



ARLINGTON
VIRGINIA

Internal Audit Report - Contract Compliance Cycle Audit

Department of Environmental Services:

FleetCor Technologies Operating Company LLC -
Contract Number-580-13

Report Date: January 30, 2018

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TRANSMITTAL LETTER



January 30, 2018

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Director, Department of Environmental Services

Ms. Maria Meredith
Deputy Director, Department of Management and Finance

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Pursuant to the contract and related statement of work for Arlington County, Virginia ("the County"), we hereby present the contract compliance cycle audit: Department of Environmental Services ("DES") – FleetCor Technologies Operating Company LLC ("FleetCor"). Our report is organized in the following sections:

Executive Summary	This section includes a background summary of the function, the objectives and approach, and a detailed description of the observation(s) noted during this cycle audit. Identified with each observation is the recommended action(s), and management's corrective action plan, including the responsible party and estimated completion date.
Background	This section provides an overview of the function within the process and pertinent operational control points and related compliance requirements.
Objectives and Approach	The cycle audit objectives and focus are expanded upon in this section as well as a review of the various phases of our approach.
Process Maps	This section illustrates process maps, which depict data flow, key control points and any identified gaps.

As described in our objectives and procedures outlined on pages 8 and 9 of this report, the observations noted are based on our analysis of the processes, documents, records and information provided to us by the County. This cycle audit focused on evaluating the soundness of internal control policies to safeguard assets and on reviewing compliance with County policies. We offer no assurances that schemes or fraudulent activities have not been, or are not currently being perpetrated by any person within the areas reviewed.

We would like to thank the staff and all those involved in assisting RSM US LLP with this contract compliance cycle audit.

Respectfully Submitted,

RSM US LLP

RSM US LLP

EXECUTIVE SUMMARY

Background

Contract compliance monitoring is an integral piece of the County’s control environment. Contract compliance encompasses all contractual agreements entered into by the County. The focus of this cycle audit was vendor agreements. Although certain aspects of the purchasing function are centralized within the Department of Management and Finance (“DMF”), and vendor selection is performed in conjunction with Purchasing (for purchases greater than \$5,000), many of the high risk areas like contract compliance and monitoring are the responsibility of the individual departments / divisions / bureaus.

Effective January 1, 2017, the County implemented a *Contract Administration Policy* for all contracts, regardless of their procurement methodology or dollar value. The purpose was to define and implement a standard policy and process for the administration of contracts and define roles and responsibilities for County personnel that monitor and manage contractual relationships.

Contract Selection

The FleetCor Technologies Operating Company LLC (“FleetCor”) contract 580-13 is a fuel management system contract with the County. FleetCor has a subcontractor, Mansfield Oil Company of Gainesville Inc. (“Mansfield”), which acts as the Contractor’s fuel supplier. This is a ten (10) year contract that was executed March 26, 2013. FleetCor provides a consigned fuel management system for use at existing County fuel sites, and allows purchases of fuel at retail locations by authorized County personnel. Mansfield sells the fuel directly to the County, and the County pays Mansfield for fuel supplied to County fuel sites at contract prices based on Oil Price Information Service (“OPIS”) plus freight, applicable taxes, and a fixed management fee. Mansfield invoices the County weekly, providing a weekly fuel transaction detail report and weekly price listing based on OPIS rates.

Fieldwork was performed October 2017 through December 2017

Objective and Scope

The scope of this cycle audit encompassed one contract from the Department of Environmental Services; contract number 580-13 with FleetCor. Although the County issued a specific *Contract Administration Policy* effective January 1, 2017, the audit period was July 1, 2016 to September 30, 2017. For transactions from July 1, 2016 to December 31, 2016, testing was limited to substantive procedures as it related to invoice accuracy, invoice compliance with contract terms, payment timeliness and verification of goods and services. For transactions January 1, 2017 to September 30, 2017, procedures also included department compliance with aspects of the County issued contract compliance policies and procedures.

The objective of this cycle audit was to assess whether the system of internal controls is adequate and appropriate, for effective contract compliance, with selected provisions of the contract as it relates to payment.

Sixty-five (65) invoices were submitted for payment during the testing period. We selected thirteen (13) invoices per RSM sampling methodology for detailed testing.

