



AUDITOR GENERAL

WILLIAM O. MONROE, CPA



STATE BOARD OF ADMINISTRATION CONTRACT ADMINISTRATION Operational Audit

SUMMARY

This operational audit, covering the period June 18, 2001, through February 28, 2005, and selected actions taken through May 19, 2005, focused on the State Board of Administration's (SBA's) contract administration procedures. In evaluating these procedures, we concentrated primarily on the SBA's purchase of an investment portfolio management system (Project). Our audit disclosed that SBA contracting procedures could be improved in the following respects:

Finding No. 1: Board records did not fully document the processes leading to selection of one Project consultant retained at a cost of over \$5.7 million.

Finding No. 2: For one key contract, under which payments totaling \$269,834 were made, the deliverables were not clearly or adequately described.

Finding No. 3: For one contract, under which payments totaling \$506,575 were made, the SBA did not document the circumstances necessitating the selection of the consultant without the benefit of competitive processes.

Finding No. 4: Some contracts did not include penalty and dispute resolution provisions.

Finding No. 5: The Board had not established policies and procedures

requiring individuals taking part in the evaluation and contract award process to attest in writing that they are independent of, and have no conflict of interest with respect to, entities evaluated and selected.

Finding No. 6: Consistent with established policy, SBA staff did monitor Project progress and contractor performance. However, the SBA had not established written procedures and standards to guide staff in the effective implementation of this policy for all contracts.

BACKGROUND

The State Board of Administration (SBA) in 2001 began the process of purchasing a new investment portfolio accounting system. Due to the size and complexity of this purchase, a Request for Information (RFI) was issued on June 18, 2001, to retain a consultant to evaluate the investment process and assist in the procurement. Subsequently, the SBA awarded a consulting contract to InvestTech Systems Consulting, Inc. (InvestTech).

Based on InvestTech recommendations, the scope of the purchase evolved from the procurement of a portfolio accounting system to the acquisition of an integrated investment portfolio management system (subsequently referred to as the Project). As part of the Project, separate RFI's were issued by InvestTech on behalf of the SBA for the following portfolio management system components:

- A Portfolio Accounting System to supply portfolio accounting functions.
- A Data Warehouse System to perform data management functions.
- A Message Broker System (also known as “middleware”) to facilitate communication between trading and accounting systems.
- A Reconciliation System to compare transaction activity shown by SBA records to activity shown by investment custodian records.

Eagle Investment Systems, Inc. (Eagle), with its “STAR” and “PACE” products, was selected by the SBA to supply the portfolio accounting system and data warehouse. Also, SunGard Business Integration (SunGard), with its “MINI” and “IntelliMatch” products, was selected by the SBA to provide the middleware and reconciliation software.

After the selection of Eagle and SunGard, the SBA issued an Invitation to Negotiate (ITN) on November 21, 2002, relating to the procurement of consultant services for the implementation of the Project. In early 2003, InvestTech was awarded the contract.

As of May 19, 2005, Project development and implementation costs totaled approximately \$8.9 million. The “go-live” date for the completed portfolio management system was September 6, 2004.

The scope of our audit addressed the management of the procurement processes associated with the selection of Project consultants and software, the negotiation of related contracts, and the monitoring of Project-related contracts. The functionality and operation of the system will be the subject of future audits by the Auditor General.

FINDINGS AND RECOMMENDATIONS

The effective and efficient procurement and implementation of any large scale system requires that an entity have in place a system of internal control that includes:

- Procedures to ensure an open, objective, and well-documented contractor selection process.
- Contracts containing provisions documenting the mutual agreement, substance, and parameters of what was agreed upon, including among other matters, clear specification of the responsibilities of the parties to the contract, deliverables, penalties for nonperformance, and dispute resolution procedures.
- Contract monitoring to ensure that contractors comply with contract terms, performance expectations are achieved, and problems are quickly identified and resolved.

As described in more detail in succeeding paragraphs, SBA contracting procedures could be improved in some respects.

Finding No. 1: InvestTech Contracts

As indicated in the BACKGROUND section of this report, the SBA selected InvestTech to assist the SBA in identifying, evaluating, and selecting a new portfolio accounting system. Subsequently, InvestTech was also selected to assist in the implementation of the integrated investment portfolio management system. As of May 19, 2005, over \$5.7 million had been paid to InvestTech.

