



**COUNTY OF LOS ANGELES
DEPARTMENT OF AUDITOR-CONTROLLER**

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April 13, 2023

TO: Mark Pestrella, Director
Department of Public Works

FROM: Greg Hellmold, Chief *Greg Hellmold*
Office of County Investigations

SUBJECT: **DEPARTMENT OF PUBLIC WORKS – IMPROVEMENT OPPORTUNITIES NOTED DURING LIMITED REVIEW (#IOR-2018-14463) FIRST FOLLOW-UP REVIEW**

We completed the first follow-up review of the Department of Public Works (DPW or Department) Improvement Opportunities Noted During Limited Review dated August 27, 2021 (Report #IOR-2018-14463). As summarized in Table 1, DPW fully implemented three recommendations, partially implemented one recommendation, and did not implement one recommendation. The Department needs to fully implement the two outstanding recommendations to strengthen controls over procurement, specifically in the areas of equipment rentals and materials/supplies at field locations, to reduce the risk of inappropriate purchases and procurement fraud.

Table 1 - Results of First Follow-up Review

PRIORITY RANKINGS	TOTAL RECOS	FULLY IMPLEMENTED	PARTIALLY IMPLEMENTED	NOT IMPLEMENTED
PRIORITY 1	2	1	1	0
PRIORITY 2	3	2	0	1
PRIORITY 3	0	0	0	0
TOTAL	5	3	1	1
			2	

For details of our review and the Department’s corrective actions, see Attachment. We will perform a second follow-up review and report back on the outstanding recommendations in accordance with our standard procedures.

We thank DPW management and staff for their cooperation and assistance during our review. If you have any questions please contact me at (213) 893-0243 or ghellmold@auditor.lacounty.gov, or your staff may contact Graciela Soto at (213) 893-0552 or gsoto@auditor.lacounty.gov.

GH:SL:GLS:gl
Attachment

c: Oscar Valdez, Interim Auditor-Controller
Audit Committee
Audit Division

REPORT #F1-2018-14463

LOS ANGELES COUNTY AUDITOR-CONTROLLER

Robert G. Campbell
ASSISTANT AUDITOR-CONTROLLER

Greg Hellmold
DIVISION CHIEF

Office of County Investigations

Report #F1-2018-14463

**DEPARTMENT OF PUBLIC WORKS
IMPROVEMENT OPPORTUNITIES NOTED DURING LIMITED REVIEW (#IOR-2018-14463)
FIRST FOLLOW-UP REVIEW**

	RECOMMENDATION	A-C COMMENTS
<p>1 Priority 1 - DPW management ensure that all business units maintain adequate procurement documentation, including:</p> <p>a) A detailed requisition for each purchase identifying the specific items requested with sufficient detail that someone not involved in the purchase could identify the items and obtain price quotes from other vendors, the purpose of the purchase, request date, and the name and documented approval (e.g., wet or electronic signature, initials) of the initial requestor and subsequent approver(s).</p> <p>b) Information about the vendor selection process including efforts to utilize existing master agreements, efforts to obtain competitive pricing/quotes, how/why the awarded vendor was chosen, name and signature of final approver, and a notation in any case where the requestor recommended reference vendors.</p> <p>Original Issue/Impact: Documentation of Procurement Transactions – DPW does not always maintain an appropriate documentary trail for purchases. Specifically, DPW’s Road Maintenance Division 4 (RMD4), Bridge Maintenance Unit was not always able to provide documentation identifying the employee who requested equipment rentals or purchases of materials/supplies, justification for the purchases, or to identify the employee who ultimately approved the rental or purchase. In addition, RMD4 did not always document the process used for soliciting quotes and selecting the awarded vendor.</p> <p>The lack of documentation to memorialize purchase requests prevented us from determining whether these purchases were necessary or that the County received competitive pricing. It also impaired the potential detection of approximately \$14.3 million in conflicted purchases involving a County employee and related vendors.</p>	<p>Recommendation Status: Partially Implemented</p> <p>DPW management revised the Purchase Request (PR) Form used by all its divisions. We noted that the revised form includes fields documenting:</p> <ul style="list-style-type: none"> • The specific items requested, with sufficient detail that someone not involved in the purchase could identify the items and obtain price quotes from other vendors • the purpose of the purchase • request date • the name and signature of the initial requestor and subsequent approver(s) • the vendor selection process and whether the purchase will utilize an existing agreement <p>Although DPW management established the new PR Form, they acknowledge that some divisions are not in full compliance utilizing this new form and they are continuing to train them. In addition, DPW management informed us that they have not yet implemented this recommendation for rental transactions.</p> <p>DPW management indicated they plan to fully implement the recommendation by May 31, 2023.</p>	

