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An Audit Report on

**The Information and  
Communications Technology  
Cooperative Contracts Program  
at the Department of Information  
Resources**

October 2011  
Report No. 12-004



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## Overall Conclusion

From September 2007 through February 2011, the Department of Information Resources (Department) reported collecting approximately \$42.6 million in fees on purchases that customers made through its Information and Communications Technology Cooperative Contracts Program (Program).

The Department should ensure that the amount of Program fees it collects is accurate and that it collects all fees that vendors owe. While the Department had policies and procedures to help ensure the accuracy, completeness, and timeliness of the Program fees it collects, it did not follow those policies and procedures.

The Department is statutorily required to recover its costs for operating the Program through the fees that customers pay vendors and that the vendors then pay the Department. Therefore, it is important for the Department to establish reasonable assurances regarding those fees to help ensure that it can recover its costs and that vendors comply with contract requirements.

The Department should address additional issues regarding Program fees. Specifically:

- The calculation that determines a customer's price for making a purchase through the Program may have resulted in customers paying fees that exceeded the fees that vendors were contractually required to pay the Department. Limitations associated with the Department's data prevented auditors from determining how much the customer fees may have exceeded the fees that vendors paid the Department.
- The fee set in the Department's Program contracts with vendors did not reflect the Department's costs to operate the Program, as required by the Texas Government Code. Instead, the Department (1) set the fees based on

### The Information and Communications Technology Cooperative Contracts Program

Cooperative contracts are information resource technology product and related service contracts established for use by state agencies and local governments that feature volume discounts not generally available to individuals and single institutions.

Texas Government Code, Section 2157.068, requires the Department of Information Resources (Department) to procure commercial software, hardware, or technology services, other than telecommunications services, that are generally available to businesses or the public and for which the Department determines that a reasonable demand exists in two or more state agencies.

Texas Government Code, Section 2157.068, further states that the Department may charge a reasonable administrative fee to a state agency, political subdivision of this state, or governmental entity of another state that purchases commodity items through the Department in an amount that is sufficient to recover costs associated with the administration of the Information and Communications Technology Cooperative Contracts Program. In fiscal year 2010, the Department reported collecting approximately \$15.1 million in fees.

In fiscal year 2010, the Department managed 871 Program contracts with vendors, and 4,208 customers made purchases that reportedly totaled approximately \$1.6 billion.

In addition to state agencies and higher education institutions, Texas Government Code, Section 2054.0565, allows local government entities, school districts, assistance organizations, and out-of-state governmental entities to make purchases through the Program.

This audit was conducted in accordance with Texas Government Code, Sections 321.0131 and 321.0132.

For more information regarding this report, please contact Nicole Guerrero, Audit Manager, or John Keel, State Auditor, at (512) 936-9500.

management's judgment or (2) reduced the fees as part of its contract negotiations with vendors to obtain higher customer discounts.

- As a result of its Program contract negotiations with vendors and its inconsistency in amending contracts in a timely manner, the Department did not set one standard fee. Instead, the fees ranged from 0 percent to 2 percent of a customer's purchase price.

### **Subsequent Events**

Since the end of the audit period (September 2007 through February 2011), the Department asserts that it has taken certain actions to improve its management of Program fees. The Department asserts that it has:

- Implemented processes to verify the accuracy, completeness, and timeliness of the Program fees it collects.
- Amended its Program contracts to ensure that the calculation of customer price does not result in customers paying fees that exceed the fees vendors pay to the Department.
- Reviewed how Program costs are captured in its fee-setting methodology.
- Strengthened its accounting processes to ensure compliance with General Appropriations Act requirements.

### **Key Points**

**The Department has accounting controls to ensure that it properly processes and documents Program fees and expenditures.**

From September 2007 through February 2011, the Department properly processed Program fees and expenditures. Specifically:

- The Department properly processed 59 (98 percent) of 60 Program fee receipts tested. The 60 receipts tested totaled \$1,086,168.
- The Department properly processed all 60 expenditures of Program fees tested. The 60 expenditures tested totaled \$269,094.

For the receipts and expenditures tested, the Department (1) accurately recorded the transactions in its accounting system, (2) ensured that management properly reviewed and approved the transactions, and (3) supported the transactions with appropriate documentation.

### **The Department used Program fees to secure procurement of a Program contract.**

In fiscal year 2010, the Department spent \$5.0 million in Program fees to secure procurement of a Program contract for security network services. One state agency later reimbursed the Department \$3.8 million of that amount, but the Department paid for the remaining \$1.2 million with Program fees. For other Program contracts, the Department procures the contract and customers then pay vendors for (1) the products or services they receive through the contract and (2) fees that allow the Department to recover its costs. However, the manner in which the Department procured the \$5.0 million contract did not allow the Department to fully recover its costs (see Chapter 3-D for additional information on how Program fees were spent).

### **The Department should comply with certain financial reporting requirements.**

The Department should improve its processes for reporting Program fees and other related information. Specifically:

- The Department should ensure that its annual encumbrance report accurately reports its outstanding financial obligations. The Department overstated encumbrances in its annual encumbrance reports for fiscal years 2008, 2009, and 2010.
- The Department should comply with reporting requirements in the General Appropriations Act. The General Appropriations Acts (80th and 81st Legislatures) required the Department to report in its annual financial report:
  - The costs avoided and/or savings obtained through Program activities.
  - A list of agencies and units of local government that the Program served.

The Department did not report the required information in its annual financial reports.

- The Department should report changes to Program fees to the Legislative Budget Board and the Office of the Governor, as required by Texas Government Code, Section 316.045. The Department changed the fee for fiscal year 2010 from 2.0 percent to 1.25 percent, but it did not report that change to the Legislative Budget Board and the Office of the Governor.

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

The Department agreed with the recommendations in this report.

## ***Summary of Information Technology Review***

Auditors examined the Department's Contract Management System, which tracks contract and financial information for each Program contract. Although the Contract Management System has reasonable and necessary controls over data processing, the Department should strengthen certain user access controls and other controls that ensure data entered into the Contract Management System is accurate and complete.

Auditors also examined the CDI Accounting System, which is the Department's internal accounting system. While that system had the necessary controls to ensure that financial transactions were complete, accurate, and authorized, the Department should ensure that the CDI Accounting System generates reliable reports and strengthen security over that system's database. The Department reported that, on September 1, 2011, it will implement a new accounting system that will correct those weaknesses.

## ***Summary of Objectives, Scope, and Methodology***

The audit objectives were to determine whether the Department:

- Sets the administrative fee for the Program at a reasonable amount sufficient to recover the costs of the Program and complies with state laws, rules, and Department policies and procedures related to the administrative fee.
- Accurately and completely records the Program's financial transactions in a timely manner and processes them in compliance with state laws, rules, and Department policies and procedures.
- Maintains proper accounting controls over the Program.

The scope of this audit covered Program fees, transfers, and expenditures from September 2007 through February 2011 and the Department's processes for collecting, analyzing, reviewing, and determining the fees.

The audit methodology included reviewing the Department's methodology for setting fees for the Program, reviewing select Program contracts and vendor sales reports, collecting information and documentation, performing selected tests and other procedures, analyzing and evaluating the results of tests, and interviewing Department management and staff.

The audit methodology also included collecting and analyzing financial records, contracts, fiscal year budgets and sales projections, and policies and procedures and reviewing samples of revenues, expenditures, transfers, and associated supporting documentation.

Auditors assessed the data reliability of the information used to manage the Program and the fees collected. That assessment included observing controls over data integrity in selected systems and databases, reviewing information about the data and the systems, performing access control testing, and tracing a random sample of data to source documents. Auditors determined that the data was sufficiently reliable for the purposes of this audit, with the exception of some data in the Department's Contract Management System. (See Chapter 4-A for additional information.)

Auditors identified other less significant issues that were communicated to Department management separately in writing.

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# Detailed Results

## Chapter 1

### ***The Department Should Implement Controls to Verify the Accuracy, Completeness, and Timeliness of the Program Fees It Collects***

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The Department of Information Resources (Department) reported collecting approximately \$42.6 million in fees on purchases that customers made through its Information and Communications Technology Cooperative Contracts Program (Program) from September 2007 through February 2011. However, the Department did not reconcile the fees it collected to vendor sales reports to ensure the accuracy, completeness, and timeliness of those fees.

While the Department had policies and procedures designed to ensure the accuracy, completeness, and timeliness of the Program fees it collected, the Department did not follow those policies and procedures or perform any other reviews to reconcile the fees that vendors paid.