With respect to these procurements and the related SBA policies and procedures, our audit disclosed the following:

- On June 18, 2001, the SBA issued an RFI to retain a consultant to evaluate the SBA’s current investment process and assist with the procurement of the new portfolio accounting system. Responses to the RFI were received from six vendors. In accordance with the

RFI, an evaluation team scored and ranked the responses and selected three finalists, each of which then made presentations to the evaluation team. Our audit disclosed that, contrary to RFI specifications, the SBA failed to document the final round of scoring.

In response to inquiries, the SBA replied that the selection committee had met and discussed each of the three presenting finalists and then recommended InvestTech. However, documentation was not available describing the scores awarded and the recommendation of the evaluation team.

- On November 21, 2002, the SBA issued an ITN relating to the procurement of consultant services for the implementation of the integrated investment portfolio management system. Two responses were received and InvestTech was awarded the contract in early 2003. The SBA was unable to provide documentation demonstrating the review and scoring of consultant responses and presentations.

The SBA in response to our inquiry indicated that the committee voted by show of hands to award the contract to InvestTech. The absence of documentation clearly showing the evaluation of responses precludes the SBA's demonstration that the consultant was selected in a fair and objective manner.

- As indicated above, the consultant, who assisted the SBA in defining the nature and scope of the Project, also submitted a proposal and was subsequently awarded the contract to implement the Project. Our audit disclosed that SBA policies and procedures do not prohibit consultants who perform needs assessments from competing for services relating to the implementation of the assessment recommendations. We found no evidence to indicate that there had been any lack of objectivity exercised with respect to the needs

assessment for this Project. However, the establishment of policies and procedures precluding those who have performed a needs assessment from competing for a contract to implement the assessment's recommendations may better ensure that the recommendations are based entirely on an objective evaluation, with no potential motivation coming from a future opportunity to profit from the implementation of the recommendations.

Recommendation: We recommend that the SBA completely document each phase of the consultant evaluation and selection processes. Additionally, to better ensure the objectivity of consultants performing needs assessments, the SBA should adopt policies and procedures precluding consultants from competing for services related to the implementation of their recommendations.

Finding No. 2: Contract Deliverables

All contracts should contain clear and adequate descriptions of deliverables. Our analysis of Project contracts disclosed that one of six contracts did not contain clear and adequate descriptions of deliverables. Specifically, the SunGard MINT contract did not sufficiently define the installation support to be provided by SunGard. As of May 19, 2005, payments totaling \$269,834 had been made under this contract.

While Parts 2.1 and 3.1(b) of the contract, as well as Part B of the contract's software schedule sought to address the installation support to be provided for the MINT product, the language of these parts lacked the necessary specificity to adequately ensure that the needed services were provided. The contract, in Part 2.1, stated that "SunGard (would) assist the Customer (the SBA) in basic installation the (sic) on or before the scheduled installation date. . ." The contract, in Part 2.1, also provided, "SunGard shall provide the installation support described on Part B of the Designated Schedule and assistance with any other implementation or related activities described on Part

B of the Designated Schedule.” However, Part B of the software schedule, in describing the installation support to be provided, merely describes the services as, “SunGard installation services for the Software (referring to MINT and MINT-related software) as mutually agreed to by SunGard and Customer (the SBA).”

The failure to more specifically define the services required for this part of the Project placed at risk the accomplishment of Project objectives. During the course of assisting the SBA with the installation of MINT, SunGard determined that it could not continue to provide staffing. As a result, the SBA had to secure the services of another consultant to assist in completing the installation.

Recommendation: We recommend the SBA ensure future contracts clearly define all deliverables.

Finding No. 3: Sakti Contract

As noted above in Finding No. 2, SunGard concluded that it was unable to provide installation support for the MINT product, and according to the SBA, the installation of the MINT software required product expertise that neither the SBA nor InvestTech could adequately supply. Consequently, the SBA sought the services of another consultant to provide the needed MINT expertise. Through contact with SunGard, the SBA was referred to Sakti, a consulting company with expertise in the installation of MINT. Subsequently, a contract was entered into between the SBA and Sakti for the provision of MINT installation support services. Records indicate that as of May 19, 2005, approximately \$506,575 had been spent for the services of Sakti.

Contrary to SBA procedure, the contractor, Sakti, was engaged without the benefit of a competitive selection process. SBA purchasing procedures in place at the time of the selection of Sakti required at least three informal quotations for procurements exceeding \$10,000 and competitive solicitation for procurements exceeding \$30,000. SBA procedures did make provision for exceptions to the competitive procurement requirements and required that the justification for such purchases be reduced to writing and approved in advance by the Executive Director. In response to our inquiries, SBA personnel have described conditions that may have qualified the selection of Sakti as an exception to the SBA’s competitive procurement policy; however, the exception was not justified in writing and approved in advance by the Executive Director.

