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REPORT: PRELIMINARY RISK ANALYSIS OF CONTRACTS

January 2004

7050-9-4-5 (CRS)



Canada 

NOTICE OF CAVEAT TO THE READER

This risk assessment was conducted as a special project and was not included in the annual Chief Review Services Work Plan. The review conclusions do not have the weight of an audit or formal evaluation. While sufficient to enable the development of recommendations for consideration by management, the assessments provided and conclusions rendered, are not based on the rigorous inquiry or evidence required of an audit or program evaluation. Accordingly, they are not represented as such.

It should also be noted that the review is not intended to assess the performance of contractors; rather it is an internal review of processes and practices within the DND/CF. Contractors have not been interviewed or otherwise asked to provide comment or feedback.



SYNOPSIS

This report presents a description and first application of a risk analysis methodology developed by the Chief Review Services (CRS) addressing service contracting within the Department of National Defence. The analysis was performed at the direction of the Deputy Minister following difficulties experienced with certain large operations and maintenance contracts. The principal objective was to design and apply a systematic methodology to anticipate other contracts which may be at risk. The methodology is intended for ongoing use by management – CRS work continues to extend the analysis to additional aspects of contracting and expenditure management.

The Analysis: *This analysis began with a total population of over 12,000 active DND contracts let by Public Works Government Services Canada (PWGSC), with total obligations of almost \$10B. Selection criteria were then applied on a systematic basis to successively isolate those contracts that can be characterized as demonstrating higher-risk attributes. Initial, macro-level selection criteria, included, for example, a \$1M materiality limit which reduced the contract population by 11,454, but retained 90 per cent of the total monetary value. Ultimately, 258 service contracts, having a total value of \$4.4B, were selected. Subsequently, risk scores were assigned to contracts based on more detailed criteria such as: sole sourcing; the number of amendments; and the results of available audits performed by Consulting and Audit Canada. The application of the selection criteria and the scoring exercise led to the identification of the “Top 25 Higher-Risk Contracts” listed at Annex F to this report. Also noteworthy is Annex D, which lists 22 NDHQ-managed service contracts which were considered to be at higher risk due solely to their having a value over \$50M.*

During the development of the analysis methodology, particular attention was given to 24 information management/technology service contract files, having a total value of \$206M. Contract files were examined to identify a variety of characteristics, including, but not limited to: overspending; the sufficiency of definition of deliverables; linkages between deliverables and payments; the number of subcontractors; and amendments as a percentage of original contract value. Four were flagged for a closer look (details are provided beginning at page 13 of the report) – management has subsequently implemented appropriate risk mitigation strategies for three of these contracts, the fourth will receive additional audit attention.

Management & Control: *Prior internal audit reports have emphasized the importance of strong comptrollership, clear guidance, training, technological enablers and reliable information to facilitate improved monitoring and early warning systems. This becomes particularly important in those instances where front-line managers may have limited contract management experience due to recent devolution of resources or to new alternate delivery options. This risk assessment found that contract managers still do not have appropriate aggregate financial and non-financial information necessary to monitor and anticipate developing difficulties. There*



remain poor linkages between the Department's financial system and critical contracting information. Accordingly, managers are employing ad-hoc information systems and spreadsheets to monitor the 12,000 active PWGSC-let contracts in the Department. An upgrade to the Financial Management and Accounting System (FMAS) planned for September 2004, may resolve this problem for those procurements captured by FMAS. However, critical procurement information captured by the Canadian Forces Supply System Upgrade (CFSSU) and the Materiel Acquisition and Support Information System (MASIS) does not migrate to FMAS – only the commitment and expenditure data. At present, the Department is challenged to conduct macro-level monitoring of the status of contracts, including emerging risks. For example, we noted \$1.6B in vendor payments, for 2002/03, for which no commitments had been established in the FMAS. ADM(Fin CS) is pursuing the recommended measures to improve commitment accounting and control.

The principal vehicle intended to provide better information tools for contract managers is the Materiel Acquisition and Support Information System (MASIS) – MASIS was to include financial information with contractual data. However, rationalization of the capital program has deferred the progress of this System. Accordingly, the CRS team's ability to use electronic filters to flag higher-risk contracts was only possible through the use of the PWGSC contract database. (We cannot attest to the accuracy of the content of the PWGSC system but will continue to perform analysis to reconcile the content of this database with information available within DND.) Although interfaces with this PWGSC database are, at this time, a low priority for the MASIS project, ADM(IM) plans to examine the potential linkages. A solution will be necessary to enable risk analysis of contracts being managed by those staff who will not have access to MASIS. Until MASIS is fully implemented, ADM(Mat) intends to undertake downloads of the PWGSC database.

The Way Ahead: Regarding the higher-risk service contracts identified in this report, responsible Groups have fully responded to the CRS request for additional information, including risk mitigation strategies. This has involved the completion of summary and detailed templates (see Annexes J and K). CRS is analyzing this information for reporting under separate cover. Additionally, follow-on work is underway to assess higher-risk goods contracts, with targeted completion for Spring 2004. An analysis of higher-risk medical contracts is also being finalized. Ultimately, a recommendation will be made respecting those individual contracts which warrant detailed audit attention.

Management Action Plan: Key improvements to be implemented in response to the recommendations of this analysis, include the following:

- ADM(Fin CS) develop standardized conventions for establishing commitments which will facilitate roll-up of expenditures to applicable contracts;
- ADM(Mat) to conduct routine downloads and analysis of the PWGSC contract database; and



- *ADM(IM) to ensure that linkages between MASIS and the PWGSC contract database enable the identification of emerging risks with respect to individual contracts.*

Further details on the management action plans appear at page 3 of this report.

Some Key Attributes of the Analyzed Population of Contracts:

- At August 2003, the Department had contractual obligations amounting to about \$10B and 12,000 active contracts let by PWGSC.
- For Fiscal Year 2002/03, 36,000 vendors were involved in the delivery of \$7.7B in contract expenditures. Fifty-eight (58) vendors were paid more than \$20M annually.
- Operating & Maintenance (O&M) contract expenditures amounted to \$4.4B, with 463 vendors receiving payments in excess of \$1M for 2002/03 – representing 78 per cent of the total business – 67 firms account for 52% of the \$4.4B.
- For 258 PWGSC-let centrally-managed O&M contracts, 81 per cent of the total value is represented by 45 contracts having a value greater than \$10M – 22 have a value greater than \$50M. Forty-four per cent (44%) of the 258 contracts were sole-sourced.
- Twenty-eight (28) of the 258 contracts are likely to be subject to audit by Consulting and Audit Canada.
- Four hundred and forty-nine (449) service contracts were let directly by DND, for a total value of \$77M – less than 1 per cent of the total contract population.



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RESULTS IN BRIEF

INTRODUCTION & BACKGROUND

In 2003, CRS examined three high-value operations and maintenance contracts. The work was driven by specific requests from senior management. Additionally, prior internal audit reports have raised warning flags regarding the sufficiency of information available for monitoring, quality assurance, commitment control and early warning mechanisms with respect to service contracting. With the advent of electronic business solutions in the Department's enterprise information systems, we observed that *Smart Controls* are required to take advantage of technology in order to assist in the identification of high-risk situations. We have also observed that devolved resources and alternate service delivery have resulted in organizations managing contracts without necessarily having the benefit of sufficient experience and expertise.

To anticipate other contracts in the Department that may be at risk, the DM directed CRS, in August 2003, to undertake a broad risk analysis of contracting.

OVERALL ASSESSMENT OF CONTRACTING INFORMATION & MONITORING

It is our view that managers do not have appropriate information to anticipate emerging risks with respect to contracts. There are poor linkages between contracts and corresponding expenditures in the Department's finance system (Financial Management and Accounting System (FMAS)). We observed significant payments to vendors without matching commitments in FMAS. Contract managers are routinely employing ad hoc databases and spreadsheets to monitor the 12,000 active contracts let by PWGSC for the Department. In our view the analysis presented in this report illustrates the utility of routine monitoring and analysis of the population of departmental contracts.

Initiatives to provide better information tools for contract managers are to be addressed by the Materiel Acquisition and Support Information System (MASIS). A Complex Contracting (CC) module will combine financial information from FMAS with procurement information associated with active contracts. However, there have been delays in funding MASIS sufficiently to deliver this capability – at the time of this analysis work, it was not expected that this would be resolved before the current calendar year. We also remain concerned that not all procurement information will be included in the CC module to identify high-risk contracts. The CRS study team's ability to use *electronic filters* to establish a view of higher-risk contracts was only possible through the use of the Public Works Government Services Canada (PWGSC) contract database, the Automated Business Environment (ABE).



