

GAO

Report to the Chairman, Democratic  
Caucus, House of Representatives

March 1989

# MASS TRANSIT GRANTS

## UMTA Needs to Improve Procurement Monitoring at Local Transit Authority





United States  
General Accounting Office  
Washington, D.C. 20548

Resources, Community, and  
Economic Development Division

B-221081.2

March 31, 1989

The Honorable William H. Gray III  
Chairman, Democratic Caucus  
House of Representatives

Dear Mr. Chairman:

This report responds to your request that we review the Urban Mass Transportation Administration's (UMTA) oversight of the Southeastern Pennsylvania Transportation Authority's (SEPTA) compliance with federal procurement requirements. Because of your concern with SEPTA's management practices and allegations that it was awarding contracts unnecessarily, you also asked UMTA to evaluate SEPTA's procurement operations. In discussions with your office, we agreed to (1) summarize the results of an UMTA-funded review of SEPTA's compliance with federal procurement requirements conducted by JRL Associates, Inc. (JRL), an independent consulting firm, and (2) evaluate the adequacy of UMTA's oversight of SEPTA's procurement system.

## Results in Brief

In its November 1988 report, JRL identified major problems in SEPTA's procurement system and concluded that SEPTA was not in compliance with UMTA procurement requirements.<sup>1</sup> SEPTA generally agreed with JRL's findings and has established a task force to substantially correct the deficiencies in its procurement system by May 1989. UMTA plans to work with SEPTA to achieve compliance and will reevaluate SEPTA's procurement system after corrective actions have been completed.

Our review showed that UMTA's monitoring procedures and practices were not adequate to ensure SEPTA's compliance with procurement requirements or to detect the deficiencies JRL found. UMTA has generally relied on SEPTA's self-certification, substantiated by pre-award and triennial reviews and independent annual audits, that it complied with procurement requirements. However, we found that UMTA's pre-award and triennial reviews at SEPTA were limited in scope and not directed at identifying procurement deficiencies. We also found that although the independent annual audits at SEPTA included an evaluation of internal controls over purchasing and receiving, they did not include an evaluation of SEPTA's compliance with UMTA procurement requirements.

<sup>1</sup>Procurement Systems Review of the Southeastern Pennsylvania Transportation Authority, JRL Associates, Inc. (Nov. 1988).

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1988, when UMTA revised its guidelines. Under the revised UMTA guidelines, SEPTA has until May 1989 to provide a written self-certification that it complies with UMTA's procurement requirements.<sup>4</sup>

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## Compliance Review Identified Major Problems in SEPTA's Procurement System

SEPTA's procurement system does not comply with all federal procurement requirements, according to the November 1988 JRL report. JRL's compliance review identified significant deficiencies or weaknesses in both SEPTA's written procurement procedures and its overall procurement operations. (App. III contains the JRL report Executive Summary, and app. IV provides a detailed discussion of JRL's approach for the compliance review.)

The most serious problem JRL found was that SEPTA's procurement system was not autonomous, as important functions were dispersed within SEPTA's decentralized organization structure. JRL also found that SEPTA does not meet the UMTA standards for written processing and selection procedures. (App. III provides a detailed discussion of these two problem areas.) SEPTA's nonautonomous procurement system and inadequate written procedures also contributed to other deficiencies JRL found in SEPTA's procurement procedures and practices, such as the use of contract procedures that restrict competition.<sup>5</sup> (App. V summarizes the major deficiencies in SEPTA's procurement system.) SEPTA generally agreed with most of JRL's findings and conclusions and has established a task force to address them and to implement corrective actions. The SEPTA task force plans to substantially complete the needed changes in its procurement system by May 1989 so that SEPTA can provide its required self-certification to UMTA.

Although SEPTA has significant weaknesses to correct in its procurement system, UMTA agrees with SEPTA's task force effort to address these problems. UMTA will (1) maintain its current policy of making pre-award reviews of proposed SEPTA contracts exceeding \$100,000, (2) require SEPTA to provide a written report of the interim and final corrective actions planned or taken, and (3) reserve the right to review and concur in the final decision for corrective actions.

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<sup>4</sup>The revised UMTA guidelines require grantees with more than 100 revenue vehicles to provide a written self-certification by May 1989 that they will comply with federal procurement requirements and standards.

<sup>5</sup>JRL's findings were based on a review of 80 SEPTA procurement actions totaling about \$140 million.

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UMTA made a determination related only to the specific contract action requiring review, but did not review the procurements for compliance with other procurement requirements. Because the pre-award reviews were not directed at identifying procurement deficiencies, UMTA's concurrence of the contract actions cannot be relied on to ensure that SEPTA's procurements comply with other procurement requirements.

