August 24, 2010

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Subject: *Medical Center Business Contracting Processes*
                     Audit Project 2010-39

The final audit report for Medical Center Business Contracting Processes, Audit Report 2010-39, is attached. We would like to thank Medical Center personnel for their cooperation and assistance during the audit.

Because we were able to reach agreement regarding corrective actions to be taken in response to the audit recommendations, a formal response to the report is not requested.

The findings included in this report will be added to our follow-up system. While management corrective actions have been included in the audit report, we may determine that additional audit procedures to validate the actions agreed to or implemented are warranted. We will contact you to schedule a review of the corrective actions, and will advise you when the findings are closed.

UC wide policy requires that all draft audit reports, both printed (copied on tan paper for ease of identification) and electronic, be destroyed after the final report is issued. Because draft reports can contain sensitive information, please either return these documents to AMAS personnel, or destroy them, at the conclusion of the audit exit conference. AMAS also requests that draft reports not be photocopied or otherwise redistributed.

                                 Stephanie Burke
                                 Assistant Vice Chancellor
                                 Audit & Management Advisory Services

Attachment

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AUDIT & MANAGEMENT ADVISORY SERVICES

Medical Center Business Contracting Processes
August 2010

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Project Number: 2010-39

Medical Center Business Contracting Processes
Audit & Management Advisory Services Project 2010-39

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Attachment A: Purchase Document Review Summary

I.   Background

Audit & Management Advisory Services (AMAS) completed a review of the Medical
Center (UCSDMC) business contracting process, as part of the approved audit plan for
fiscal year 2009/2010.   This report summarizes the results of our review.

Supply Chain Services (SCS) is responsible for assisting UCSDMC department personnel
with procuring and distributing goods and services, and ensuring that vendor invoices are
appropriately paid. Purchasing and Accounts Payable within SCS employs 12 buyers
who facilitate purchasing and vendor management activities, and six staff who process
accounts payable transactions. These staff are grouped into three functional teams:
Clinical, Information Technology/Facilities, and Services and Administration.

In recent years, the University of California (UC) has significantly increased the number
of strategic sourcing purchasing agreements, which leverage the purchasing power of its
multi-campus system. SCS management regularly participates in UC systemwide
purchasing initiatives and management meetings, and sometimes coordinates with other
UC campuses to procure services from a single vendor.

SCS utilizes the MediClick materials management system to capture and manage
purchasing and contract data. MediClick is a vendor hosted, web based application that
integrates the materials management, general ledger, and accounts payable functions and
provides a number of management reports to assist department personnel monitor
purchase transactions.

To initiate the procurement/contracting process authorized UCSDMC employees
complete a purchase requisition and forward it to SCS buyers for further evaluation. The
requisition can be prepared electronically in the MediClick system or by completing a
manual Form 390, *Purchasing Request for Non-Stock Materials*, which is used to procure
services, capital acquisitions, and goods or services that require a formal bid process.
SCS buyers convert approved requisitions into POs, and when appropriate, a formal
contract.

SCS buyers consider departmental requests as one of the criteria in the evaluation they
perform when selecting a vendor for a specific product. Formal quotes are obtained for
purchases of goods and services with a total annual value of $50K or more through the
request for proposal (RFP) process, and/or price and quality surveys. Vendor cost
analyses may be superseded by the designation of a sole source vendor. The use of a sole
source vendor must be justified in writing and approved by the SCS Director.

A purchase order contract that includes UC standard Terms and Conditions of Purchase
(Appendix A) included as governing terms is prepared for all purchases, including
agreements that exceeded the $50K high value threshold. However, a contract with

unique terms and conditions is not negotiated with each vendor. Because the negotiation of a contract requires additional resources throughout the process, contracts are generally used primarily for high dollar purchases or for multi-year service agreements. As noted above, UC negotiates contracts for goods or services required by all UC Health Sciences campuses. When strategic sourcing agreements have not been completed, SCS buyers use professional judgment and on-line resources available to determine when obtaining a contract provides the best price and limits potential UCSDMC liability.