In addition, certain Department contract management practices have increased the risk that the Department cannot properly ensure that vendors comply with fee payment and reporting requirements for the Program.

#### Chapter 1-A

### **The Department Should Follow Its Policies and Procedures for Collecting Program Fees**

The Department established policies and procedures for collecting Program fees in May 2006. However, it did not follow those policies and procedures to ensure the accuracy, completeness, and timeliness of Program fees it collected from September 2007 through February 2011. Those policies and procedures defined processes that would enable the Department to verify the fees it collects. Specifically, if it followed those policies and procedures the Department could:

- Verify the accuracy, completeness, and timeliness of fees it collects from vendors.
- Properly monitor the receipt and amount of fees that it has collected from vendors or that vendors owe on current and expired contracts. Although the Department recorded its receipt of fees, it did not consistently ensure that its accounting records included information necessary to properly reconcile fees to the appropriate contracts (see Chapter 3-A for additional information).
- Ensure that vendors submit monthly vendor sales reports (which the Department uses to determine fees) in a timely manner.



### Vendor Sales Reports

Program contracts require vendors to electronically submit to the Department detailed monthly reports in the format the Department requires. These reports, referred to as vendor sales reports, show the dollar volume of any and all sales under the contract for the previous month, including the following information for each transaction:

- Sales for the period.
- Order fulfiller's company name (if applicable).
- Customer name.
- Invoice date.
- Invoice number.
- Product/service description.
- Quantity, unit price, and extended price.
- Customer purchase order number.

Source: The Department.

- Periodically verify the accuracy and completeness of vendor sales reports (see text box for additional information).

As of March 2011, the Department revised its policies and procedures and, with one exception, removed the policies and procedures for collecting fees it had established in May 2006. The Department retained the requirement to periodically verify the accuracy and completeness of the vendor sales reports.

By not reviewing to ensure the accuracy, completeness, and timeliness of the fees it collects, the Department is not able to ensure that vendors (1) comply with contract requirements and (2) provide reliable sales data that the Department uses to assess the fees that it sets.

The Department should ensure that the Program fee is not a factor in calculating the customer price.

Requirements in the Department's Program contracts with vendors describe the methodology for determining the customer price. The language in those requirements may include the fee as a component of the customer discount. If the fee is included as a part of the customer discount, the fee may be calculated as a percentage of the manufacturer's suggested retail price, which is higher than the customer price. If the fee is calculated as a percentage of the manufacturer's suggested retail price, customers may pay a higher amount in fees to vendors than vendors pay to the Department. The fee a vendor pays to the Department is based on the customer price.

Auditors were unable to determine whether customers were actually paying fees that exceeded the fees vendors were paying to the Department because the vendor sales reports did not capture information necessary to make that determination (see Chapter 1-B for additional information).

After auditors brought this matter to its attention, the Department reported that it had amended its Program contracts with vendors to remove the language that could result in the fee being assessed against the manufacturer's suggested retail price instead of the lower customer price.

### Recommendations

The Department should:

- Restore, revise, and comply with its previous policies and procedures to ensure that it verifies the accuracy, completeness, and timeliness of the Program fees it collects.

- Ensure that Program fees are not included in the customer discount so that the fees that customers pay vendors are equal to the fees that vendors pay the Department.

### Management's Response

*The Department agrees with the State Auditor's recommendations. The Department completed a comprehensive update of the Program's procedures in March 2011, and will conduct an annual review of all procedures in accordance with the recommendations of the Contract Advisory Team. The Department has segregated the administration of reporting and administrative fee payments to a newly dedicated full-time employee. This position will ensure that program fees paid by the vendors are equal to the fees the customers pay.*

**Responsible Party:** Director of ICT Cooperative Contracts

**Target Implementation Date:** October 31, 2011

Chapter 1-B

### **The Department Should Strengthen Its Contract Management Practices to Help Ensure That Program Vendors Comply with Fee-related Contract Requirements**

The Department has established certain contract management practices that hinder its ability to provide reasonable assurance that Program vendors have complied with contract requirements.

The Department should ensure that Program vendors submit monthly vendor sales reports in a timely manner.

The Department has a reasonable process to collect monthly vendor sales reports and notify the appropriate contract manager about vendors that did not submit those reports. However, it does not ensure that contract managers consistently follow up with vendors to ensure that they submit vendor sales reports. Auditors determined that, for 119 (92 percent) of 129 contracts tested with missing vendor sales reports, the Department did not have documentation to show that contract managers followed up with vendors.

In addition, a significant number of Program vendors have not consistently provided vendor sales reports as required by their contracts.

Table 1 shows the number of contracts for which vendors did not submit one or more required vendor sales reports during the applicable fiscal year.

Table 1

Number of Contracts for Which Vendors Did Not Submit at Least One Vendor Sales Report Fiscal Years 2008 Through 2011				
Category	Fiscal Year			
	2008	2009	2010	2011 <sup>a</sup>
Number of Contracts for Which Vendors Did Not Submit One or More Required Vendor Sales Reports	294	230	186	207
Total Number of Contracts	543	735	871	851
Percent of Total Contracts	54.1%	31.3%	21.4%	24.3%
<sup>a</sup> As of March 2011.				

Source: The Department.

When vendors do not submit monthly vendor sales reports in a timely manner, it prevents the Department from properly verifying the fees it collects from vendors.

Monthly vendor sales reports should capture key sales information.

Monthly vendor sales reports do not capture key sales information that would enable the Department to ensure that vendors give customers the correct discounts on their purchases. Specifically, vendor sales reports do not include:

- The manufacturer's suggested retail price.
- The customer discount specified in the vendor's contract.

Because monthly vendor sales reports do not capture this information, auditors were unable to determine whether customers paid higher fees to vendors than vendors paid to the Department (see Chapter 1-A for more information).

The Department should amend all Program contracts in a timely manner when it changes Program fees.

The Department reported that it had reduced the fee for all Program contracts in fiscal years 2010 and 2011. Specifically, the Department reduced the fee for fiscal year 2010 from 2.00 percent to 1.25 percent, and it reduced the fee for fiscal year 2011 from 1.25 percent to 0.50 percent. (See Chapter 2 for more information on how the fee is set.) However, as of March 2011, auditors identified a significant number of contracts for which the fee was still specified as either 1.25 percent or 2.00 percent (see Appendix 5 for additional information).

The Department reported that, when it decides to reduce fees, it first amends the contracts for the top 50 vendors by sales. It amends the remaining contracts as time allows throughout the year. In addition, the Department reported that, in some cases, it may not reduce the fee specified in a contract because the vendor will not pass the reduction on to the customer as an increase in the customer discount (see Chapter 2 for additional information on contract negotiations with vendors).

Not amending contracts to reflect fee reductions in a timely manner increases the risk that customers could pay excessive fees.

**The Department should include provisions in Program contracts that define the corrective actions it may take against vendors that do not comply with payment and reporting requirements.**

The standard terms and conditions in the Department's Program contracts with vendors do not include provisions for corrective actions or financial penalties the Department may impose against vendors that do not comply with fee payment requirements or reporting requirements.

The Department reported that it amends contract provisions for corrective actions only after it determines that a vendor had a history of non-compliance with reporting requirements during the contract year. The Department reported that, as part of its annual contract renewal process, it performs an annual review to determine whether a vendor submitted any vendor sales reports late. For the period from September 2007 through February 2011, the Department reported that it amended 30 contracts as a result of vendor non-compliance with reporting requirements.

By not including specific corrective actions in its Program contracts with vendors, the Department does not have the tools necessary to enforce vendor compliance with payment and reporting requirements.

**The Department should have policies and procedures to assess and collect financial penalties from Program vendors.**

For contracts the Department amended to include financial penalties and other corrective action measures, the Department does not have policies and procedures to assess and collect financial penalties when vendors did not comply with requirements. Without policies and procedures to assess and collect financial penalties, the Department cannot ensure that it collects and documents financial penalties as part of a vendor's contract performance history.

Certain Program contracts continue to report sales activity after the contract expiration date.

**Contract Survivability Provision**

Program contracts include the following provision to allow vendors to fulfill outstanding customer purchase orders after the contract expiration date:

Survival. All applicable [service agreements] that were entered [into] between the vendor and a customer under the terms and conditions of the contract shall survive the expiration or termination of the contract. All purchase orders issued and accepted by the vendor shall survive expiration and termination of the contract.

Source: The Department.