To determine whether UMTA performed a pre-award review for the other 33 procurements, we obtained information from SEPTA. SEPTA provided us with copies of the pre-award review requests, supporting documentation, and UMTA's concurrence letters for 31 of the 33 procurements. However, we were unable to determine from this information what analyses UMTA performed to support its concurrence of the procurements. We also could not determine whether UMTA performed a pre-award review for two of the 73 procurements because we could not locate documentation at either UMTA or SEPTA.

We believe that a more in-depth review and analysis of procurements during the pre-award review would have detected some of the deficiencies JRL identified. We identified six procurements, totaling about \$2.9 million, that UMTA concurred with during the pre-award review process, which JRL's compliance review identified as having major deficiencies. For example, JRL found that four of these procurements, totaling about \$593,000, required performance bonds for nonconstruction, which the UMTA standard discourages. Two procurements, totaling about \$147,000, had contract specifications restricting competition, which is expressly prohibited by the UMTA standards. Two procurements, totaling about \$192,000, lacked an evaluation of the contractor's ability to meet contract terms, supporting JRL's finding that no formal system existed within SEPTA to evaluate contractor performance as required by UMTA standards. One procurement, totaling about \$92,000, did not follow the UMTA requirement for a cost or price analysis to ensure the reasonableness of the contract price. Finally, one procurement, for \$2.1 million, contained a change order clause that provides for additional payment on a cost-plus-percentage-of-cost basis, which is prohibited by the UMTA standards.

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## Triennial Review Did Not Emphasize Procurements

Since 1983, the Urban Mass Transportation Act has required UMTA to review and evaluate, at least every 3 years, a section 9 grantee's compliance with statutory and administrative requirements. A triennial review covers 19 specific areas, including competitive procurements. UMTA completed its only triennial review of SEPTA in December 1986 and issued a

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carried out its certification that it complies with procurement requirements. UMTA relies on the annual audits required by the Single Audit Act of 1984 (P.L. 98-502) to achieve the section 9 audit requirement. The single annual audit covers all major federal grant programs, including UMTA's section 3 and section 9 programs.

We reviewed the independent audits performed at SEPTA for the last 4 fiscal years (1984 through 1987) and found they did not focus enough attention on SEPTA's procurement system. While these annual audits included a study and evaluation of internal controls over purchasing and receiving, they did not include a detailed evaluation of SEPTA's procurement system for compliance with federal procurement requirements. This was confirmed by representatives of the accounting firm, who said that such a review was not required by the OMB guidelines.<sup>8</sup> These representatives also said that without specific guidance, they would not have done an evaluation of SEPTA's compliance with procurement requirements unless they believed that problems existed that would have a material effect on SEPTA's financial condition.

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## Conclusions

UMTA has generally relied on SEPTA's self-certification, supplemented by pre-award and triennial reviews and independent annual audits, that it complied with UMTA's procurement requirements. However, UMTA's reviews were limited in scope and not directed at identifying procurement deficiencies, and the independent annual audits did not evaluate SEPTA's compliance with procurement requirements. Consequently, SEPTA's procurement weaknesses went undetected until identified by JRL's review. UMTA needs to improve its internal controls by increasing monitoring procedures and practices to ensure that SEPTA remains in compliance with procurement requirements after it takes corrective actions.

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## Recommendations

We recommend that the Secretary of Transportation direct the Administrator, UMTA, to

- increase the scope of pre-award reviews of SEPTA contracts to include the analyses needed to identify procurement weaknesses and problems in complying with UMTA procurement requirements,

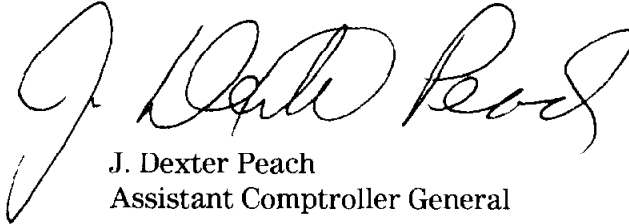
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<sup>8</sup>Compliance Supplement for Single Audits of State and Local Governments, Executive Office of the President, OMB, (revised Apr. 1985).

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methodology. This work was performed under the direction of Kenneth M. Mead, Director, Transportation Issues. Other major contributors are listed in appendix VIII.