II.   Audit Objective, Scope, and Procedures

The objective of our review was to determine whether SCS contracting process controls were adequate to ensure that goods and services were consistently available to UCSDMC departments at the best available price, in compliance with University procurement policy requirements. The audit scope included processes and related data for the period July 1, 2008 through December 31, 2009.

We completed the following audit procedures to achieve the project objectives:

- Reviewed University of California (UC) and UCSD Medical Center Policies (MCP) related to the contracting process including:
     - UC Business and Finance Bulletin (BUS) 43, *Materials Management;*
     - UCSD PPM 523, *Basic Purchasing Policy;* and
     - UC DA2100, *Delegation of Authority--Execution of Purchase Contracts, Subcontracts, and Standard Purchase Orders for Materials, Goods; and, Services to be Supplied to the University;*
- Evaluated the SCS organizational structure;
- Interviewed SCS personnel involved with the contracting process;
- Differentiated purchase order (PO) contracts from formal contracts;
- Evaluated the processes for authorizing and managing sole source and blanket POs;
- Documented the contracting process and evaluated process control strengths and weaknesses; and,
- Selected a judgmental sample of POs and contracts analyzed supporting documents to verify that purchase agreements were created and managed as required by SCS and University policies and procedures (*Attachment A*).

III.   Conclusion

Based on the audit work performed, we concluded that SCS contracting process controls were adequate to ensure that goods and services were consistently available to UCSDMC departments at the best available price, in compliance with University procurement policy requirements.

Over the past several years, SCS has re-organized its operations beginning with the integration of purchasing and accounts payable personnel. In November 2008, SCS also implemented the MediClick purchasing/accounts payable system which has had a positive impact on UCSDMC operations.

SCS has successfully implemented Electronic Data Interchange (EDI)[1], for a limited number of vendors. EDI transactions reduce the need for warehousing products through just-in-time orders, and improve the efficiency of the purchasing process. SCS management is in the process of identifying additional vendors for EDI conversion.

We noted some opportunities for process improvement, including updated policies and procedures, improved monitoring of efforts to secure best prices and retention of associated documents, and modifications to existing systems and procedures. These issues are discussed in the remainder of this report.

IV.   Observations and Management Corrective Actions

A.   Purchasing Support Documents

Source documents supporting compliance with relevant UC and UCSDMC purchasing policies and procedures were not available in all vendor files reviewed.

UC BUS-43 requires that goods and services be acquired "at the lowest overall cost, while affording the maximum opportunity practicable to those who wish to become suppliers to the University."   We noted that SCS utilized a number of tools to achieve this goal including:

- Formal bids
- Price surveys
- UC negotiated strategic sourcing contracts
- UC multi-campus contracts
- UCSDMC contracts

In addition, SCS maintained a membership in Novation[2], MD Buyline[3] and ECRI Institute[4] which provide access to vendor contract rates, and research data and

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[1] Electronic data interchange (EDI) is the structured transmission of data between organizations by electronic means. It is used to transfer electronic documents, including purchase orders and invoices from one computer system to another, i.e. from one trading partner to another trading partner.
[2] Novation was established Jan. 1, 1998, when VHA Inc. and University HealthSystem Consortium (UHC), two national health care alliances, consolidated their supply-contracting functions. Novation acts as the supply contracting company for nearly 25,000 VHA and UHC member organizations to help them manage and reduce supply costs.

advice regarding the selection of healthcare vendors. SCS buyers utilize these services to assist with evaluating vendors and selecting the best available price.

To evaluate the completeness of supporting documents for high value purchases, 17 POs with a dollar value of over $50K annually were selected for focused review. The audit test results are provided in *Attachment A.* In summary:

- A purchase requisition and PO were on file for all 17 POs in the sample.

- Thirteen of the 17 POs in the sample should have been supported by a "best price" analysis. However, those documents were located for only seven of the 13 POs. For purposes of our review, such documents would include comparative price information obtained from MC Buyline or another service.

- Thirteen POs in the sample should have been supported by Request for Proposal and/or competitive bid documents. Those documents were available for eight of the 13 POs.

The inconsistency of documentation indicates that required procedures may not be followed in all cases. As a result, SCS would not be able to provide documented proof of compliance with relevant UC Purchasing policies.

