



# SUMMARY AUDIT REPORT

## CONTRACT MANAGEMENT AND ADMINISTRATION

Q2 F2012

SEPTEMBER 30, 2011

AU1205CORP

*Prepared By:*

*J. Coles-Nash*

*F. Nishi*


*A. D'Andrea*

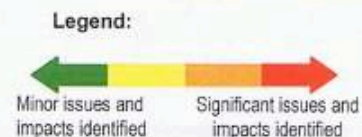
*P. Howard*

*A. Lagnado*

**Distributed To:** D. Olsen Finance Directors  
T. Pekeles  
C. Reid  
D. Cobb  
Audit & Risk Management Committee

## Contract Management & Administration Audit F2012

AUDIT TYPE	AUDIT RATING
CORE FINANCIAL PROCESS	



### Audit Objective and Scope

- Review the effectiveness of contract management and administration practices at BC Hydro and assess specific contracts for compliance with policies and procedures.
  - ◆ This audit focused on the post award phase and contract management practices.
  - ◆ The audit reviewed active "medium sized" contracts from \$50K to \$1M for the period May 1, 2010 to June 30, 2011. Selected contracts were examined in detail using audit criteria and data analytics.
  - ◆ Audit Services performs separate audits on contract management practices for larger value contracts such as Capital Projects and Independent Power Producers.

### Background

- The post award phase begins with a signed contract that binds the parties to obligations, deliverables and fees for services to be rendered. Contract management includes understanding the terms and conditions, coordination at site, ensuring deliverables and quality are met, administering invoices and payments, and contract close out.
- Contract management at BC Hydro is a decentralized function with many individuals assigned to oversee contract responsibilities with varying degrees of guidance. Generation and T&D have a specific group responsible for contract management primarily to oversee capital work.
  - ◆ Generation Contract Management is focused primarily on construction projects. The group recently updated written contract management procedures, trained contract management staff and reduced the number of active contracts.
  - ◆ T&D has contracts in transmission, distribution materials and capital works and with the merger of BCTC are consolidating the T&D practices for consistency.
  - ◆ Corporate Departments generally manage contracts independently.
  - ◆ The Procurement organization has been working to improve documentation and file management.
- Based on the audit data analysis there were approximately 4,600 "medium sized" active contracts with a total current commitment of \$842M. Of these 47% were in T&D, 23% in Corporate, 20% in Generation and 10% relate to blanket orders used throughout the company.
  - ◆ Contracts from \$50K to 500K account for 93% of the value with only 7% of the contracts in the range from \$ 500K - \$ 1M.
  - ◆ Contracts varied greatly and include services such as: equipment rental, inspections, purchase of goods and services, consultants, construction, information technologies, and communications.

## Contract Management & Administration Audit F2012

### Key Findings

#### Contract Administration and Compliance

The management of contracts is not always compliant with BC Hydro policies and procedures. In addition there are situations arising where practices and policies do not align.

Current practices relating to how work is planned and orders released in the field contravene existing policies and guidelines. These findings relate to "medium sized" contracts and it is not assumed that the same compliance issues apply to large contracts.

- Work is starting before a contract is in place which places BC Hydro at risk to liability and/or legal exposure in the event of a safety incident, performance issue or contract default.
  - ◆ Although contracts were in place, 29% of the sample contracts reviewed had work started prior to the contract being finalized. Testing of invoices identified that Hydro was billed for work started before the contract was finalized.
- Contract change orders are used extensively and in some cases inappropriately. The findings indicate a need for better planning and thought given to the full scope of the services required.
  - ◆ Data analysis of the 4,600 contracts showed that 41% with a contract commitment of \$394M had associated change orders. Of these 10% exceeded their original value by 11% to 50%. A further 19% exceeded their contract value by 51% to over 150%.
  - ◆ Detail testing of the sample of 55 change orders identified only one third of change orders were appropriate and followed correct procedures. Common issues with change orders included;
    - Work performed and paid beyond the original scope of contracts.
    - Approvals of change orders and equitable adjustments received after work had started.
    - Where no contract extension options existed, contracts were extended rather than going out to tender or market.
    - Contract extension options exercised for significantly higher dollar amounts without a breakdown or forecast of the additional work to be performed.
- Contract files are not always being kept current and there is little guidance on the minimum requirements.
  - ◆ Contracts reviewed had signed hard copy of the contract with initial support documents. Standard contract templates were used and financial approval authority was obtained.
  - ◆ However, key documents required to keep files current were not always added. Key documents were missing for 22% of files reviewed. In particular updated insurance certificates were not always obtained from the vendor and filed when a contract was extended.
  - ◆ Electronic documentation process implementation to address procurement documents were delayed then re-initiated in August 2011 and will take time for full implementation.

## Contract Management & Administration Audit F2012

- Contract payments did not always agree to the terms of the contract and were sometimes delayed.
  - ◆ Of the sampled invoices processed for goods or services, 19% did not meet the provisions of the contract. For example there were differences in price, shipping terms and services provided.
  - ◆ Payments to suppliers were not made in accordance with contract terms. For 24 of 31 (77%) of contracts at least one invoice was not paid within the 30 day contract terms, and some payments were late by over 60 days.

### Contract Management Oversight

Responsibility has not been established to oversee contract management for BC Hydro.

- Primary responsibility to effectively administer contracts and protect BC Hydro's interests lies with the many individuals managing contracts in their respective areas. However individuals do not always understand their responsibilities or have the appropriate guidance for administering contracts.
  - ◆ After contract award, Procurement's responsibility with respect to contract management is limited to the administrative processes associated with contract changes.
    - However, individuals in the field or various departments are making commitments in the field without approvals and work may already be underway with the result that Procurement/Contract Management are left to process change orders retrospectively.
  - ◆ Generation and T&D have contract management groups who assume responsibility for their contracts however there are many contracts handled independently.
  - ◆ It is unclear who should provide direction and guidance to all contract management groups and individuals requiring assistance, and challenge non compliance.
- Current contract management policies, practices and procedures are not consistent throughout the organization and do not ensure that "medium sized" contracts are managed in accordance with BC Hydro policy.
  - ◆ Contract Management groups have developed detailed contract management procedures to assist their individual contract managers. However there are no specific guidelines available to individuals acting in the role of "Contract Managers".

### Management Comments and Action Plans

- Management agrees with the recommendations in the audit report and has committed to their implementation by October 2012 with the exception of those action plans impacted by ongoing initiatives such as the SAP Supply Chain and Plan Schedule Work. These actions will be completed in conjunction with the associated initiative.