The Department allows expired contracts to continue under survival clauses (see text box for additional information). While it is reasonable for the Department to extend the life of a contract as a result of outstanding purchase orders against the contract, certain expired contracts have survived for extended lengths of time. Table 2 shows Program contracts that have been in effect for at least six years.

Table 2

Program Contracts in Effect for at Least Six Years					
Product/Service	Contract Start Date	Contract End Date	Last Date of Reported Activity <sup>a</sup>	Number of Years Active after Contract End Date	Total Years Contract Was Active
Hardware and Maintenance	August 2004	August 2009	April 2011	1.7	6.7
Information Technology Recovery Services	July 2003	July 2010	May 2011	0.8	7.8
Information Technology Recovery Services	December 2003	December 2010	May 2011	0.4	7.4
Software Contract	November 2003	November 2007	October 2010	2.9	6.9
Computer Management Services	May 2002	May 2007	April 2011	3.9	8.9
Computer Management Services	May 2002	May 2007	May 2011	4.0	9.0
<sup>a</sup> Reported activity represents the most recent of either (1) fee payment activity by the vendor or (2) vendor submission of sales reports.					

Source: The Department.

The *State of Texas Contract Management Guide* recommends that state contracts, generally, should not exceed four years, including any renewal or extension periods.

**Recommendations**

The Department should:

- Develop, document, and implement policies and procedures that:
  - Establish processes for contract managers to identify and collect past-due monthly vendor sales reports.

- Ensure that the Department amends Program contracts to reflect fee changes in a timely manner.
- Establish processes to assess and collect penalties when vendors submit Program fees late.
- Review and revise the format of its vendor sales report to require Program vendors to report (1) the manufacturer's suggested retail price for products and services at the time of purchase and (2) the customer discount applied to the purchase.
- Ensure that its Program contracts include provisions that define (1) the corrective actions and (2) late fee penalties the Department may assess for non-compliance with payment and reporting requirements.
- Revise survival provisions in Program contracts to include provisions that establish a time limit for how long after the contract expiration date a vendor has to fulfill a customer order.

#### **Management's Response**

*The Department agrees with the State Auditor's recommendations. The Department has segregated the administration of reporting and administrative fee payments to a newly dedicated full-time employee. The Department will implement procedures to amend Program contracts to reflect fee changes in a timely manner. The Department will work with vendors to develop a process to report manufacturer's suggested retail price for products and services to include customer discounts applied to the purchase. The Department agrees that it must ensure that its Program contracts include provisions that define the corrective actions and late fee performance remedies that the Department may assess for non-compliance with payment and reporting requirements, and is amending the contract template to do so. The Department will review contract templates on a product and service basis and revise the survival provisions in Program contracts to establish a recommended time limit for how long after the contract expiration date a vendor has to fulfill a customer order.*

***Responsible Party:*** Director of ICT Cooperative Contracts

***Target Implementation Date:*** December 31, 2011

## The Department Should Ensure That Program Fees Reflect Its Costs

The fee the Department sets in its Program contracts should reflect the Department's actual costs for operating the Program. However, for some contracts the Department set a fee based on management's judgment of whether a fee would meet its proposed budget goals. For other contracts, the Department based the fee on its contract negotiations with vendors, through which the Department may reduce the fee to obtain a higher customer discount.

### Fee Review Process

The Department's annual review of the fee determines whether projected fee revenue will offset projected Program costs. The Department's review includes:

- Preparing the annual operating budget for the Program, which includes the direct and indirect costs for the Program.
- Projecting Program sales for the applicable fiscal year.

Source: The Department.

While the Department reviewed its fees annually to determine whether the fees would meet its budget goals (see text box), its review process was based on unverified, vendor-reported sales data. In addition, the Department (1) included non-Program contracts in its sales projections and (2) did not have certain documentation for its sales projections that was necessary for auditors to assess the reasonableness of the Program's sales projections and budget. The use of unverified and incomplete data hinders the Department's ability to ensure the reasonableness and reliability of its sales projections, which affects the reliability of its reviews of the fees.

The fee should reflect the costs associated with the Department's administration of the Program, as statutorily required.

Texas Government Code, Section 2157.068, allows the Department to charge a reasonable fee to Program customers in an amount that is sufficient to recover costs associated with its administration of the Program. The fees in Program contracts that the Department procured from September 2007 through fiscal year 2011 were based on management's judgment. Specifically:

- For fiscal years 2008 and 2009, the Department set a fee of 2.00 percent in its Program contracts. The General Appropriations Acts (80th and 81st Legislatures) stated that the maximum amount for all administrative costs to be applied to state agency receipts and local government receipts shall not exceed 2.00 percent per receipt. The Department reported that it set the fee at the maximum because it did not have information necessary to properly evaluate the Program's sales performance.
- For fiscal years 2010 and 2011, the Department set Program fees at 1.25 percent and 0.50 percent, respectively.

The Department reviewed the fees to determine whether the fees would meet its Program budget goals. However, it did not develop the fees using cost data for the operation of the Program.

The Department should identify the Program costs for performing key contract management activities, including:

- Planning.
- Procurement.
- Contract formation.
- Rate/price establishment.
- Contract administration.

A 2004 State Auditor's Office report recommended that the Department should ensure that the fees reflect the Department's cost of operating the Program.<sup>1</sup>

By identifying the actual cost of performing certain Program activities, the Department can make a more informed decision on using Program resources. For example, auditors determined that, from September 2007 through February 2010, 264 (30.9 percent) of the 854 contracts procured by the Department had no reported sales (see Appendix 6 for additional information). If the Department had information on the cost of various contract management activities it performs for the Program, it could make cost-effective decisions on the number of contracts that the Program should procure and manage.

The Department used the fee as a contract negotiation tool for establishing customer discounts for some contracts.

The Department reported that it negotiated reductions in the fee for some Program contracts in exchange for a higher customer discount. However, the fee should be set so that the Department can recover its costs for managing the Program. Reducing a fee after it has been set increases the risk that the Department may collect less than is needed to recover its costs.

In addition, making any future fee changes would require the Department to renegotiate customer discounts. However, the Department's inconsistency in promptly and successfully amending current contracts for fee reductions (see Chapter 1-B for additional information) increases the risk that (1) contracts may not be amended in a timely manner for future fee changes or (2) contracts may not be amended at all. This could result in customers paying inappropriate fees on Program purchases.

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<sup>1</sup> See *An Audit Report on Two Cost-Recovery Programs at the Department of Information Resources* (State Auditor's Office Report 05-001, September 2004).



**Texas Government Code,  
Section 2157.068(b)**

The Department shall negotiate with vendors to attempt to obtain a favorable price for all of state government on licenses for commodity items, based on the aggregate volume of purchases expected to be made by the state. The terms and conditions of a license agreement between a vendor and the Department under this section may not be less favorable to the State than the terms of similar license agreements between the vendor and retail distributors.

The Department asserted that it must consider the fee in its negotiations with vendors to establish customer discounts because the customer discount may not be competitive with the market when the fee is considered as an additional cost to the customer (see Chapter 1-A for additional information). However, the customer discount that the Department sets in Program contracts should be driven by the volume purchasing power of the State, as required by Texas Government Code, Section 2157.068 (b) (see text box for additional information).

**Subsequent Event**

Senate Bill 1 (82nd Legislature, First Called Session) amended Texas Government Code, Section 2157.068 (b), to state that, effective September 28, 2011, Program contracts will be negotiated according to best value (see Appendix 3 for additional information).

The Department set a variety of fees in Program contracts.

As a result of the Department's contract negotiations with vendors and its inconsistency in amending contracts in a timely manner (see Chapter 1-B for additional information). Program contracts have a variety of fees that range from 0.00 percent to 2.00 percent (see Appendix 5 for additional information). In some instances, contracts for the same product or service have different fees.

The variety of fees the Department sets in Program contracts hinders its ability to ensure that the fee it collects are reasonably sufficient to recover Program costs.

The Department should ensure non-Program contracts are not included in its annual review of the Program fee.

**Texas Government Code,  
Section 2170**

The Department is responsible for obtaining telecommunication services serving the state government. The Department may own, lease, or lease-purchase as statutorily allowed any or all of the facilities or equipment necessary to provide telecommunications services.

The Department incorrectly included sales projections in its annual Program fee review for fiscal years 2010 and 2011 that were related to contracts procured to support telecommunication services provided under Texas Government Code, Section 2170 (see text box). Contracts procured under that statute are not considered Program contracts. Specifically:

- A new procurement, which was a telecommunication contract for internet subscription services, that was yet to be awarded was included in the Department's fiscal year 2011 sales projections.