Sincerely yours,



J. Dexter Peach  
Assistant Comptroller General

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**Abbreviations**

A/E	architect/engineering
DOT	Department of Transportation
GAO	General Accounting Office
JRL	JRL Associates, Inc.
OMB	Office of Management and Budget
SEPTA	Southeastern Pennsylvania Transportation Authority
UMTA	Urban Mass Transportation Administration

9. Grantees will maintain records sufficient to detail the significant history of a procurement. These records will include, but are not necessarily limited to the following: rationale for the method of procurement, selection of contract type, contractor selection or rejection, and the basis for the contract price.

10. Grantees will use time- and material-type contracts only after a determination that no other contract type is suitable and only if the contract includes a ceiling price that the contractor exceeds at its own risk.

11. Grantees alone will be responsible, in accordance with good administrative practice and sound business judgment, for the settlement of all contractual and administrative issues arising out of procurements.

12. Grantees will have written procedures to handle and resolve protests relating to their procurements and shall, in all instances upon UMTA request, disclose information regarding a protest to UMTA.

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## **Competition Requirements**

1. All procurement transactions will be conducted in a manner providing full and open competition consistent with UMTA procurement standards. Some of the situations considered to be restrictive of competition include, but are not limited to, placing unreasonable requirements on firms in order for them to qualify to do business, requiring unnecessary experience and excessive bonding, and specifying only a "brand name" product instead of allowing "an equal" product to be offered and describing the performance of other salient characteristics of the brand name product.

2. Grantees will conduct procurements in a manner that prohibits the use of statutorily or administratively imposed in-state or local geographical preferences in the evaluation of bids or proposals, except in those cases in which applicable federal statutes expressly mandate or encourage geographic preference.

3. Grantees will have written selection procedures for procurement transactions. These procedures will ensure that all solicitations incorporate a clear and accurate description, except when a "brand name or equal" description may be appropriate, of the technical requirements for the material, product, or service to be procured and identify all requirements that the offerors must fulfill and all other factors to be used in evaluating bids or proposals.



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# UMTA Third Party Contracting Procurement Methods

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UMTA Circular 4220.1B, effective May 5, 1988, identifies the following methods of procurement that grantees may use, as appropriate.

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## Procurement by Small Purchase Procedures

Small purchase procedures are those relatively simple and informal procurement methods for securing services, supplies, or other property that do not cost more than \$25,000 in the aggregate. If small purchase procurements are used, price or rate quotations will be obtained from an adequate number of qualified sources.

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## Procurement by Sealed Bids (Formal Advertising)

Bids are publicly solicited and a firm-fixed-price contract (lump sum or unit price) is awarded to the responsible bidder whose bid, conforming with all the material terms and conditions of the invitation for bids, is the lowest in price. The sealed bid method is generally the preferred method for procuring construction.

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## Procurement by Competitive Proposal

The competitive proposal technique is normally conducted with more than one source submitting a proposal, and either a fixed-price- or cost-reimbursement-type contract is awarded. It is generally used when conditions are not appropriate for the use of sealed bids.

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## Procurement by Noncompetitive Negotiation (Sole Source)

Sole source procurement is accomplished through solicitation or acceptance of a proposal from only one source, or after solicitation of a number of sources, when competition is determined inadequate. Procurement by noncompetitive negotiation may be used only when the award of a contract is infeasible under small purchase procedures, sealed bids, or competitive proposal and at least one of several circumstances, such as the item is available only from a single source, applies.

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Purchasing and contract administration of stock items were handled in the Purchasing Department. However, acquisition of construction services and architect/engineering (A/E) services (large dollar items) was performed by personnel with general administrative backgrounds in SEPTA's Capital Grant Compliance Office of the Planning and Construction Division. While the Purchasing Department was minimally involved by mailing solicitations, replying to inquiries, and receiving and opening bids or proposals, the Planning and Construction Division performed the most critical duties of conducting technical evaluations of proposals, making selection decisions or recommendations, negotiating with potential contractors, and performing contract administration. Selection of all professional services contractors, including A/E firms, was restricted to the SEPTA Board, with a recommendation made by a selection committee comprised of Board members. SEPTA's Office of General Counsel handled contracting for outside legal services and performed contract administration. The latter contracting functions should have been handled by the Purchasing Department.

OTHER SIGNIFICANT WEAKNESSES

- o SEPTA's Purchasing Policies and Procedures manual does not clearly describe steps necessary to carry out purchasing transactions. Specifically, it does not adequately address areas such as standards of conduct, sole-source justification, evaluation factors, selection procedures, cost and price analysis, negotiation summaries, and issuance and pricing of contract changes. Failure to have clear and updated written regulations and instructions may adversely affect the procurement process.
- o SEPTA had an insufficient system for evaluating contractor performance and inadequate contract administration activity.
  - o For example, SEPTA frequently had problems with A/E consultants providing estimates that were substantially below the actual construction project proposals received, with actual proposals sometimes being twice the amount of the estimate. The alleged causes for low estimates were such matters as incorrect quantity take-offs or failure to factor in the costs of construction of an operating facility; cost elements that a competent A/E should estimate correctly.

