developing a comprehensive statewide contract management system is not feasible at this time, the Department should work with state agencies and institutions of higher education to identify baseline contract information and standardized data that are critical to effective contract management. The Department should then assist agencies with implementing their own internal contract tracking systems to include these standardized data elements. This would help ensure that agencies collect and track the appropriate information needed to effectively manage their contracts. In addition, since all agencies would be collecting some standard data, the Department could request reports from agencies periodically to evaluate and monitor contracting performance at the statewide level.

### **Recommendation No. 1:**

The Department of Personnel & Administration should evaluate the cost-benefit of implementing an integrated, statewide contract management system. If the Department determines such a system is not feasible at this time, the Department should identify the standard information that is critical to effective contract management and assist state agencies and institutions of higher education with implementing their own internal contract tracking systems that include these standard data elements.



## Department of Personnel & Administration Response:

**Agree. Implementation Date: August 2005.** After the 1995 audit, the State informally conducted a market research assessment of expected costs to add a more robust contract management module to COFRS. However, at the time it was considered cost prohibitive. The Department will again conduct market research to quantify the costs of acquiring a centralized contract management system.

If development and purchase of a centralized contract administration system is not considered cost effective, the Department will work with the Colorado Contract Improvement Team (CCIT) to facilitate a dialogue among the agencies about recommended data elements, and the feasibility of sharing and adapting tools used by the departments to manage their contracts.

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## Delegated Review Authority

Statute requires that all state contracts be reviewed and approved by the State Controller's Office prior to execution. [Section 24-30-202(2), C.R.S.] However, statute also allows the State Controller to delegate this review and approval authority to each of the individual state agencies and institutions of higher education upon request. For agencies and institutions to receive delegated authority, they must enter into a delegation agreement with the State Controller's Office that includes provisions requiring the agency to abide by State Fiscal Rules, the *Contract Procedures and Management Manual*, and the *Contract Processing Guide*. The agreement also includes a provision that, by accepting the delegation, the agency consents to the State Controller's Office conducting peer assessments or reviews of its internal controls and procedures related to state contract processing, approving, accounting, and management. Agencies and institutions that receive delegated authority are responsible for reviewing their own contracts to ensure that the contracts adhere to state contracting requirements and sufficient funds are available to cover the cost of the contract. In addition, State Fiscal Rules require the Attorney General's Office to review all state contracts for legal sufficiency and to ensure compliance with the Colorado Constitution, statutes, regulations, and executive orders. The State Controller and the Attorney General's Office can delegate the required legal review to qualified legal staff at an agency or institution who are then responsible for reviewing all contracts.

At the time of the audit, 53 out of 70 (76 percent) state agencies and institutions of higher education had at least partial delegation of State Controller review authority and 33 out of 70 (47 percent) had at least partial delegation of Attorney General review authority. Of the four agencies and one institution we reviewed, only the University of Colorado has fully delegated authority to conduct the State Controller and Attorney General reviews. Although all state agencies have the option of requesting delegation authority, according to the State Controller's Office, many agencies do not make this request because they lack the appropriate resources to conduct an internal contract review. Agencies that do not have delegated review authority must still submit their contracts for review by the State Controller's and the Attorney General's Offices. Currently the State Controller's Office has 1.25 FTE to review approximately 2,200 contracts per year, while the Attorney General's Office has 1.5 FTE to review approximately 1,200 contracts per year. On average, in Fiscal Year 2004 the centralized contract review process took about eight days – three days for the State Controller's Office review and five days for the Attorney General's Office review.

Although both offices have taken steps to help make the centralized contract review process more efficient, it is important that they continue to identify opportunities for streamlining the process further. Both offices should continue to evaluate the resources they currently have allocated to the review function and determine if changes are needed. In addition, both offices should continue to work with state agencies to identify those that have the expertise and skills to conduct their own in-house review of contracts. This can help shorten the contract review process and encourage more accountability at the agency-level. Agencies are in the best position to review the scope of work, deliverables, deadlines, and remedies set forth in contracts. We found that several other states, including Washington and Arizona, have delegated all contract review and approval authority to state agencies. This has allowed state-level resources to be directed toward other areas, including increased oversight of the entire contracting process. Similarly, this would allow the State Controller's Office to direct additional resources to its oversight responsibility. It is important that the Department adequately monitor contract management practices to ensure compliance with state contracting requirements and delegation agreements considering the numerous contract management issues discussed throughout this report, especially for agencies and institutions with delegated authority. This should include conducting periodic risk-based reviews of contracts and required documentation to ensure that agencies with delegated authority are complying with all appropriate requirements.

## **Recommendation No. 2:**

The Department of Personnel & Administration and the Attorney General's Office should continue to evaluate the resources they currently have allocated to the contract review process and determine if changes are needed. Additionally, both offices should continue to work with state agencies and institutions of higher education to identify those that have the expertise and skills necessary to conduct their own internal contract reviews. Finally, the Department of Personnel & Administration should evaluate mechanisms for improving its oversight of agencies and institutions with delegated authority. This should include conducting periodic risk-based reviews of contracts and required documentation to ensure that agencies and institutions with delegated authority are complying with state contracting requirements and delegation agreements.

### **Department of Personnel & Administration Response:**

**Agree. Implementation Date: June 2006.** The State Controller's Office, in conjunction with the Office of the Attorney General, is continuously discussing resources devoted to review, as well as the capabilities of agencies to conduct their own reviews. Given the resource constraints and priorities of competing requirements, the Department believes that resources have been appropriately allocated to contract review. Recognizing that certain agencies have continued to develop the expertise, skills, and resources for proper contract review, the Department continues to work to identify suitable candidates for delegation.