Priority Ranking: Recommendations are ranked from Priority 1 to 3 based on the potential seriousness and likelihood of negative impact on the Agency’s operations if corrective action is not taken.

RECOMMENDATION	A-C COMMENTS
<p>The lack of formal documentation by initial requestors/end-users who are not users of the County's enterprise accounting and purchasing system (eCAPS) impairs the ability of management or other reviewers to follow-up on questionable or potentially conflicted transactions and identify the staff responsible for them. This also prevents management from ensuring that procurement transactions are necessary and relevant to the specified DPW project.</p>	
<p>2 Priority 1 - DPW management ensure that all business units maintain proper segregation of duties over procurement transactions including between the request/requisition, purchase approval, vendor solicitation and selection, and receiving processes.</p> <p>Original Issue/Impact: Segregation of Procurement Duties – DPW staff did not always segregate key responsibilities for procurement transactions. For example, we noted transactions processed in RMD4's Bridge Maintenance Unit in which one individual initiated the request, specified the equipment rentals or materials/supplies to be purchased, and identified the vendor from which to procure the items.</p> <p>We noted that a single requestor/end-user frequently specified the materials/supplies to purchase, obtained quotes for the materials/supplies directly from vendors they selected, then forwarded the quotes to procurement staff for processing. For equipment rentals, a single requestor/end-user routinely specified the equipment to rent and the duration of the rental, selected the equipment rental vendor, and forwarded the request to DPW Fleet Management Division (Fleet) for processing. Staff from DPW Procurement and Fleet Divisions often issued the purchase orders and rental agreements to the requested vendors without soliciting other quotes. This enabled the requestor to control all significant aspects of the procurement process, and to direct \$14.3 million in procurement activity over a ten-year period to select vendors with which the requestor had personal, familial, and/or financial relationships.</p> <p>County Fiscal Manual (CFM) Section 4.1.3 – General Internal Controls, requires that a department's internal controls over expenditures should at a minimum ensure the segregation of the following duties:</p>	<p>Recommendation Status: Implemented</p> <p>On January 26, 2022, DPW Workforce Support (Workforce) management e-mailed all divisions to remind staff to maintain appropriate segregation of duties over procurement transactions, "including between submitting a request, approving the request, soliciting quotes from vendors, ordering, and receiving the order in eCAPS." In addition, in February 2023, DPW began training staff with updated reference guides and training material to reinforce the importance of separation of duties in the procurement process.</p> <p>Further, DPW's Internal Audit Group (IAG) has incorporated a review of proper segregation of duties in their audits. We reviewed IAG's Audit Program and completed audit workpapers for one of their reviews, and noted that they selected a sample of ten procurement transactions and confirmed that approvals of the requisition, purchase, approval, receipt, and payment were adequately segregated.</p>