The sales estimate for the anticipated contract was projected to result in approximately \$25,000 in fees. However, the estimates were based on a fee rate of 0.50 percent. As of March 2011, the fee rate was reported as 4.00 percent.

- Two telecommunication contracts for interpreter services were included in the Department's fiscal year 2010 and 2011 sales projections. The combined fees expected to be collected from those two contracts were approximately \$69,000 and \$44,000 for the respective fiscal years. However, the estimates were based on fee rates of 1.25 percent for fiscal year 2010 and 0.50 percent for fiscal year 2011. As of March 2011, the fee rate for those contracts was reported as 7.00 percent. In addition, the Department also incorrectly deposited fees associated with those two contracts into the Program's account (see Chapter 3-A for additional information).

The inclusion of non-Program related sales projections increases the risk that the Department's assessment of the fee will be inaccurate and unreliable.

The Department did not maintain certain documentation for its sales projections and Program budget.

Auditors reviewed the Program sales projections the Department prepared for fiscal years 2008 through 2011 to attempt to determine the reasonableness of those projections. The Department did not have certain documentation necessary to properly assess the reasonableness of the projections.

Specifically:

**Program Sales Projections Methods**

The Department defined the following methodologies to project sales for Program contracts:

- Based on sales trend.
- Minimum guarantee.
- Estimate from contract staff.
- Based on average of sales.
- Year-to-date sales.
- Contract no longer active.

Source: The Department.

- The Department did not have certain documentation for its fiscal year 2008 sales projection. Specifically:
  - The Department did not consistently identify its methodology for projecting sales for each contract. The Department defined six methodologies that can be considered for projecting sales for a contract (see text box for additional information).
  - The Department did not have documentation for the total number of information technology staffing services contracts that it considered in its fiscal year 2008 projection.
- The Department did not have documentation for its sales projection for fiscal year 2009.
- For the fiscal year 2010 sales projection, the Department did not have documentation showing the basis for a \$10.0 million sales estimate that the Department used for a telecommunication services contract that was in the procurement process when the Department did the sales projection. The fiscal year 2011 sales projections showed that, after that contract was procured, it had approximately \$48.7 million in sales through May 2010.
- For the fiscal year 2011 sales projection, the Department did not identify its methodology for projecting sales for each contract.

In addition, the Department should document how it determines the sales growth rate it uses in its sales projections. The Department obtained a

recommendation for a sales growth rate from its information technology research and advisory firm (firm), as required by its policies and procedures. However, the sales growth rates it used in its sales projections differed from the rates the firm recommended.

The Department also should consistently document the indirect cost allocations it uses in its budget projections. While auditors determined that the Department's methodology for allocating indirect costs was reasonable, the supporting documentation the Department provided supported only the indirect costs shown on its fiscal year 2011 operating budget.

## Recommendations

The Department should:

- Develop, document, and implement a methodology for establishing the Program fee that includes identifying the actual costs for performing key Program contract management activities, including planning, procurement, contract formation, rate/price establishment, and contract administration.
- Discontinue using the Program fee as tool to negotiate higher customer discounts with vendors.
- Establish a standard fee for Program contracts. Because of the variety of products and services offered through the Program, the Department should consider establishing standard fees by product and service type.
- Ensure that it does not include non-Program contracts in its annual review of Program sales projections.
- Maintain complete records of the documentation it uses to develop sales projections and the Program budget.

## Management's Response

*The Department agrees with the State Auditor's recommendations. Although the Department does consider Program costs and other costs that need to be funded by Program fees as part of the development of the annual operating budget, the Department agrees that improvements can be made. The Department began taking action to improve its fee setting process during fiscal year 2011 with the establishment of a cost accounting function within the Finance division. This function is now responsible for ensuring that Department fees are set at levels necessary to recover the costs incurred to deliver services.*

*The Department will incorporate identification of the cost of key contract management activities and other costs associated with providing legislatively*

*mandated services as part of the fee setting methodology. The Department will ensure that only Program contracts are included in projections and will maintain adequate documentation to support the fee establishment process. The Department has also established standard fees based on product and service type. The Department will discontinue using the Program fees as a tool to negotiate higher discounts with vendors when amending contracts.*

***Responsible Parties:*** Chief Financial Officer and Director of ICT  
Cooperative Contracts

***Target Implementation Date:*** December 31, 2011

## ***The Department's Management and Use of Program Fees***

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The Department has accounting controls to ensure that it properly processes and documents the Program fees it collects. However, it should strengthen those processes by ensuring that it documents information necessary to

### **The Clearing Fund**

The Office of the Comptroller of Public Accounts has established in the State Treasury a Clearing Fund Account (Clearing Fund) that the Department uses for administration of cost-recovery activities related to the Program. (See Appendix 2 for more information.)

Source: General Appropriations Acts (80th and 81st Legislatures).

reconcile the Program fees it collects to Program contracts and that non-Program fees are not deposited into the Clearing Fund Account (see text box).

In addition, the Department should ensure that it (1) complies with certain financial reporting requirements regarding the Program and the fees, (2) maintains accurate and complete documentation on the transfer of funds from the Program fund account, and (3) avoids using Program fees to secure procurement of Program contracts.

Auditors also identified opportunities for the Department to clarify and update provisions in the General Appropriations Act regarding the Program.

### Chapter 3-A

## **The Department Has Accounting Controls to Process and Document Program Fees and Expenditures; However, It Should Strengthen Certain Processes for Documenting Transactions, Depositing Fees, and Reconciling Transactions**

From September 2007 through February 2011, the Department properly processed Program fees and expenditures. Specifically:

- The Department properly processed 59 (98 percent) of the 60 Program fee receipts tested. The 60 fee receipts tested totaled \$1,086,168.
- The Department properly processed all 60 expenditures of Program fees tested. The 60 expenditures totaled \$269,094.

For the receipts and expenditures tested, the Department (1) accurately recorded the transactions in its accounting system, (2) ensured that management properly reviewed and approved the transactions, and (3) supported the transactions with appropriate documentation.

The Department should include necessary identifying contract information in its fee collection documentation.

The Department did not consistently record key reference information in its accounting system that is necessary to correctly reconcile Program fees collected with the Program contracts. Specifically:

- The Department did not record the contract number for 19 (32 percent) of the 60 fee receipts tested. Those 19 fee receipts totaled \$431,746.

- The Department did not record the reporting period for 17 (28 percent) of the 60 fee receipts tested. Those 17 fee receipts totaled \$242,147.

The Department's Program contracts with vendors require vendors to provide the contract number on all remittances of fees to the Department. Not consistently recording the contract and reporting period associated with Program fees it collects prevents the Department from ensuring that it reconciles the fees collected to the correct contract and reporting period.

The Department should ensure that fees collected from non-Program contracts are not deposited into the Clearing Fund.

#### The Telecommunications Revolving Account

The Telecommunications Revolving Account is the account that the Department uses to meet the statutory provisions for providing the telecommunication services defined by Texas Government Code, Chapter 2170.

Source: General Appropriations Acts (80th and 81st Legislatures).

From November 2008 through March 2011, the Department reported depositing approximately \$1.3 million in fees it collected on two telecommunication contracts for interpreter services into the Clearing Fund. The fees collected for telecommunication contracts should be deposited into the Department's Telecommunications Revolving Account (see text box). Depositing these non-Program fees into the Clearing Fund overstates the fund balance of the Clearing Fund and increases the risk that the Telecommunications Revolving Account will not have sufficient funding to pay for its applicable costs.

The Department should consistently reconcile its internal accounting system with the Uniform Statewide Accounting System on a monthly basis.

The Department periodically reconciled its internal accounting system with the Uniform Statewide Accounting System (USAS) and corrected all identified discrepancies. However, the Department should consistently perform those reconciliations on a monthly basis as required by its policies and procedures. The Department did not perform reconciliations in a timely manner for 21 (50 percent) of 42 months tested. For example, it performed the reconciliations for November 2010 through March 2011 when it completed the reconciliation for March 2011. By not performing reconciliations in a timely manner, the Department is at increased risk of providing inaccurate or incomplete financial information to decision makers.

### Recommendations

The Department should:

- Record in its accounting system both the contract number and reporting period for all Program fees it collects.
- Ensure that the fees deposited into the Clearing Fund are only for Program contracts.

- Ensure that the Telecommunications Revolving Account recovers the funds that were incorrectly deposited into the Clearing Fund.
- Consistently perform monthly reconciliations of its accounting system with USAS.

