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INTEROFFICE MEMORANDUM

MEMORANDUM INTERIEUR

INTERNAL AUDIT DIVISION I
OFFICE OF INTERNAL OVERSIGHT SERVICES

TO: Mr. Sukehiro Hasegawa,
A: Special Representative of the Secretary General
UNMISSET

DATE: 29 December 2004


FROM: Patricia Azarias, Director
DE: Internal Audit Division I, OIOS 

REFERENCE: AUD- (0983/04)

SUBJECT:

OBJET: **Audit of Procurement Contracts in UNMISSET**

1. I am pleased to present herewith our final report on the audit of the above subject, which was conducted during August- September 2004.
2. We note from your response to the draft report that UNMISSET has generally accepted the recommendations. Based on the response, we are pleased to inform you that we have closed all recommendations except recommendation 7, which will be closed after the revised cost for the change in the scope of work has been finalized and approved. Recommendation 6 has been withdrawn.
3. IAD is assessing the overall quality of its audit process and kindly requests that you consult with your managers who dealt directly with the auditors and complete the attached client satisfaction survey form.

I. INTRODUCTION

4. OIOS conducted an audit of procurement contracts in the United Nations Mission of Support in East Timor (UNMISSET) during August and September 2004. The audit was conducted in accordance with the standards for the professional practice of internal auditing in United Nations organizations.
5. The estimated annual procurement of goods and services for the Mission was \$20 million during the financial year 2003/2004 and \$2.5 million during 2004/2005 according to the respective annual acquisition plans. The comments made by the Management of UNMISSET on the draft report have been included in the report as appropriate and are shown in italics.

II. AUDIT OBJECTIVES

6. The objectives of this audit were to assess the adequacy and effectiveness of internal controls in the area of procurement including the system for acquisition, registration of vendors, bidding process and award of contracts. The audit also reviewed the Mission's compliance with UN Financial Rules and Regulations, and the Procurement Manual.

III. AUDIT SCOPE AND METHODOLOGY

7. The audit reviewed the annual acquisition planning, bidding process, award and execution of major contracts covering the period from July 2003 to July 2004. The methodology comprised detailed reviews of relevant documentation and interviews with key personnel in the Mission.

IV. OVERALL ASSESSMENT

8. The annual acquisition plan was not prepared with adequate details to facilitate the procurement activities on a timely manner. The bidding process was less effective due to lack of competition as a result of lower participation among the short listed vendors. The Mission explained that this was due to the unique condition prevailing in Timor Leste where very few local suppliers are available and also lack of easy access to other market due to limited shipment facilities. The registration process of the vendors in UNMISSET Approved Vendor List needs proper scrutiny to ensure adequate details are available for registration and also needs periodical review for updating. There is also need for improvement in the short listing of vendor and adequate time be given to the bidders for submission of the bid and delivery period to achieve effective competition.

V. AUDIT FINDINGS AND RECOMMENDATIONS

A. Acquisition planning

9. The Annual Procurement Plan for 2003/2004 indicated the estimated value of procurement but did not present quantitative details even for the major items. Furthermore, the Plan for 2004/2005 even did not have estimated value of procurement in respect of Engineering Section, General Services Section and Medical Section even though a significant volume of procurement related to these sections.

10. An effective acquisition plan requires planning in advance and devising appropriate strategy in order to acquire goods in an economical and timely manner. This requires the requisitioning sections to work out detailed plans and provide information including quantitative details to the Procurement Section for the latter to develop a strategy to procure the goods and services economically and efficiently. However, OIOS found that requisitioning sections did not provide adequate details to Procurement Section. The Procurement Section also did not take any initiative on its own based on the annual acquisition plan; instead, it took action on a case-by-case basis after receiving the specific requisition.

11. OIOS found that normally the requisitioning sections raised requisitions only two months prior to the scheduled delivery date even for purchases above \$30,000 where tendering process is required. Hence, it restricts the Procurement Section from giving sufficient time to prospective bidders to respond to invitations to bid and plan their delivery time.

12. The Procurement Section generally provided 10 to 14 days' notice to vendors for submission of bids and awarded contracts to those who offered to supply within a month. In some cases the time given for submission of bids was less than 10 days, even though when there was no exigency. Those bidders who offered to deliver within two to three months were rejected. For example, with regard to ITB-5, the lowest bid was for \$104,248 which was rejected as the bidder proposed delivery time for two to three months. Instead, the contract was awarded to the second lowest bidder for \$124,240 because he offered a delivery period of one month. In this single case alone, the short lead-time resulted in additional cost to UNMISSET in the amount of \$19,992.

Recommendation 1

OIOS recommends that the UNMISSET Administration ensure that requisitioning sections provide adequate details including quantitative details for the preparation of Annual Acquisition Plan and based on that, the Procurement Section develop an appropriate strategy to acquire the goods and services in an efficient and economical manner (AP2004/682/03/001).