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- o little evidence that SEPTA conducted price negotiation of contract modification prices, rather than the price proposed by the contractor was the price accepted by SEPTA;
  - o file documentation inadequate to support either the basis for or the cost of the modifications;
  - o cost plus percentage of cost payment clauses used on construction modifications; and
  - o inaction on contract modification problems brought to SEPTA's attention in a 1984 Internal Audit report. While SEPTA indicated to the Audit Department that procedural recommendations had been initiated, the review found that there were still similar problems in this area.
- o The contract files showed little evidence that SEPTA conducted price negotiation of the basic contracts, rather it appeared that the prices proposed by contractors were the prices accepted by SEPTA. There was also little evidence of cost or price analysis to support the reasonableness of contract prices. These weaknesses present another vulnerability to fraud, waste, and abuse.

While SEPTA has significant weaknesses to correct, UMTA concurs with SEPTA's stated Task Force efforts to bring about needed changes in its procurement system and to comply with UMTA Circular 4220.1B for self-certification in May 1989. In light of SEPTA's stated commitment, UMTA will:

- o maintain its current preaward review of proposed SEPTA contracts exceeding one hundred thousand dollars in accordance with UMTA Circular 4220.1B;
- o hold SEPTA responsible for a written report of the interim and final actions which have been or plan to be taken to correct identified problems in the SEPTA procurement system with major emphasis on SEPTA's actions to:
  - o update and clarify written procedures particularly in the area of standards of conduct;
  - o place control of all procurement and contract actions under professional contracting people; and

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# JRL's Approach to Reviewing SEPTA's Procurement System

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UMTA retained JRL Associates, Inc., to review the SEPTA procurement system to determine whether SEPTA is in compliance with UMTA Circular 4220.1B, Third Party Contracting Guidelines, Office of Management and Budget (OMB) Circular A-102, and Department of Transportation (DOT) Order 4600.9B, Change 5. In addition, JRL was asked to determine whether SEPTA is following good procurement standards and has the technical capability to properly conduct all the necessary contracting and procurement functions.

A five-member team of specialists from JRL Associates, Inc., performed an on-site procurement system review of SEPTA between July 11 and July 29, 1988. The on-site portion of the review encompassed analysis of SEPTA's procurement organization and procedures, interviews with SEPTA officials, and review of 80 procurement actions.

The 80 procurement actions were selected randomly from a listing of 627 purchase orders, or contracts. They included 36 Requests for Proposal from a total listing of 67, 38 Invitations for Bid from a listing of 500, and five small purchases (under \$25,000) from an unlisted universe. Change orders were not listed as procurement actions. The procurement actions reviewed represented a total dollar value of approximately \$140 million dollars. The listing of 627 contracts from which these actions were selected represented a dollar value of approximately \$383 million dollars. While it was not feasible to statistically correlate the sample size in dollar value or number of contracts to the universe from which the selection was made, the sampling was random and was intended to be representative of all types of purchases and to include a substantial portion of the SEPTA expenditures.

The JRL review team interviewed SEPTA senior managers, procurement specialists, and technical personnel about specific contracts and to obtain general information on procurement activities. The review team also defined and discussed major problem areas with SEPTA personnel. This was done to ensure that if they had overlooked any procedures, practices, or documentation or had misinterpreted them, SEPTA personnel would have sufficient time to bring the omissions to the team's attention before the exit interview.

# UMTA Pre-Award Review Requirements Under UMTA Circulars 4220.1A and 4220.1B

UMTA requirement	Grantee third party contracts subject to UMTA pre-award review	
	UMTA C 4220.1A, effective 6-28-82 to 5-4-88 <sup>a</sup>	UMTA C 4220.1A, effective 5-5-88 to present <sup>a</sup>
For grantees providing self-certification: <sup>b</sup>		
Single bid or offer contracts	Over \$10,000	For procurements of 14 or more buses
Sole source contracts	Over \$10,000	Over \$1 million
Brand name contracts	Over \$10,000	c
Contracts proposing award to other than low bidder	All	c
For grantees not providing self-certification: <sup>b</sup>		
Single bid or offer contracts	All	Over \$100,000
Sole source contracts	All	Over \$100,000
Brand name contracts	All	Over \$100,000
Contracts proposing award to other than low bidder	All	Over \$100,000
All other contracts	All	c

<sup>a</sup>Excludes contracts using operating assistance grants.