Overall Summary / Highlights

The observations identified during our assessment are detailed within the pages that follow. We have assigned relative risk or value factors to each observation identified. Risk ratings are the evaluation of the severity of the concern and the potential impact on the operations of each item. There are many areas of risk to consider in determining the relative risk rating of an observation, including financial, operational, and/or compliance, as well as public perception or ‘brand’ risk.

Number of Observations by Risk Rating

(See page 9 for rating definitions)

	High	Moderate	Low
Contract Compliance Cycle Audit – DES – FleetCor	1	-	-

We would like to thank all Arlington County team members who assisted us throughout this cycle audit.

EXECUTIVE SUMMARY (CONTINUED)

Detailed Observation(s)

<u>Risk Rating</u>	<u>Observation</u>	<u>Recommendation</u>	<u>Management's Action Plan</u>
High	1. Invoice Review		
	<p>Per the County Contract Administration Policy, Section D Purchase Orders, Invoices and Payments:</p> <ul style="list-style-type: none"> • <i>“The Contractor must provide appropriate backup documentation with the invoice remitted for payment to substantiate charges. This could include Milestone Deliverables, timesheets, daily tickets of material used, etc...”</i> • <i>Verify that the Contractor’s invoice(s) comply with all contractual requirements prior to approving the invoice for payment...</i> • <i>Ensure that ...goods with unit prices match the Contract Pricing...</i> • <i>Invoices should be detailed on a “line item” basis unless dictated otherwise in the contract’s Payment Schedule. Each billed item should match the contract’s Payment Schedule. Each billed item should match the contract’s Payment Schedule and be easily verifiable by the Office of the Purchasing Agent, and others. “</i> <p>We noted the following:</p> <ul style="list-style-type: none"> • Per Exhibit A of the 580-13 contract with FleetCor, accurate pricing support must be provided with each invoice. Currently, DES receives invoices from FleetCor weekly, along with a supporting transaction file. Although the Project Officer reviews and approves each invoice before payment, sufficient supporting documentation is not submitted in order to completely reconcile weekly transactions to the invoice total that is ultimately paid. Due to an unknown reason, the transaction file obtained weekly does not provide a one-to-one match with the total amount incurred included with the corresponding invoice. 	<p>We recommend the following:</p> <p>Supporting documentation for FleetCor invoices should include enough detail, as required by the contract, to allow for proper reconciliation to invoices received for services rendered. This includes the fuel transactions totals matching the total included on the invoices, and OPIS pricing utilized. DES should work with FleetCor to update the supporting documentation format to allow for this level of review.</p> <p>Once a sufficient supporting documentation format has been adopted, a retroactive review should be performed, on a sample basis, to determine what (if any) discrepancies exist between supporting documentation and past invoices to determine if any overpayments were made.</p>	<p>Our summary of findings / unresolved issues after reading the report are as follow:</p> <ul style="list-style-type: none"> • Although the Equipment Bureau has actively reviewed detailed transaction logs for years, the transaction logs actually reflect daily fueling at daily OPIS prices. Our contract pricing is based on weekly OPIS pricing. This partially explains why we have been unable to exactly match the weekly invoices provided to us by Mansfield. The amount of the delta varies with the ebb and flow of OPIS fuel pricing and most markedly on whether pricing increases or decreases over any given week. Until this issue is resolved, we are using a tighter verification threshold of \$100 rather than the historical \$500 when reviewing weekly invoices. Although FleetCor sends the Equipment Bureau weekly charts reflecting the corresponding weekly OPIS rates for our fuel purchases (diesel, biodiesel, unleaded – E10), we have only occasionally verified the OPIS prices they send us. Once the transaction logs have been corrected to reflect the correct weekly tax free pricing, we will continue our practice of matching up totals and verify weekly OPIS pricing. We have requested a weekly OPIS subscription from FleetCor. <p><i>(continued on next page)</i></p>

EXECUTIVE SUMMARY (CONTINUED)

Detailed Observation(s) (Continued)