Recommendation: We recommend the SBA adhere to established purchasing procedures for all procurements.

Finding No. 4: Contract Provisions

To encourage contractor performance, SBA contracts should contain penalty provisions. Absent such provisions, the SBA may lack an effective means, other than litigation, to compel contractor performance.

Further, disputes between contracting parties may emerge during the course of a project, and at times, place at risk the effective and efficient completion of projects. Incorporating into contracts a mechanism to promptly and adequately address disputes in a good faith manner may help to avoid litigation.

Our review of Project-related contracts disclosed:

- The InvestTech, SunGard MINT, and SunGard IntelliMatch contracts did not include a penalty provision.
- The InvestTech, SunGard MINT, SunGard IntelliMatch, and Sakti contracts did not

incorporate dispute resolution procedures as part of the agreement.

Recommendation: We recommend the SBA ensure future contracts include clauses that provide mechanisms to address consultant nonperformance issues and contract disputes.

Finding No. 5: Conflict of Interest Statements

Our audit tests disclosed that for the six Project procurements, SBA records did not contain evidence that individuals taking part in the evaluation and contract award processes had attested in writing that they were independent of, and had no conflict of interest with respect to, the entities evaluated and selected. Additionally, we determined that the SBA had not adopted policies and procedures requiring independence attestations for those involved in the evaluation and contract award processes.

Such attestations help to ensure the integrity and objectivity of the procurement and contracting processes. In response to inquiry, the SBA stated that a conflict of interest disclosure requirement will be incorporated into future ITN-based acquisitions.

Recommendation: We recommend policies and procedures be developed to ensure the independence of evaluation team members is clearly documented for all evaluation and award processes.

Finding No. 6: Contract Monitoring

Throughout the life of a contract, monitoring is necessary to ensure contractors provide high quality products and services in accordance with contract terms. It is essential that written policies, procedures, and standards be developed and communicated to contract managers to

ensure that contract monitoring is performed in a consistent and comprehensive manner.

SBA Executive Director Policy and Procedure 10-031, effective November 1, 2004, states, "It is the policy of the Executive Director of the SBA that all contracts in which the SBA is a party shall be properly...monitored." Consistent with this policy, SBA staff did monitor the progress of the Project and the performance of Project contractors. However, our review did disclose that the SBA had not implemented the policy by establishing written procedures and standards to reasonably ensure that for all contracts, contractor performance is effectively monitored and that such monitoring efforts are appropriately documented.

The SBA has adopted as part of its 2005-2007 Strategic Plan the objective to develop and implement a contract administration program by the end of 2005. The SBA further indicated that it was in the process of recruiting a contract administrator and implementing a program by the end of the 2005 calendar year.

Recommendation: We recommend the SBA continue to develop and adopt monitoring procedures and standards that address, among other matters:

- The assignment of contract management responsibilities, including those relating to the documentation of monitoring efforts.
- A methodology for determining the nature and timing of contract monitoring. Such a methodology may be based on a risk assessment process that takes into consideration, among other matters, the dollar value of the contract, the nature of the contracted services and associated inherent risks, and past performance of the contractor.
- A mechanism to accumulate information with respect to the various contractors, evaluate their performance under the

contract terms, track payments to contractors, track the acceptance of contract deliverables, and provide performance feedback.

OBJECTIVES, SCOPE, AND METHODOLOGY

This operational audit focused on the SBA's contract administration procedures. In evaluating these procedures, we concentrated primarily on the SBA's purchase of an investment portfolio management system. Our specific objectives were to:

- Obtain an understanding and assess the effectiveness of related SBA internal controls.

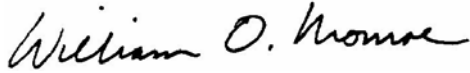
- Evaluate SBA compliance with selected controlling laws and other guidelines.

In conducting our audit, we obtained an understanding of governing laws and guidelines. We also reviewed SBA manuals, interviewed personnel, performed tests of compliance with applicable laws and rules, performed tests of pertinent records, and conducted tests of the effectiveness of relevant SBA controls.

Our audit included examinations of various transactions occurring during the period June 18, 2001, through February 28, 2005, and selected actions taken through May 19, 2005.

AUTHORITY

Pursuant to the provisions of Section 11.45, Florida Statutes, I have directed that this report be prepared to present the results of our operational audit.