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<ul style="list-style-type: none"> • Employees ordering goods or services must not approve purchases, receive goods, or account for purchases. • Employees approving purchases must be independent of the ordering function and the receipt and control of goods or services. • Employees receiving goods or services and certifying quantities received must not be associated with nor have responsibilities related to ordering the goods or services or accounting for purchases. • Employees making disbursements for goods or services (i.e., through the online vendor payment system) should not be associated with or have responsibilities related to the procurement, encumbrance, approval, and receiving functions. <p>Increased risk of procurement fraud and conflicts of interest in the procurement process. Increased costs to the County and decreased opportunity for vendors due to the lack of a competitive procurement process.</p>	
<p>3 Priority 2 - DPW Management develop a comprehensive and effective monitoring program to provide reasonable assurance that procurement controls are functioning as intended and procurement transactions comply with County and Departmental policies. The program should include reviewing required supporting documentation for a representative sample of procurement transactions.</p> <p>Original Issue/Impact: Compliance Monitoring of Procurement Transactions – DPW did not have an effective process to continually monitor internal controls over procurement by periodically reviewing documentation supporting transactions processed in eCAPS. DPW conducted periodic eCAPS reviews, but they did not include reviewing documentation maintained at the field offices to support the transactions processed in eCAPS. As a result, RMD4 staff routinely did not maintain basic documentation supporting procurement transactions that were processed in eCAPS and did not segregate key procurement responsibilities (as discussed in recommendations 1 and 2 above), and these field office issues went undetected for at least 10 years.</p> <p>CFM Section 1.0 states that management of each County department is primarily responsible for designing, implementing, and maintaining a system of internal controls that provides reasonable assurance</p>	<p>Recommendation Status: Implemented</p> <p>DPW management reported that IAG will incorporate reviews and enforcement of procedures identified from recommendation #1 and #2, including reviewing and validating PR Forms to ensure all required documentation is maintained to support procurement transactions and ensure proper segregation of duties.</p> <p>Additionally, IAG developed two new review procedures to determine the adequacy of internal controls over procurement/purchasing where Procurement and divisional staff will work collectively to:</p> <ol style="list-style-type: none"> 1) Review frequently purchased non-agreement items. Specifically: <ul style="list-style-type: none"> • To identify high-volume purchases without a purchase agreement • Take steps to enter into a purchase agreement 2) Review vendor solicitations / bid rotations. Specifically: <ul style="list-style-type: none"> • Identify the specific vendors solicited and awarded per each request • Determine if the solicited vendors are adequately rotated, and thereafter

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<p>that important departmental and County objectives are being achieved. The CFM also states that management must monitor internal controls on an ongoing basis to ensure that any weaknesses or non-compliance are promptly identified and corrected.</p> <p>CFM Section 4.1.3 requires management to continually monitor its control system to ensure all expenditures are necessary to perform departmental assigned functions and an adequate system of checks and balances (segregation of duties) exists to minimize the risk of fraud and abuse in the procurement/ disbursement functions.</p> <p>Increased risk of procurement fraud when internal controls over procurement processes are not routinely reviewed. The absence of a comprehensive and effective review process increases the risk that improper purchase transactions and awards could go undetected. This also impairs the ability of management to assess the organization's compliance and risk factors associated with procurement transactions.</p>	<ul style="list-style-type: none"> Notify divisional management if vendor rotation for solicited vendors is not sufficient (same three vendors solicited >50%) to ensure the DPW division sought and obtained the most favorable terms available <p>IAG work papers indicate that DPW initiated a review of procurement requests in October 2022. As of March 2023, DPW identified 19 commodities recommended for agreement pursuant to their review of non-agreement purchases (excludes equipment rentals covered in Recommendation #5) and indicated they are currently working with Internal Services Department to formulate such agreements.</p> <p>DPW management indicated they will continue to conduct audits using IAG's audit program, ensure all divisions respond to DPW Procurement requests to complete the review of frequently purchased non-agreement items, and utilize data obtained from the review of vendor rotations to implement changes as needed. DPW further indicated that due to the decentralized nature of DPW's existing procurement procedures they will continue to revise and implement additional reviews on an as-needed basis to provide reasonable assurance that procurement controls are functioning as intended.</p>
<p>4 Priority 2 - DPW management:</p> <p>a) Train all employees with procurement responsibilities on the overall procurement process, the importance of and their role in internal controls over procurement, and red flags to look out for. The training should reinforce to employees that they are empowered to question, follow-up, and report to management on any irregular or suspicious transactions.</p> <p>b) Consider implementing an acknowledgment form for staff with procurement responsibilities to memorialize that they have been trained on and understand procurement functions.</p> <p>c) Consider periodically rotating staff with procurement responsibilities to facilitate cross-training and a more comprehensive and holistic understanding of the procurement process.</p>	<p>Recommendation Status: Implemented</p> <p>a) We reviewed the training materials and sign-in sheets for eleven procurement trainings DPW conducted during September to November 2021 for non-eCAPS users involved in the procurement process. As of January 2023, DPW expanded the training presentation to include internal control responsibilities and common procurement red flags which are used to train both e-CAPS and non-eCAPS users.</p> <p>b) DPW management retained sign-in sheets in lieu of requiring employees to sign acknowledgement forms to document procurement training attendance.</p> <p>c) DPW reported that Workforce and IAG considered the recommendation to periodically rotate staff. On</p>