<u>Risk Rating</u>	<u>Observation</u>	<u>Recommendation</u>	<u>Management's Action Plan</u>
High	<p>1. Invoice Review (continued)</p> <ul style="list-style-type: none"> FleetCor's subcontractor (Mansfield Oil) provides a file that includes the vehicle number, fuel date, station identifier, number of gallons, cost per gallon, tax, employee name, and total cost of each transaction along with each weekly invoice. The Project Officer then calculates the anticipated invoice total, based on multiplying the total gallons by total cost per gallon. The reviewer expects that this total will differ from the actual invoice total, as off-site pump locations include a fuel tax on transactions. Because small variances are anticipated, the Project Officer uses an acceptable difference threshold of \$500 (this is typically 1-2% of a normal weekly invoice) between his recalculation and the invoice total. If the difference is greater than \$500, the Project Officer follows up with Mansfield Oil to explain the variance and/ or revise it if necessary. This method does not allow the Project Officer the ability to reconcile transaction detail exactly to the total amount charged to the County. The \$500 threshold is not a documented approved threshold, but was judgmentally determined by the previous Project Officer. As part of detailed testing, we attempted to recalculate anticipated invoice totals based on supporting documentation, but were unable to do so. Our recalculations were within 1% of the invoice totals. Both RSM and the Project Officer were unable to determine why discrepancies existed between the supporting documentation and actual invoice totals. 	<ul style="list-style-type: none"> The County should obtain an OPIS subscription in order to perform an adequate review of invoices. Invoice review procedures should include price testing, on a sample basis, as compared to OPIS and the contract terms prior to invoice approval for payment. Review procedures should be documented and maintained, including supporting documentation of the price testing utilized, in order allow for an audit trail. 	<p>Management Action Plan: (continued)</p> <ul style="list-style-type: none"> It is important to remember that our chosen fuels are blends (B5, B20, E10) and per our contract, the pricing of these "virtual" blends is calculated from their OPIS priced individual content. Further complicating the pricing is the difference of freight charged for biodiesel coming out of the Baltimore rack. Finally, our chosen percentage blend of bio content for biodiesel fuel changes throughout the year, to offset the possibility of "gelling" in cold weather, further complicating the weekly verification of individual/total transaction lines. While reconciling invoices, it will be impossible to check thousands of individual lines. We will, however, spot check the pricing components for each product type at each of our three fuel sites. The Equipment Bureau has contacted the Director of Bids and Contracts for FleetCor who was aware of the requirement and renewed commitment to provide a detailed transaction log that matches our weekly invoice. FleetCor's Operations staff has been working with our Business Manager to understand and rectify the issue and has already submitted a request to their IT department to work this out. <p><i>(continued on next page)</i></p>

EXECUTIVE SUMMARY (CONTINUED)

Detailed Observation(s) (Continued)

<u>Risk Rating</u>	<u>Observation</u>	<u>Recommendation</u>	<u>Management's Action Plan</u>
High	<p>1. Invoice Review (continued)</p> <ul style="list-style-type: none"> Per Exhibit B of the 580-13 contract with FleetCor, <i>“transactions at on-site locations (County sites) shall be priced based on the following components: OPIS price plus freight, taxes and margin as listed below...”</i> Fuel pricing is based on OPIS standard pricing, but OPIS pricing is not included with the supporting documentation. As such, invoices paid by the County are not validated against OPIS. The County does not have a subscription to OPIS. As part of our detailed testing, we received pricing from OPIS for a sample of our sample. We validated that all prices incurred fell within the OPIS range for the sampled timeframe. <p>A critical function of contract compliance is validating the accuracy of invoices. Without appropriate supporting documentation for each invoice and testing for accurate OPIS pricing, DES cannot validate that the County is being accurately charged for fuel transactions. Limited transparency into the Mansfield's billing process increases the risk of invoices being paid based on erroneous price calculations from the vendor.</p>		<p>Management Action Plan:</p> <p>The core issue has been identified as a data formatting challenge. FleetCor's IT department is attempting to develop a new report with tax free weekly pricing in the same ".txt" format required by our fleet software company (FA) to be able to upload the data. We have contacted FA to see if their programming requirements have changed over the years whereby they could now upload the data in ".xlsx" format rather than ".txt" format. One of the two paths should provide success in the next 30-60 days and we will be able to receive individual daily transaction logs billed at weekly OPIS pricing reflecting various blends net of any retail taxes in order to verify weekly summary invoices.</p> <p>Estimated Completion Date: April 2, 2018</p> <p>Responsible Party: Equipment Bureau Chief</p>