<sup>b</sup>UMTA may require a grantee to submit any third party contract for review, in addition to those specifically subject to review, when such submission is in the interest of UMTA.

<sup>c</sup>Not applicable.

Source: UMTA Circulars 4220.1A and 4220.1B.

examined prior GAO reports on SEPTA and discussed an investigation then in progress with a representative of the Department of Transportation Office of the Inspector General.

UMTA retained the firm of JRL Associates, Inc., to conduct the compliance review to determine whether SEPTA was in compliance with UMTA's Third Party Contracting Guidelines. We interviewed the JRL team leader to determine the approach used in conducting the review. We also discussed the JRL findings and conclusions contained in the November 1988 report with UMTA officials. We did not participate in or assist the firm with devising or implementing its study approach. Consequently, we have no basis to endorse or dispute the firm's methodology, assess the accuracy of the work performed, or confirm its findings. However, both UMTA and SEPTA generally agreed with the contents of the JRL report.

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# Objectives, Scope, and Methodology

On December 22, 1987, the Chairman, House Budget Committee, requested GAO to determine whether a review of SEPTA's efficiency and effectiveness was warranted. In subsequent discussions with the Chairman's staff, we agreed to evaluate UMTA's oversight of SEPTA's procurement system. We also agreed to summarize the results of an UMTA-contracted study to review SEPTA's compliance with federal procurement requirements.

In order to determine the adequacy of UMTA's oversight, we reviewed UMTA's files documenting SEPTA procurements made under section 3 and section 9 grants programs from July 1, 1984, to May 31, 1988. Detailed information on some procurements was not available in the UMTA Region III office. In these cases we obtained relevant information directly from SEPTA.

We also examined pertinent legislation, regulations, and directives to identify UMTA's monitoring and enforcement responsibilities for ensuring grantee compliance. Both UMTA headquarters and Region III officials were interviewed and provided us with documentation on their oversight activities. We determined whether UMTA identified any compliance problems at SEPTA, and what enforcement actions, if any, UMTA had taken. In addition, we discussed the results of UMTA's 1987 triennial review report of SEPTA and examined the documentation obtained during this review. At SEPTA, we interviewed transit officials to obtain information and documentation pertinent to our review that we could not obtain at UMTA.

We reviewed the Secretary of Transportation's 1986, 1987, and 1988 annual statements and reports required by the Federal Managers' Financial Integrity Act of 1982. The reports did not identify any material weaknesses related to UMTA's internal controls for compliance monitoring. We also examined, on a limited basis, the extent to which UMTA was adhering to the internal control practices set forth in program regulations and agency directives.

To determine the extent to which the independent annual audits conducted at SEPTA covered its internal procurement controls and compliance with federal procurement requirements, we examined the audit reports issued for fiscal years 1984, 1985, 1986, and 1987. We also discussed the scope of these audits with the firm that conducted them.

We reviewed reports by state agencies on SEPTA to determine whether weaknesses in SEPTA's procurement system had been identified. We also

# Summary of Major Deficiencies in SEPTA's Procurement System Found in Compliance Review by JRL

Dollars in thousands

Major deficiency	Procurement actions with major deficiencies	
	Number of actions	Contract amount
File documentation not complete	60	\$132,986
Cost or price analysis not performed according to standards	44	116,054
No evidence of evaluation of contractor performance and determination of responsibility	40	112,839
Limited contract administration	37	95,813
Little evidence of effective contract negotiations	36	111,817
Performance bond requirement for nonconstruction solicitations restricted competition	27	38,894
Awards made on solicitations when only a single bid or few bids received	15	103,417
Construction contracts contain a change order clause that provides for additional payment on a cost-plus-percentage-of-cost basis	15	27,017
Restrictive specification in contracts for both products and services	15	4,504
Inadequate support for either the basis for, or the cost of, change orders and contract amendments and modification	7	9,653

Appendix III  
JRL Report Executive Summary on the  
Review of SEPTA's Procurement System

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- o ensure the procurement office has autonomy to a degree that protects against undue influence over procurement and contracting decisions.
- o work with SEPTA incrementally as the Task Force completes phases of its ongoing review and has developed approaches for corrective action; and
- o reserve the right to review and concur in the final decision for corrective actions needed in SEPTA's procurement activity.

