State of New York

Barry L. Kluger
Inspector General

Office of the Inspector General
Metropolitan Transportation Authority
Two Penn Plaza, 5th Floor
New York, New York 10121
212-878-0000

August 8, 2017

Veronique Hakim
Managing Director
Metropolitan Transportation Authority
2 Broadway, 20th Floor
New York, NY 10004

Re: **BSC Procurement Consultant Services Contracts**
MTA/OIG #2017-06

Dear Ms. Hakim:

As you know, the MTA Business Service Center (BSC) was established in 2009 to provide consolidated services for MTA headquarters and the six constituent agencies; one of those services was the procurement of goods and services common to all agencies. In October 2013, the first MTA Chief Procurement Officer (CPO) was hired and charged with overseeing the consolidation of non-core procurements (i.e. materials/services common across agencies and/or not directly affecting rolling stock). While this initiative required the development of a larger procurement operation in the BSC, it also represented an opportunity to reengineer MTA's purchasing and contracting methods and achieve potentially significant savings through the agencies' substantial combined purchasing power. To assist with this transition and capacity building effort, MTA officials determined there was a need for management consultants to provide strategic advice on the approach to the procurement consolidation and ways to achieve the cost savings from consolidated contracting.

The Office of the MTA Inspector General (OIG) is auditing two of these management consulting contracts entered into by the CPO with KPMG, LLP. Specifically, the audit is focused on cost controls over the Procure to Pay Process Review contract (P2P) awarded on July 25, 2014 and the Procurement Transformation contract (PT) awarded on December 4, 2014. These two contracts signed by the CPO and KPMG and the subsequent supplemental agreements to the original contracts totaled $11.88 million.

Overall, we found that cost and internal controls exercised by BSC Procurement over these contracts and supplemental agreements were inadequate. While efforts are currently underway by BSC officials and OIG to review the specific deliverables produced and expenditures charged under these contracts, this letter identifies the following control weaknesses we observed and which need to be addressed for future contracts:

- The cost of the initial PT contract increased substantially—from \$1.05 million to \$9.21 million—without scrutiny by any MTA officials outside of BSC Procurement. This growth was authorized under the signature of the CPO, but, given that his department also requested the supplemental funds, this represented an inadequate "separation of duties." The separation of duties is critical to prevent the opportunity for misconduct and fraud and reduce the likelihood of error in disbursing funds.

- Reports to the MTA Board lacked adequate transparency about how BSC Procurement had spent funds approved for as-needed consulting services.

- The two contracts were structured so that KPMG would be reimbursed for out-of-pocket expenses (expenses) at actual cost. However, the contracts did not cap these expenses nor were the expenses audited or reviewed in detail by MTA personnel, even though the contracts provided for this cost-control step. Expenses accounted for approximately \$1.43 million of the amount invoiced to date.

To improve cost controls and the oversight of management contracts, OIG recommends that for any similar contracts proposed by MTA, management consultants must provide an estimate of out-of-pocket expenses as part of the original contract, as well as any subsequent supplemental agreements, and MTA should audit the expenses before authorizing reimbursement. We further recommend that when BSC Procurement is both the contract manager and the end user of a contracted service, requests for supplemental work must be authorized by the MTA Chief Financial Officer in order to establish an adequate separation of duties. And finally, we recommend that a regular report should be made to the MTA Board on how as-needed consultant funds are being used.

BACKGROUND

The Procure to Pay Contract

In late 2013, MTA BSC Procurement began a competitive Request for Proposal (RFP) process to select a firm to provide a P2P across MTA agencies.[1] In providing justification for MTA Board approval, the Staff Summary explained that a consulting firm was sought to map the purpose and function of the current P2P process at each Agency and MTA headquarters, and provide a cost estimate for each existing step. The consultant was then to evaluate the potential for improved

[1] Procure to Pay (P2P) is a process that comprises all activities associated with purchasing and paying for goods and services, including but not limited to: requisitioning, advertising for and distributing the solicitations, carrying out procurement methodologies (e.g. sealed bid, request for proposals, request for quotes, e-procurement, sole source, procurement cards, etc.), establishing contracts, generating and handling of purchase orders and vouchers, processing of invoices for payments.

effectiveness or efficiency in the P2P processes that could result from greater use of PeopleSoft 9.2 functionality, improved procedures at each Agency and HQ, or the use of alternative software.

