

MEMORANDUM

CITY OF GRAND RAPIDS

DATE: January 06, 2021

TO: Stacy Stout, Director Office of Equity and Engagement
Patricia Caudill, Diversity and Inclusion Manager
Max Frantz, Comptroller
Curt Reppuhn, Deputy Comptroller

FROM: Rachelle Selmon, CFE, Internal Auditor

SUBJECT: **Internal Audit Report for Office of Equity and Engagement Micro-Local Business Enterprise Supplier Diversity Program**

In accordance with the provisions of Administrative Policy 04-01 (Rev. 9-1-2020) *Equal Business Opportunity – Certification* and the City Commission Policy 600-12 (Rev. 10-27-2015) *Equal Business Opportunity – Construction*, Internal Audit has undertaken a Compliance Audit on the Micro-Local Business Enterprise Program practices by the Office of Equity and Engagement for the period of March 1, 2014 through October 26, 2021.

A summary of observations and key findings are as follows:

1. OEE Leadership is very experienced and knowledgeable of the mission and goal of the Micro-LBE Supplier Diversity Program.
2. Interdepartmental relationships between OEE and the respective contracting departments is collegial in nature and results in positive resolutions of identified issues.
3. Review of the OEE's Micro-LBE Supplier Diversity Program demonstrated a low level of compliance with the internal audit criteria derived from the Administrative Policy 04-01. Internal Audit determined non-compliance in six of the seven audit criteria for first term (nine (9) year period) and seven of the seven audit criteria for extended (additional five (5) year period) Micro-LBEs.
4. Annual reviews for all certified Micro-LBEs are not being conducted in accordance with section 2.3 of Administrative Policy 04-01. Furthermore, annual review procedures appear to lack standardization and may result in inadequate review of Micro-LBE vendor performance and reported total dollars spent within a calendar and/or fiscal year.
5. OEE does not appear to have written policies and procedures which define key controls and responsibilities, establishes accountability and describe expected outcomes with the department.
6. The City does not have clear, concise conflict of interest policy for staff. During our review we noted two OEE staff members have self-owned businesses that partnered and/or received \$14,700 in City funds between 2018 and 2021.

Attached please find our Internal Audit Report for the aforementioned program.

Internal Audit Report



*Office of Equity and Engagement
Compliance Audit Report on Micro-Local
Business Enterprise Program Practices*

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ABOUT INTERNAL AUDIT TEAM

The Internal Auditor under the Comptroller Department reports directly to the Citizen's of Grand Rapids. We conduct independent City-wide internal audits, reviews and investigations of the City's operations and departments in order to:

- Find ways to improve processes, programs, functions, and activities
- Provide information that supports effective decision making
- Identify real or potential misuse of City resources
- Prevent and detect fraud, waste, and abuse within the City
- Ensure compliance with City commission policies and Administrative orders

Through our work we strive to assist the City in their efforts to provide a sense of accountability, transparency, collaboration to the citizens of Grand rapids and our fellow colleagues in the City.

REPORT DISTRIBUTION

This report is intended solely for the information and use of the Comptroller Audit Team, the Auditee, and the Executive Office Management Team, and is not intended to be and should not be used by anyone other than these parties outside of the Comptroller Department knowledge. This report may not be released in full or in part, to any entity outside of the City of Grand Rapids or to any internal department without the prior approval of the Comptroller Department.

INTERNAL AUDIT TEAM

This audit was conducted by the Internal Audit Team under the direction of the Comptroller Department:

- Rachelle Selmon, CFE, Internal Auditor
- Curt Reppuhn, CPA, CGMA, Deputy Comptroller
- Max Frantz, Comptroller

EXECUTIVE SUMMARY

We conducted an audit of the Office of Equity and Engagement (OEE) Micro-Local Business Program. The objective of the audit was to determine whether systems were in place to provide reasonable assurance that OEE's supplier diversity program was in compliance with city policy and to evaluate effectiveness of internal controls.

Background

The City of Grand Rapids Micro-Local Business Enterprise Program was established by the Office of Equity and Engagement in support of the City of Grand Rapids' Mission Statement and the City Commission Sustainability Plan. The City's vision is to enhance the growth and development of small businesses and provide access and equal opportunity in the performance and administration of the City's acquisition process. The program was developed to also provide transparency amongst Kent County, Michigan residents desiring to do business with the City, by ensuring non-discrimination in the performance and administration of City contracting and subcontracting; promoting supplier diversity by providing all business enterprises access and an equal opportunity to participate in the performance of all City contracts; and utilizing strategies that enhance the growth and development of local small and emerging businesses. The City's Equal Business Opportunity (EBO) Administrative Policy 04-01 enables Office of Equity and Engagement Department to certify Micro Local Business Enterprises (Micro-LBEs) that desire to participate as such under the City's Supplier Diversity Equal Business Opportunity Certification Program who meet the established criteria.