### **Management's Response**

*The Department agrees with the State Auditor's recommendations. As reported by the State Auditor, on September 1, 2011 the Department became the first State agency to implement the new Centralized Accounting and Payroll/Personnel System (CAPPS). The implementation of this new system will significantly improve the Department's accounting and financial reporting functions. The Department will capture Program vendor contract numbers and reporting periods for all Program fees collected. The Department is also implementing a financial compliance and reporting calendar system application to ensure that all reconciliations are performed timely.*

*The Department transferred the \$1.3 million, identified by the State Auditor as being incorrectly deposited into the Clearing Fund, to the Telecommunications Revolving Account on September 15, 2011.*

***Responsible Party:*** Chief Financial Officer

***Target Implementation Date:*** December 31, 2011

## The Department Should Comply with Certain Financial Reporting Requirements for the Program

The Department should improve its processes for reporting certain Program information. Specifically:

- The Department should ensure that its annual encumbrance report accurately specifies its outstanding financial obligations. The Department's annual encumbrance reports for fiscal years 2008 through 2010 overstated encumbrances for the Program. Table 4 shows the amounts by which the Department overstated Program encumbrances in its encumbrance reports at the end of each fiscal year.

Table 4

Amounts by Which the Department Overstated Program Encumbrances Fiscal Years 2008 Through 2010 (In Millions)			
Fiscal Year	Reported Encumbrance Amount	Actual Encumbrance Amount	Overstated Encumbrance Amount
2008	\$ 6.6	\$1.2	\$ 5.4
2009	\$11.4	\$2.4	\$ 9.0
2010	\$14.6	\$1.4	\$13.2

Source: The Department.

The Office of the Comptroller of Public Accounts' Accounting Policy Statement 018 requires state agencies and higher education institutions to provide an annual binding encumbrance report on outstanding obligated funds for each appropriation year. For fiscal years 2008 through 2010, the Department included unobligated funds for the Program on its annual encumbrance reports.

- The Department should comply with reporting requirements in the General Appropriations Act. The Department did not have documentation to show that it complied with certain reporting requirements in the General Appropriations Acts (80th and 81st Legislatures). Specifically, the General Appropriations Acts required the Department to report the following in its annual financial report:
  - The costs avoided and/or savings obtained through Program activities.
  - A list of agencies and units of local government that the Program served.

Auditors also identified concerns with the specific language in the General Appropriations Acts (80th and 81st Legislatures) regarding this reporting



requirement and certain other requirements with which the Department must comply (see Chapter 3-F for additional information).

- The Department should report changes in Program fees to the Legislative Budget Board and the Office of the Governor. While the Department reviewed the Program fees annually (see Chapter 2 for additional information), for fiscal year 2010, it did not report the Program fee reduction from 2.00 percent to 1.25 percent in its budget requests to the Legislative Budget Board and the Office of the Governor. Texas Government Code, Section 316.045, requires each state agency that sets a fee to cover administrative costs to:
  - Review the amounts charged as fees on a biennial basis.
  - Perform the review prior to the beginning of each state fiscal biennium and include its recommendations based on that review in its budget request to the Legislative Budget Board and the Budget Division of the Office of the Governor.

If an agency determines that fees are set at a level that exceeds the administrative costs of the agency as of the date of the review, the agency shall reduce the amount of the affected fees to the appropriate level and is required to charge the reduced fees during the subsequent biennium.

If the Department does not report accurate and complete information or comply with reporting requirements, there is an increased risk that decision makers will not have reliable information that is necessary to effectively manage and evaluate the Program.

## Recommendations

The Department should:

- Include on its annual encumbrance report only actual financial obligations, in accordance with the Office of the Comptroller of Public Accounts' requirements.
- Comply with reporting requirements in Texas Government Code, Section 316.045, and the General Appropriations Act.

## Management's Response

*The Department agrees with the State Auditor's recommendations. The Department previously recorded all fund balances as encumbered due to its interpretation of the General Appropriations Act which previously appropriated all unexpended balances to the Department. The Department will now record only actual encumbrances on its annual encumbrance report.*

*As stated by the State Auditor, the Department does review program fees annually. The Department will ensure that it complies with the reporting requirements as described in Texas Government Code, Section 316.045, and the General Appropriations Act.*

**Responsible Party:** Chief Financial Officer

**Target Implementation Date:** December 31, 2011

Chapter 3-C

### **The Department Should Accurately Document the Program Fees It Transfers from the Clearing Fund**

The Department should accurately and completely document transfers from the Clearing Fund.

From September 2007 through February 2011, the Department transferred approximately \$10.7 million from the Clearing Fund to pay for the Program's share of indirect costs. However, the Department's records did not have complete and accurate information regarding the transfers the Department made out of the Clearing Fund. Specifically:

- The Department did not have documentation for 112 (34 percent) of the 326 transfers recorded in USAS. Those 112 transfers totaled approximately \$1.2 million.
- The Department's records showed 11 transactions that totaled approximately \$4.0 million that were not recorded in USAS. A review of these transactions determined that the Department:
  - Recorded seven transfers (totaling approximately \$3.4 million) in USAS using a transaction code that differed from the transaction code the Department had documented in its records.
  - Documented four transactions incorrectly in its records. The four transactions totaled approximately \$600,000.

Inaccurate and incomplete transfer documentation hinders the Department's ability to properly track and account for the use of Program fees.

The Department should ensure that temporary transfers from the Program to other cost-recovery programs are consistently reimbursed in a timely manner.

Auditors identified five temporary transfers totaling approximately \$3.6 million from the Clearing Fund to the State Data Center accounts. Three (60 percent) of the five transfers identified had not been reimbursed as of May 2011. Specifically:

- The Department made two transfers totaling \$3.0 million from the Clearing Fund to State Data Center accounts in fiscal year 2010. The Clearing Fund was subsequently reimbursed the full amount within 30 days.
- The Department made three transfers totaling \$590,000 to State Data Center accounts during fiscal year 2009. The Department reported that those amounts should have been reimbursed by the State Data Center accounts. The Clearing Fund had not been reimbursed.

If the Department does not ensure that temporary transfers from the Clearing Fund are reimbursed in a timely manner, the Department risks not having sufficient funds to pay Program operating costs.

### Recommendations

The Department should:

- Maintain accurate and complete documentation of its transfer transactions.
- Develop, document, and implement policies and procedures to ensure that temporary transfers from the Clearing Fund to other Department fund accounts are reimbursed in a timely manner.

### Management's Response

*The Department agrees with the State Auditor's recommendations. The Department will develop procedures to ensure that adequate documentation is maintained for all transfers. The Department's Chief Accounting Officer will review all transfers on a regular basis to ensure that temporary transfers from the Clearing Fund are reimbursed on a timely basis. In addition, the Department plans to transfer \$590,000 from the State Technology Account to the Clearing Fund by September 30, 2011, to reimburse the Clearing Fund for the unpaid temporary transfers identified by the State Auditor.*

**Responsible Party:** Chief Financial Officer

**Target Implementation Date:** December 31, 2011

## The Department Used Program Fees to Secure Procurement of a Program contract

### Use of Program Fees

From September 2007 through April 2011, the Department spent approximately \$20.3 million of the Program fees it collected. The Department spent portions of that amount on professional services fees related to the state data center projects and Texas.gov (formerly TexasOnline). Specifically:

- The Department spent approximately \$4.8 million on professional services fees related to state data center projects.
- The Department spent approximately \$1.0 million on professional services fees related to Texas.gov (formerly TexasOnline).

Source: The Department.

In fiscal year 2010, the Department used \$5.0 million of Program fees to secure procurement of the security network services Program contract (see text box for additional information on the use of Program fees). A state agency later reimbursed the Department \$3.8 million of that amount, but the Department paid for the remaining \$1.2 million with Program fees. The Department's use of Program fees to procure a Program contract and pay for products and services on customers' behalf is a practice that differs from how the other Program contracts are procured. For other Program contracts, the Department procures the contract and customers then pay vendors for (1) the products or services they receive through the contract and (2) fees that allow the Department to recover its costs. However, the manner in which the \$5.0 million contract for security network services was procured did not allow the Department to fully recover its costs.

### Recommendation

The Department should ensure that it does not use Program fees to secure the procurement of Program contracts.