Currently the interface between the MASIS CC module and ABE is a low priority for the Department. As well, we noted that up to 40 per cent of the contracts in the Department will be administered by contract managers outside of the Materiel Group and who will not have access to MASIS. This situation will improve once MASIS is rolled out to all maintenance organizations across the DND/CF. However, there will remain a number of contract managers that will not have access to MASIS. Procurement information with respect to goods is also available in the Canadian Forces Supply System Upgrade (CFSSU) application with an interface with FMAS. Although, MASIS is also interfaced with FMAS, only the financial information migrates from MASIS and CFSSU to FMAS – not the procurement information. Within FMAS there is a seldom-used materiel management module that could be utilized to capture procurement information. We are concerned that there is no single enterprise system that can provide critical procurement information to identify higher-risk contracts.

RECOMMENDATIONS

It is recommended that the following actions be taken:

- ADM(Fin CS) develop standardized commitment recording conventions to better ensure a clear linkage between expenditures and contracts, so as to enable expenditure reconciliation to pertinent contract ceilings;
- ADM(Fin CS) take measures to improve commitment accounting through the identification/monitoring of those Level 1s that are making significant expenditures to vendors without commitments;
- Pending full implementation of MASIS, ADM(Mat), as the lead Level 1 for contract management, conduct routine downloads from the PWGSC ABE and apply appropriate automated criteria to detect contracts becoming at high risk – this will require the further development of a performance measurement regime for contract management;
- ADM(IM) ensure that PMO MASIS develops linkages with PWGSC ABE to enable the identification of high risk contracts; and,
- ADM(Mat) take the lead in coordinating the preparation of status reports, including risks and mitigation strategies, for the contracts listed in Annexes D and F, as well as those identified at page 13 of this report. CRS has provided draft summary and detailed templates at Annexes J and K respectively. The contracts listed at page 13 are a priority.



MANAGEMENT ACTION PLAN

Ser	CRS Recommendation	OPI	Management Action
1	ADM(Fin CS) develop and promulgate standardized commitment conventions which will allow consistent linkages between expenditures and corresponding contracts – to enable expenditure reconciliation with contract ceilings.	C Fin O	Standardized commitment conventions will be developed and promulgated which will allow consistent linkages between expenditures and corresponding contracts. A commitment field will be made mandatory once the impact on feeder systems is fully assessed and tested as part of the SAP 4.7 implementation.
2	ADM(Fin CS) identify/monitor those Level 1s making significant expenditures to vendors without commitments having been established.	C Fin O	C Fin O has already instituted active monitoring through FMAS and will enhance both the procedures and the monitoring capability through Director of Budget.
3	ADM(Mat), as the lead Level 1 for contract management, conduct routine downloads of the PWGSC ABE and apply appropriate automated criteria to determine higher-risk contracts as an interim measure until MASIS is fully implemented. This can build on the analysis presented in this report.	DMASP 4 DC Pol	To address the short-term requirement for this level of contract management, the ADM(Mat) Group will request, and review, quarterly ABE downloads for high-risk contracts, for all Level 1 organizations. The capability to identify high-risk contracts will be enabled in MASIS as soon as possible for ADM(Mat) initiated procurement. For non-ADM(Mat) initiated procurements, a separate reporting scheme will have to be developed that will likely be based on PWGSC-generated information.
4	ADM(IM) ensure that PMO MASIS develops linkages with PWGSC ABE, to support early warning with respect to higher-risk contracts.	PM MASIS	COS ADM(IM) has directed PM MASIS to take action as soon as possible and to advise when completed.

Note: CRS has been provided completed templates (as per report Annexes J and K) for all contracts as requested.

OBJECTIVES, SCOPE & METHODOLOGY

OBJECTIVES

This risk analysis and assessment were directed by the DM. The purpose was to develop a methodology and undertake an analysis to identify Operations and Maintenance (O&M) contracts that demonstrate warning signs consistent with high risk.

SCOPE

The scope of the risk assessment was limited to O&M contracts in the Department. In view of recent CRS reviews/audits of O&M contracts, service contracts were considered to be higher risk than those for goods acquired as part of the capital acquisition program. Risks associated with O&M contracts have been identified in the following recent CRS reports:

- Audit of Contracting for Advertising & Related Services (March 2003);
- Audit of Contracting for Professional & Technical Services (November 2001); and
- Assurance Audit of the Management of Local Funds (Drafts August 2003 and January 2004).

METHODOLOGY

The assessment of higher-risk contracts commenced in mid August 2003. Below is the four-step methodology followed:

- Step 1 – Development of selection criteria (high risk) in consultation with PWGSC/Consulting Audit Canada (see Annex A);
- Step 2 – Application of criteria to information contained in contract data bases and FMAS contract expenditure history;
- Step 3 – Interviews with DND contract managers to confirm a directed sample of contracts identified through data analysis;
and
- Step 4 – Development of a listing of contracts demonstrating risk, based on steps 1 to 3.



OBSERVATIONS AND FINDINGS

This section of the report examines in detail:

- the number of vendors that provided goods and services to the Department;
- the number and types of active contracts in the Department;
- a first level of criteria to select higher-risk contracts (global filter);
- a second level of automated contract risk criteria;
- a third level of judgmental risk assessment filters;
- observations gleaned through a directed sample of contracts; and
- assessment of other systemic issues.

THE VENDOR UNIVERSE

Currently, the Department has contractual undertakings with approximately 36,000 vendors. As indicated in Table 1, since 1998/99, annual contract expenditures have grown from \$5.7B to \$7.7 B – an increase of 35 per cent. This increase is due primarily to alternate service delivery initiatives entered into by the Department for certain functions that were previously performed by the military or public servants.

	98/99	99/00	00/01	01/02	02/03
Vendor Co. > \$20M	34	42	47	56	58
Sum of pymts to Vendor Co. > \$20M	\$2.4B	\$3.2B	\$4.0B	\$4.5B	\$4.3B
% of Total DND pymts to Vendors	43%	48%	56%	56%	57%
Total DND pymts to Vendors	\$5.7B	\$6.8B	\$7.2B	\$8.0B	\$7.7B

Table 1 – Vendor Trend Analysis



Vendor Concentration: Regarding the vendor concentration for goods and services, Table 1 indicates a diversification trend over five years. Currently, 58 vendors are each paid more than \$20M per year, whereas only 34 vendors were contracted for this value of services and goods five years ago. Although the Department’s contractual commitments have increased over the last five years, there are more vendors in the private sector providing the high-dollar value services.

OPERATIONS AND MAINTENANCE (O&M) CONTRACT EXPENDITURES

With respect to O&M contracts, fiscal year 2002/03 expenditures amounted to \$4.4B – (military/civilian pay and capital acquisition not included). Table 2 stratifies the number of vendors with high and low value contracts. The stratification excludes credit card payments to banks and one-time vendors. We determined that there were only 463 vendors that received payments more than \$1M – representing 78 per cent of the total business. It is possible to limit vendor analysis to 67 firms and still examine 52 per cent of O&M contract expenditures. Annex B lists the top ten vendors.

Total Payment Range	# of Vendors	Total Payments	% Value
>= 100 Millions	3	\$423,236,791.92	10.25
>= 20 Millions to < 100 Millions	31	\$1,260,388,344.52	30.51
>= 10 Millions to < 20 Millions	33	\$451,077,458.38	10.92
>= 1 Million to < 10 Millions	396	\$1,107,334,045.42	26.81
< 1 Million	35,250	\$888,360,916.33	21.51
SUB / TOTAL	35,713	\$4,130,397,556.57	100.00

Excluded		
BANK OF MONTREAL	1	\$115,724,968.70
AMEX BANK	1	\$112,057,004.72
ONETIME	1	\$88,796,226.65
VENDOR NAME is blank	1	\$42,083.34
SUB / TOTAL		\$316,620,283.41
Total General	35,717	\$4,447,017,839.98

Table 2 – Vendor Stratification – O&M FY 2002/03



CONTRACT UNIVERSE

As of August 2003, for those contracts let by PWGSC, the Department had contractual obligations amounting to more than \$10B. This amount does not include those contracts initiated before year 2000, or the contract option years that have not yet been exercised. Our primary source for current information was a DND extract from the PWGSC ABE information system. This ABE database included approximately 50,000 DND contracts let by PWGSC of which approximately 16,000 were still active. Table 3 outlines the breakout between active contracts, standing offers, purchase orders and agreements. A definition of the types of contracts may be found in Annex C to this report.

