

Attachment AB
Grand Jury Report

GRAND JURY FINDINGS

SACRAMENTO MUNICIPAL UTILITY DISTRICT

SUMMARY AND FINDINGS

The 1988/89 Grand Jury reviewed the Sacramento Municipal Utility District's (SMUD) operations and made eight recommendations for improvement. Recommendation No. 3 stated: "Sole source bids should be kept to a minimum and fully justified prior to award. SMUD should award contracts to the lowest bidder unless a serious question arises regarding the bidder's ability to perform."

SMUD's response stated:

"...it is this District's policy to award all contracts on a competitive basis. When competitive bidding is not possible or feasible, General Manager's Directive 89-16requires that a written justification for the sole source award be provided describing why the competitive bid process was not followed and what steps were taken to assure that fees in the contract are reasonable and competitive.

"In addition, contracting policy #9 (District Contracting Handbook) requires that the justification for sole source contracts be clearly described, supported by documented and verifiable facts, and approved by the appropriate management level prior to the award of the contract. It further details the specific criteria which must be met before an award on a sole source basis may be justified."

After reviewing this response, the 1989/90 Grand Jury requested and received, a copy of General Manager's Directive 89-16 referenced in SMUD's response. This Directive states in part:

"Competitive bids will be solicited for all contracts whenever possible and practical. Sole source contracts will be used only as an exception to the rule, and then only when it has been determined that no other bidder can meet the terms of the contract.

"...If the normal competitive bid process was not followed, an explanation shall be provided on the staffing summary sheet as to why and what steps were taken to assure that fees in the contract are reasonable."

The Grand Jury was also provided a copy of General Manager's Directive 89-6....which states in part:

"Contracts must be approved (with all appropriate signatures) prior to any ordering of merchandise or any services performed by contractors, consultants, or others. This policy also applies to any items previously authorized/ approved in the budget."

The Jury reviewed three recent sole source contracts:

An \$18,000 contract with a consulting firm for various production cost models and analysis was signed by the firm's president on November 28, 1989, and by a SMUD representative on December 11, 1989. The term of the agreement was December 1, 1989, through December 31, 1989. The contract was not routed to Risk Management, Legal, and Accounting Departments for review and formal approval until February 6, 1990, well after the work had been completed.

At the time this contract was routed for review and approval, no sole source justification was attached. The required justification was added later.

An \$8,000 contract with a firm to assist in development, production and distribution of a Spanish language safety film was approved in advance of its effective term of December 1989 through June 1990. No justification of the need for a sole source contract was attached.

A \$15,000 contract with an individual to review the 1990 budget for Rancho Seco was signed by SMUD on December 21, 1989, and by the individual on January 3, 1990. The term of the contract was December 10, 1989, through January 31, 1990. Work was actually performed between December 19, 1989, and December 21, 1989, plus a subsequent appearance in late January 1990.

The contractor was to be paid \$125.00 per hour or \$1,000.00 per day. Actual payments to date have been \$6,593.75 for four days' work.

The sole source agreement was justified on the basis of the contractor's known expertise and reputation in electrical, nuclear and utility activities.

On March 1, 1990, the SMUD Board of Directors approved a resolution which requires that all future consultant contracts must be approved by the SMUD Board in advance.

Two of the three contracts reviewed by the Grand Jury had not been approved in advance as required by General Manager's Directive 89-6 and as stated in SMUD's response to the 1988/89 Grand Jury Report.

Two of the three contracts reviewed by the 1989/90 Grand Jury had no sole source justification attached at the time the contracts were approved by SMUD management although one justification was added later.

Documentation for the third contract (with the individual) included a paragraph which purported to justify the need for a sole source contract. However, this paragraph does not address the issue of compensation and does not explain why it was appropriate to pay him \$6,593.75 for four days' work.

Appropriate criteria for sole source contracting are established in General Manager's Directives 89-6 and 89-16, and in SMUD's response to the report of the 1988/89 Grand Jury.

Many of the problems inherent in sole source contracts can be avoided if SMUD rigidly enforces its own directives.

SMUD is developing a detailed manual of contracting procedures. Such a manual should help to avoid future problems related to controversial contracts.

RECOMMENDATIONS

1. Existing Sacramento Municipal Utility District (SMUD) directives require that contracts must be approved in advance of performance. This policy

should be enforced by the General Manager or SMUD Board of Directors as appropriate.