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- o Little evidence was presented that SEPTA took contractual remedies against the contractors for the poor estimates in estimating project costs or that SEPTA recorded the contractor's performance to be used in future responsibility determinations.
- o Effective contract administration controlled by trained procurement professionals is crucial to curbing fraud, waste, and abuse in the procurement process and to ensuring nonresponsible contractors will not continue to receive awards.
- o SEPTA used restrictive contractual specifications in the procurement of both products and services. A single bid or few bids were obtained on 15 of the 80 sampled procurement actions. The impact of competition on price is a well-known market reality. When restrictive specifications are written, contractors know better than anyone else what affect the restriction will have on competition, hence, they adjust their bid price accordingly. Examples of the types of restrictions were:
  - o detailed product specifications in the technical specifications for vehicles;
  - o excessive professional qualifications, inappropriate application of geographic preference and noncompetitive awards on professional services contracts;
  - o the use of nonminimum retainer contracts which circumvented competition on professional and other consultant services; and
  - o frequent requirement for bid and performance bonds on nonconstruction contracts.
- o SEPTA's files on contract modifications showed a pattern of weaknesses indicative of inadequate and ineffective contract administration. Contract modifications are by their nature changes that are negotiated without the benefits of competition and should be carefully controlled. In SEPTA where millions of dollars are spent annually on procurements, tight control over contract modifications is critical to uphold the integrity of the procurement system and to prevent abuse. Examples of the weaknesses were:
  - o a trend of multiple change orders, time extensions, and large dollar value changes relative to the initial contract amounts;

# JRL Report Executive Summary on the Review of SEPTA's Procurement System

## EXECUTIVE SUMMARY

The Urban Mass Transportation Administration (UMTA) contracted for a procurement system review of the Southeastern Pennsylvania Transportation Authority (SEPTA), the nation's fourth largest transit authority. The on-site portion of the review was completed on July 29, 1988, and encompassed analysis of SEPTA's procurement organization and procedures, review of 80 procurement actions, and interviews with SEPTA officials.

During calendar year 1987, SEPTA processed more than 23,000 purchase orders valued at approximately \$350 million. Of this \$350 million, \$213 million was spent on operations including \$24 million for stock inventory items and \$107 million for new rolling stock. The remaining \$137 million was used for capital projects. As of December 1987, SEPTA had approximately 14,000 open purchase orders with a value of \$445 million, of which \$293 million was outstanding.

SEPTA entered into complex contractual arrangements and procured millions of dollars worth of supplies and services, in fact SEPTA's spending level and complexity of procurements exceeds that of many federal government agencies. However, SEPTA's Purchasing Department did not control the most critical and important of its procurement functions thereby contributing to weaknesses throughout the procurement system. While the deficiencies are significant, we are encouraged by SEPTA's General Manager's cooperative attitude and initiative to form a Task Force which is responsible for developing and implementing any required procurement changes by May 1989.

Following are highlights of the review of SEPTA's procurement system.

### SEPTA'S PROCUREMENT ORGANIZATION

Over the years, the United States Congress and various Administrations have had many deliberations and have concluded that personnel responsible for carrying out program responsibilities are not in an objective position to assume or direct procurement responsibilities. The procurement office should be in control of the procurement process and the administration of contracts. Further, the procurement office should be autonomous without undue influence exerted upon the office by other offices or parties. In SEPTA, the Purchasing Department did not control all procurement processes; rather, important procurement responsibilities were dispersed within SEPTA's organization and performed by program personnel without the requisite procurement expertise. Consequently, sound procurement practices were not always followed, autonomy of the contracting function was negated, and checks and balances were minimized, thereby jeopardizing the integrity, efficiency, and effectiveness of the procurement system.

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**Appendix I**  
**UMTA Third Party Contracting Procurement**  
**Standards and Competition Requirements**

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4. Grantees will ensure that all prequalified lists of persons, firms, or products that are used in acquiring goods and services are current and include enough qualified sources to ensure maximum open and free competition. In addition, grantees will not preclude potential bidders from qualifying during the solicitation period.

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# UMTA Third Party Contracting Procurement Standards and Competition Requirements

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UMTA Circular 4220.1B, effective May 5, 1988, identifies the procurement standards and competition requirements that apply to all UMTA grant assistance programs.

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## Procurement Standards

The following standards are applicable to UMTA third party procurements.