Type of Contract	Contract Value	No of Contracts
National Individual Standing Offers (NISOs)	\$152,216,630	199
Regional Individual Standing Offers (RISOs)	\$523,919,340	3,499
Contract	\$8,454,405,895	8,433
Contract (Non-Commercial Goods & Services Only)	\$100,783,489	6
Formal Agreements	\$886,940,278	9
Purchase Order (Low Dollar Value)	\$65,519,916	3,023
Purchase Order (Electronic and Telephone)	\$5,632,038	190
Supply Arrangement	\$134,501,754	65
DND Managed Contracts DC Pol	\$76,576,739	449
Total	\$10,400,496,069	15,873

Table 3 – DND Contracts as of August 2003

Information regarding the contracts where DND is the contracting authority was provided by the Director of Contract Policy (DC Pol). These 449 service contracts amount to \$77M and represent less than 1 per cent of the total contract population value. Given the relatively insignificant materiality of the DND-managed contracts, our focus was on those contracts that were tendered through PWGSC.

Regional Individual Standing Offers (RISOs) were also excluded from the initial risk assessment due to their relatively low unit value. On average, the ceiling of a RISO would be \$150K, with a number of lower value call-ups administered by CF bases/wings in the five regions of Canada. The higher unit value National Individual Standing Offers (NISOs) managed by NDHQ were of greater concern in this analysis and will be addressed in more detail in a subsequent report. This initial risk analysis was limited to approximately 12,000 contracts let by PWGSC on behalf of DND and amounting to approximately \$9.8B.



GLOBAL CONTRACT FILTERS

In order to isolate higher-risk contracts, global filters, summarized in Table 4, were applied to the PWGSC database to reduce the population to 258 contracts. A schematic diagram on page 9 of this report provides a visual portrayal of the rationale and the caveats for each of the global filters listed below:

- Active DND contracts;
- Contracts with significant material value;
- Service contracts; and
- Contracts managed by NDHQ.

	Type of Filter			
	Active Contracts	Materiality >\$1M	Service Contracts	NDHQ Contracts
No of Contracts	12,168	714	334	258
Value of Contracts	\$9.8B	\$8.8B	\$4.7B	\$4.4B

Table 4 – High Risk Global Contract Filters

Materiality: Recent problematic contracts that have come to the attention of senior management have ranged in value from \$76M to over \$400M. It was decided that a conservative filter would be a \$1M threshold – reducing the population to 714 contracts. This first filter eliminates 11,454 contracts (93 per cent), but retains 90 per cent of the dollar value of the total contract population.

Service Contracts: To date, there has been relatively less apparent risk associated with contracts for goods. We have observed that the scope of work for service contracts can be underestimated and the verification of services rendered can be more difficult, particularly for maintenance contracts. By eliminating goods contracts with the second filter, the population of contracts greater than \$1M in value was reduced from 714 to 334 contracts. The value of these service contracts amounts to \$4.7B. A risk analysis/assessment of goods contracts will be the subject of a separate report.

NDHQ-Managed Contracts: Those contracts that provide services for defence establishments across the country, but are managed centrally by NDHQ, have proven to be more difficult to manage. The third global contract filter isolated those service contracts greater than \$1M that were initiated by NDHQ organizations and resulted in 258 contracts that amount to \$4.4B.

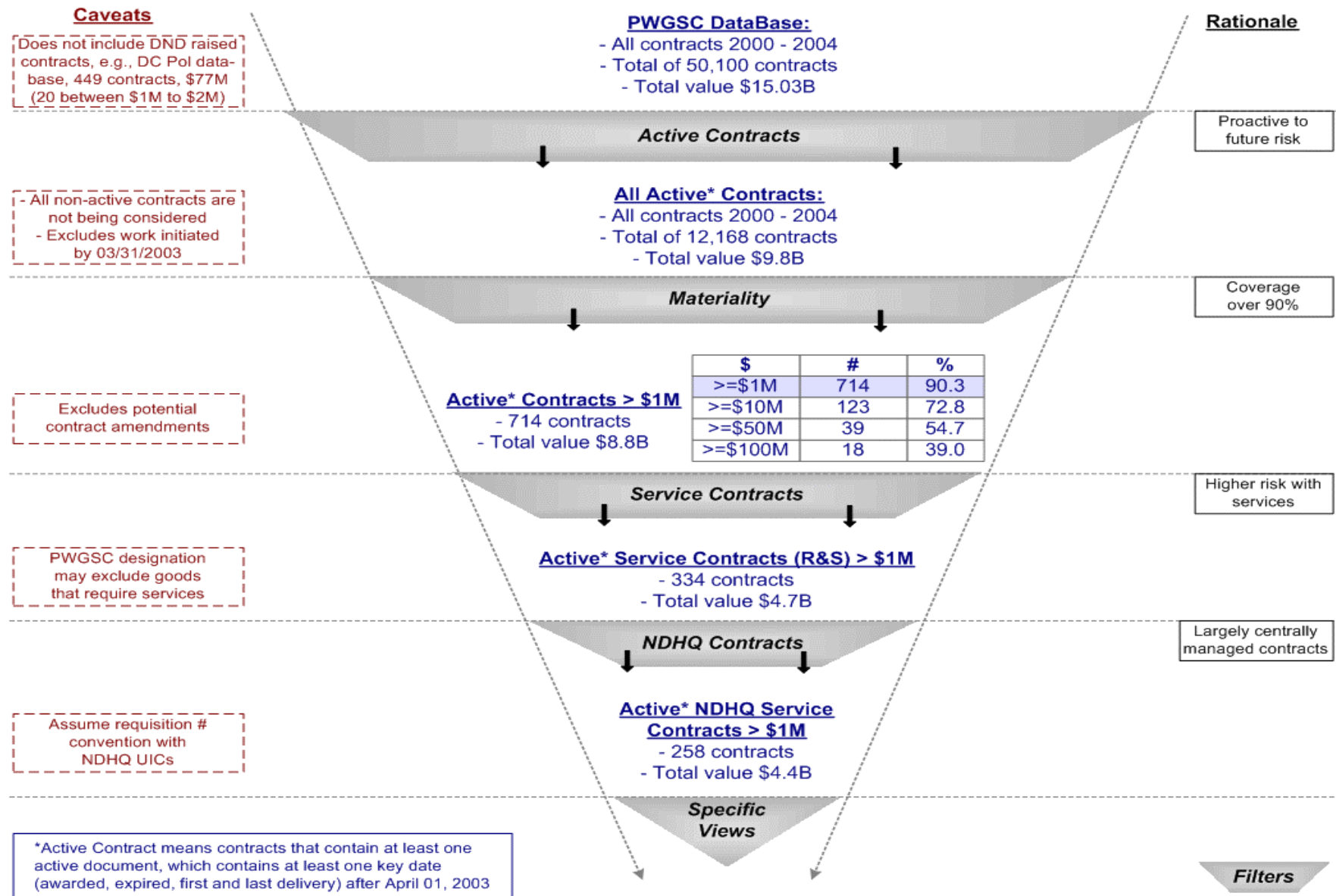


Figure 1 Global Contract Filters



Once the three global filters were applied, the 258 NDHQ-managed contracts were stratified by dollar value. As portrayed in Table 5, 81 per cent of the total contract dollar value is represented by the 45 contracts that are greater than \$10M. Annex D lists those 22 contracts greater than \$50M. This filter methodology resulted in the selection of all three service contracts that have been the object of concern by senior management.