William O. Monroe, CPA
Auditor General

AUDITEE RESPONSE

In a letter dated October 25, 2005, the Executive Director provided responses to our preliminary and tentative findings. The letter is included in its entirety at the end of this report as Exhibit A

To promote accountability in government and improvement in government operations, the Auditor General makes operational audits of selected programs, activities, and functions of State agencies. This operational audit was made in accordance with applicable *Government Auditing Standards* issued by the Comptroller General of the United States. This audit was conducted by Matthew Tracy, CPA, and supervised by Kathryn Walker, CPA. Please address inquiries regarding this report to Don Hancock, CPA, Audit Manager, via e-mail at donhancock@aud.state.fl.us or by telephone at (850) 487-9037.

This report, as well as other audit reports prepared by the Auditor General, can be obtained on our Web site (<http://www.state.fl.us/audgen>); by telephone at (850) 487-9024; or by mail at G74 Claude Pepper Building, 111 West Madison Street, Tallahassee, Florida 32399-1450.

EXHIBIT A
AUDITEE RESPONSE



STATE BOARD OF ADMINISTRATION
1801 HERMITAGE BOULEVARD
TALLAHASSEE, FLORIDA
32308
(850) 488-4406

Post Office Box 13300
32317-3300

JEB BUSH
GOVERNOR
AS CHAIRMAN
TOM GALLAGHER
CHIEF FINANCIAL OFFICER
AS TREASURER
CHARLIE CRIST
ATTORNEY GENERAL
AS SECRETARY
COLEMAN STIPANOVICH
EXECUTIVE DIRECTOR

October 25, 2005

Mr. William O. Monroe
Auditor General, State of Florida
G74 Claude Pepper Building
111 West Madison Street
Tallahassee, Florida 32399-1450

Dear Mr. Monroe:

As requested in your September 1, 2005 letter, following are our responses to the preliminary and tentative findings and recommendations which may be included in your report on the operational audit of the State Board of Administration's contract administration procedures for the period June 18, 2001 through February 28, 2005, and selected actions taken through May 19, 2005:

Finding No. 1: Board records did not fully document the processes leading to selection of one Project consultant retained at a cost of over \$5.7 million.

SBA Response:

- While the final meeting of the selection committee on the hiring of InvestTech to assist the State Board of Administration (SBA) in identifying, evaluating, and selecting a new portfolio accounting system was not fully documented, the selection committee chair did prepare an email to the Executive Director outlining the search process and the final vote of the team members. (See attached copy of email dated September 26, 2001.)
- Due to the limited number of respondents, we determined the decision to interview both firms and the subsequent meeting of the selection team to identify a finalist, to be sufficient. We concur that we failed to document the review and scoring process. However, the ITN and the responses received were retained by the SBA.
- When the selection committee decided to select the Eagle suite of products, we knew that due to the leading edge nature of the technology, there would be a limited number of firms with significant experience or expertise implementing the products. However, the committee determined that the Eagle suite of products offered the SBA the best long term effectiveness when compared to the other products which were evaluated. With just two respondents, if InvestTech were prohibited from consideration, we would have been required to select a firm with no experience implementing Eagle products, therefore placing undue risk on the project and the SBA.

With an updated Procurement Policy that took effect on December 1, 2004, the SBA is confident that the issue on documentation has been adequately addressed. Moreover, during the past three years, the SBA established a number of new policies and procedures to guard against any actual or perceived conflict of

EXHIBIT A
AUDITEE RESPONSE (CONTINUED)

interest. The contract with the consultant mentioned in the report was an exception because of extenuating circumstances.

Finding No. 2: For one key contract, under which payments totaling \$269,834 were made, the deliverables were not clearly or adequately described.

SBA Response:

\$235,000 of the \$269,834 was for licensing of the Message Broker System (also known as middleware or Mint software), which was clearly and adequately described in the contract. The contract also adequately described SunGard's installation and support services, the additional services negotiated and included in the licensing cost such as 5 days of training and 66 hours of consulting to be used for installation, consulting or additional training, and the negotiated consulting fee rate of \$200 per hour for the additional professional services related to implementation. We, however, agree that the supporting narrative should have clearly described the implementation responsibilities of SunGard. In the future when a contract provides for both the installation and the implementation of a software product, the SBA will better delineate the two processes, and separately describe each.

Finding No. 3: For one contract, under which payments totaling \$506,575 were made, the SBA did not document the circumstances necessitating the selection of the consultant without the benefit of competitive processes.