The City of Grand Rapids spends millions of dollars in Construction, Goods and Services, and Professional Services to improve the City annually and seeks to increase spending with registered Micro-Local Business Enterprises. Certified Micro-LBEs are prioritized businesses that the City of Grand Rapids encourages departments to utilize for spending needs. Micro-LBEs range from various industry areas to cover a variety of Goods & Services needs across the organization. The City certifies businesses for a period of nine consecutive years and for five additional consecutive years for continued Micro-LBE status upon graduation as meeting special business requirements found within the Administrative Policy 04-01.

Micro-LBEs Benefits and Advantages:

- Free Micro-LBE Certification designation
- Priority Vendor Status with the City and Partners
- 3% Bid Discount for Goods and Services and Professional Services suppliers
- Construction Contractors provided up to 5% Bid Discount with Micro-LBE subcontractors

Micro-LBE Eligibility Requirements include verification of:

- 1) Business Age – in operation for at least 12 months
- 2) Registration with City of Grand Rapids Purchasing Department
- 3) Business Location – Kent County, MI
- 4) Business Size must be 25% or lower than the Standard Business Administration standards as determined by North American Industry Classification System (NAICS) Code for permanent employee or revenue number 3-year average
- 5) Personal Net Worth Statement signed by a CPA or Bank validating that net worth is less than \$305,500 (Year 2019) plus annual inflation rate (thereafter \$916,501 (Year 2019) plus annual inflation rate).
- 6) Continual eligibility determination by submitting Annual Reviews to OEE during the nine-year period

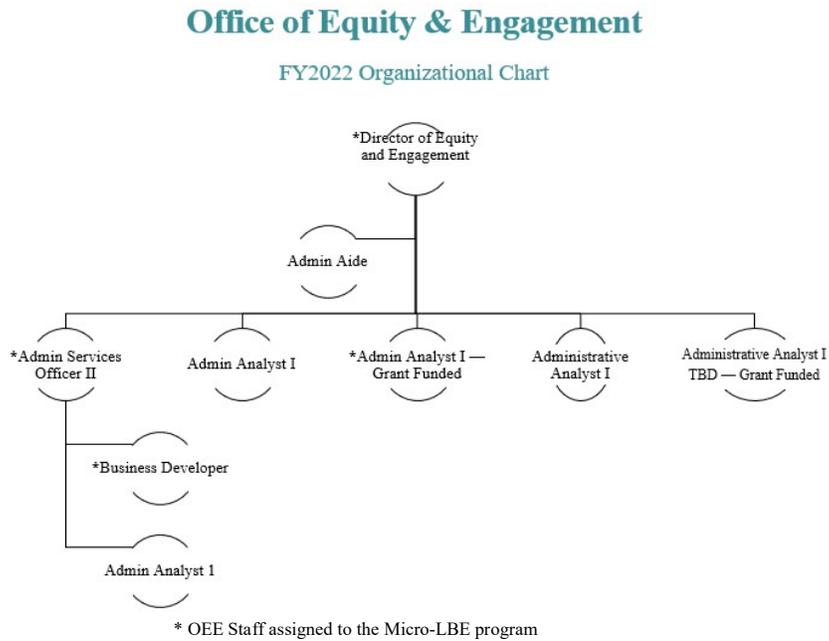
Extension of Micro-LBEs status for additional five (5) years:

- 1) Written request from Business owner to continue as Micro-LBE
- 2) Verification that the latest 3-year average business revenue or number of employees must be 50% or lower than the SBA standard business Size as determined by NAICS
- 3) Identify any Changes of business ownership
- 4) Recent Capability Statement
- 5) Personal Net Worth is less than \$916,501 (Year 2019) plus annual inflation rate
- 6) Continual eligibility determination by submitting Annual Reviews to OEE during the five-year period

OEE Department Personnel Org Chart

The Micro-LBE Program falls under the direction of the City’s Supplier’s Diversity Program within the OEE Department which is responsible for the oversight and monitoring of the Micro-LBE program. Figure 1 below describes the organization chart of the OEE Department Micro-LBE staff.

Figure 1
Organizational Chart



Audit Objective, Audit Questions, and Scope

We conducted this 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 audit covered the period from July 1, 2014 through October 26, 2021. We conducted our audit from October 26, 2021 to December 14, 2021.