13. *UNMISSET accepted recommendation 1 and stated that the Annual Acquisition Plan for 2004-2005 was prepared in July 2004 and it would be inappropriate to revise it at this point since the Mission is now on its final 6-months extension till 19 May 2005. Moreover, one of the main activities of the Procurement Section for this liquidation phase is the completion and closure of the procurement files. Should there be a further follow-on mission beyond May 2005, the UNMISSET Administration shall ensure that the requisitioning sections together with the Procurement Section include quantitative details in the preparation of the Annual Acquisition Plan and develop an overall strategy for major procurement in an efficient and economical manner. Based on the Mission's response, OIOS has closed the recommendation in its database.*

B. Registration of vendors

14. Section 7.7.1 of the Procurement Manual requires the Chief Procurement Officer (CPO) to establish minimum standards for registration in the vendor database. However, the CPO has not defined such minimum standards and procedures for registration in UNMISSET's approved vendor list. The Procurement Section receives information about the prospective vendors from various sources and includes their names in the list maintained in the Mercury system. There was no practice of formal registration by submitting a registration form. OIOS' review of the procedures followed while registering 43 vendors during July 2003 to June 2004 in Mercury system revealed that the registration of vendors was done without adequate details (type and nature of business, year of establishment, email address and bank details, etc.).

15. The Supplier Review Committee (SRC) under the chairmanship of the CPO was constituted on 5 January 2004. The responsibility of the SRC, as defined in the memo, includes review of the evaluation of prospective suppliers' applications for inclusion in the vendor roster and also to review recommendations for removal of suppliers from the roster, as proposed by Supplier Roster Officer (a procurement assistant assigned to this responsibility). OIOS found that as of September 2004, the SRC had not held any meeting. Furthermore, the amendment of data relating to approval and suspension of vendors in the Mercury System can be made by any staff in the Procurement Section.

There must be access control limited to persons who have been given such authority for making amendments to the vendor database.

16. Section 9.3.8 of the Procurement Manual states about deletion of non-responding vendors from the list of invitees. Accordingly, the CPO can approve removal from the list of registered vendors who have not replied or acknowledged three previous invitations to bid. Many vendors had not responded to the Invitation to Bid or Request for Quotation. However, the Procurement Section did not have system to identify non-responding vendors for removal from the list. OIOS could not find any case where the vendor's name was removed on the above basis.

Recommendation 2

OIOS recommends that the UNMISSET Procurement Section define a procedure for registering vendors in the approved vendor list and ensure that the Supplier Roster Officer records the registration and removal of the vendor in the Mercury system based on the decision of the Supplier Review Committee (AP2004/682/03/002).

17. *UNMISSET accepted recommendation 2 and stated that to this end it has already defined and implemented a procedure for registering new vendors.* In view of the action taken by the Mission, OIOS has closed the recommendation in its database.

C. Bidding process and award of contract

18. The Procurement Section sends invitations to bid (ITB) or requests for quotation (RFQ) to only short listed vendors. The Procurement Section was of the opinion that it was not possible to invite all registered vendors as the list becomes very long. Therefore, the Procurement Section generally selected five to six vendors to send ITB or RFQ based on its experience of potential vendors from UNMISSET Approved Vendor List and the vendor list of Procurement Division at UN Headquarters. This procedure provides opportunity to only the short-listed vendors to participate in bidding process.

19. Section 9.3.1(3) of the Procurement Manual states "The identification of potential vendors for receipt of solicitation document shall be undertaken in such way as to ensure the integrity of the process and the confidence of all users and oversight bodies". OIOS' review of ITB and RFQ contracts revealed that there was no documentation explaining the criteria on which vendors were short listed. In OIOS' opinion, this is of paramount importance to ensure and effective competitive bidding because only selected vendors had opportunity to participate in the bidding.

Recommendation 3

OIOS recommends that the UNMISSET Procurement Section document the procedures and the criteria applied for short listing of vendors for competitive bidding (AP2004/682/03/003).

20. *UNMISSET agreed with recommendation 3 and stated that Procurement Section endeavors to follow the guidelines provided in the Procurement Manual, i.e. by direct solicitation of invited suppliers as allowed for in Section 9.3.1(2). There are no other written procedures or criteria established by UNMISSET other than which are already provided in the Procurement Manual.*

However, UNMISSET will document the procedure and criteria it has developed for short-listing of vendors for competitive bidding. In view the Mission's response, OIOS has closed recommendation 3 in its database.

21. OIOS' analysis of data pertaining to the number of vendors invited and their bid submissions showed that the Procurement Section had invited an average of six vendors per ITB (total 125 vendors in 21 ITBs) during 2003/2004 and the actual submission of bids was less than three vendors per ITB (59 bids submitted in response to 21 ITBs). Therefore, in general there was less effective competition among the bidders. The objective of inviting certain numbers of the vendors was to get their participation and achieve economy through competition. Considering the low participation of vendors, OIOS believes that the Procurement Section should review and analyze the reasons for poor participation which could be because appropriate vendors were not chosen, sufficient time was not given for bid submission and/or delivery period etc. This requires further improvement in the bidding system.