### Management's Response

*The Department agrees with the State Auditor's recommendation. The Department will ensure that any costs associated with procuring State enterprise solutions are fully reimbursed by participating agencies so that Program fees are not used to secure the procurement of Program contracts.*

**Responsible Party:** Chief Financial Officer

**Target Implementation Date:** On-going

## The Department Should Seek Clarification and Updating of Provisions in the General Appropriations Act That Describe the Clearing Fund

The General Appropriations Acts (80th and 81st Legislatures) included certain provisions regarding the Clearing Fund that require clarification and updating. Specifically:

- The Department should seek clarification on how it receives Program fees. The General Appropriations Act requirements stated the following:

[The Clearing Fund shall be used]...To pay salaries, wages, and other costs directly attributed to the services provided to state agencies and units of local government for which the department receives payment from those agencies and governmental units.

While the Department received Program fees from state agencies and local governments during fiscal years 2008, 2009, and 2010, it also received fees from vendors. As of fiscal year 2011, the Department reported that all Program customers pay fees to vendors and vendors then pay fees to the Department.

- The Department should seek an increase in the maximum account balance that it carries forward each fiscal year. The General Appropriations Act requirements stated the following:

The balance of the account [Clearing Fund] at the end of the fiscal year shall not exceed more than 10 percent of the total revenue processed through the account in the prior fiscal year.

The Department did not comply with that requirement for fiscal years 2008, 2009, and 2010 because the carry forward threshold, as it was defined, would not have provided the Department with sufficient funding to operate the Program at the start of the next fiscal year. Table 5 on the next page shows the amounts the Department carried forward and the maximum amounts it could have carried forward according to the General Appropriations Act.

Table 5

Clearing Fund Amounts the Department Carried Forward Fiscal Years 2008 Through 2010 (In Millions)			
Fiscal Year	Prior Fiscal Year Total Revenue	Maximum Amount the Department Could Carry Forward	Actual Amount the Department Carried Forward
2008	\$30.3	\$3.0	\$ 6.6
2009	\$33.0	\$3.3	\$11.5
2010	\$19.1	\$1.9	\$14.7

Source: The Department.

Instead of carrying forward a balance of 10 percent of total revenue, the Department carried forward the full balance of the Clearing Fund at the end of the year. The Department reported that it interpreted the threshold to be based on total Program sales instead of total Program revenue.

- The Department should seek a correction in the name of the annual financial report it prepares. The General Appropriations Act stated the following:

As part of its Comprehensive Annual Financial Report, showing the use of appropriated funds, the Department of Information Resources shall include information showing the costs avoided and/or savings obtained through its cooperative activities and a list of the agencies or units of local government for which the clearing fund account is used.

The Department does not prepare a “comprehensive annual financial report.” Instead, it prepares an “annual financial report” that it submits to the Office of the Comptroller of Public Accounts.

## Recommendations

The Department should coordinate with the Legislative Budget Board during the 83rd legislative session to clarify and update General Appropriations Act Clearing Fund requirements to:

- State that the Department receives Program fees from vendors.
- Increase the amount of the total revenue that the Department can carry forward each year to an amount that will provide it with sufficient funding to maintain the Program at the start of a new fiscal year.
- Correctly identify the annual financial report that the Department prepares.

## Management's Response

*The Department agrees with the State Auditor's recommendation. The Department will work with the Legislative Budget Board to clarify and update the General Appropriations Act sections identified by the State Auditor.*

***Responsible Party:*** Chief Financial Officer

***Target Implementation Date:*** On-Going

## **The Department Should Strengthen Certain Information Technology Controls**

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The Department should correct weaknesses in certain information technology controls to improve the accuracy and security of data and systems. Auditors examined two information systems that support the Department's collection and management of Program fees:

- The Contract Management System, which is the information system the Department uses as its contract repository to manage and monitor contract information and monthly vendor sales reports.
- The CDI Accounting System, which is the Department's internal accounting system.

Chapter 4-A

### **The Department Should Correct Certain Weaknesses in Its Contract Management System**

#### **Contract Management System**

The Contract Management System includes:

- Salesforce, a Web-based application maintained in a cloud computing environment. The Department uses Salesforce to manage and report information on each Program contract.
- Data Warehouse, a database application that manages a database of contract information obtained from Salesforce and vendor sales reports.

Source: The Department.

Application controls over the Department's Contract Management System include edit controls to help ensure that required contract information is entered into that system; however, those edit controls do not ensure that the system has complete, accurate, and timely contract information (see text box for additional information about the Contract Management System). There are weaknesses in (1) how that system maintains records of Program fees, (2) how staff enter contract information and monthly vendor sales reports into that system, and (3) controls over access to that system.

**The Contract Management System should maintain the current and prior fees for each Program contract.**

The Contract Management System can record only one fee for each Program contract. However, Program contracts may have more than one fee specified in the contract, and the fee for a given contract can change during the life of that contract (see Chapter 2 for additional information). In addition, Data Warehouse, another component of the Contract Management System, does not have the ability to track fee changes by effective dates. While it can provide the current fee for a Program contract, it cannot provide historical information on the fees previously set for that contract.

If the Contract Management System does not maintain complete records of the fees specified in a vendor's contract, the Department cannot rely on its ability to recalculate fees for reconciliation purposes.



The Department should ensure that data manually entered into the Contract Management System and data uploaded to the Contract Management System from monthly vendor sales reports is accurate and complete.

The Department does not have a secondary review process to ensure that data entered into the Contract Management System is accurate and complete. The accuracy of data in the Contract Management System relies on review of the data as it is entered into that system. Specifically:

- The Department does not review for the accuracy of the contract information that contract managers manually enter through Salesforce. While Salesforce has edit checks to ensure that users enter all required information, there is no control to identify errors in data entry. Auditors identified the following errors in contract records in the Contract Management System:
  - Thirteen Program contracts were incorrectly classified as telecommunication contracts.
  - The contract effective start date was incorrect for two Program contracts tested.
- Sales data did not consistently upload correctly. Data Warehouse uploaded correctly into the Contract Management System 53 (88 percent) of the 60 monthly vendor sales reports that auditors tested. For the seven monthly vendor sales reports that were not uploaded correctly, auditors identified the following errors:
  - For three monthly vendor sales reports, the reporting periods differed from the reporting periods recorded in Data Warehouse.
  - For three sales reports, the calculation of the fee was incorrect because of the way the fee was defined in Data Warehouse.
  - For one sales report, not all of the reported transactions were uploaded.

The absence of a secondary review of data entered into the Contract Management System increases the risk the Department may report inaccurate or incomplete information to decision makers.

The Department should record amendments to contract fees in the Contract Management System in a timely manner.

Fee reductions for 21 (57 percent) of 37 contract records tested were updated in the Contract Management System in a timely manner. However, auditors identified the following for the 16 contract records for which fee changes were not updated in a timely manner:

- For 10 contracts, fees were updated in the Contract Management System prior to the effective date of the fee reduction contract amendments. By changing the fee prior to the effective date of contract amendments, the

Department may incorrectly calculate the fees owed for the period before the effective date.

- For five contracts, fees were updated in the Contract Management System more than 30 days after the effective date of the fee reduction contract amendments.
- One contract had an amendment to reduce the fee that was effective in January 2011. As of May 2011, the Department had not updated the fee in the Contract Management System.

If the Department does not update fees in the Contract Management System in a timely manner, there is an increased risk that it will provide decision makers inaccurate information on Program fees.

The Department should correct access control weaknesses in the Contract Management System.

Auditors identified weaknesses in access to the Contract Management System. Specifically:

- Two user accounts for the Salesforce application that were assigned to former staff were still active.
- Non-Program staff had access to add, change, and delete Program information in Salesforce.
- Data Warehouse had an administrative account password that was more than three years old.
- Four current staff shared a user account that had the ability to update Data Warehouse. Sharing an account prevents the Department from maintaining an audit trail of the specific staff who add, change, or delete information.
- Eleven active user accounts for Data Warehouse were not assigned to specific staff. Seven of those accounts had administrative access rights.

The access issues increase the risk of alteration or deletion of data, which could affect the Department's ability to ensure the integrity of the data.

## Recommendations

The Department should:

- Ensure that the Contract Management System can record both current and prior fees for each Program contract.
- Develop, document, and implement policies and procedures that:

- Establish and implement a quality assurance process, including a review process, to verify that all data entered into the Contract Management system is accurate and complete.
- Establish and implement a process to ensure that amended Program fees are updated in the Contract Management System in a timely manner.
- Establish and implement processes to ensure that:
  - The Department deactivates and removes all former employees' access to the Contract Management System in a timely manner.
  - Only Program staff can add, change, and delete Program-related information in Data Warehouse.
  - The Department reviews, and changes as necessary, the user access rights of non-Program staff.
  - The Department changes the password to the administrative account in Data Warehouse on a periodic basis.
  - Each employee is assigned an individual user account.
  - All active user accounts are assigned to specific staff.