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<p>Original Issue/Impact: Procurement Cross-Training – We noted instances where DPW staff involved in some aspect of reviewing, approving, and/or processing procurement requests did not understand the overall procurement process, and were not trained on risk factors/red flags, which should have triggered additional scrutiny. For example, RMD4 staff who processed requests for materials/supplies and equipment rentals stated they were not trained on other responsibilities such as the importance of obtaining independent vendor quotes, documenting communication with vendors, and understanding approval requirements to ensure the requested materials/supplies or equipment rentals were necessary. They also stated they were not instructed on indicators of fraud (e.g., a requestor regularly recommending awards to the same small group of vendors).</p> <p>Reduced effectiveness in identifying questionable and/or inappropriate procurement transactions, and increased risk of fraudulent and/or conflicted procurement transactions going undetected.</p>	<p>January 26, 2022, Workforce management sent an e-mail to all DPW divisions strongly encouraging the rotation of staff assigned to procurement roles. However, DPW management indicated that they will not enforce or track staff rotations.</p>
<p>5 Priority 2 - DPW plan and perform a periodic analysis of rental equipment utilization and costs to provide Department management the information needed to optimize the composition of DPW's equipment fleet, and to make informed cost-benefit determinations about renting versus buying commonly used equipment items.</p> <p>Original Issue/Impact: Equipment Rent-Lease-Purchase Analysis – DPW routinely rents construction equipment and spent over \$160.5 million on such rentals between July 1, 2011 and May 17, 2021. However, the Department has not comprehensively analyzed equipment rentals to determine whether purchasing or leasing commonly used equipment might be more cost effective. Periodically analyzing rental equipment utilization may identify opportunities to reduce costs and improve operational effectiveness by purchasing or leasing commonly used equipment, and to tailor/optimize equipment master agreements to better meet the Department's needs.</p> <p>Without a periodic analysis of rental equipment utilization trends and costs, DPW management lacks the information necessary to optimize the Department's equipment fleet or make fully informed cost-benefit decisions, potentially resulting in excess equipment rental costs and operational inefficiencies.</p>	<p>Recommendation Status: Not Implemented</p> <p>DPW has not developed a plan to perform a periodic analysis of rental equipment utilization and costs to optimize the composition of DPW's rented and owned equipment fleet.</p> <p>DPW management indicated they plan to fully implement the recommendation by May 31, 2023.</p>

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We conducted our review in conformance with the International Standards for the Professional Practice of Internal Auditing. For more information on our auditing process, including recommendation priority rankings, the follow-up process, and management's responsibility for internal controls, visit auditor.lacounty.gov/audit-process-information.

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