Range (\$M)	Contracts	Value (\$M)	Percent
>=\$100M	13	\$ 2,529	57.9%
\$50M to \$100M	9	696	15.9%
\$20M to \$50M	9	305	7.0%
\$10M to \$20M	14	196	4.5%
\$1M to \$10M	213	\$ 641	14.7%
Total	258	\$ 4,367	100.0%

OTHER RISK-BASED SELECTION CRITERIA

Table 5 – Dollar Value of NDHQ Managed Service Contracts

- **Automated Criteria:** To determine which of the 258 centrally-managed O&M contracts greater than \$1M in value were at highest risk, the eight automated criteria below were applied with weighted scores, as outlined in Annex E. Most of this information was available on the PWGSC ABE database. The top 25 contracts with the highest risk score are listed in Annex F and will be the subject of further/manual review by CRS.
 - **Materiality:** Risks associated with higher-value contracts were assessed to have a greater impact. The amended contract value was taken from the PWGSC ABE database.
 - **Contract Amendments:** An amendment greater than 30 per cent of the contract value was considered significant, particularly if the amended value of the contract was greater than the original requisition amount. For the 258 NDHQ-managed service contracts, the average increase in contract value was 11.4 per cent, not including the exercise of option years.
 - **Tender Process:** Although contracts can still be poorly managed if they are awarded through the competitive process, there is an additional element of risk if the Department has limited the contract award to a single contractor. Of the 258 NDHQ-managed O&M contracts, we found that 115 contracts (44 per cent) were sole-sourced – a total contract value of \$2.2B (50 per cent).
 - **Type of Commodity:** Certain contracted services such as information system maintenance, medical services, advertising and repair and overhaul, were scored as higher risk. Only 56 of the contracts were not in the high-risk category. The most significant commodity was the 113 repair and overhaul contracts.



- **Method of Payment:** The most common methods of payment are milestone payments, payment upon delivery, and progress claims. However 16 per cent of the NDHQ-managed O&M contracts have ‘multiple’ methods of payment. The ‘multiple payment’ method was scored as a higher risk.
- **Higher Risk Organizations:** There are some Level 1 organizations that may be relatively less experienced in managing contracts and have only recently explored contracted services as alternate means of service delivery. As well, we rated organizations that initiate common-user contracts as higher risk, due to the decentralized nature of contracted services. Higher risk organizations were considered to be ADM(HR-Mil)/CFMG, ADM(IM), ADM(Mat)/DCPS, ADM(S&T) and OCIPEP (note that OCIPEP is no longer part of DND).
- **Consulting Audit Canada (CAC):** A database of 131 CAC cost audits was accessed. We were able to identify some vendors that required significant adjustments to claims and profit. Vendors for which CAC commented on the adequacy of cost records were also given a high-risk score – see Annex G. As well, a series of expenditure analysis tests were done to examine the source, frequency and size of payments/commitments to determine higher risk vendors.
- **Over-consumption:** From our FMAS data analysis, we were able to identify some contracts for which the ceiling price was exceeded or individual commitments were exceeded. In the absence of standard commitment numbering conventions, only 130 FMAS commitments could be matched to the 258 O&M contract numbers.
- **Judgmental Criteria:** Once the higher risk contracts were identified through electronic criteria, the next step will be to apply the 15 judgmental criteria listed below through an examination of contract information provided in risk assessment templates to be completed by Level 1 contract managers. Contract summary and detailed risk assessment templates are shown at Annexes J and K. The maximum risk score that will be possible using the judgmental criteria will be 15 – one point for each criterion not met:
 1. Contract managers workload was reasonable. (The average number of contracts per manager was 14);
 2. A competitive process was the basis of the contract award;
 3. Less than four contract amendments were necessary;
 4. Contract escalation was less than 30 per cent - not including option years;



5. The deliverables were within the contract scope of work;
6. Most of the work was performed by the prime contractor;
7. The contracted services were provided to one or two locations;
8. The contracted services were not a new alternate service delivery initiative;
9. Performance incentives related to the base amount of the contract;
10. The contract expenditures were within the ceiling price of the contract;
11. Commitment accounting practices were in place;
12. Terms of payment did not include a cost plus arrangement;
13. There was sufficient supporting documentation to verify the receipt of goods and services;
14. The contract provided for linkage of payments to deliverables; and
15. The contract statement of work clearly defined the deliverable.

DIRECTED SAMPLE – OBSERVATIONS

Initial Directed Sample: Prior to the full development of the electronic risk criteria, the study team examined the contract files for 24 information management/technology services contract files – a total contract value of \$206M. Four of the contracts listed in Table 6 on the following page, were found to be candidates for a closer look. With the exception of serial 1, we found that management was putting in place improved controls to mitigate the risk – some of these improved controls were due to the CRS work. Our concerns regarding the implementation of new controls for the contract at serial 1, will be addressed as part of the ongoing audit on similar IM/IT maintenance contracts.



Section 20(1) c) of AIA 3rd Party

Ser	Contract Number	OPI	Dollar Value	Type of Service	Initial Risks Identified by CRS	Management Risk Mitigation Action
1	..... .....	ADM(Mat)/ DGEPS/ DCPS	\$18M	..... ..... .....	<ul style="list-style-type: none"> * Contract expired in June 2002 with 96 per cent escalation to \$17.6M. * Insufficient evidence to support payment for software upgrade deliverables. 	<ul style="list-style-type: none"> * June 2003 ADM(IM) developed improved controls – 10% sampling of invoices, monthly reporting, work order reconciliation. * Closer expenditure tracking through FMAS.
2	..... .....	ADM(I&E)/ DIECS	\$23M	..... .....	<ul style="list-style-type: none"> * Removal of holdback clauses. * Lack of verification of off-site services. * Cost increase of deliverables. 	<ul style="list-style-type: none"> * Exercise of warranty provisions. * Co-location of consultants by December 2003. * Incorporation of performance incentives in contract renewal.
3	..... ..... (Note, DCPS staff requested that CRS examine this contract.)	ADM(Mat)/ DGEPS/ DCPS	\$47M	..... ..... ..... .....	<ul style="list-style-type: none"> * Cost escalation from \$35M to a forecast of \$52M over three years (48 per cent). * Employer/employee relationships. * Poorly defined job descriptions that appeared inflated. 	<ul style="list-style-type: none"> * DCPS requirement for HR staffing plan for long term consultants. * Distribution of work to three other vendors in new contract series with more detailed scope of work/ improved definition of consultant qualifications. * Higher per diem rate in new contracts will result in a one-time only cost of \$1.7M in the transition from the current contract.
4	..... .....	ADM(Mat)/ DGEPS/ DCPS	\$10M	..... ..... ..... .....	<ul style="list-style-type: none"> * Forecasted cost escalation of 15 per cent once the final option year of the contract is exercised – \$13.9M vs a CRS estimate of \$12.1M. 	<ul style="list-style-type: none"> * DCPS requirement for detailed job description and HR staffing plan will mitigate the cost escalation.

Table 6 Results of Directed Sample of Information Management/Technology Services Contracts

OTHER SYSTEMIC ISSUES

In reviewing the 24 IM/IT contracts we noted a number of systemic issues of concern:

- Commitment numbers in FMAS often bore no resemblance to the contract number or client reference number. This was the case for 15 of the 24 contracts in the directed sample. Without clear linkages between a contract ceiling and individual commitments/expenditures, it is difficult to forecast the potential for overspending on a contract. Although FMAS does prescribe a commitment numbering convention, our detailed analysis of fiscal year 2002/03 indicated a lack of compliance. (See Annex L.) Director General Finance and Accounting staff believe this issue could be resolved by taking advantage the seldom-used materiel module in FMAS to capture procurement information.
- Given the numerous commitments assigned to each contract, it was common practice for contract managers to reconcile total expenditures on a contract on spreadsheets outside the enterprise information systems.
- A significant number of payments were made to vendors without commitments having been established in FMAS – \$1.6B in 2002/03. The top 27 organizations, in this respect, are listed in Annex H.
- Contract managers had created their own information systems to manage contracts. These systems did not provide sufficient information to provide early warning of contracts becoming at high-risk.
- Although MASIS delivered a Complex Contracting (CC) module one year ago, there were significant deficiencies that have delayed full implementation until January 2004. Four hundred and fifty MASIS users in NDHQ received their training by October 2003, but there remains a training backlog of 300 personnel. The procurement information will not be input until technical difficulties are resolved. Funding delays in this gateway project have delayed the resolution of the CC deficiencies. It is expected that the CC module will provide six of the nine CRS automated criteria listed on Annex 11 of this report. The three exceptions will be FMAS over-consumption, methods of payment, and high-risk vendors identified by CAC audits. Additional MASIS programming could accommodate two of these exceptions. At present, linkage to the PWGSC ABE is a low priority and all of the necessary high-risk contract indicators may not be incorporated. Annex I portrays the integration of financial and procurement information in the MASIS CC module.