### Management's Response

*The Department agrees with the State Auditor's recommendation. IT will work with the ICT Division to establish a process that can effectively capture and retain changes in unit price with the associated effective dates. ICT Division will establish a quality assurance and review process to verify that the data entered into the Contract Management System is accurate and complete and that program fees are updated in a timely manner.*

*Removing employees' access to the Contract Management System is a defined and documented process that has been in place since 2008 and is dependent upon receiving notification from HR when employees are separating. However, IT is in the process of implementing additional security controls within the office of the Information Security Officer ("ISO") to validate user lists against active user records gathered from HR for both contractors and employees. The new Security Control Matrix will also include new controls to verify that the overall level of permissions associated with a user are appropriate given the user's job function. This will be managed by the ISO and provide new governance over the defined IT procedures. This will be in place in September 2011.*

*IT production support staff must retain the ability to change data in the Data Warehouse. This level of permission is required due to the batch processing of vendor provided data that is gathered by spreadsheet and not as a result of a systemic front end process. Therefore the variability of data submitted by vendors is high and fluctuates from month to month. As a result the program procedures in place include a great deal of reconciliation and batch controls. The IT staff will exercise data removals or corrections when batch processing fails because a vendor report has invalid or duplicate data. The process itself provides an alert for failed processing to both program and IT staff so that the program staff is fully aware and able to make corrections before re-processing the failed batch load. The monthly load and reconciliation process, as exercised by the program staff, ensures that IT staff does not alter data outside the explicit expectations of the program staff.*

*IT production changes the Data Warehouse administrative account password at least once every 6 to 12 months. The password is changed immediately if there are any IT separations, and based on a 90 day rotation under normal circumstances. Password changes are recorded in a sealed/tamper proof envelope and stored in a “two key” safe at a separate facility.*

*Each employee is assigned an individual user account. In some cases a system or application account is created for unattended automated processes that required authentication to/from external systems. However, the new Security Control Matrix is being updated to reflect a new control to establish a list of all systems accounts that will be monitored via system log files for execution.*

**Responsible Party:** Information Security Officer/Director, ICT Cooperative Contracts

**Target Implementation Date:** November 2011

Chapter 4-B

## **The Department Should Strengthen Certain Control Weaknesses in Its CDI Accounting System**

The CDI Accounting System, which is the Department’s internal accounting system, had the necessary controls to ensure that financial transactions were complete, accurate, and authorized. However, auditors identified weaknesses in certain application and access controls associated with that system. The Department reported that, on September 1, 2011, it will implement a new accounting system that will correct those weaknesses.

Controls help ensure that financial transactions were complete, accurate, timely, and authorized.

The CDI Accounting System has controls to help ensure that financial transactions are complete, accurate, and authorized. The CDI Accounting System properly recorded:

- All 42 check transactions tested.
- All 60 expenditure items tested.

The CDI Accounting System is unable to generate reliable reports.

While the CDI Accounting System uses a reporting application to generate various financial reports, the Department reported that it relies on manual processes to add data to those reports to produce the desired financial reports. In addition, the Department reported that database limitations on the size of fields in certain tables prevent the CDI Accounting System from properly transferring data into a report format. The inability of the CDI Accounting System to create reliable system-generated reports increases the risk that the Department could provide decision makers with financial reports that may be inaccurate or incomplete.

The Department should strengthen access controls for the CDI Accounting System.

Auditors identified the following weaknesses in the CDI Accounting System's user access controls:

- Two user accounts assigned to former staff were still active.
- The CDI Accounting System does not have database security, and all users have unrestricted access to that system's database. However, the complex nature and antiquated programming of the system minimizes the risk that the data could be inappropriately accessed and modified. As of March 2011, 192 staff had access to the CDI Accounting System.

The access issues increase the risk of alteration or deletion of data, which could affect the reliability of financial data the CDI Accounting System generates.

## Recommendations

The Department should:

- Ensure that the new accounting system provides reliable, system-generated reports.
- Deactivate and remove CDI Accounting System user accounts associated with former staff.

- Limit access to the CDI Accounting System to only users who need access to perform their job duties.
- Develop, document, and implement policies and procedures for the new accounting system to ensure that:
  - The Department deactivates and removes user access of former staff in a timely manner.
  - The Department properly restricts users' access to the system's database.

### Management's Response

*The Department agrees with the State Auditor's recommendation. Former staff accounts are disabled in CDI (logically deleted) but cannot be physically deleted. This legacy system, with no market or vendor support for enhancements, requires that historical records reference the users that updated the records, even when the users are no longer employed by DIR. Physically deleting the accounts will create terminal processing errors. In addition, because timesheets are a function of CDI, all DIR employees have access so that monthly timecards can be processed. This is being moved into a different system effective Sept 1, 2011 so thereafter only accounting users will retain CDI access. CAPPS, the new accounting system, is hosted by CPA and DIR will not have the ability to add and remove user access, however Accounting and IT have been working very closely for two years to migrate to the new system to ensure new processes and procedures will work. Accounting will review reports generated from CAPPS to ensure that they are reliable.*

**Responsible Party:** Chief Financial Officer/Information Security Officer

**Target Implementation Date:** September 2011

# Appendices

Appendix 1

## **Objectives, Scope, and Methodology**

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### **Objectives**

The audit objectives were to determine whether the Department of Information Resources (Department):

- Sets the administrative fee for its Information and Communications Technology Cooperative Contracts Program (Program) at a reasonable amount sufficient to recover the costs of the Program and complies with state laws, rules, and Department policies and procedures related to the administrative fee.
- Accurately and completely records the Program's financial transactions in a timely manner and processes them in compliance with state laws, rules, and Department policies and procedures.
- Maintains proper accounting controls over the Program.

### **Scope**

The scope of this audit covered Program fees, transfers, and expenditures from September 2007 through February 2011 and the Department's processes for collecting, analyzing, reviewing, and determining the fees.

### **Methodology**

The audit methodology included reviewing the Department's methodology for setting fees for the Program, reviewing selected Program contracts and vendor sales reports, collecting information and documentation, performing selected tests and other procedures, analyzing and evaluating the results of tests, and interviewing Department management and staff.

The audit methodology also included collecting and analyzing financial records, contracts, fiscal year budgets and sales projections, and policies and procedures and reviewing samples of revenues, expenditures, transfers, and associated supporting documentation.

Auditors assessed the data reliability of the information used to manage the Program and the fees collected. That assessment included observing controls over data integrity in selected systems and databases, reviewing information about the data and the systems, performing access control testing, and tracing a random sample of data to source documents. Auditors determined that the

data was sufficiently reliable for the purposes of this audit, with the exception of some data in the Department's Contract Management System.

Information collected and reviewed included the following:

- Contracts between the Department and vendors that participate in the Program.
- Contract procurement documents.
- Monthly vendor sales reports.
- Contract information from the Contract Management System.
- Financial transactions from the Department's CDI Accounting System.
- Financial transactions from the Uniform Statewide Accounting System (USAS).
- Department interoffice memoranda and accounting records.
- Board meeting minutes and presentations.
- Budget forecasts.
- Sales projections.
- Department organizational charts.
- Department policies and procedures.
- Prior State Auditor's Office reports.

Procedures and tests conducted included the following:

- Interviewed Department management and staff.
- Verified and compared budget forecasts and sales projections.
- Tested a sample of revenues, expenditures, and transfers.
- Reviewed contracts between the Department and Program vendors.
- Reviewed monthly vendor sales reports.
- Reviewed Department contract management and financial management policies and procedures.

Criteria used included the following:

- Texas Government Code, Chapters 316, 2054, 2157, 2170, and 2262.



- General Appropriations Acts (80th and 81st Legislatures).
- Contracts between the Department and Program vendors.
- *State of Texas Contract Management Guide*, Office of the Comptroller of Public Accounts, Version 1.6.
- Office of the Comptroller of Public Accounts accounting policy statements.
- Department policies and procedures.