The objectives of the Audit of OEE’s Micro-LBE Program processes were to:

- Assess compliance with City policies and procedures
- Verify the current Micro-LBE assessment process is comprehensive in nature and conforms to industry best practices to provide effective monitoring of new or and continuing Micro-LBE vendors.
- Analyze the Micro-LBE approval process for efficiency and adequacy of monitoring procedures.
- Identify improvement opportunities related to the efficiency and effectiveness of the Micro-LBE approval procedures and monitoring controls

As noted above, the objective of this audit is to assess the Office of Equity and Engagement’s Micro-Local Business Enterprise Supplier Diversity Program and test compliance with the provisions of the Administrative Policy 04-01 and the City Commission Policy 600-12. In doing so the following internal audit questions were also addressed:

- 1) Do the required verifying documents contain all the necessary information and are they approved by relevant authorities prior to Micro-LBE certification and/or recertification?
- 2) Do Micro-LBEs submit quality bids and is the best supplier selected for the right reasons?
- 3) Can total spent within a calendar and/or fiscal year be appropriately evaluated according to contracts awarded?

The scope of this audit included:

- Evaluating comprehensiveness and assessing adherence to current City policies and procedures in place governing the Micro-LBE processes — Administrative Policy 04-01.
- Reviewing the Micro-LBE Risk Assessment Process to validate:
 - ✓ Micro-LBE vendors are given the Micro-LBE designation upon approval under the business type classification within the Accounting system (CGI)
 - ✓ Micro-LBEs are reviewed on a recurring, periodic basis to ensure necessary changes and updates are documented within CGI
 - ✓ Appropriate evidence or supporting data is obtained to evaluate new and continuing Micro-LBEs
- Assessing if monitoring functions have been established to annually evaluate Micro-LBE eligibility and compliance with agreed upon policy terms.
 - ✓ Annual Reviews are obtained annually for all Micro-LBEs ensuring eligibility remains valid

Methodology and Audit Approach

This audit was conducted based on information provided by OEE, Engineering, and documents obtained from the City of Grand Rapids website. The approach for the audit included review of the Administrative Policy 04-01, City Commission Policy 600-12, supporting documentation and mapping of the various Micro-LBE processes, assessment of the key internal controls, walkthroughs; and fraud interviews with appropriate key personnel from the OEE, Comptroller, Engineering, and Fiscal Services Department. Audit tests were based on the most recent EBO Administrative Policy 04-01—Appendix C.

EVALUATION OF INTERNAL CONTROLS

In accordance with *Government Auditing Standards*, we obtained an understanding of internal control that is significant within the context of the audit objectives. We assessed whether internal control was properly designed and implemented. For those controls that were deemed significant, we obtained sufficient, appropriate evidence to support our assessment about the effectiveness of those controls.

We are required to report deficiencies in internal control that are significant within the context of the audit objectives. A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct (i) impairments of effectiveness or efficiency of operations, (ii) misstatements in financial or performance information; or (iii) noncompliance with provisions of laws, regulations, contracts, or grant agreements on a timely basis. Based on our audit, we found certain deficiencies in internal control that are significant to the objectives of this audit. Those findings are reported in the Key Audit Findings.

RESULTS OF AUDIT QUESTIONS

The Micro-LBE program undertaken by OEE were analyzed and a representative sample was taken for detailed testing of compliance with the criteria. Relevant personnel of the OEE, Comptroller, Fiscal Services, and the Engineering department were interviewed to obtain information and verify the information already obtained. All the audit findings as and when they were identified were discussed with management and their comments were obtained and incorporated where appropriate.

The substantive audit approach was used to address the audit questions below and a sample of 20 first term certified Micro-LBE vendors out of a population of 68 and 16 extended Micro-LBE vendors out of a population of 16 was selected from the Micro-LBE November 2021 Directory on the OEE City's webpage. The 36 Micro-LBE vendors selected were tested using the designed audit procedures to reveal program and policy weaknesses, which would result in non-compliance to the requirements of the related policy.

Audit question 1: Do the required verifying documents contain all the necessary information and are they approved by relevant authorities prior to Micro-LBE certification and/or recertification?

Internal Audit cross-referenced the verifiable supporting documents against the relevant criteria to ensure that the verifiable documents contained all the necessary information, and that approval was granted by relevant authorities prior to certification and recertification of the Micro-LBE. Relevant personnel of OEE, Comptroller, Fiscal Services, and the Engineering department were interviewed to gather information and this information was verified against the documents obtained.

Internal Audit experienced significant difficulties obtaining supporting documentation to review and perform data analysis during the audit. Accordingly, Internal Audit noted that data reporting is haphazard and inconsistent, resulting in an inability to effectively assess and utilize data analytics to improve current operations and determine actual Micro-LBE spent within a calendar or fiscal year. Further, Internal Audit noted insufficient maintenance of key reports or supporting evidence of procedures performed.