This consulting personal services contract was awarded on July 25, 2014 to KPMG, as a result of a competitive procurement process, in the amount of $1,835,988 for professional fees plus out-of-pocket expenses at cost. As stated in the staff summary to the MTA Board, the cost for this contract was $2,114,840 with a contingency of $500,000 for a total of $2,614,840. In the end, after three supplemental agreements were also executed, the project took eight months. Final invoices for P2P totaled $2.86 million: $2.40 million for professional fees and $0.46 million for expenses.[2]

Procurement Transformation Contract

In September 2013, MTA officials requested MTA Board approval to enter into base contracts with pre-approved New York State consulting firms for anticipated services to help "complement and enhance MTA's efforts to improve its business processes, identify and implement opportunities for operating and capital cost savings, and increase revenue generation."[3] The MTA Board approved an initial $5 million to fund such future consulting projects, increasing that amount to $10 million in October 2015 and then $15 million in October 2016. Another modification added $636,130 to the base contract without requiring Board approval, bringing the total available funding to $15.6 million. The award process was designed to work as follows: When a specific need for consulting services arose, MTA would hold a competitive "mini-bid" process among the pre-approved firms that had established base contracts under the Business Transformation Consulting Services Contract (BT Contract).

KPMG was awarded a competitive mini-bid contract on December 4, 2014. This contract, referred to as Work Assignment #2 (WA#2), authorized the firm to analyze MTA expenditures, assist with the definition of core vs. non-core procurement categories, assess the capability of the existing organization and personnel, and identify potential savings through proactive sourcing and contracting approaches. According to the signed contract, "This Work Assignment No. 2 shall be completed in accordance with contract requirements within the amount obligated." The agreement specified that professional fees would be $901,973 and out-of-pocket expenses were estimated at $145,200 for a total of $1,047,173.

The initial scope and value of WA#2 grew substantially over the following two years. Seven supplemental agreements were signed between the CPO and KPMG totaling $8.16 million, bringing the obligation for professional fees to $7.70 million and estimated out-of-pocket expenses to $1.51 million. When OIG began its review, three more supplementals were being

---

[2] These expenses exceeded the contract's authorized amount, and the excess amount was charged against the Procurement Transformation budget.

[3] From the September 2013 Board Book staff summary.

negotiated for an additional $1.78 million. These have since been put on hold for further review or cancelled.

FINDINGS

Inadequate Separation of Duties

Generally, the user department, or requester of a good or service, is a separate entity from the procurement department, which provides expertise in the acquisition of that good or service. However, under the P2P and PT contracts, BSC Procurement was both the user of KPMG's consulting service and the procurer of that service. Therefore, the CPO was in the position to request and authorize any modifications (i.e. supplementals or change orders) to his own contracts without additional scrutiny. Although approving a supplemental request (within certain parameters) is an authority given to the CPO, the supplemental request is normally initiated by the user department —organizationally outside of the procurement department—who must provide justification for the proposed change to the contract. This process allows for an independent level of review and scrutiny by the procurement department of the user's request.

According to the MTA All Agency Service Contract Procurement Guidelines, when a proposed contractual change does not exceed $750,000 (or $250,000 if the change exceeds 15 percent of the contract's adjusted value), a supplemental or change order can be approved by the agency president or a designee (e.g. the CPO). The size of the WA#2 supplementals was small in relation to the contract authorization for the *entire* Business Transformation Services Contract, which had Board authorizations at the high levels of $5 million, $10 million, and $15 million. As a result, none of the proposed supplementals for WA#2 triggered an approval level higher than that of the CPO, who was thus authorized to approve the changes in his role as the agency president's designee.

Typically, three signatures are required to process a supplemental: those of the requester, in this case a subordinate of the CPO's; an MTA Legal staff member who reviews the agreement for form; and the CPO. In this case, the CPO was essentially both requester and approver, and as a result, contract increases could be processed without significant scrutiny outside of BSC Procurement.

This contracting structure—in which a base retainer contract is negotiated and then specific work assignments are awarded via mini bid—is regularly used for consulting services at MTA. However, usually the original requester is a project manager from a department other than BSC Procurement and that user department is requesting the CPO's approval and signature, a process that preserves a separation of duties thereby reducing opportunities for misconduct, fraud, and unintentional error.

Recommendation 1: When BSC Procurement is both the user of a service and the procurer of the related contract, and a proposed modification to the contract would increase its value substantially, the MTA Chief Financial Officer must approve the change.