- There will be a significant number of contract managers outside of the Materiel Group that may not have access to MASIS to conduct the risk analysis of procurement information until MASIS is fully rolled out. We estimate 4,900 of the 12,000 active contracts (\$1.2B in value) are managed by Level 1s other than ADM(Mat). At this time most of CC procurement information is being entered by Navy staff to accommodate the rollout of the Navy MASIS module.

RECOMMENDATIONS

- ADM(Mat) and ADM(IM) complete Annex J contract summary risk template for the IM service contracts listed in Table 6, page 13 (CRS to assist).
- The identified Level 1s prepare, and provide to CRS, through ADM(Mat), a completed summary template (Annex J) to be followed by more detailed templates (Annex K) for the top 25 high-risk service contracts listed in Annex F and the 22 high-value service contracts listed in Annex D and not listed in Annex F.
- ADM(Fin CS)
 - Develop and promulgate standardized commitment conventions which will allow consistent linkages between expenditures and corresponding contracts - to enable expenditure reconciliation with contract ceilings; and
 - Take measures to identify/monitor those Level 1s making significant expenditures to vendors without commitments.
- ADM(Mat), as the lead Level 1 in contract management expertise, conduct routine downloads of the PWGSC ABE of DND contract and apply appropriate automated criteria to determine higher-risk contracts as an interim measure until MASIS is fully implemented. This can build on the analysis presented in this report.
- ADM(IM) ensure that PMO MASIS develops linkages with PWGSC ABE to support early warning with respect to higher-risk contracts.



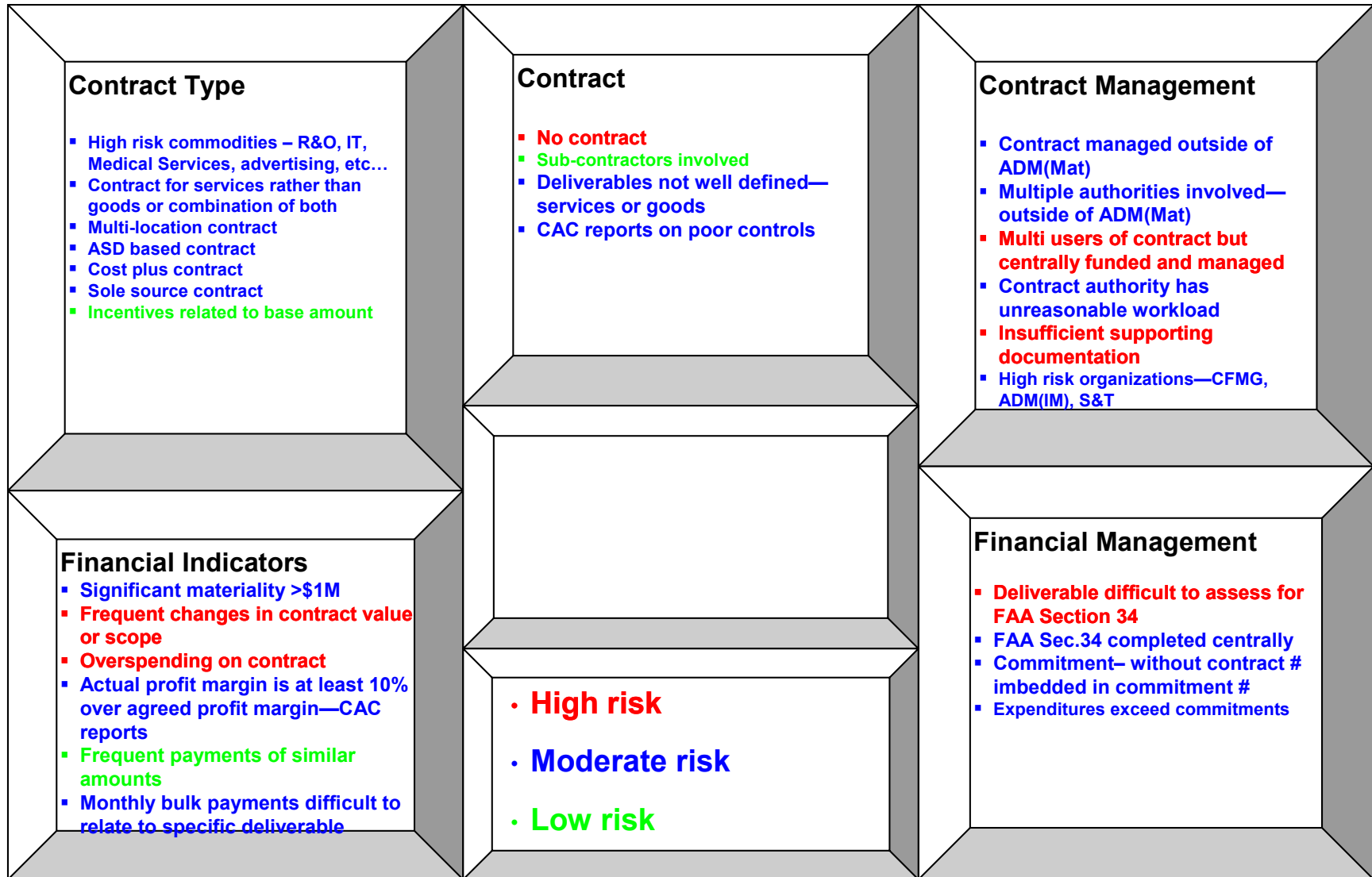
PROPOSED FOLLOW-ON WORK BY CRS

The detailed analysis will continue to be refined and extended to a series of reports that will include:

- A report on service contract risks and mitigation strategies associated with contracts listed at Annexes D and F and include –
 - Assessment of significant payments for which no commitment has been established,
 - Analysis of standing offers for which specified ceilings have been exceeded, and
- A report on goods contract risks and mitigation strategies; and
- A report on higher risk contract management centres.



ANNEX A – HIGH RISK CONTRACT CRITERIA



ANNEX B – FISCAL YEAR 2002/03 TOP TEN VENDORS – OPERATIONS AND MAINTENANCE

Vendor Name	Total Payments
ROYAL LEPAGE SERVICE	\$172,930,357
MONTREAL TRUST COMPANY OF CANADA	\$138,513,076
BOMBARDIER	\$111,793,359
SNC	\$99,491,613
FEDERAL RESERVE BANK NEW YORK	\$72,859,135
CANADIAN FORCES PERSONNEL SUPPORT	\$62,522,715
IMP AEROSPACE	\$61,066,390
SPAR LTD	\$61,058,365
US DEFENCE FINANCE AND ACCOUNTING S	\$60,404,363
MORRISON FINANCIAL SERVICES LIMITED	\$53,067,373
SubTotal	\$893,706,747

Excluded

BANK OF MONTREAL	\$115,724,969
AMEX BANK	\$112,057,005
ONETIME TEMPLATE	\$88,796,227
SubTotal	\$316,578,200
TOTAL	\$1,210,284,947

Note that excluded vendors were for acquisition card payments.



ANNEX C – CONTRACT DEFINITIONS

Contract	A formalized procurement event that includes a call-up on a Standing Offer.
Active Contract	Those contracts that have not past their expiry date are considered active.
Requisition	A requisition for goods or services can result in several contracts. In some cases we observed as many as 15 contracts resulting from a single requisition.
Standing Offer	<p>A procurement instrument to permit procurement of specified goods and services up to specified financial limits. There are three types:</p> <ul style="list-style-type: none"> ▪ Master Standing Offer for all government departments; ▪ National Individual Standing Offer for DND; and ▪ Regional Standing Offer – excluded due to low dollar value.
Umbrella Contract	A common use contract, which is used by a number of organizations, but for which payments are approved by one organization.
Purchase Order	A low value goods contracts with a local vendor.
Formal Agreement	Obligations with allies or other government departments.
Supply Arrangement	<p>Identification of qualified suppliers that results in a family of contracts. These also tend to lead to umbrella type contracts.</p>