BACKGROUND, OBJECTIVES AND APPROACH

Background

Overview

Contract compliance encompasses all contractual agreements entered into by the County. Although certain aspects of the purchasing function are centralized within the Department of Management and Finance, and vendor selection is performed in conjunction with Purchasing, many of the high risk areas like contract administration, compliance and monitoring are the responsibility of the individual departments/divisions/bureaus. These monitoring responsibilities specifically include:

- Understanding the scope of work and terms and conditions of the contract;
- Management of contract billings to avoid cost overruns;
- Validation of complete and satisfactory performance of work through physical walkthroughs and site visits, when appropriate;
- Ensuring timely performance of contracted work;
- Providing updates to the Department Director, Division Chief and Department of Management and Finance related to progress and budget, as necessary;
- Maintaining appropriate documentation, in compliance with the County level document retention policy and respective contract; and
- Review and approval of invoices for payment to the Contractor in line with the payment terms and conditions outlined in the agreement.

Effective January 1, 2017, the County Implemented a *Contract Administration Policy* for all contracts, regardless of their procurement methodology or dollar value. The purpose was to define and implement a standard policy and process for the administration of contracts and define roles and responsibilities for County personnel that monitor and manage contractual relationships. Specifically, the policy establishes Project Officer and Task Officer Responsibilities, defines internal controls surrounding contract payment, quality assurance and recordkeeping, and outlines all applicable regulations to which the contract administration process must adhere.

FleetCor Contract

The FleetCor contract 580-13 is a fuel management system contract with the County. FleetCor has a subcontractor, Mansfield, which acts as the Contractor's fuel supplier. FleetCor provides a consigned fuel management system for use at existing County fuel sites, and allows purchases of fuel at retail locations by authorized County personnel. Mansfield sells the fuel directly to the County, and the County pays Mansfield for fuel supplied to County fuel sites at contract prices based on OPIS plus freight, applicable taxes, and a fixed management fee. Mansfield invoices the County weekly, providing a weekly fuel transaction detail report and weekly price listing based on OPIS rates.

Contract 580-13					
Contractor	Contract Title	Execution Date	Total Dollars Spent on Contract ^{1,2}	Contract Type	County Division
FleetCor	DES – Fuel Management Systems	March 26, 2013	\$11,610,173	Unit Price	DES

¹As of 9/30/17

²Total dollars spent during audit period (July 1, 2016 – September 30, 2017): \$2,403,717

BACKGROUND, OBJECTIVES AND APPROACH (CONTINUED)

Background (continued)

Roles and Responsibilities

The following departments play key roles in the contract compliance process:

Department of Environmental Services

DES is responsible for providing project management and oversight services for this contract. DES is also responsible for completing all Project Officer functions as outlined in the contract, overall contract compliance, and reviewing and approving vendor invoices for accuracy prior to payment.

Department of Management and Finance

DMF oversees all of the processes and recordkeeping of the County financial transactions. The Purchasing and Accounts Payable divisions are part of DMF and act as support functions for departments managing vendor contracts. Specifically, Purchasing administers the competitive bid process and processes requests for procurement of services and goods by signing the contract and executing purchase orders for approved amounts. Accounts Payable is responsible for processing payments to contractors based on invoices approved by the respective departments.

Common Definitions

Some common definitions for construction terminology used throughout this section of the report are as follows:

- *Contract Owner/Project Officer* – refers to the County representative responsible for general control, review, and approval of all aspects of the contract, once executed. The Project Officer is appointed by the County's Department of Environmental Services Director or a designee as identified in the contract, who is the primary point of contact for the Contractor in executing the terms of the contract.
- *Change Order* – refers to an approved additional cost for unforeseen work outside of the original work plan considered in the development of the contract price. If the cost is deemed necessary and appropriate, an executed change order is established to allow the Contractor to invoice for the additional work.

Timeline

Below is a timeline of major events for the contracted project.