1. Grantees and subgrantees will use their own procurement procedures that reflect applicable state and local laws and regulations, provided that the procurements conform to applicable federal law.
2. Grantees will maintain a contract administration system that ensures that contractors perform in accordance with the terms, conditions, and specifications of their contracts or purchase orders.
3. Grantees will ensure that ethical conduct is adhered to by maintaining a written code of standards of conduct governing the performance of their employees engaged in the award and administration of contracts; prohibiting its officers, employees, or agents from either soliciting or accepting gratuities, favors, or anything of monetary value from contractors, potential contractors, or parties to subagreements; and including procedures for identifying and preventing real and apparent organizational conflicts of interests in its written policy.
4. Grantee procedures will provide for a review of proposed procurements to avoid purchase of unnecessary or duplicative items.
5. To foster greater economy and efficiency, grantees are encouraged to enter into state and local intergovernmental agreements for procurement or use of common goods and services.
6. Grantees are encouraged to use federal excess and surplus property in lieu of purchasing new equipment and property, whenever such use is feasible and reduces project costs.
7. Grantees are encouraged to use value engineering clauses in contracts for construction projects of sufficient size to offer reasonable opportunities for cost reductions.
8. Grantees will make awards only to responsible contractors possessing the ability to perform successfully under the terms and conditions of a proposed procurement.



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- increase the emphasis on the procurement area during triennial reviews at SEPTA by including the reviews and tests of selected procurements needed to determine that proper procurement procedures are in place and being followed, and
- request SEPTA to have the independent auditor conducting the annual audit include the reviews and tests necessary to determine compliance with UMTA procurement requirements.

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## Views of Agency Officials

We discussed the report's contents with UMTA headquarters and Region III officials; however, as requested by your office, we did not obtain official agency comments. The UMTA officials agreed that UMTA relies on SEPTA's self-certification and that its pre-award and triennial reviews are limited to determining whether a grantee has a competitive procurement process. Because increasing the scope of these reviews would defeat UMTA's current policy of reducing federal oversight in grantee activities, the UMTA officials suggested that a more feasible approach to ensure compliance is for UMTA to hire contractors to periodically review a grantee's procurement system to detect procurement deficiencies and to assist the grantee in correcting these deficiencies. While a compliance review should help UMTA grantees to identify procurement problems and to establish proper procurement procedures, we do not believe that such a review, by itself, provides UMTA reasonable assurance that SEPTA will continue to follow established procedures.

The UMTA officials expressed concern that our report may unfairly criticize SEPTA, when most UMTA grantees need to improve their procurement systems. According to the officials, SEPTA's procurement system may be typical of about 90 percent of all UMTA grantees. Our review was limited to evaluating UMTA's oversight of SEPTA's procurements and relied on the JRL compliance review results as an indication of whether SEPTA complied with procurement requirements. If other UMTA grantees are experiencing procurement problems, UMTA should consider implementing our recommendations on a broader basis.

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We performed the field work for this review from May 1988 to November 1988 in accordance with generally accepted government auditing standards. Appendix VII contains details of our objectives, scope, and

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report on its findings in July 1987. The report stated that SEPTA's procurement policy "promotes the concept of competition to the maximum extent possible" and concluded that SEPTA maintains a competitive procurement system as required by UMTA.

However, we reviewed the documentation supporting UMTA's triennial review at SEPTA and found that the review did not emphasize the procurement area. UMTA did not perform a detailed review and analysis of SEPTA procurements to identify deficiencies in SEPTA's procurement procedures and practices or to ensure that SEPTA complied with procurement requirements. UMTA's desk audit was comprised of reviewing SEPTA's written procurement policy and its own pre-award reviews. As previously discussed, however, we found that UMTA's pre-award reviews of SEPTA's contracts were limited in scope and not directed at identifying procurement deficiencies.

During UMTA's on-site visit at SEPTA, procurement was one of five topics discussed in an approximately 3-hour period. However, neither the manager of SEPTA's Purchasing Department nor the manager of Capital Grants Compliance was present at the meeting. Furthermore, UMTA did not review SEPTA's procurement files, test transactions for compliance with federal procurement requirements, or request summary data on the number, type, or dollar value of procurements. Such information would provide UMTA an overview of SEPTA procurement activity and would enable UMTA to target its review to specific transactions.

UMTA's approval of SEPTA's competitive procurement policies and procedures in the 1987 triennial review report contrasts with JRL's compliance review conclusion that SEPTA's procurement system does not comply with federal procurement requirements. Because it did not emphasize the procurement area during the triennial review, UMTA did not detect major weaknesses in SEPTA's procurement system. We believe that an in-depth review and analysis of SEPTA's procurement organization and procedures would have revealed its nonautonomous procurement system and inadequate written procurement procedures. In addition, we believe that reviews and tests of selected transactions would have identified deficiencies in SEPTA's procurement procedures and practices.