The Division of Finance and Procurement has been working to apply a risk-based approach to reviews of delegated procurement and contract files, modeled after the State Purchasing Office's peer review program. Reviews were conducted at Colorado State University, Arapahoe Community College, and Aurora Community College in the past year. The Department has been evolving the "risk" concept for purposes of program oversight. We expect to have a documented approach to risk-based oversight, consistent with our resource constraints, completed in the summer of 2006.

## Attorney General's Office Response:

**Agree. Implementation Date: July 2005.** The Office of the Attorney General continually works with the State Controller and agencies to both improve the contract review and approval process, and optimize the efficient use of resources. The Office will implement this recommendation by evaluating the types, numbers, and complexities of the contracts the office reviews and, also, by contacting various state agencies and institutions of higher education to consider what training and monitoring agencies will need to ensure the necessary expertise and skills to conduct internal contract reviews. This evaluation must also consider the need for consistency in legal review and conformance to State Fiscal Rules that the Attorney General review now brings to the process. If the Office requires additional resources, the Office may need to seek additional appropriations.

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## Contract Review and Approval Process

Statute provides that state contracts are not valid until they have been reviewed by the State Controller or his or her delegate to determine whether the proposed expenditure is authorized and within the unencumbered balance of the agency's or institution of higher education's appropriation and whether the prices are fair and reasonable. [Section 24-30-202(1), C.R.S.] In addition, State Fiscal Rules provide that each "agency and institution of higher education is responsible for assuring that all constitutional and statutory requirements have been met prior to signing a state contract." This includes obtaining all of the necessary approvals and signatures prior to contract execution. Our review of 31 state contracts found that some agencies and institutions are not complying with statute, State Fiscal Rules and the *State Contract Procedures and Management Manual*. Specifically, we found the following:

- **Some contracts do not contain a maximum dollar amount.** State Fiscal Rules require that contracts contain a provision specifying the maximum amount of state funds that can be spent under the contract. Contracts spanning multiple fiscal years must contain language specifying the maximum amount of funds available for a specific year. We found that 3 of the 7 University of Colorado contracts (43 percent) we reviewed did not contain a maximum dollar amount. The first was a one-year contract that contained the "projected cost" of the contract, but not a maximum amount. At the time of the audit, \$317,000 had been paid on this contract. The second was a one-year contract that included a fixed fee per employee, but did not specify a maximum amount. The third contract spanned two fiscal years and contained a price summary, but did not specify the maximum amount to be spent for the current fiscal year, as required by State Fiscal Rules. At the time of the audit, there had not been any payments made on either the second or third contracts. Failure to include a maximum dollar amount in contracts exposes the State to the risk of having a contractual cost in excess of the amount appropriated for a particular purpose.
- **Work commenced on some contracts prior to their approval by the State Controller or a delegate.** As mentioned previously, Section 24-30-202(1), C.R.S., states that contracts are not valid until they have been approved by the State Controller or his delegate. In addition, the *State Contract Procedures and Management Manual* states that work should not commence prior to the contract being approved by the State Controller or delegate. We found that work commenced on 3 of the 6 Department of Human Services contracts (50 percent) we reviewed and 1 of the 7 University of Colorado contracts (14 percent) prior to the contracts being approved by the State Controller or delegate. The total dollar amount for these contracts was approximately \$2 million. According to State Fiscal Rules, "if an attempt is made to execute a state contract without the approval of the State Controller or a delegate, the state contract shall be null and void and not binding against the State. However every person involved in incurring the obligation shall be jointly and severally liable for the obligation."

- **Some contracts do not contain the appropriate signatures.** According to the *State Contract Procedures and Management Manual*, it is the state agencies' and institutions' responsibility to ensure that the contractor has the authority to enter into the proposed contract and the individual signing the contract on behalf of the contractor has the authority to legally bind that contractor to the obligations of the contract. The existence and extent of the contractor's authority to enter into the proposed contract, and whether the authority has been properly delegated to the individual signing the contract, can be determined by looking at applicable statutes, articles of incorporation, by-laws, and resolutions of corporate contractors; partnership agreements of partnership contractors; charters of home rule local government contractors; and powers of attorney. We found problems with the signatures for 5 of the 7 University of Colorado contracts (71 percent) and 2 of the 6 Department of Human Services contracts (33 percent) we reviewed. For example, the contract signature page for one of the University of Colorado contracts did not include the full, legal name of the contractor and the contract was signed by the Engineering Manager, who was not an officer of the corporation. There was no indication in the contract administration file that the University had verified that the Engineering Manager was authorized to enter into a contract on behalf of the contractor. The two Department of Human Services contracts failed to include the state of the contractor's incorporation on the signature page. The total dollar amount for these contracts was \$16.7 million. Failure to comply with signature requirements could invalidate the contracts and may impact the State's ability to enforce contract provisions.

As mentioned previously, state agencies and institutions are responsible for ensuring that contracts comply with constitutional and statutory requirements before they are executed. Therefore, it is important that the Department of Human Services and the University of Colorado strengthen their own internal review processes to ensure that all state contracting requirements are met. This should include identifying ways to ensure that work does not commence on a project prior to final contract approval, developing procedures for ensuring that contracts contain the appropriate signatures, and for the University of Colorado, verifying that all contracts contain a maximum dollar amount.

To assist all state agencies and institutions with this review process the Department of Personnel & Administration should revise the standard contract signature page to ensure that it contains all of the necessary information (e.g., title of person signing, state of incorporation, date of Attorney General signature). The Department should also develop guidelines for identifying and documenting the legal status of the contractor and the authority of the person signing the contract in order to mitigate the State's risk. These guidelines could also be incorporated into the contract administration file checklist discussed in Recommendation No. 9 and included in contract management training as discussed in Recommendation No. 13.