SBA Response:

The circumstances and the required approval in advance of the noncompetitive procurement were not documented; however, they were known and discussed in status and management meetings. The decision not to rebid these implementation services was due to 1) Competitive implementation rates had already been established within the Eagle implementation ITN. 2) Rates with SunGard were negotiated down from their established rate based on the competitive rates in the ITN process. 3) Expertise in the Mint product was very limited. 4) The negotiated rate with Sakti was a better rate than SunGard had agreed to. These factors and the circumstances were discussed with management prior to contract approval.

The SBA believes that the updated Procurement Policy that took effect on December 1, 2004 provides clearer guidance to SBA employees. The SBA is confident that the issues on documentation and approval have been adequately addressed through the required monitoring activities identified in the updated policy.

Finding No. 4: Some contracts did not include penalty and dispute resolution provisions.

SBA Response:

The SBA understands the significance of including penalty and dispute resolution provisions in contracts. These provisions have been selectively included in contracts in the past. As we continue to improve our contracting processes, the SBA will give serious consideration to the increased use of penalty and dispute resolution provisions in the future when deemed appropriate.

EXHIBIT A
AUDITEE RESPONSE (CONTINUED)

Finding No. 5: The Board had not established policies and procedures requiring individuals taking part in the evaluation and contract award process to attest in writing that they are independent of, and have no conflict of interest with respect to, entities evaluated and selected.

SBA Response:

The SBA has revised its Procurement Policy to require individuals taking part in the evaluation and contract award process to certify in writing they are independent and have no conflict of interest with respect to entities being evaluated. The required form has also been developed and is required to be completed prior to receipt and review of proposals.

Finding No. 6: Consistent with established policy, SBA staff did monitor Project progress and contractor performance. However, the SBA had not established written procedures and standards to guide staff in the effective implementation of this policy for all contracts.

SBA Response:

As acknowledged in the report, the SBA management understands the importance of prudent contract administration. Hence, the inclusion of this function in the SBA 2005-2007 Strategic Plan. The SBA created a Contract Analyst III position and filled it on July 25, 2005. The SBA is also working on procuring a new contract management software package. Work will be ongoing by the Contract Analyst III, the Procurement Manager, and the Senior Operating Officer-Policy, Planning, and Administrative Services developing processes and procedures for the SBA's new contract administration function and additional written procedures will be developed as we implement the new processes.

Thank you for the opportunity to respond to these findings and recommendations. If you have any questions, please do not hesitate to contact Ms. Rivera-Alsing at (850) 413-1259 or me at (850) 413-1250.

Sincerely,



Coleman Stipanovich
Executive Director

cc: Gwenn Thomas, Chief Operating Officer
Florida D. Rivera-Alsing, Chief of Internal Audit
Bruce R. Meeks, Inspector General

EXHIBIT A
AUDITEE RESPONSE (CONTINUED)

Copeland_Robert

From: Stipanovich_Coleman
Sent: Friday, September 28, 2001 10:52 AM
To: Copeland_Robert
Subject: RE: Phase one provider selected

Thanks

-----Original Message-----

From: Copeland_Robert
Sent: Wednesday, September 26, 2001 4:55 PM
To: Thomas_Gwenn; Stipanovich_Coleman
Cc: Mathes_Greg; Nelson_Eric
Subject: Phase one provider selected

First, my apologies for not having sent this email you earlier. In my mind, I had sent this email.

On August 22, 23, and 24, the steering committee interviewed three candidates for the provider in phase one of the project to replace GPVS. The candidates selected for presentations were Cutter Associates, InvestTech Systems, and Pricewaterhouse Coopers. The rankings after the review of the responses to the RFI were in that order.

On September 4th, the committee reconvened to discuss the presentations by the three candidates. By unanimous vote, InvestTech Systems was selected as the number one and Pricewaterhouse Coopers was a close number two. The decision was made to contact references for InvestTech and assuming everything checked out, to proceed with contract negotiations. The references contacted gave InvestTech an outstanding recommendation. Bill Beck was assigned the task of drafting a Master Services Agreement to send to InvestTech. The final document is currently being staffed.

InvestTech's cost proposal is well within the lower tier of the proposals submitted in the responses to the RFI. Their estimate of \$338,380 excluding travel expenses is well under the budgeted amount. Again we are relying on the involvement of SBA staff in the completion of this phase of the project. InvestTech has committed some top-notch people to this project including one of the principals himself, Bruce Vollert. Additionally, Bruce was involved in a project with the Treasurer's office in 1993 and was complemented by Lee Richardson as having performed a very professional job.

It is our expectation to wrap-up the contract work this week and have InvestTech in house by the week of October 8 to begin work on the project.

Again, I apologize for not sending this to you earlier.

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