2. Existing SMUD directives state that sole source contracts will be used only when it has been determined that no other bidder can meet the terms of the contract, and that this determination must be documented in writing prior to awarding the contract. This policy should be enforced by the General Manager or SMUD Board of Directors as appropriate.
3. Existing SMUD directives require written documentation of steps taken to assure that fees in sole source contracts are reasonable. This policy should be enforced and reasonableness should be documented by the General Manager or SMUD Board of Directors as appropriate.
4. Existing SMUD policy requires Board review of all consultant contracts. The effectiveness of this policy should be evaluated. The SMUD Board may wish to establish some time or dollar limits on this requirement in order to minimize workload impact.

DRAFT

**RESPONSE OF THE BOARD OF DIRECTORS OF THE
SACRAMENTO MUNICIPAL UTILITY DISTRICT
TO THE RECOMMENDATIONS OF THE
SACRAMENTO COUNTY GRAND JURY REPORT (1989-90)**

Introduction

The Grand Jury reviewed three Sacramento Municipal Utility District contracts for compliance with District contract requirements and procedures and made four recommendations to the District as a result of that review. The Board of Directors wishes to extend its appreciation to the Grand Jury for its efforts, and to state that the Board and the District are committed to ensuring that proper contract procedures are followed in all District activities. The District has made significant progress toward this goal. However, as the Grand Jury noted in its findings, there is still room for improvement.¹ The District engages in thousands of contract actions each year, and while it is difficult to provide absolute assurance that each action will be error-free, it is the

¹ The District concurs in part with findings on the three contracts examined by the Grand Jury. However, District policies and procedures were followed in part in the case of the \$18,000 consultant contract for production cost models and analysis. A mis-filed document has been located which evidences the fact that the contract had been routed for approval by appropriate departments within the contract period and not after services terminated, although the contract itself was not properly signed prior to commencement of work. As a result, the document reviewed by the Grand Jury was routed for approval after contract completion on the assumption that there was no prior approval document in place. In addition, with respect to the Grand Jury's finding on the Rancho Seco budget review contractor, the billing rate was \$125 per hour and the contract expressly specifies the same rate for overtime (more than 8 hours per day or 40 hours per week). The contractor worked portions or all of 8 days, not 4, and was also reimbursed for travel and expenses, since his place of business is in New York. The payments made under the contract correctly reflect the work performed and the expenses incurred.

goal of the District to develop and enforce contract processes to eliminate any problem potential. The District's response to the Grand Jury's specific recommendations is set forth below.

Recommendation #1

Existing Sacramento Municipal Utility District (SMUD) directives require that contracts must be approved in advance of performance. This policy should be enforced by the General Manager or SMUD Board of Directors as appropriate.

Concur

As stated in the Grand Jury Report, SMUD General Manager Directive 89-6 (Administration of Contracts) mandates that all necessary approvals be in place before the commencement of work under a contract. That directive also provides that managers and executive management are responsible for ensuring compliance with this directive.

SMUD operates a public business -- providing electric power to customers around the clock. That service obligation requires immediate procurement from time to time to meet an emergency in power supply. An exception to GM Directive 89-6 occurs when there is an emergency situation. It is SMUD's policy that under exigent circumstances verbal approval of a contract may be given so that the immediate problem may be alleviated, with a written contract approved under the normal but expedited approval process and executed as soon as possible thereafter. Such situations that may require immediate attention include, but are not limited to, the protection of SMUD or other personnel from death or injury; the avoidance of unnecessary work stoppages; and maintaining generation, transmission, and distribution systems

online. Moreover, before the follow-up written contract is approved and executed there must be provided with it, documentation which explains and justifies the emergency contracting procedure.

To more stringently enforce compliance with this directive and policy, managers and executive management have been instructed to be scrupulously circumspect in their efforts to ensure that proper contracting procedures are followed. This requires that the contract be routed to, reviewed and approved by, the appropriate departments in accordance with the delegations of authority approved by the Board of Directors and the General Manager. When emergency work must be performed prior to approval and execution of a written contract, written justification must be provided to management for such action. In addition, SMUD's internal auditing department has been directed to vigorously perform random audits of all contracts to monitor adherence to the directive and policy.