Date	Event Description
March 26, 2013	Arlington County executes contract 580-13 with FleetCor
November 4, 2014	Change order #1 executed – related to increased costs for fuel additives
December 21, 2022	Contract expires

BACKGROUND, OBJECTIVES AND APPROACH (CONTINUED)

Objectives and Approach

Objectives

Contract compliance encompasses all contractual agreements including, but not limited to, vendor agreements. Although certain aspects of the purchasing function are centralized within the Department of Management and Finance, many of the high risk areas like contract administration and monitoring are decentralized to the individual departments.

The scope of this cycle audit encompassed one (1) contract from the Department of Environmental Services; contract number 580-13 with FleetCor. Although the County issued a specific *Contract Administration Policy* effective January 1, 2017, the audit period was July 1, 2016 to September 30, 2017. For transactions from July 1, 2016 to December 31, 2016, testing was limited to substantive procedures as it related to invoice accuracy, invoice compliance with contract terms, payment timeliness and verification of goods and services. For transactions January 1, 2017 to September 30, 2017, procedures also included department compliance with aspects of the County's *Contract Administration Policy*.

The objective of this cycle audit were designed to assess whether the system of internal controls is adequate and appropriate, for effective contract compliance, with selected provisions of the contract as it relates to payment.

Approach

Our approach to the audit execution consisted of the following phases:

Understanding and Documentation of the Process

During the first phase, we performed the following:

- Conducted entrance conferences with representatives from DES and DMF to discuss the scope and objectives of the cycle audit, obtain preliminary data, and establish working arrangements;
- Obtained copies of financial reports and other documentation deemed necessary and appropriate to gain an understanding of the existing control environment;
- Reviewed the County's *Contract Administration Policy* related to this cycle audit;
- Conducted interviews with responsible personnel from the selected department/division to obtain an understanding of the unique aspects of the process in order to perform walkthroughs and our testing; and
- Developed flowcharts of the process(es), which are included in this report.

Evaluation of the Process and Controls Design and Testing of Operating Effectiveness

The purpose of this phase was to test compliance and internal controls. This phase also consisted of an evaluation of the design and testing of operating effectiveness. We performed walkthroughs and detailed testing, on a sample of thirteen (13) invoices, which occurred during the testing period. Specific procedures performed included:

- Gathered background information on the County's contract compliance and monitoring procedures and any required controls or documentation, including County Board authorization, if necessary;
- Determined whether the selected department/division had related contract compliance procedures outside of County-level procedures;
- Obtained background information on the selected contract, including a copy of the contract, contract administrator information, and detail of expenditures under each contract during our audit period;

BACKGROUND, OBJECTIVES AND APPROACH (CONTINUED)

Objectives and Approach (Continued)

Evaluation of the Process and Controls Design and Testing of Operating Effectiveness (Continued)