Reports to the Board Lacked Transparency on How Consultant Budget Was Spent

The initial staff summary for Business Transformation Consulting Services requested MTA Board authorization in September 2013 to spend up to $5 million on as-needed consulting services to "complement and enhance MTA's efforts to improve its business processes, identify and implement opportunities for operating and capital cost savings, and increase revenue generation." While the document does not specify projects, the staff summary stated that "consultant services will only be used in connection with initiatives where the expected savings is a significant multiple of the associated consulting fee."

In October 2015, the Board approved another contract modification request to increase the funding authorization for the BT contract by $5 million, bringing the total available funds to $10.6 million.[4] The staff summary stated that $4.7 million was committed to the MTA Procurement Transformation project. The staff summary further noted that $3 million more was needed to perform additional work in procuring energy-related products and services and property management services. This additional work was projected to deliver $7.9 million in annualized savings starting in 2016. While the language suggested that KPMG was involved or held the sole contract for the initial phase, the company was not clearly identified either as the consultant who was awarded the funds or as the firm who would be doing the additional $3 million in consulting work. The staff summary mentioned three other projects but did not make it clear if they had been completed, were ongoing, or merely planned. No specific consulting firm was mentioned in relation to those contracts.

A year later, in October 2016, the Board approved the final contract modification of another $5 million, bringing the BT contract value to more than $15 million. The staff summary noted that $7.9 million had been spent on procurement transformation and listed the projected benefits of the work, without naming any consulting firm. This was followed by a list of the same three projects included in the 2015 staff summary, again without clarity as to whether these had been accomplished and which, if any firm, had won the mini-bid for each project.

If the Board authorizes a sum to be used for consulting on an as-needed basis, OIG believes that the Board should be made aware of how the money was spent, i.e. on what projects and to which consulting firms.

---

[4] The first modification of $636,130 did not require Board approval due to its smaller value.

Recommendation 2: Funds committed for "as-needed consulting services contracts" should be reviewed by the Auditor General semi-annually to ensure that the awards and supplementals, were procured properly, and have scopes and terms consistent with the board authorization of the "as-needed funds." Additionally, a report to the Board should be made on an annual basis on how the money was spent, on what projects, and to which consulting firms.

Consultants' Time and Out-of-Pocket Expenses Were Not Verified

Both the P2P and PT contracts required KPMG to maintain and make available upon request timekeeping and expense records documenting the consultants' actual labor hours and reimbursable expenses.[5] OIG found, however, that BSC Procurement did not request such documentation as part of its contract oversight process. In our meetings with BSC Procurement and KPMG personnel, their recollections differed as to why such documentation was not required. Although KPMG did produce summaries of the professional fees and expenses invoiced for each consultant, these reports did not always accompany KPMG's invoices unless they were requested by BSC Procurement. On several occasions, the MTA Project Manager for the P2P and PT contracts asked KPMG specific questions about these costs, but at no point did BSC Procurement staff review or audit KPMG's timekeeping or expense records to determine if the invoiced amounts were consistent with the compensation provisions of the contracts.

BSC Procurement officials were warned by MTA Legal staff about the dangers of entering into contracts without establishing caps to limit allowable expenses. Further, in the case of P2P, the agreement also omitted a baseline *budget* for expenses. To minimize cost overruns and ensure adherence to the contract compensation provisions, BSC Procurement should have regularly audited KPMG's professional charges and expenses.

Recommendation 3: For consulting services contracts that allow time to be paid on an hourly rate and out-of-pocket expenses to be paid at actual costs, MTA should require the consultant to submit timekeeping and expense records with each invoice. These should be reviewed by the Project Manager before payment is authorized. The Project Manager should take a risk-based approach in reviewing expenditures in order to establish vendor compliance.

[5] The contracts specifically required each invoice to be accompanied by itemized detail of hours worked by date and in the aggregate for each person, including subcontractors covered by the invoice.

Recommendation 4: Services contracts that reimburse actual out-of-pocket expenses should include a budget for such expenses as part of the contract and must be closely monitored.

MTA Response

MTA agreed with our findings and related recommendations by letter dated July 17, 2017.

****

We appreciate your attention to the issues we raised, as well as the courtesy and cooperation afforded to us at all times by the MTA Business Service Center staff. We will continue to monitor the implementation of these recommendations, as appropriate. Should you have any questions regarding this final report, please contact me or Executive Deputy Inspector General Elizabeth Keating at (212) 878-0022.

Very truly yours,

Barry L. Kluger

Cc: Bob Foran
Donna Evans
Phil Eng
Wael Hibri