### **Recommendation No. 3:**

The University of Colorado and the Department of Human Services should strengthen their contract review processes to ensure that all state contracting requirements are met. This should include identifying and developing procedures to ensure that work does not commence on a project prior to final contract approval and for ensuring that contracts contain the appropriate signatures. In addition, the University of Colorado should verify that all contracts contain a maximum dollar amount.

## University of Colorado Response:

**Partially Agree. Implementation Date: December 2005.** The University of Colorado strives to comply with all contracting requirements and has policies in place to provide guidance to the university community on them. Furthermore, the Procurement Service Center (PSC) encourages the campus Chief Financial Officers to send annual reminders to campus staff that it is important no work begin on a contract prior to the contract being signed, and that should this occur they could be held personally liable. In its highly decentralized environment, however, given that many contracting responsibilities reside in the university departments and several functions may be involved in approving contracts, on a rare occasion, work may commence prior to the contract being fully signed. In those cases, the PSC enforces the State Controller's Policy entitled *Managing Commitment Vouchers that Violate State Statutes*. The PSC does not pay vendors unless a signed contract is in place. In addition, as part of the risk-based department audits included in its annual internal audit plan, the University's Department of Internal Audit incorporates a review of significant contracts. The University is uncertain that additional procedures are cost beneficial and will further research this issue to determine whether further work is needed. At a minimum, the PSC will reinforce this aspect of compliance as part of the training to be developed in response to recommendation #10.

The University has never experienced any issues where the contractor has claimed the person signing the contract on their behalf was not authorized to do so. The Contract Services manager for the PSC has eleven years of experience and has never seen this as an issue on any contract at any point of the contracting process. Contractors are not paid until after the work begins, which represents a ratification of the contract. The University does not believe that additional procedures to verify the authority of the signatures would be cost effective.

The University of Colorado, Procurement Service Center, will develop a policy to ensure that all procurement contracts include a maximum dollar amount or that the provisions under *State Contract Form and Provisions .02; B* of Chapter 3 of the State Fiscal Rules are included when the identification of a maximum dollar amount is not practical.

## Department of Human Services Response:

**Partially Agree. Implementation Date: January 1, 2006.** Notwithstanding that the three contracts cited were approved by the State Controller and the vendors properly paid under the contracts, the Department agrees that ensuring that work does not start without an approved commitment voucher is of great importance. Therefore, the Department agrees that on or before January 1, 2006, DHS Contract Management Unit will identify additional ways and implement additional procedures to further ensure that work does not commence on a project without there being in place for such work an approved commitment voucher. This effort will involve and be coordinated with the Department's Contract User Group, the Department Controller, Department senior management staff, and the state's Contract Central Approvers Taskforce (State Controller's Office).

It is the Department's position that not including the state of incorporation for the vendor on the signature page of a state contract does not affect the legal sufficiency of the contract. The *State Fiscal Rules* mandate the format for the signature page for state contracts, and the vendor's state of incorporation is not required thereby. The *State Contract Procedures and Management Manual* is advisory. The *State Fiscal Rules* are mandatory. The signature page of all Department contracts is reviewed and approved for form and legal sufficiency by the Attorney General's Office and/or the State Controller's Office prior to approval of the contract by the State Controller. All past and current Department contracts contain appropriate, legally sufficient signatures. No additional procedures are needed to ensure that Department contracts contain appropriate signatures.

## Recommendation No. 4:

The Department of Personnel & Administration should assist state agencies and institutions of higher education in the contract review process by:

- a. Revising the standard state contract signature page to ensure it includes all of the necessary information.
- b. Developing guidelines for identifying and documenting the legal status of the contractor and the authority of the person signing the contract in order to mitigate the State's risk. These guidelines should be incorporated into the contract administration file checklist discussed in Recommendation No. 9 and included in the contract management training discussed in Recommendation No. 13.

## Department of Personnel & Administration Response:

**Implementation Date: September 2005.**

- a. **Agree.** The Department will evaluate the signature page to determine whether the information is adequate
- b. **Partially Agree.** Chapter 6 of the *Contract Procedures and Administration Manual* contains adequate guidance on contract signatures. The audit recommendations suggest additional documentation, contrary to training that the Department has conducted that identifies true risk associated with contract signatures, which we believe is minimal. The State Controller's contracts unit manager reports that in his 20 years of experience no contractor has ever disavowed a contract based on an allegation of insufficient authority. The Manual guidance is intended to provide comprehensive information concerning authority and signatures. The new edition of Chapter 6 of the Manual counsels agency personnel on less formal ways to establish the existence of authority. The Department does not believe that additional paperwork prescriptions related to signature authority are cost effective.

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## Personal Services Certification

Statute encourages the use of private contractors to provide personal services if it increases the efficiency of service delivery and does not undermine the principles of the state personnel system. [Section 24-50-501, C.R.S.] However, before a state agency can contract for personal services, Section 24-50-503(1), C.R.S., requires the State Personnel Director to determine that the proposed contract will result in overall cost savings to the State and will provide at least the same quality of services as that offered by state employees. The State Personnel Director has delegated this responsibility to the Division of Human Resources which is required to review and approve all personal service contracts. According to Section 24-50-504(2), C.R.S., personal services contracts that meet one of the following criteria are permissible:

- The contract is for an existing state program that has never been performed by state employees.
- The contract is for a new state program and the General Assembly has statutorily authorized the use of private contractors.
- The contracted services are not available or cannot be performed satisfactorily within the state personnel system or are of such a highly specialized or technical nature that state employees do not possess the necessary abilities.