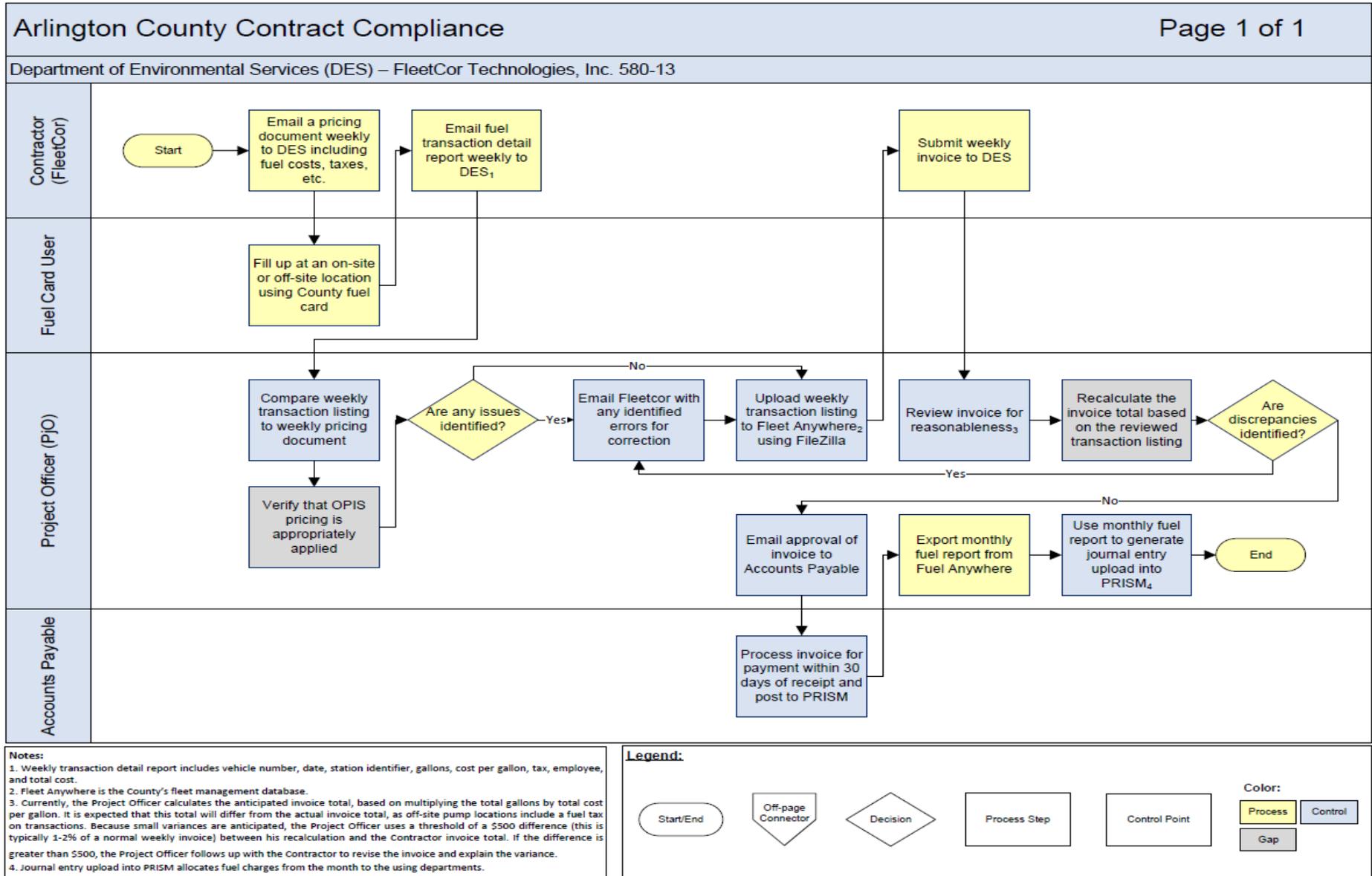
- Tested invoices for the selected contract to determine if the supporting documentation agreed to the payment amount;
- Verified that each invoice was charged appropriately against a purchase order as required by the *Contract Administration Policy*;
- Inspected invoices to confirm that unit costs per invoice supporting documentation tied to the agreed upon contract unit prices;
- Determined accuracy of the weekly fuel pricing schedules provided by FleetCor against OPIS pricing;
- Inspected invoices for Project Officer sign-off as required by the *Contract Administration Policy*;
- Determined if payment was made in a timely manner and in accordance with the pricing terms of the contract and the *Contract Administration Policy*, and that payments did not exceed amounts authorized;
- Determined whether goods and services received under the contract were properly verified or monitored prior to payment of the invoice as required by the *Contract Administration Policy*; and
- Assessed the overall contract compliance process and controls to determine effectiveness.

Reporting

At the conclusion of this audit, we vetted the facts of this cycle audit with DES. The draft report was submitted to DES and DMF for review. An exit meeting was held with DES and DMF to formally review and discuss the draft report and modify accordingly. Management’s corrective action plan with estimated completion dates has been provided and included in the report.

Observation Risk Rating Definitions	
Rating	Explanation
Low	Observation presents a low risk (i.e., impact on financial statements, internal control environment, public perception/brand, or business operations) to the organization for the topic reviewed and/or is of low importance to business success / achievement of goals and internal control structure.
Moderate	Observation presents a moderate risk (i.e., impact on financial statements, internal control environment, public perception/brand, or business operations) to the organization for the topic reviewed and/or is of moderate importance to business success / achievement of goals and improve its internal control structure. Action should be in the near term.
High	Observation presents a high risk (i.e., impact on financial statements, internal control environment, public perception/brand, or business operations) to the organization for the topic reviewed and/or is of high importance to business success / achievement of goals and improve its internal control structure. Action should be taken immediately.

PROCESS MAP:





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