ANNEX D – NDHQ – MANAGED SERVICE CONTRACTS GREATER THAN \$50M

Contract Number	Vendor Name	Contract Value	Type of Service	OPI
W0153-01FF70/001/ZH	Serco Facilities Management Inc	\$555,597,063	Property Management - Office Space	ADM(Mat)/DMSDP
W8485-98RH01/001/NX	Nasittuq Corporation	\$310,933,786	North Warning System	ADM(Mat)/DGAEPM
W8485-7-VA01/001/ZD	BOMBARDIER INC	\$292,861,267	NFTC Flying Training	ADM(Mat)/DGAEPM
W8485-9-AQ10/001/BX	Bombardier Inc. Aerospace,	\$256,225,000	CF18 Repair and Overhaul (Military)	ADM(Mat)/DGAEPM
W8475-00HG60/001/CSH	IMP Group Ltd - Aerospace Division	\$184,000,000	Cormorant Repair and Overhaul	ADM(Mat)/DGAEPM
W8485-03B008/001/BQ	IMP GROUP LIMITED	\$136,186,450	Sea King Repair and Overhaul	ADM(Mat)/DGAEPM
W8488-00AAZZ/001/ZH	ALNAV Platinum Group Inc.	\$132,720,000	Relocation Services	ADM(Mat)/J4-DGLOG
W8483-8-K106/001/SLE	VICKERS SHIPBUILDING & ENGR	\$121,256,551	Submarine Maintenance	ADM(Mat)/DGMEPM
W8488-00AAZZ/003/ZH	United Van Lines (Canada) Ltd.	\$116,130,000	Relocation Services	ADM(Mat)/J4-DGLOG
W2203-99CA02/001/SS	Med-Emerg International Inc.	\$108,917,036	Medical/Dental Clinic Services	ADM(HR)/CFMG
W8474-01BF31/001/ZZ	IBM Canada Ltd.	\$107,553,446	MASIS Systems Integration	ADM(IM)/PMO MASIS
W8486-02ZM01/001/NJ	General Dynamics Canada Ltd.	\$105,000,000	Land Tactical Command & Comms Sys	ADM(Mat)/DGGLEPM
W8485-0-PH01/001/BF	Air Canada	\$101,748,744	CC150 Air Bus Maintenance	ADM(Mat)/DGAEPM
W8484-7-AB09/001/EY	BCE Nexxia Inc.	\$99,531,086	Data Transmission Service	ADM(IM)
W8485-01QL01/001/BF	Standard Aero Limited	\$89,516,735	CC130, CP140 Engines Components	ADM(Mat)/DGAEPM
W8488-00AAZZ/002/ZH	ATLAS VAN LINES (CANADA) LTD	\$82,950,000	Relocation Services	ADM(Mat)/J4-DGLOG
W8483-01MD01/001/ML	SNC-Lavalin Defence Programs Inc.	\$78,110,000	Minor War Vessel Maintenance	ADM(Mat)/DGMEPM
W8484-9-0054/001/EW	Compaq Canada Incorporated	\$76,057,639	Automatic Data Processing Equipment	ADM(Mat)/DCPS
W8482-014F02/001/BQ	Raytheon Canada Limited/Raytheon	\$74,013,140	Navy Weapon Maintenance CIWS	ADM(Mat)/DGMEPM
W8482-6-9G04/001/BQ	Lockheed Martin Canada Inc.	\$73,261,543	Navy Combat SW Maintenance	ADM(Mat)/DGMEPM
W8476-5-GFLB/001/UA	GENERAL MOTORS OF CANADA	\$68,480,000	LAV Maintenance	ADM(Mat)/DGGLEPM
W8485-02KH66/001/BF	IMP Group Ltd - Aerospace Division	\$53,746,400	CP140 Aurora - Repair and Overhaul	ADM(Mat)/DGAEPM
W0153-01FF70/001/ZH	Total	\$3,224,795,886		

Note that the above table includes the three contracts which have been the object of recent concern on the part of DND senior management.



ANNEX E – ELECTRONIC HIGH-RISK CONTRACT SELECTION CRITERIA WEIGHTED SCORES

Section
20(1) c)
of AIA
3rd Party

Contract/ Criteria	Dollar Value	Overspent/ Amdts	Tender Process	Commodit	Method of Pay	CAC Problem	Over spent	High Risk Org
Score Weight	1.0>\$100M .75 >\$75M .20 >\$20M .10>\$10M 0.<=\$10M	1.0>30% 0.0<=30%	0.5 if sole sourced 0.0 if competed	0.75 if R&O, prof svcs or IM/IT maint	1.0 if multiple payments	1.0>10% Adjusted or other significant problems 1.0 for high risk payments	1.0 if payments exceeds commit ment	1.0 if High Risk Org
.....	\$444M 9 Yrs	\$176M	Sole Source	R&O	Multiple	Spares Pricing	No FMAS Match	DGMEPM No
.....	\$92M 3 Yrs	\$30M	Competed	Prof Svcs	Multiple	No	No FMAS Match	CFMG Yes
.....	\$76M 3 Yrs	\$28M	Competed	IM/IT Maint	Payment on delivery	Yes	No FMAS Match	DCPS Yes

High-risk selection criteria score weighting was rationalized with respect to three problematic service contracts listed above. Maximum score per contract is 8.25.

ANNEX F – TOP 25 HIGHER-RISK CONTRACTS – BASED ON ELECTRONIC RISK CRITERIA

Section
20(1) c)
of AIA
3rd Party

Ser	Contract Number	Vendor Name	Contract Value	Total Score	Type of Service	OPI
1	\$76,057,639	4.51	.....	ADM(Mat)/DCPS
2	\$8,078,500	4.33	.....	ADM(Mat)/DGMEPM
3	\$5,300,000	4.30	.....	ADM(Mat)/DGAEPM
4	\$5,151,595	4.30	.....	ADM(Mat)/DGMEPM
5	\$4,280,000	4.29	.....	ADM(Mat)/DGMEPM
6	\$1,065,000	4.26	.....	ADM(Mat)/DGLPEM
7	\$256,225,000	4.25	.....	ADM(Mat)/DGAEPM
8	\$74,013,140	4.24	.....	ADM(Mat)/DGMEPM
9	\$24,075,000	4.00	.....	ADM(Mat)/DCPS
10	\$17,966,596	3.93	.....	ADM(HR Mii)/CFMG
11	\$41,607,062	3.92	.....	ADM(Mat)/DGMEPM
12	\$15,575,390	3.91	.....	VCDS/CFPM
13	\$4,641,497	3.80	.....	ADM(Mat)/DCPS
14	\$2,942,500	3.78	.....	ADM(Mat)/DGLPEM
15	\$107,553,446	3.75	.....	ADM(IM)/PMO MASIS
16	\$132,720,000	3.75	.....	ADM(Mat)/DGLPEM
17	\$116,130,000	3.75	.....	ADM(Mat)/DGLPEM
18	\$99,531,086	3.75	.....	ADM(IM)
19	\$82,950,000	3.58	.....	ADM(Mat)/DGLPEM
20	\$1,553,556	3.52	.....	ADM(S&T)
21	\$73,261,543	3.48	.....	ADM(Mat)/DGMEPM
22	\$19,800,620	3.45	.....	ADM(Mat)/DGMEPM
23	\$14,366,246	3.39	.....	ADM(Mat)
24	\$11,839,473	3.37	.....	ADM(Mat)/DGAEPM
25	\$9,913,327	3.35	.....	ADM(IM)/CFSSU
		Total	\$1,206,598,216			

Twenty-eight of the 258 NDHQ managed contracts will be audited by CAC. The maximum risk score is 8.25.