- The contracted services are incidental to a contract for purchase or lease of real or personal property.
- The legislative, administrative, or legal goals and purposes cannot be accomplished by using state employees.
- The contractor will provide equipment, materials, facilities, or support services that could not feasibly be provided by the State in the location where the services are to be performed.
- The contractor will conduct training courses for which appropriately qualified state employee instructors are not available.
- The services are of an urgent, temporary, or occasional nature.

In October 2003 the Division implemented a state-wide waiver pilot program that allows state agencies and institutions of higher education with certified human resource personnel to conduct their own personal services certification review for contracts meeting one of the criteria listed above. The purpose of the waiver program is to streamline the personal services contract review process and reduce the number of contracts requiring Division review. According to the Division, since this program has been implemented, the number of contracts reviewed by the Division has decreased from approximately 3,000 to 500 (an 83 percent decrease), annually. If a contract does not meet one of the statutory criteria, the agency must complete a cost-benefit analysis and submit the contract to the Division for review and approval.

We found there are instances where the statutory criteria do not cover common situations that require services to be contracted out. For example, statute requires the Department of Human Services to investigate and approve applications to operate childcare facilities. Statute also authorizes the Department of Human Services to contract out this function to counties or other publicly or privately operated organizations. However, the statutory authorization to contract for these services with private organizations does not meet the statutory criteria detailed above. Therefore, the Department of Human Services is required to conduct a cost-benefit analysis and submit these contracts to the Division of Human Resources for review. Requiring agencies to submit contracts for review even though statute authorizes outsourcing may unnecessarily lengthen the contract review and approval process and increase the amount of resources the Division must allocate to personal services certification reviews. Therefore, the Division should consider proposing statutory change to include additional criteria outlining situations where personal services contracts are permissible without Director review. This would help streamline the review and approval process and reduce the number of contracts submitted for Division review. As a result, the Division could focus more resources on monitoring, auditing, and developing state-wide policy on personal services contracting activities.

### **Recommendation No. 5:**

The Department of Personnel & Administration should further improve and streamline the personal services contract review process by considering proposing statutory change to include additional criteria outlining situations where personal services contracts are permissible under the State Constitution.

### **Department of Personnel & Administration Response:**

**Partially Agree. Implementation Date: July 2005.** The Department agrees that the contract review process can be further improved and is currently revising Chapter 10 of the Director's rules regarding the analysis of all personal services contracts, including those implicating the State Personnel System.

New legislation authorizing the use of independent contractors under any circumstances regardless of its impact upon the State Personnel System will likely be litigated and may be potentially constitutionally flawed under Civil Service Amendment and case law interpreting it. The Department of Human Services (DHS) example cited in the report involves services currently performed by state personnel system employees. To the extent DHS uses local governments to provide these services, Section 24-50-508, C.R.S., exempts the contracts from Director review. However, contracts with private vendors for these services implicate the State Personnel System and must either satisfy the cost analysis in Section 24-50-503, C.R.S., or meet the criteria for new or existing programs under Section 24-50-504(2), C.R.S.

This Department did seek legislative changes that would have accomplished all of the issues addressed in the recommendation last year. This legislation was passed, but did not become law when the companion referendum was defeated during the November election. Further, at the time of this response, there is pending legislation regarding outsourcing of personal services contracts.

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## Performance Measures

Performance measures in contracts provide information to assess the quality of the product the agency is receiving and set standards and outcome objectives against which the product can be evaluated. There are two basic types of performance measures that can be used in contracts – output measures and outcome measures. Output measures generally look at the quantity or type of services to be provided (e.g., build 20 new highway lane miles), while outcome measures generally evaluate the result of the services provided (e.g., reduce average commute time by 10 minutes). We reviewed a sample of 31 state contracts to determine if agencies and institutions are using performance measures in their contracts. Of the 31 contracts reviewed, we found that only six contracts (19 percent) included some type of performance measures. These six contracts were all Department of Human Services federal grant contracts that identified output measures related to providing services to specific populations. For example, one of the contracts was with a company to provide substance abuse treatment to a specified number of clients. However, the contract did not require the contractor to report any measures of quality, such as clients completing the required treatment plan goals. Without performance measures, agency staff must either spend more time monitoring contractor performance or trust the contractor to provide the level of quality required by the contract.

Although the Department of Personnel & Administration includes a general discussion of performance measures in the *State Contract Procedures and Management Manual*, it should also develop a methodology for state agencies and institutions of higher education to apply when determining what performance measures (both output and outcome measures) should be used in their personal services contracts. Performance measures can help improve accountability in the contracting process because they provide an objective standard for staff to use when determining if a contractor has successfully completed its contractual obligations. In addition, performance measures let contractors know up front what criteria will be used to measure their performance. Although the Office of the State Auditor made a similar recommendation in its 1995 Contract Management Oversight Audit, we found that it has not been fully implemented. It is still important that the Department provide this guidance to agencies and institutions through training and reference materials. The training and materials should also clarify the types of information the agencies and institutions should maintain to be able to evaluate contractor performance using the established measures.



## **Recommendation No. 6:**

The Department of Personnel & Administration should help state agencies and institutions of higher education improve contractor performance and accountability by developing a methodology for determining what performance measures should be used in personal services contracts and what information will be needed to evaluate contractor performance using the established measures. This information should be communicated to agencies and institutions through training and reference materials.

### **Department of Personnel & Administration Response:**

**Agree. Implementation Date: December 2005.** The Manual discussions related to performance-based contracts and performance specifications will be revised as part of the Manual re-write. The topic will be covered in both the procurement and contracts management training.