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## Annual Audits Do Not Focus on Procurements

The Urban Mass Transportation Act requires UMTA to conduct, or require a section 9 grantee to have independently conducted, an annual audit or review to determine, among other things, that the grantee has

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## UMTA's Monitoring Activities Did Not Identify SEPTA's Noncompliance

UMTA's monitoring procedures and practices were inadequate to detect the weaknesses in SEPTA's procurement system. In monitoring SEPTA's procurements, UMTA has not taken full advantage of the available monitoring mechanisms (pre-award and triennial reviews and annual audits), and the scope of its monitoring activities has not been broad enough to identify noncompliance. As a result of these control weaknesses, SEPTA's noncompliance with procurement requirements went undetected until JRL's compliance review.

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## Pre-Award Reviews Were Limited in Scope

Until self-certified under UMTA's revised guidelines, SEPTA is required to submit specific documentation for all proposed noncompetitive procurement contract actions over \$100,000 that involve sole source, single bid, brand name, or award to other than low bidder. UMTA reviews the required documentation to determine whether the noncompetitive contract action is justified. At its discretion UMTA can also review the proposed procurement for compliance with other procurement requirements, such as requirements for bonding and maintaining a system for evaluating a proposed contractor's ability to meet the contract terms. On the basis of its review, UMTA may concur in or deny awarding of the proposed contract.

From about July 1, 1984, to about June 30, 1988, 73 SEPTA procurements funded with UMTA assistance were subject to pre-award review.<sup>6</sup> We reviewed UMTA grant files to obtain supporting documentation for the procurements and to assess UMTA's pre-award review practices. Good internal control practices dictate that documentation be accurate and complete to show that appropriate analyses have been done to support decisions.<sup>7</sup> However, we found information supporting only 40 of the 73 SEPTA procurements in the UMTA files.

Our review of these 40 procurements showed that UMTA's pre-award reviews were generally limited to ensuring that SEPTA submitted the required supporting documentation and written justifications. While UMTA did not concur in any procurement until it had received the required documentation, the UMTA files did not typically contain records of the analyses UMTA performed to support its concurrence. In addition,

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<sup>6</sup>These procurements were subject to the \$10,000 pre-award review requirements in effect prior to UMTA's revised guidelines. App. VI compares pre-award review requirements prior to and after UMTA revised its guidelines.

<sup>7</sup>The Standards for Internal Controls in the Federal Government issued by the Comptroller General in 1983 requires that all transactions and significant events be clearly documented.

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Compliance monitoring is an important internal control strategy for ensuring that SEPTA uses a competitive procurement process that meets the procurement requirements. UMTA needs to improve its monitoring procedures and practices to ensure that SEPTA remains in compliance with UMTA procurement requirements after SEPTA completes its corrective actions.

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## Background

The Urban Mass Transportation Act of 1964, as amended (49 U.S.C. App. 1601 *et seq.*), authorizes UMTA to provide mass transportation assistance through two primary grant programs—the Section 3 Discretionary Grant program and the Section 9 Formula Grant program. SEPTA has received over \$1.7 billion from UMTA during the past 22 years and has used these funds primarily for capital improvements, such as the acquisition of buses and trains, and for operating costs. From October 1985 to mid-April 1988, SEPTA received 14 section 3 grant obligations totaling \$217 million and 8 section 9 grant obligations totaling \$321 million. During calendar year 1987, SEPTA processed more than 23,000 purchase orders valued at about \$350 million.

As a condition to receiving UMTA grants, SEPTA is required to use a competitive procurement process that fosters full and open competition and reasonable prices. On May 5, 1988, UMTA revised its guidelines<sup>2</sup> to implement the federal procurement requirements codified in the new governmentwide uniform grant regulations, known as the Common Rule.<sup>3</sup> (App. I contains a detailed discussion of UMTA's procurement standards and competition requirements and app. II discusses the procurement methods that UMTA grantees may use.)

Unless UMTA has reviewed and certified SEPTA's procurement system, SEPTA is required to provide a written self-certification that it complies with the procurement requirements. While UMTA has not certified SEPTA's procurement system, SEPTA was self-certified from July 1985 to May

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<sup>2</sup>UMTA Circular 4220.1B, Third Party Contracting Guidelines, (May 5, 1988).

<sup>3</sup>The Common Rule was published in March 1988 by 22 federal agencies, including the Department of Transportation (49 C.F.R. part 18). Prior to the Common Rule, the federal procurement standards were contained in Attachment O of the Office of Management and Budget (OMB) Circular A-102 (Uniform Requirements For Assistance To State and Local Governments).