ANNEX G – HIGHER-RISK CONTRACTS – CAC ADJUSTMENTS GREATER THAN 10 PER CENT

Section
20(1) c)
of AIA
3rd Party

Contract Number	Vendor	Type of Services/Goods	Audited Amount	Audit Adjustment	Audit Issues
.....	\$24,553,237	\$3,757,418	Lack of documents to support changes and adjustments, weak accounting system.
.....	\$6,441,529	\$717,609	Numerous reports of profit excesses, unauthorized additional work and inter-company charges.
.....	\$4,330,344	\$4,120,166	No supporting documentation for invoices. Poor record keeping practices. Over invoice of over \$2 M. Labour recording system inadequate.
.....	\$3,082,481	\$1,669,654 labour not auditable	Lack of system and documentation.
.....	\$2,794,140	\$2,283,183	Limited verification possible due to lack of accounting system.
.....	\$2,032,475	\$1,601,561	Unsupported subcontractors cost. Difficulty with documentation related to claims for subcontract work.
.....	\$1,336,953	\$866,957	Lack of supporting documentation (royalty agreement).
.....	\$2,400,000	\$960,239	No proper accounting records for recording costs.
.....	\$57,137,325	\$10,532,087	Profits exceeded by approximately \$5M.
.....	\$26,749,971	\$2,949,384	Profits exceeded by \$1.3 M.
.....	\$23,812,196	\$1,569,425	Profits exceeded by \$1.1 M.
.....	\$9,887,411	\$1,535,046	
.....	\$7,626,947	\$2,646,566	Profit excesses from 100 K to over \$1M.
.....	\$1,308,817	\$167,238	Minor excess profit.
.....	\$1,189,326	\$164,457	



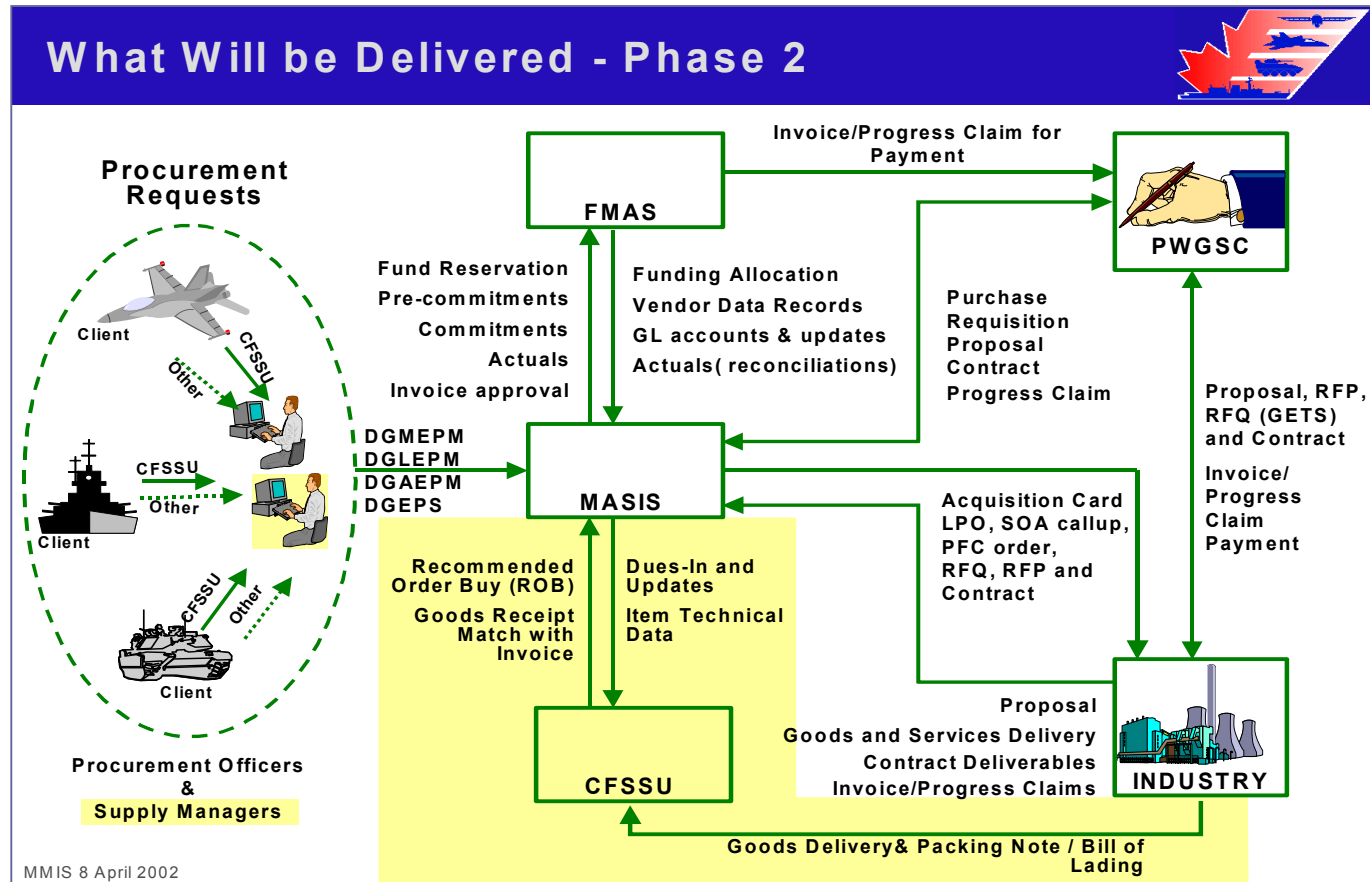
ANNEX H – TOP 27 COST CENTRES MAKING PAYMENTS WITHOUT A COMMITMENT IN FMAS

Section
15(1) i)
International
Affairs and
Defence

Cost Centre	Cost Centre Description	No of Payments	Payments Value	Avg Value of Payment
3398AP	DGMC FINANCIAL MANAGEMENT SERVICES	366	\$101,110,111	\$276,257
3650AA	CC STAFF-CCIBH-NATIONAL COMMAND ELEMENT	2,083	\$47,061,522	\$22,593
0123CE	WCE CONTRACTS-5WG	838	\$37,082,750	\$44,251
0134XX	FINANCIAL OPERATIONS - 4 WING	1,794	\$30,177,704	\$16,821
0150UN	CC4A-DCDS DEPLOYED OPS UNITS	166	\$28,725,097	\$173,043
3703AA	CFHA CHILLIWACK	147,111	\$26,290,143	\$179
0100GY	PRODUCTION	7,116	\$24,690,738	\$3,470
2203AA	CHIEF HEALTH SERVICES (CHS)	217	\$23,611,380	\$108,808
0105LW	CE BR – CDL - CFB GAGETOWN	20,840	\$21,651,396	\$1,039
.....
0153FF	MAT GROUP TRANSLATION	129	\$18,908,756	\$146,580
.....
3398BD	COST MOVES - AIR FORCE	4,436	\$17,384,595	\$3,919
3398BQ	COST MOVES – SUPPORT	5,187	\$17,166,200	\$3,309
0149AA	ASSISTANT DEPUTY MINISTER PERSONNEL (CC6)	94	\$16,710,788	\$177,774
3371BY	MARITIME STAFF COMPTROLLER	551	\$16,655,683	\$30,228
43648A	0127 ASU EDMONTON WKS COY	2,613	\$15,044,510	\$5,758
0114DS	ESS CONSTRUCTION ENG ASU KINGSTON	8,053	\$13,578,816	\$1,686
4877AD	LOGISTICS – CANADIAN FLEET PACIFIC	335	\$13,063,615	\$38,996
0103NV	MAINTENANCE – CFB ESQUIMALT	3,495	\$12,984,299	\$3,715
3398BH	COST MOVES – ENGR	3,351	\$11,807,919	\$3,524
3371AN	DIRECTOR MARITIME FORCE EMPLOYMENT (DMFE)	564	\$11,782,580	\$20,891
3398AZ	COST MOVES – ARMY	3,669	\$11,633,585	\$3,171
0107EX	CONSTRUCTION ENGINEERING CFB PETAWAWA	7,721	\$11,419,471	\$1,479
.....
3078BV	N3 ACOS P&O-SURFACE OPS	180	\$10,321,893	\$57,344
	Total	223,117	\$587,858,365	\$2,635

It may only be practicable for those cost centres with a significantly high value per payment to set up commitments.