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## **Contract Disputes**

The Attorney General's Office is responsible for litigating all state contractual disputes. We found that the Office does not maintain or track state-wide information on contracts that result in litigation or mediation. Currently, attorneys assigned to specific agencies may maintain information on any contract disputes for their agency; however, information for all state agencies is not consolidated into a centralized database. For example, we had to go to each individual agency that we reviewed to find out whether they had any contractual disputes during Fiscal Year 2004. Although both agency staff and their attorneys verbally reported that the agencies did not have any disputes during Fiscal Year 2004, neither the individual agencies nor the Attorney General's Office consistently track this information. The lack of statewide information on contract disputes makes it difficult to determine and monitor the total cost of these disputes to the State. It also makes it difficult to identify trends in the types of issues that are disputed. Therefore, the Attorney General's Office should compile information related to contract disputes for all agencies on an annual basis. This information should then be reported annually to the Department of Personnel & Administration which could use the information to identify recurring contracting problems, issues with contract language, and contractors with a history of contract problems with the State.

## **Recommendation No. 7:**

The Attorney General's Office should improve statewide contract management information by maintaining and tracking information for all state agencies on contracts that result in litigation or mediation. The information should include at a minimum, the cost of the dispute to the State, the issues being disputed, and the parties (the state agency as well as the contractor) involved in the dispute. This information should then be reported to the Department of Personnel & Administration on an annual basis and be used to identify recurring contracting problems and issues with contract language and contractors.

### **Attorney General's Office Response:**

**Agree. Implementation Date: March 2005.** Litigation or mediation involving contract disputes is relatively rare. Nonetheless, tracking and reporting information on disputes that do occur may assist the State in avoiding similar issues in future contract negotiations.

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# CHAPTER 2 – CONTRACT MONITORING

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## Background

Contract monitoring occurs throughout the life of a contract – from the time a project is initially conceptualized until the project is complete. Effective contract monitoring can include developing a clear scope of the services to be provided, managing and documenting ongoing, day-to-day contract issues, monitoring the progress of the work performed by a contractor to ensure the quality of the services provided, and ensuring the State receives value for the money spent. Each state agency and institution of higher education typically has a central contract office. Generally, staff within the central contract office are responsible for contract administration (as discussed in Chapter 1), while day-to-day contract monitoring is performed by individuals outside of the central contract office who work in the area related to the contract subject-matter.

We reviewed statewide contract monitoring practices, as well as practices for four state agencies and one institution of higher education. These areas are a significant risk exposure for the State and in this chapter we make recommendations for improvements.

## Advance Payments

Advance payments are payments made prior to the receipt of goods or services. State Fiscal Rules prohibit the use of advance payments, unless it is an established industry standard or unless the advance payment provides a benefit to the State equal to the cost and risk of the payment. Advance payments generally require the written approval of the State Controller, or a delegate authorized by the State Controller to approve advance payments. During the audit, we reviewed a sample of 31 state contracts and found that advance payments were made inappropriately for two of the contracts. One \$180,000 University of Colorado contract for five chartered transportation services specified that a 25 percent deposit was due at the start of the contract and that payments for the individual flights were due 30 days prior to the scheduled flights. We found, however, that the University paid 50 percent of the total contract amount at the start of the contract and then paid the remaining 50 percent in one lump sum payment approximately 90 days before the first flight was to occur and about 120 days before the last flight was to occur. In addition, one of the Department of Corrections contracts for \$86,000 in computer software maintenance services stated that the contractor should submit monthly invoices for services provided. We found that the contractor only submitted one invoice during the term of the contract, and was paid the full contract amount prior to all services being provided. Neither the University of Colorado nor the Department of Corrections obtained the State Controller’s approval prior to these payments. In addition, neither agency could provide evidence that these advance payments met one of the State Fiscal Rule exceptions described above.

When advance payments are made inappropriately, it puts the State at risk of not receiving services equal to the value of the monies paid on a contract. Therefore, it is important that the University of Colorado and the Department of Corrections ensure that contractor payments are not made in advance of services being provided, unless State Controller approval is obtained prior to payment. Payment procedures should be included in each agency’s training curriculum as discussed in Recommendation No. 13.

## Recommendation No. 8:

The University of Colorado and the Department of Corrections should ensure that advance contract payments are not made without the written approval of the State Controller. Payment procedures should be included in each agency's training curriculum as discussed in Recommendation No. 13.

### University of Colorado Response:

**Agree. Implementation Date: July 2005.** The University of Colorado, Procurement Service Center, will develop a policy to ensure that all advance contract payments are approved by the State Controller designee(s) on the campus. That policy will be included as part of the training course described in the response to Recommendation No. 10, below.

### Department of Corrections Response:

**Agree. Implementation Date: July 2004.** The Department of Corrections (DOC) has changed its review procedure for all payments to insure that all advance payments are made in accordance with the State Controllers Policy. The DOC Controller is requiring an approved contract with advance payment terms or SCO waiver for advance payments prior to making any advance payments.

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## Contract Monitoring

Contract monitoring is critical to ensuring that contractors fulfill all of their legal obligations and the State receives appropriate value for the money it spends for a service. According to the *State Contract Procedures and Management Manual*, contracts should identify how the State will monitor the progress of the work performed by the contractor. For example, the contract may require that the contractor provide weekly written updates or status reports and that there be monthly meetings between the contractor and the contract monitor. In addition, the *Manual* recommends that monitors maintain a contract administration file that contains information such as a copy of the signed contract, any contractor updates or status reports, all general correspondence related to the contract, and a copy of all invoices and payments. According to the *Manual*, the contract administration file provides a record of the monitoring activities that have occurred, as well as a basis for settling claims and disputes that may arise with respect to the contract.