Management Corrective Action:

SCS management will implement a quality assurance process to provide increased oversight of vendor purchase orders and contract files.

B.   **Formal Contracts**

A formal contract had not been negotiated for five of 17 POs reviewed during audit testing.

As previously stated, SCS buyers determine if a formal contract should be negotiated with certain vendors to obtain competitive prices or include unique contract terms.   The absence of a formal contract did not indicate an audit deficiency, but could identify an opportunity for cost savings.

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[3] MD Buyline is dedicated to providing the most comprehensive information and consulting services to assist hospitals and healthcare facilities with the researching, planning, budgeting, and purchasing of healthcare products.
[4] ECRI Institute is a nonprofit organization dedicated to bringing the discipline of applied scientific research to discover which medical procedures, devices, drugs, and processes are best, all to enable you to improve patient care.

Management Corrective Action:

SCS management will consider implementing a questionnaire to document the buyer's decision to pursue or not to pursue a contract for high value purchases.

C.   **Purchasing Policies and Procedures**

Purchasing websites for buyers and end users contained out of date materials. In addition, a formal procedure manual had not been developed.

SCS maintained two web pages to provide electronic access to purchasing guidelines for buyers and department personnel. The purchasing website (www.ucsdhealthcare.ucsd.edu/purchasing) was available to both buyers and end users, to provide policy and guidelines, as well as detailed instructions for the purchasing process. The SCS file server M drive was accessible only to buyers, and provided internal operating guidelines. Selected documents on each of those sites were outdated.

Purchasing procedures and documents should be periodically updated to provide accurate information to SCS and UCSDMC personnel, and to ensure that processes are consistently followed.

Management Corrective Actions:

1. SCS is in the process of updating the Internal Operating Procedures (IOP).

2. SCS management will:

   a. Create a formal procedure manual to consolidate all critical procedures into one source.

   b. Update the buyer and end user websites to ensure that content is accurate and complete.

D.   **Authorization to Requisition Goods and Services**

The signature authorization forms used to verify the names and signatures of department staff who prepared purchase requisitions were not always current, and did not include a reference to any purchasing restrictions, such as dollar limits.

Signature authorization forms were completed by department management to provide evidence of staff authority to prepare purchase requisitions. The forms were scanned into the Lason document management system and accessed by SCS buyers to verify that authorizations prior to preparing a vendor PO. AMAS was advised that documentation in the Lason system was not consistently updated to include all authorized staff. When a buyer was not able to find the appropriate authorization form in Lason, the affected purchase requisition was returned to the department for verification, and the timeline for completing the purchase transaction was extended.

We also noted that signature authorization forms included the employee name, and signature sample. However, the dollar limits for purchase transactions were not included on the form.

Accurate and complete purchase authorization forms would assist SCS buyers with completing purchases timely and in accordance with University policy.

Management Corrective Actions:

SCS management and Medical Center Financial Services will consider:

1. Expediting the update of departmental signature authorizations when buyers discover that the information on file is not accurate.

2. Modifying the signature authorization template and/or related electronic files to include a dollar limit for purchase transactions and/or other restrictions on an end user's authority to requisition goods and materials.

E. **Electronic Purchase Requisitions**

Certain departments have continued to use a manual Form 390 to request purchase transactions rather than using the MediClick system. The manual Form 390 takes longer to process, resulting in delays in the purchasing process.

Although SCS staff have been promoting the use of MediClick since it was implemented in 2008, certain departments have continued to use a manual Form 390, rather than the electronic purchase requisition to initiate purchase transactions. There were several contributing factors:

- Form 390 can be downloaded from the internet, but it cannot be completed on-line and printed for department files.

- Certain types of purchase requisitions, such as capital equipment, require multiple approvals. Electronic approvals were not available in MediClick.

When manual 390 Forms are submitted to SCS buyers, the information must be manually entered into MediClick, using additional staff resources. Routing of manual requisitions for approval extends the time needed to process transactions.

Management Corrective Actions:

SCS management will:

1. Continue to promote the use of electronic purchase requisitions through department outreach.

2. Request MediClick system enhancements, such as online electronic approvals that will result in increased use of the system by departments.