### Project Information

Audit fieldwork was conducted from March 2011 through July 2011. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The following members of the State Auditor’s staff performed the audit:

- Willie J. Hicks, MBA (Project Manager)
- Michael O. Clayton, CPA, CFE, CISA, CIDA (Assistant Project Manager)
- Erin Cromleigh, CGAP
- Joseph Curtis, CPA, CIA
- Melissa Dozier
- Joseph Mungai, CIA, CISA
- Ken Wade, CIA, CGAP
- Michael Yokie, CISA
- Charles P. Dunlap, Jr., CPA (Quality Control Reviewer)
- Nicole M. Guerrero, MBA, CIA, CGAP, CICA (Audit Manager)

## **Requirements from the General Appropriations Acts (80th and 81st Legislatures)**

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Below are excerpts from the General Appropriations Act (80th and 81st Legislatures) that describe the purpose of the Department of Information Resources (DIR) Clearing Fund Account.

### **Rider 3, page I-68, General Appropriations Act (81st Legislature)**

3. DIR Clearing Fund Account. The Comptroller shall establish in the state treasury the Department of Information Resources Clearing Fund Account for the administration of cost recovery activities pursuant to authority granted under Chapters 771, 791, 2054, 2055, and 2177, Government Code. The account shall be used:

- a. As a depository for funds received as payments from state agencies and units of local government for services provided;
- b. As a source of funds for the department to purchase, lease, or acquire in any other manner services, supplies, software products, and equipment necessary for carrying out the department's duties relating to services provided to state agencies and units of local government for which the department receives payment from state agencies and local governmental units; and
- c. To pay salaries, wages, and other costs directly attributable to the services provided to state agencies and units of local government for which the department receives payment from those agencies and governmental units. However, the maximum amount for all administrative costs to be applied to state agency receipts and local government receipts shall not exceed 2.0 percent per receipt. The Department of Information Resources shall report the amount of all administrative costs allocated to each agency and unit of local government annually to the Legislative Budget Board.

The balance of the account at the end of the fiscal year shall not exceed more than 10 percent of the total revenue processed through the account in the prior fiscal year. Included in the amounts appropriated above are all balances as of August 31, 2009 (estimated to be \$5,838,787), and all revenues accruing during the 2010-11 biennium (estimated to be \$6,005,701 in fiscal year 2010 and \$10,063,505 in fiscal year 2011 in Strategies A.1.1, Statewide Planning; A.1.2, Rule and Guideline Development;

A.1.3, Statewide Security; B.1.1, Contract Administration of IT Commodities and Services; B.2.3, Shared Services and/or Technology Centers; D.1.1, Central Administration; D.1.2, Information Resources; and D.1.3, Other Support Services) to the Department of Information Resources Clearing Fund Account. In addition to amounts identified herein and included above, all unexpended balances remaining as of August 31, 2009, and all revenue generated on or after September 1, 2009, are hereby appropriated for the same purposes.

As part of its Comprehensive Annual Financial Report showing the use of appropriated funds, the Department of Information Resources shall include information showing the costs avoided and/or savings obtained through its cooperative activities and a list of the agencies or units of local government for which the clearing fund account was used.

**Rider 3, page I-69, General Appropriations Act (80th Legislature)**

The language regarding the DIR Clearing Fund Account was the same language quoted above, with the exception of the following additional information:

The balance of the account at the end of the fiscal year shall not exceed more than 10 percent of the total revenue processed through the account in the prior fiscal year. Included in the amounts appropriated above are all balances as of August 31, 2007 (estimated to be \$1,726,948), and all revenues accruing during the 2008-09 biennium (estimated to be \$3,310,220 in 2008 and \$4,529,348 in 2009 in Strategy B.1.1, Contract Administration of IT Commodities and Services) to the Department of Information Resources Clearing Fund Account. In addition to amounts identified herein and included above, all unexpended balances remaining as of August 31, 2007, and all revenue generated on or after September 1, 2007, are hereby appropriated for the same purposes.

**Excerpts from Senate Bill 1 (82nd Legislature, First Called Session)**

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Below are excerpts from Senate Bill 1 (82nd Legislature, First Called Session), which amended Texas Government Code, Sections 2157.068 (b). The effective date of the amended statute is September 28, 2011.

Texas Government Code, Section 2157.068 (b)

(b) The department shall negotiate with vendors [~~to attempt~~] to obtain the best value for the state in the purchase of commodity items. The department may consider strategic sourcing and other methodologies to select the vendor offering the best value on [a favorable price for all of state government on licenses for] commodity items[, ~~based on the aggregate volume of purchases expected to be made by the state~~]. The terms and conditions of a license agreement between a vendor and the department under this section may not be less favorable to the state than the terms of similar license agreements between the vendor and retail distributors.

## Program Fees Collected from September 2007 Through February 2011

Table 6 presents the fees the Department of Information Resources (Department) reported collecting through its Information and Communications Technology Cooperative Contracts Program (Program) from September 2007 through February 2011.

Table 6

Program Fees the Department Reported Collecting September 2007 Through February 2011	
Fiscal Year	Fees Collected
2008	\$ 8,616,447
2009	11,763,526
2010	15,117,070
2011	7,085,571
Total	\$42,582,614

Source: The Department's CDI Accounting System.

## Program Fees from September 2007 Through March 2011

Table 7 presents the fees set in the Department of Information Resources' (Department) 860 Information and Communications Technology Cooperative Contracts Program (Program) contracts reported in the Department's Contract Management System as of March 2011.

Table 7

Fees for Program Contracts as of March 2011									
Product or Service	Fee (Percent of Purchase Price)								Totals
	0.00%	0.25%	0.35%	0.50%	0.75%	1.00%	1.25%	2.00%	
	Number of Contracts								
Comprehensive Web Development and Management Services				1			39		40
Computers		1	2	5		2	3	1	14
Computers - Desktop				1					1
Computers - Portable							2		2
Court Case Software							2		2
Data Storage							12	1	13
Deliverables-based IT				63	18				81
Digital Cameras								1	1
Disaster Recovery Services								1	1
Document Management Services					1				1
Emergency Preparedness Hardware and Related Services				4			2	7	13
Hardware				10			22	4	36
Instructor-led Training				7					7
IT Staffing Services				161		15			176
Managed Document Output Services					4				4
Managed Services - Computers					6			1	7
Mobile Digital Video							18		18
Network				1			3	4	8
Network Services							1		1

Fees for Program Contracts as of March 2011

Product or Service	Fee (Percent of Purchase Price)								Totals
	0.00%	0.25%	0.35%	0.50%	0.75%	1.00%	1.25%	2.00%	
	Number of Contracts								
Networking Equipment				17		13	15	22	67
Networking Products and Services				32		2	47	2	83
Office Machines		1							1
Printers							12	2	14
Projectors							1		1
Regulatory Software				2					2
Research Services							1		1
Ruggedized Computers						1	4		5
Security Services				10			7	1	18
Software	2			65		5	99	5	176
Surveillance Cameras				1			4	4	9
Technical Services				6	1	2	1	1	11
Technology-based Recording							1		1
Technology-based Training				8				4	12
Tele - Cable Modem Services				1					1
Tele - Interpreter Services				3					3
Tele - Local Telephone Services								1	1
Tele - Network Services								1	1
Tele - Paging Services							2		2
Tele - Satellite Services								1	1
Tele - Seat Management - Telecom					4				4
Tele - Telecommunication Equipment							1		1
Tele - Telephone Equipment				1					1
Tele - Video Services								1	1
Tele - Wireless/Cellular								4	4
Training				1				1	2

Fees for Program Contracts as of March 2011

Product or Service	Fee (Percent of Purchase Price)								Totals
	0.00%	0.25%	0.35%	0.50%	0.75%	1.00%	1.25%	2.00%	
	Number of Contracts								
Technology-based Recording Equipment, Software, and Services							1		1
Video Conferencing				1			9		10
<b>Totals</b>	<b>2</b>	<b>2</b>	<b>2</b>	<b>401</b>	<b>34</b>	<b>40</b>	<b>309</b>	<b>70</b>	<b>860</b>



## Summary of Program Contracts Procured from September 2007 Through February 2010 with No Reported Sales

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Table 8 summarizes contracts that the Department of Information Resources (Department) procured for its Information and Communications Technology Cooperative Contracts Program (Program) but for which no sales were reported during the term of the contract.

Table 8

Program Contracts With No Reported Sales September 2007 Through February 2010			
Fiscal Year in which the Department Procured the Contracts	Number of Contracts With No Reported Sales	Total Number of Contracts the Department Procured	Percent of Contracts With No Reported Sales
2008	72	184	39.1%
2009	109	276	39.5%
2010	83	394	21.1%
<b>Totals</b>	<b>264</b>	<b>854</b>	<b>30.9%</b>

Source: The Department's Contract Management System.

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