We reviewed a sample of 31 contracts at four state agencies and one institution of higher education to evaluate contract monitoring activities. Overall, we found that the contract administration files for all of the contracts we reviewed contained very little documentation to support what monitoring activities had occurred. For example, the contract administration files for 4 of the 7 (57 percent) University of Colorado contracts and 1 of the 6 (17 percent) Department of Corrections contracts we reviewed contained no documentation related to contract monitoring activities. These included contracts for consulting and computer software maintenance services. There was no information in the files indicating that monitors had made sure the State received the services or that the services were of sufficient quality. In general, we found the agencies were able to locate contract monitoring information when requested, but only after consulting multiple staff and locations throughout the agency. One exception was the University of Colorado which could not locate a copy of the procurement authorization for one of its contracts or a current insurance certificate for another contract. The absence of contract administration files limits the State's ability to defend its position if a dispute arises with respect to a contract.

Currently state agencies and institutions are not required to maintain comprehensive contract administration files. Although the *State Contract Procedures and Management Manual* recommends this practice, it is up to the individual agencies' and institutions' discretion. To help ensure the State's interests are protected and that state funds are spent appropriately, the Department of Personnel & Administration should establish standards for monitoring and maintaining contract administration files that contain all of the essential documentation related to a contract and the monitoring that occurs on the contract. In addition, the Department should revise the checklist currently included in the *State Contract Procedures and Management Manual* to indicate which items are essential and should be maintained in all contract administration files and encourage agencies to develop checklists specific to their own contracts. Further, the Department should communicate these standards and the importance of maintaining contract administration files to agencies during the contract management training discussed in Recommendation No. 13.

Finally, the individual state agencies and institutions of higher education should ensure that monitoring occurs on state contracts and that staff document monitoring activities. As discussed later in this chapter, agencies and institutions should provide training to staff on contract monitoring responsibilities, including how to use the checklist described above. In addition, staff within an agency's central contract office should periodically review contract administration files to ensure that monitoring has occurred and has been adequately documented. Periodic reviews would put contract monitors on notice that they will be held accountable for carrying out their duties effectively.

### **Recommendation No. 9:**

The Department of Personnel & Administration should improve the statewide contract monitoring process by establishing standards for monitoring and maintaining contract administration files that contain all of the essential documentation related to a contract and the monitoring process. To assist with this process, the Department should revise the checklist currently included in the *State Contract Procedures and Management Manual* to indicate which items are essential and should be maintained in every contract administration file and encourage agencies to develop their own checklists of required documentation for their files. The Department should communicate these standards and the importance of maintaining contract administration files to agencies during the training discussed in Recommendation No. 13.

### **Department of Personnel & Administration Response:**

**Agree. Implementation Date: December 2005.** The Department will revise Chapter 10 guidance in the Manual in collaboration with other agencies and institutions to better define expectations on contract administration documentation retention. These criteria will be used as part of the risk-based oversight program discussed in Recommendation No. 2. The Department will also stress the importance of maintaining contract administration files during its Contract Management Training sessions. Finally, the Department will revisit Fiscal Rule 2-3 (receiving reports) to determine whether additional clarification of standards relating to contract administration documentation need to be published.

### **Recommendation No. 10:**

The Department of Corrections and the University of Colorado should ensure that monitoring occurs on state contracts and that staff appropriately document those monitoring activities by providing training to staff on contract monitoring responsibilities and periodically reviewing contract administration files.

## University of Colorado Response:

**Agree. Implementation Date: December 2005.** The University of Colorado agrees that contract monitoring is essential. In the University's decentralized purchasing model contract monitoring occurs at the departments where the product/service is being delivered. Furthermore, we understand that more formal documentation of contract monitoring activities is appropriate for significant contracts. The Procurement Service Center (PSC) will develop a training course, for departmental representatives, on contract monitoring procedures. Further, the University's Internal Audit department will incorporate reviews of departmental contract monitoring activities as a part of their risk-based departmental audits.

## Department of Corrections Response:

**Agree. Implementation Date: July 2005. New Policy and Monitoring Plan:** The Contracts Unit of the Department of Corrections is in the process of developing an additional contract monitoring policy which will include a monitoring plan specific to each contract, identifies which DOC staff member is responsible for each phase of contract administration, and what their duties are. The appointing authority of each such assigned staff member will be advised of the monitoring plan.

**Training:** Beginning in the late summer of 2004, the DOC's Contracts Unit implemented a "Contracts, Leases and Grants" intranet site, available to all DOC staff, which contains all pertinent information regarding the Colorado State Contract Management Training Course training available through the State Controller's Office, as well as link to Chapter 10 of the Contracts Manual. Once the proposed monitoring plans are in place, then a complete list of staff that have contract administration duties will be evaluated for the level and content of in-house contract training which may be required.

**Administrative Regulations:** The DOC's Administrative Regulation 200-12, paragraph IV.E. specifically requires that the office which originates the contract, monitor the terms of the contract (for example, to pay according to the contract terms) and meet with the vendor at least annually. That Administrative Regulation provision will now be amended to require adherence to Chapter 10 of the Controller's Contract Procedures and Management Manual.