Audit question 2: Do the Micro-LBEs submit quality bids and is the best supplier selected for the right reasons?

Internal Audit reviewed all contract award documents to include Bid Packages and Final Pay Packages within the calendar year of 2020 for the top two prime contractor Micro-LBEs. The supporting documents were provided by the Engineering Department and were reviewed against the Purchasing Policy and the Equal Business Opportunity Policy and Guidelines as per the related criteria to ensure that proper processes were followed. Internal Audit reviewed the processes involved in bidding and awarding of contracts to Micro-LBEs against the bidding requirements and the awarding of contracts to ensure that bidding procedures established by the City and the law were followed and provided for fair, equal, and open opportunities for all bidders. Further, relevant personnel of the Engineering department and Fiscal Services Department were interviewed to gather information and this information was verified against the documents obtained.

Audit question 3: Can total spent within a calendar and/or fiscal year be appropriately evaluated according to contracts awarded?

Internal Audit selected two top prime contractors for the City with a Micro-LBE designation, one in which was awarded a total of \$4.8M from four bids and the other awarded \$6.8M from five bids in 2020. Further, relevant personnel of the Engineering department and Fiscal Services Department were interviewed to gather information and this information was verified against the documents obtained. Engineering personnel stated that it would be near impossible to obtain actual Micro-LBE spent within a fiscal or calendar year given that majority of Micro-LBEs are construction contractor that have projects that span anywhere from two to 10 years. Fiscal Services stated that the accounting system is not designed to generate a report that could pull Micro-LBE spent within a fiscal or calendar year. As the City looks to gaining a new ERP system in the future, this impossibility may become a reality.

Engineering explained, that although final payment may be received in a particular year that payment could be for work performed over a course of several years and not just for that particular year. Currently the OEE and the Engineering department work together to internally report total Micro-LBE contracts awarded within a calendar year. Engineering is currently brainstorming ways in which the City can calculate total actual Micro-LBE spent within a year to assess the value and impact the Micro-LBE program has on the community.

KEY AUDIT FINDINGS

Review of the OEE’s Micro-LBE Supplier Diversity Program demonstrated a low level of compliance with the internal audit criteria derived from the EBO Administrative Policy 04-01. Internal Audit determined non-compliance in six out of the seven audit criteria for first term (nine (9) year period) and seven of the seven audit criteria for extended Micro-LBEs as summarized below:

Findings

Micro-LBEs— Nine (9) year period:

Number of Micro-LBEs without supporting documentation for the following criteria:	
Business Age	00/20
Registration with City	01/20
Location in Kent County at 6 months	01/20
Business Size (25%)	11/20
Personal Net Worth	01/20
Annual Reviews	11/20
Initial Application Completed	04/16

Extended Micro-LBEs— Five (5) year period

Number of Micro-LBEs without supporting documentation for the following criteria:	
Written Request	01/16
Business Size (50%)	07/16
Changes of Ownership	05/16
Capability Statement	01/16
Personal Net Worth	16/16
Annual Reviews	15/16
Initial Application Completed	03/16

Issues Noted:

Micro-LBEs

Inactive Vendors in CGI	03/36
Business Type not Selected in CGI	07/36

No.	FINDINGS	Risk Ranking
1.	<p>Lack of Annual Reviews: The Administrative Policy 04-01 does delineate an on-going process or formalized framework to establish minimum requirements for Micro-LBE monitoring by the City through annual reviews. However, OEE implemented the annual review requirement in FY 2020 despite its existing requirement since 2017. OEE utilizes a “random selection” approach, therefore not all Micro-LBE vendors are monitored for compliance annually.</p>	High
2.	<p>Lack of Supporting Documentation for Micro-LBEs: Internal Audit experienced significant difficulties obtaining supporting documentation to review and perform data analysis during the audit. Accordingly, Internal Audit noted that data reporting is haphazard and inconsistent, resulting in an inability to effectively assess and utilize data analytics to improve current operations and determine actual Micro-LBE spent within a calendar or fiscal year. Further, Internal Audit noted insufficient maintenance of key reports or supporting evidence of procedures performed.</p>	High
3.	<p>Lack of Monitoring of Administrative and City Policies: Published Administrative City policies uploaded and updated by the Executive Office are not periodically reviewed or requested to ensure that the most recent departmental policy is published on the City’s website by OEE. Further, Internal Audit noted that the policy did not include clear requirements and needed more detailed guidance over annual reviews, continued eligibility requirements, and documentation requirements. As a result, the City may be utilizing outdated and unclear Administrative policies, City Commission Policies, or guidelines that position the City in a detrimental legal or financial position when engaging with outside vendors.</p>	High
4.	<p>Lack of Conflict of Interest — Employee Monitoring: Internal Audit noted that two employees in OEE have self-owned businesses that partnered and/or received \$14,700 City funds between 2018 through 2021, in which the City did not retain evidence of completion of Conflict of Interests forms from these individuals. As a result, the City may have entered into contracts, with City employees that had conflicting interests that may not align with the City’s financial and legal interests.</p>	High
5.	<p>Inconsistent Vendor Records within the CGI system and OEE MLBE Directory: Internal Audit identified approved MLBEs with incomplete vendor records. Internal Auditor identified one vendor that was not a vender in CGI, indicating that the MLBE vendor did not register with the City prior to certification approval. Additionally, the Internal Auditor identified that not all MLBE vendors on the November Directory were marked as MLBE under the Business Type in CGI. Further, Internal Audit identified one vendor that provided incorrect tax information during the registration process which resulted in an incomplete registration within CGI, however, the vendor was still approved to be an MLBE. As a result, OEE is approving ineligible vendors as Micro-LBEs which diminishes the value of the program and regulations set in place.</p>	High

Summary of Results

Summary of Results – Areas of Strength

As part of the above documented procedures, Internal Audit noted the following strengths present in the Vendor and Contract Management processes.

- Leadership over the OEE department is experienced and knowledgeable of the subject matter.
- OEE personnel, in conjunction with the City’s Attorney’s office, have recently completed a revision of the Administrative Policy 04-01 to improve best practices.
- Internal Audit noted that the engineering department responsible for the majority of Micro-LBE usage are knowledgeable of services provided by the respective Micro-LBE vendors and can clearly articulate operational expectations and spend that have been agreed upon with the vendor to the OEE Business Developer.
- Interdepartmental relationships between OEE Department and the respective contracting departments is collegial in nature and results in positive resolutions of identified issues.

Summary of Results – Opportunities for Improvement

The following **opportunities for improvement** were observed during the review. Control and process improvement opportunities identified by Internal Audit are discussed more thoroughly in the Detailed Improvement Opportunities and Action Plans section that follows.

No.	Opportunities for Improvement	Risk Ranking
1.	Internal Audit noted that OEE did not have written policies and procedures that define responsibilities, establish accountability, and describe expected outcomes within the department. As a result, the City is placed in a position where staff does not have a means to retain organizational knowledge and mitigate the risk of having that knowledge limited to a few personnel. Therefore, management lacks control activities to achieve objectives and respond to risks in the internal control system.	Medium
2.	Micro-LBE Performance Feedback is not obtained from City departments by OEE Department in anticipation of Micro-LBE extensions of existing Micro-LBE vendors. As a result, the City may be renewing contracts with vendors that are not adequately performing according to City expectations, may have a divisive relationship with the City, and/or are not adhering to established financial and operational service level agreements.	Low
3.	Micro-LBE Monitoring performed by OEE department lacks standardization and may result in an inadequate review of Micro-LBE program vendor performance and total dollars spent within a calendar and fiscal year. Internal Audit noted that MLBE performance measures within each department is inconsistently monitored and lacks a consistent depth or understanding of key requirements.	Low

*Risk Ranking: Includes High, Medium, and Low. See Risk Ranking Definitions in Appendix A & B for further detail.

In addition to the observations noted above, Internal Audit identified process enhancements for management’s consideration. However, due to their low nature of risk, Management responses for identified process enhancements are not required. Please review Appendix A & B for additional information on process enhancements identified during the audit.

Conclusion

The Office of Equity and Engagement in recent years has made efforts to improve compliance with the laws and regulations in its EBO Policy, however the audit identified material instances of non-compliance with the policies and regulations. These examples of noncompliance have not resulted in significantly affecting the department's validity of the program.

Review of the OEE's Micro-LBE Program demonstrated low level of compliance with all of the selected criteria but one from the Administrative Policy 04-01. However, the program demonstrated a high level of compliance with vendors not exceeding the established business size as determined by the SBA. Further, during the audit it was noted the MLBE vendors submitted competitive and quality bids and the winning vendor was selected according to City Purchasing Policy Guidelines. Nevertheless, noncompliance was noted in the Micro-LBE EBO Administrative Policy 04-01 due to lack of proper review and approvals and lack of proper evaluation and monitoring.

Consequently, in this respect OEE was non-compliant with the City's Administrative Policy 04-01 regarding Micro-LBE certification approvals.

Appendix