3. Develop a customer satisfaction survey to identify system enhancements that would increase departmental use of MediClick.

Medical Center Contracting Processes
Audit Management Advisory Services Project #2010-39
Purchase Document Review Summary

PO #	TYPE	Vendor	Product/Service	Date	Amount	Requisition/ PO	Contract (A)	Best Price Analysis	RFP/ Vendor bids	Right to Audit Clause
CA4017	Regular	AGFA Corp	Radiology system software - conversion of an operating lease to a capital lease	5/8/09	$450,000	♦	♦	N/A	N/A	N/A
87170	Regular	Guidant Sales Corp	Novation Contract - pacemakers and related medical supplies (1)	6/26/09	$205,682	♦	♦	♦	♦	N/A
CA3031	Regular	Jeskell	IBM server equipment (2)	10/1/08	$658,054	♦	○	○	♦	N/A
CA5082	Regular	Olympus America, Inc.	Novation Contract - endoscopy equipment (1)	7/7/09	$298,747	♦	♦	♦	♦	N/A
BL5083	Blanket	Chatfield Air Ambulance	Ground and air transportation for the liver transplant program	11/13/08	$250,000	♦	○	○	○	N/A
BL4193	Blanket	Chinn & Louie LLC	Services to obtain additional Medicare reimbursement (3)	8/5/08	$2,517,778	♦	♦	N/A	○	N/A
BL5095	Blanket	Focus Technologies	Laboratory tests	11/17/08	$300,000	♦	○	○	○	N/A
BL4352	Blanket	Ikon Management Services	UCOP Contract - lease for copier services	6/26/09	$2,275,979	♦	♦	N/A	N/A	♦
CA7030	Regular	Nuance Communications	Sole source purchase - Dragon software and maintenance	2/12/09	$161,831	♦	♦	○	N/A	○
BL4158	Blanket	Olympus America, Inc.	Novation contract for medical equipment rental (1)	8/15/08	$190,053	♦	♦	♦	♦	N/A

♦ = Document(s) Reviewed

○ = Document(s) Not Prepared or on file

(A) The buyers decided whether a formal contract is needed based on professional judgment and other criteria. The absence of a contract did not necessarily indicate an audit deficiency, but could identify an opportunity for cost savings.

(1) Novation has been approved by UC General Counsel as having best price analysis and vendor bid process that are consistent with UC requirements.

(2) UCOP contract #900/OP/080 was the basis for this PO. However, it was not referenced in the contract file.

(3) The service agreement in the contract file was dated in 2001 and referenced a review of 1996 cost report regulations. The service agreement terms were outdated because the most current PO referenced a review of 1998 and 1999 cost report regulations

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Purchase Document Review Summary

PO #	TYPE	Vendor	Product/Service	Date	Amount	Requisition/ PO	Contract (A)	Best Price Analysis	RFP/ Vendor bids	Right to Audit Clause
BL7517	Blanket	Bayer Corp	Hemophilia Factor kogenate	11/24/09	$500,000	♦	O	N/A	N/A	N/A
BL4306	Blanket	International Medical Care	Arabic translation & marketing	6/16/09	$288,000	♦	♦	O	O	O
BL3590	Blanket	John Carey Construction	Kitchenette Construction (4)	6/18/09	$549,683	♦	♦	♦	♦	N/A
BL3440	Blanket	K.D. Stahl Construction	Convey Court remodel (4)	8/7/09	$476,492	♦	♦	♦	♦	N/A
92694	Regular	Medtronic Interventional	Novation contract - cardiac devices	8/4/09	$593,092	♦	♦	♦	♦	N/A
76038	Regular	Organ Recovery Systems	Kidney perfusion kits	4/19/09	$903,930	♦	O	O	O	N/A
BL4146	Blanket	Pacific Ambulance	Patient transport	8/11/08	$1,000,000	♦	♦	♦	♦	O

♦ = Document(s) Reviewed

O = Document(s) Not Prepared or on file

(4) Contracts were negotiated by campus Facilities Design and Construction based on UCSD contracting policies.