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## Contractor Evaluations

Contractor performance evaluations help determine if the State received full value for the funds that were expended on a contract, if the contractor's work was completed in accordance with state standards, and if there were any lessons learned on the contract that could be applied to future contracts. An evaluation can also help an agency or institution determine if a contractor should be used on future projects. According to the *State Contract Procedures and Management Manual*, there are several different ways that an evaluation can be completed. For example, depending on the magnitude and complexity of a contract, the agency or institution can have the contract monitor, a knowledgeable committee, an internal or external auditor, or another agency complete the evaluation. In our review of completed state contracts, we found that performance evaluations were not always completed for University of Colorado contracts. Specifically, we found that evaluations were not completed for 2 of the 7 (29 percent) University contracts we reviewed. Without performance evaluations, it can be difficult to determine if contractors meet the performance expectations and standards included in the contract.

Although the *State Contract Procedures and Management Manual* recommends that state agencies and institutions of higher education complete contractor performance evaluations at the end of a project, they are not required to do so. Implementing such a requirement would help ensure that the State receives full value for the funds it expends and that contractor performance meets state quality standards. The federal government recognized the importance and usefulness of evaluations and now requires contractor evaluations for all contracts using federal funds. Ideally, evaluations would be included in agencies' contract tracking systems as discussed in Chapter 1. At a minimum, contractor performance evaluations should be maintained in a central location and be made available to contract monitors within an agency or division. Contractor performance evaluations should also be included on the checklists discussed in Recommendation No. 9. In addition, the University of Colorado should have staff within its central contract office periodically review contract administration files to ensure that contract monitors complete contractor performance evaluations at the end of each project.

### **Recommendation No. 11:**

The Department of Personnel & Administration should require contractor performance evaluations be completed at the end of every contract, as appropriate, and included in the contract administration file and agencies' contract tracking systems as discussed in Recommendation No. 1. In the meantime, the Department should encourage agencies to maintain evaluations in a central location that can be accessed for future projects. Performance evaluations should also be included on checklists as discussed in Recommendation No. 9.

### **Department of Personnel & Administration Response:**

**Partially Agree. Implementation Date: December 2005.** The Department modified the State's Bid Information and Distribution System (BIDS) three years ago to include an on-line capability to research a vendor's history with state awards. A report is available to each purchasing agent that lists awards to each vendor and the agency. This permits the purchasing agent to contact agencies to discuss past performance as part of the responsibility determination. Additionally, Section 8-1 of Chapter 10 of the Manual has a fairly comprehensive discussion of contractor evaluation in conjunction with contract close-out. This is a good "best practice," especially where program personnel may need to re compete a contract requirement and can learn from such an evaluation.

The Department will evaluate the inclusion of information regarding actual litigation against the vendor in making procurement decisions. However, the Department is hesitant to include subjective analysis of a vendor's past performance as part of a centralized procurement system.

### **Recommendation No. 12:**

The University of Colorado should require staff within its central contract office to periodically review contract administration files to ensure that contract monitors complete contractor performance evaluations at the end of each project.

## University of Colorado Response:

**Agree. Implementation Date: December 2005.** The University of Colorado agrees that contract performance evaluations can be a valuable tool. Given the University's decentralized purchasing model we believe that performance evaluations are more appropriately completed, for certain contracts, by the campus departments. The Procurement Service Center (PSC) will include concepts on contract performance evaluations in the training course with guidance on how to communicate evaluations back to the PSC. Further, University's Internal Audit department will incorporate the evaluation process in its contract reviews as a part of their risk-based departmental audits.

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## Contract Management Guidance

The Department of Personnel & Administration is responsible for managing the state contracting process. As part of this responsibility, the Department must provide guidance to state agencies and institutions of higher education on how to manage state contracts. There are currently several written sources for obtaining contract management guidance. These include statutes, State Fiscal Rules, the *State Contract Procedures and Management Manual*, and the *State Contract Processing Guide*. The Department has also provided some contract management training to state personnel in the past. In addition, although the Department oversees the state contracting process, the individual state agencies and institutions of higher education are responsible for the actual day-to-day management of their own contracts and for providing guidance to their own staff on how to manage contracts.

We reviewed the contract management guidance currently provided by the Department of Personnel & Administration, as well as the guidance provided by the individual state agencies and institution of higher education in our sample and noted the following areas for improvement:

- **The Department of Personnel & Administration should update the *State Contract Procedures and Management Manual*.** The Department developed the *Manual* in response to a recommendation in the Office of the State Auditor's 1995 Contract Management Oversight Audit. The *Manual*, which has been recognized as a best practice by other state purchasing programs, provides guidance on all phases of the contracting process, including planning, vendor selection, contract pricing, writing the contract, accounting procedures, and contract management. Although the *Manual* is an excellent resource for state contracting staff, we found that it needs to be updated to reflect current contracting requirements and practices. We found several examples of requirements that are still included in the *Manual* even though they are no longer applicable. For example, the *Manual* states that a minimum of three bid responses are required to establish adequate competition. However, the State Procurement Rules, which were last revised in 2004, state that a minimum of two bid responses are required. Further, the State Controller's Office has developed new policies on contract modifications that have not been included in the *Manual*. Although some revisions were made to the *Manual* in 1999, the entire *Manual* has not been updated since it was first developed in 1997. According to the Department, it has recently begun to update Chapter 1 in the *Manual*, which provides a general overview of the state contracting process in Colorado, and Chapter 6, which provides information on drafting a contract. However, the majority of the *Manual* updates, along with any rule changes, have not yet been made. Therefore, it is important that these revisions occur as quickly as possible because state contracting staff rely on the *Manual* as part of their daily contract management activities.