ANNEX I – MASIS COMPLEX CONTRACTING MODULE – FINANCE AND PROCUREMENT INFORMATION INTEGRATION



ANNEX J – CONTRACT SUMMARY TEMPLATE

Contract Summary Template		
Ser	Contract Information Requested	Management Response
1	Vendor Name:	
2	Contract Number:	
3	Nature/Category of Service Provided:	
4	Award: Competitive / Non-Competitive:	
5	Duration of Vendor Continuous history providing this specific service to DND:	
6	Principal DND Officer Acting as Technical Authority:	
7	Original Contract Value/Ceiling:	
8	Key Option Provisions: Contract Extensions Available/ Contract Off-ramps:	
9	Original Contract Term/Duration:	
10	Current Contract Value/Ceiling:	
11	Current Contract Term/Duration:	
12	Current Total Expenditures:	
13	Current Total Expenditures and Commitments:	
14	Current Forecast Total Expenditures:	
15	Advance payments made/required: details	



ANNEX J

Contract Summary Template		
Ser	Contract Information Requested	Management Response
16	Per cent completion of work and per cent of contract ceiling utilized:	
17	Number of Substantive Contract Amendments:	
18	Key Risks Facing Contract: Schedule / Cost / Performance / Other:	
19	Key Risk Mitigation Strategies: Schedule / Cost / Performance / Other:	
20	Key Internal Management Reports capturing information on the contract:	
21	Other systems/measures which will provide early-warning of problems:	



ANNEX K – DETAILED CONTRACT MANAGEMENT RISK ASSESSMENT

Detailed Contract Management Risk Assessment Template	
Contract Number _____ Vendor Name _____ Technical Authority (<u>Name, Appointment, Ph #</u>)	
General	Management Response
G1. Within your directorate, how many contract managers/technical authorities are there, and how many contracts are active?	
G2. What are the five most common goods and services for which your organization contracts? (e.g., IT/IM maintenance, repair and overhaul, medical services)	
G3. What overall reporting and early-warning strategies are employed to monitor contracts?	
Specific Contract Questions	Management Response
S1. Does the Statement of Work (SOW) define the deliverables? Please provide a copy of the SOW, or an abbreviated version if the SOW is lengthy.	



ANNEX K

Detailed Contract Management Risk Assessment Template	
Contract Number _____ Vendor Name _____ Technical Authority <u>(Name, Appointment, Ph #)</u>	
Specific Contract Questions	Management Response
<p>S2. What evidence is provided to the technical authority to determine if goods or services have been received in accordance with the contract? What supporting documentation does the Section 34 signing authority have that the goods and services were received? (e.g., packing slips, timesheets, etc.) Did the technical authority sign all such supporting documents? Please provide an example of supporting documentation.</p>	
<p>S3. Who is signing for Section 34 of the FAA to certify that performance and price is in accordance with contract? Please provide name, organization and phone number.</p>	
<p>S4. What was the original contract period and contract value? How many option years were provided for in the contract. What is the current cumulative value of contract amendments and the length of time that the contract has been extended. Please summarize the contract value/date of the contract award and each amendment?</p>	



ANNEX K

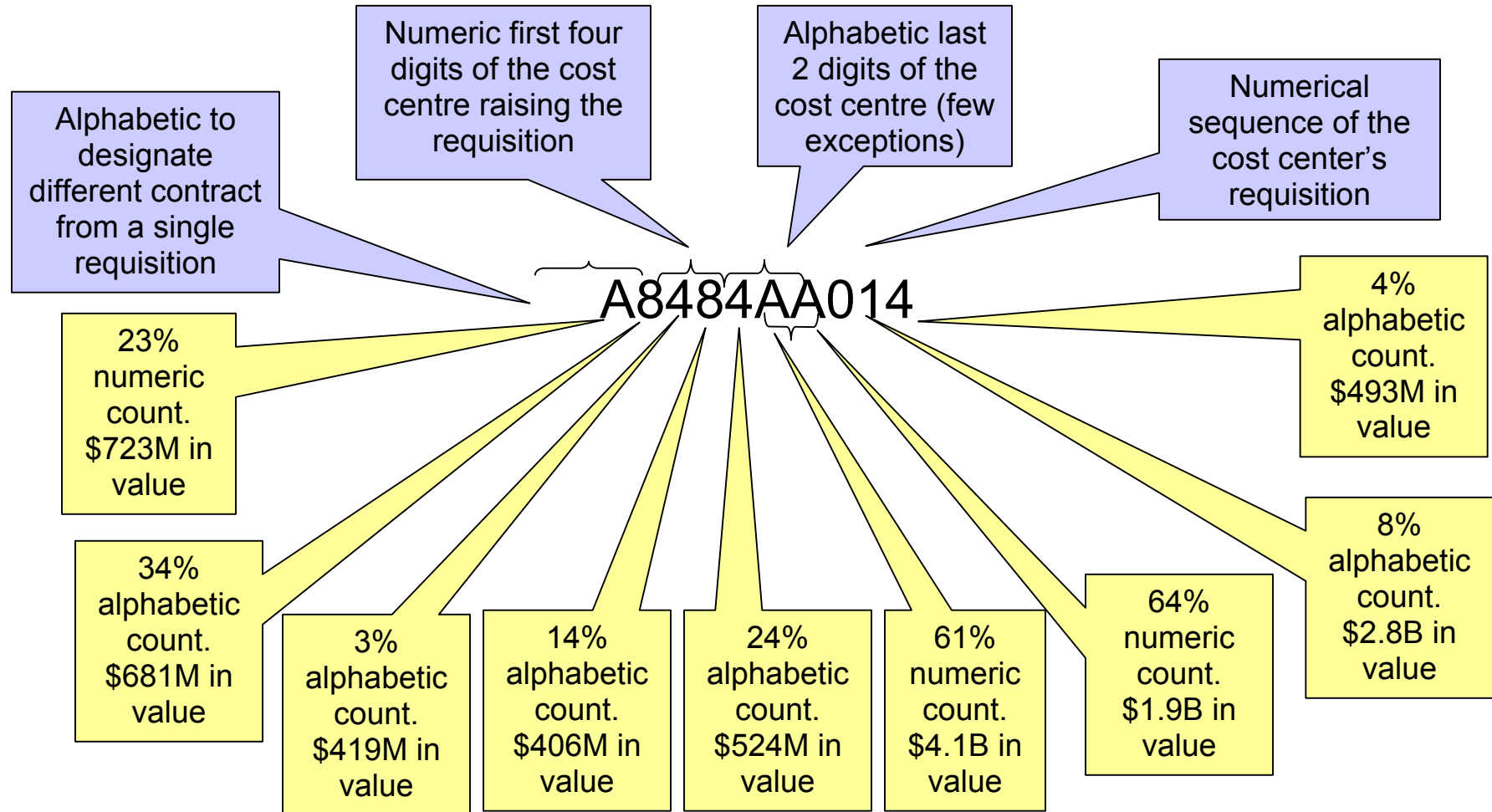
Detailed Contract Management Risk Assessment Template	
Contract Number _____ Vendor Name _____ Technical Authority <u>(Name, Appointment, Ph #)</u>	
Specific Contract Questions	Management Response
S5. What are the terms of payment for the contract (e.g., Firm price, a unit cost or a target price)? Are payments calculated by cost to contractor, plus a mark-up? Are advance payments made? Please attach the request for authority to make such payments. Any specific mark-up provisions for work by subcontractors?	
S6. Are terms of payment linked to deliverables? (Reasonableness of work performed compared to statement of work/deliverables in contract.)	
S7. Are there performance incentives/penalties/holdbacks in the contract? Please specify or attach copies of the relative terms of the contract.	
S8. Were the services in this contract recently (within the last 3 years) performed by DND?	



ANNEX K

Detailed Contract Management Risk Assessment Template	
Contract Number _____ Vendor Name _____ Technical Authority <u>(Name, Appointment, Ph #)</u>	
Specific Contract Questions	Management Response
S9. Was this contract sole-sourced? What is the substantiation for sole-source? Was an ACAN posted? If so, was the ACAN ever challenged by other potential suppliers? Please provide the documents pertaining to the challenge and our response.	
S10. Are there subcontractors associated with this contract? If so, how many and what portion of the work is being performed by them vis-a- vis the prime contractor.	
S11. Are the services of this contract provided to several DND locations across Canada? How many cost centres (approximate, if necessary) are charged for the use the goods or services of this contract? Please provide a list of the cost centres.	
S12. How are the expenditures against the contract tracked? FMAS commitments, MASIS, separate spreadsheet, etc. Please provide a list of the FMAS commitment numbers, and a copy of any other expenditure-tracking tools.	

ANNEX L – FISCAL YEAR 2002/03 COMMITMENT NUMBER ANALYSIS



The figure above indicates the FMAS commitment convention prescribed in the light blue text boxes. In fiscal year 2002/03 there were 133,863 commitment numbers assigned with a total value of \$6.3B. Our analysis of the actual digits assigned to the commitment numbers in the yellow text boxes indicates the variance from the prescribed numbering convention. The greatest variance is in the sixth digit. Although the sixth digit should normally be an alphabetic digit from a cost center (DGMEPM cost centers excepted) often procurement staff will assign the calendar year of the contract.