Recommendation #2

Existing SMUD directives state that sole source contracts will be used only when it has been determined that no other bidder can meet the terms of the contract, and that this determination must be documented in writing prior to awarding the contract. This policy should be enforced by the General Manager or SMUD Board of Directors as appropriate.

Concur

Section 12751 of the Municipal Utility Act (MUD Act) in the Public Utilities Code requires that purchases of all supplies and materials (but not services) when the expenditure required exceeds \$20,000 be let by competitive bid. Section 12753 of the MUD Act provides an exception to this requirement in the case of

a great emergency. The Board of Directors, by resolution passed by a 4/5 vote, may declare and determine that such an emergency exists and may enter into contracts and expend sums necessary in such emergency without observance of the competitive bid requirement for purchases of supplies and materials.

There is no statutory requirement to competitively bid service, consulting, or other non-supply and materials purchase contracts. However, General Manager's Directive 89-16 (Awarding of Sole Source and Competitively Bid Contracts) requires that a competitive bid process be initiated for all contracts whenever possible and practical. The Board's approved delegations of authority for contracts require more stringent and higher levels of review for sole source contracts. When a sole source contract is awarded, the explanation and justification therefor must be fully documented prior to final contract approval.

Sole source contracts may be quite appropriate in some cases where the expertise needed is best available from a single supplier. Price is not necessarily the primary criteria for some highly specialized and valuable professional services. But the reasons supporting such a determination must be documented. To more stringently enforce compliance, managers and executive management have been instructed to be scrupulously circumspect in their efforts to ensure that no sole source contract is approved or awarded without a written, reasoned and supportable explanation of why a competitive bid process is not possible or not practical and that all other proper contracting procedures have been

followed. Moreover, managers and executive management have been instructed that no department or manager, at whatever level, shall approve and continue to route a sole source contract unless the sole source justification is fully documented.

In addition, SMUD's internal auditing department has been directed to vigorously perform more frequent random audits of all contracts to monitor adherence to the directive.

Recommendation #3

Existing SMUD directives require written documentation of steps taken to assure that fees in sole source contracts are reasonable. This policy should be enforced and reasonableness should be documented by the General Manager or SMUD Board of Directors as appropriate.

Concur In Part

General Manager Directive 89-16 (Awarding of Sole Source and Competitively Bid Contracts), in addition, requires that the explanation and justification for sole source contracts include an explanation as to why and what steps are taken to assure that fees in the contract are reasonable.

To more stringently enforce compliance with this directive, managers have been instructed to be scrupulously circumspect in their efforts to ensure that sole source justifications for contracts include an explanation of the steps taken to ensure that the fees in such contracts are reasonable and competitive, and that all other proper contracting procedures have been followed. This requires that the contract be routed to, reviewed and approved by, the appropriate departments in accordance

with the delegations of authority approved by the Board of Directors.

Under the delegations of authority, final authority to approve contracts is either retained by the Board or delegated to the General Manager or other subordinate managers, depending upon the type and dollar amount of the contract. Thus, the reasonableness of fees in a sole source contract is documented by, and is the ultimate responsibility of, the manager at the level at which final approval of award is given. In many cases, though not all, such documentation will be at the Board of Directors or General Manager level. However, managers and executive management have been instructed that no department or manager, at whatever level, shall approve and continue routing a sole source contract unless the sole source justification is fully documented, including an explanation of the steps taken to ensure the reasonableness of the fees to be paid under such a contract.

In addition, SMUD's internal auditing department has been directed to vigorously perform frequent random audits of all contracts to monitor adherence to this policy and directive.

Recommendation #4

Existing SMUD policy requires Board review of all consultant contracts. The effectiveness of this policy should be evaluated. The SMUD Board may wish to establish some time or dollar limits on this requirement in order to minimize workload impact.

Concur

SMUD Board Resolution 90-3-1, adopted March 1, 1990, requiring all consulting contracts to be approved by the Board, was

rescinded by Board Resolution 90-6-12, adopted June 7, 1990. Board Resolution 90-6-12 authorizes the General Manager to approve non-nuclear consulting contracts for up to \$100,000 and nuclear consulting contracts for up to \$500,000, pursuant to the revised delegations of authority. That resolution also authorizes the General Manager to redelegate consulting contract approval authority. The General Manager will ensure that SMUD directives and policy are followed by all managers to whom he delegates contract approval authority.