- The Department of Personnel & Administration should provide contract management training to agency and institution personnel.** In the past, the Department has only provided contract administration training to agencies and institutions as requested. Because of resource issues, however, the Department discontinued these trainings until recently. In July 2004, the Department provided contract administration training to Department of Public Health and Environment staff. The training focused primarily on how to administer contracts (i.e., the procurement and contract approval process) and did not address the contract monitoring process. At the time of the audit, the Department did not have any plans to offer similar training sessions in the future. (Since work concluded on the audit, the Department has offered five training sessions, all of which were well attended, and has plans for two more.) During the audit, staff at the agencies and institution we reviewed indicated that contract administration and contract monitoring training would be beneficial. All three of the other states we reviewed (Arizona, Florida, and Washington) provide contract management training to agency staff. Providing standardized training to all state agencies and institutions can help ensure that contract management procedures, State Fiscal Rules, and statutes are applied appropriately across the State. Training could provide agencies with tools and best practices for assessing the risk associated with contracts and determining how to allocate limited contract monitor resources. If resources are still an issue, the Department could provide the training to the primary contract administrators for each agency and institution and then require the administrators to convey the information to their own contracting staff as discussed below.
- State agencies and institutions of higher education should provide training to their contract management staff.** Of the five agencies and institutions we reviewed, only the Departments of Personnel & Administration and Human Services currently provide training to their staff with contracting responsibilities. During the audit, fewer problems were noted at these two agencies with respect to their contract monitoring practices and contract administration files than at some of the other agencies that do not provide training to their staff. According to State Fiscal Rules, each state agency and institution of higher education is responsible for ensuring that its contracts comply with statutory and constitutional requirements. Providing contract management training to staff with contracting responsibilities will help ensure that staff understand the contracting process, are aware of their own individual responsibilities with respect to the process, and adequately monitor contractor progress to ensure the State receives value for its monies. Therefore, the Department of Personnel & Administration should ensure that agencies have established adequate controls and standards regarding training for contract management staff. At the agency level, this process should include evaluating training needs and ensuring that staff receive contract management training, as appropriate.

### **Recommendation No. 13:**

The Department of Personnel & Administration should improve the contract management process by:

- Updating its *State Contract Procedures and Management Manual* in a timely manner.
- Providing contract administration and contract monitoring training to agency and institution staff on a regular basis.
- Ensuring that agencies and institutions have established adequate controls and standards regarding training for contract management staff. At the agency level, this process should include evaluating training needs and ensuring that staff receive the appropriate contract management training.



## Department of Personnel & Administration Response:

### Implementation Date: December 2005.

- a. Agree. Revisions have been underway for some time, as the most difficult chapter – Chapter 6, Drafting the Contract – was targeted first. Chapters 1 and 6 of the Manual are complete and have been published on the website. We expect to complete the remainder of the Manual by the end of 2005.
- b. Agree. Contract Management Training has been scheduled and announced through the end of the fiscal year.
- c. Partially Agree. As stated above, the Department will provide an updated manual and regular contract management training to state agencies. Additionally, the Department will make contract management training a recurring topic in Colorado Contract Improvement Team meetings, Procurement Advisory Council meetings, and risk-based program oversight activities. However, the ultimate responsibility for ensuring agency personnel are adequately trained remains with the procuring agency. With the tools provided by the Department and the standard performance planning process, state agencies have the necessary mechanisms for supervisors and employees to identify and provide formal, informal, and on-the-job training needs necessary to adequately monitor contracts.

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## Employee Performance Expectations and Evaluations

Performance evaluations are the primary mechanism for assessing employees' abilities with respect to contract administration and monitoring. We found that although contract administrators are evaluated on their contracting skills, agency staff reported that contract monitors are not. Generally, contract administrators are part of an agency's central contracting office and contracting responsibilities are included in their job description and performance expectations. Based on interviews with staff at the departments and institutions of higher education we reviewed, contract administration skills are included in the performance expectations and evaluations for all of their contract administrators. However, as mentioned previously, contract monitors are generally individuals outside of an agency's central contract office, who work in the area related to the contract subject-matter. According to staff at the state agencies and institution of higher education we reviewed, contract monitors are not consistently provided with performance expectations surrounding their contracting responsibilities, nor are they evaluated on their contract monitoring skills. Contract monitoring activities are often added to the existing workload of these staff. Staff are then expected to monitor the contract as well as complete their primary job duties. As a result, many contract monitors are not aware of the performance expectations surrounding this position and are not evaluated on these expectations. This can lead to a lack of accountability with respect to contract performance.

As many agencies and institutions may not be familiar with contract monitoring expectations, the Department of Personnel & Administration should assist state agencies and institutions of higher education with performance planning and evaluations for contract monitor staff. This information should be included in the *State Contract Procedures and Management Manual* as well as in the training curriculum. Similar recommendations were made in the Office of the State Auditor's 1995 Contract Management Oversight Audit, but have not been implemented.

## **Recommendation No. 14:**

The Department of Personnel & Administration should assist state agencies and institutions of higher education with performance planning and evaluations for contract monitor staff. This information should be included in the *State Contract Procedures and Management Manual* as well as the Department's training curriculum as discussed in Recommendation No. 13.

### **Department of Personnel & Administration Response:**

**Agree. Implementation Date: December 2005.** The Contract Manual has a comprehensive description of contract management responsibilities, as well as tables of contents that map adequately the tasks and competencies that are common in contract management. Agencies will have to tailor the general considerations to the specifics of any project. For example, what would be expected of an employee in construction contract management will differ widely from expectations of an employee monitoring an audit contract.

The Department will work with other agencies through the Colorado Contract Improvement Team (CCIT) to identify model "desired experience" statements that might be useful in recruiting highly qualified personnel. The Department will also assist agencies in developing model performance objectives for evaluation plans.

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