22. Section 9.3.4 of the Procurement Manual states that as a general rule all registered vendors for particular goods or services should be invited for goods costing more than \$2,500 for a single award. It also states that if it is impractical or not feasible to invite all registered vendors, then minimum number of vendors suggested is five for acquisition between \$2,500 to \$30,000 and ten for \$30,000 to \$200,000. However, OIOS found the actual number of vendors invited was less than that indicated in the Procurement Manual in some cases (see table below) although those were not emergency purchases.

Bid no	No of Vendors invited	Contract value	Item
4ITB-18	3	87,292.16	Generator
4RFQ-132	2	39,057.14	Mobile lighting
4RFQ-87	3	29,758.46	Antenna for VHF

Recommendation 4

OIOS recommends that the UNMISSET Procurement Section invite adequate number of bidders in compliance with the requirements of the Procurement Manual (AP2004/682/03/004).

23. UNMISSET accepted recommendation 4 and stated that it will continue to follow the guidelines provided in the Procurement Manual Section 9.3.4. However, the Procurement Section's experience is that there will be exceptional cases where a flexible application of the guidelines is required. Procurement Section will document reasons for such cases accordingly. In view of the Mission's response, OIOS has closed the recommendation in its database.

24. Requisitioning units indicate the estimated cost in the requisition based on the previous purchase price and for new items based on its own information. OIOS found that in some cases, only one or two vendors submitted their bids and the offer price was substantially higher than the estimated cost. However, the estimate was not considered as a basis to compare the reasonableness of the price.

- a) The Transport Section raised a requisition (4TRP-10) for the procurement of Hyundai spare parts. The estimated cost as mentioned in the requisition was

\$38,835 for 72 items. The Procurement Section received two bids for 4ITB-4. The lowest bid was \$61,716 for 67 items and the contract was awarded to it. If the estimated cost for seven items not quoted is excluded, the revised estimated cost would be \$ 37,254. Therefore, the contract was awarded at a higher amount by \$24,461 (65%).

- b) The Communications and Information Technology Section raised a requisition (4CIT-10) for the procurement of EDP spare parts and expendable items. The estimated cost was \$66,845 for 32 items. Only two vendors submitted their bids for 4ITB-24 but a vendor had quoted for 12 items only and his bid was considered as incomplete and rejected. So the contract was awarded based on a single valid bid for \$87,857, which was higher than the estimated cost by \$21,012 (31%).
- c) The Engineering Section raised a requisition (4ENG-120) for the procurement of two numbers of Mobile Lighting Equipment at a total estimated cost of \$10,000. Only two vendors were invited to submit their quotations in RFQ-132 and the lowest offered price was \$ 39,057, which was higher than the estimated cost by \$ 29,057 (190%).

Recommendation 5

OIOS recommends that the UNMISSET Procurement Section consider the estimated price as a basis to determine the reasonableness of bid prices and go for re-bidding if the offered price is substantially higher, particularly when only one or two bidders have responded to the ITB (AP2004/682/03/005).

25. *UNMISSET accepted recommendation 5 and stated that in general, the estimated prices indicated in the requisition are considered by Procurement Section as one of the basis to determine the reasonableness of the bid prices. However, in some instances it has been discovered that after the bids are received and evaluated, the estimated price indicated by the requisitioners was unrealistic, as in per the sample cases cited by OIOS. The respective requisitioners were made aware of this situation since Procurement Section provided them copies of the bids received for evaluation. In the sample cases cited by OIOS, there was at least one another bid with a price even higher than the awarded bid, which is clear indication that the estimated price by the requisitioner was not realistic. In such cases Procurement Section does not believe it is appropriate to re-bid. In those cases where re-bidding might be considered and time is of the essence, Procurement Section will work in consultation with the requisitioner on the issue of re-bid. In view of the clarifications provided by the Mission, OIOS has closed recommendation 5 in its data base.*

26. OIOS noted that generally the time given for submission of bids/quotation was 10 to 14 days but in some cases it was less than 10 days although those were not emergency purchases. The short lead-time may also be a cause for low participation by bidders. For effective bidding, bidders need reasonable time particularly because of limited economic activities in Timor Leste (most of the vendors are from outside the country). Examples of short period given for bid/quotation submission are shown in the following table:

Bid No	Estimated cost	Days to submit bid	Item	No. of vendors invited	Bids received
4ITB-14	56,536.97	9 days	Office Supplies	4	3
4ITB-24	66,845.00	9 days	EDP Parts	7	2
4ITB-25	30,205.00	10 days	Cables	8	2
4RFQ-132	10,000.00	7 days	Mobile Lighting	2	2
4RFQ-87	19,750.00	6 days	Antennas	3	2
4RFQ-21	16,003.67	7 days	Uniform	4	2

27. Requisitioning sections raise requisitions normally only two months prior to the delivery date. This requires expeditious processing from the time the requisition is created, till the award of contract. OIOS found some cases of delay in procurement process as indicated below:

- (a) The Procurement Section sent bids relating to ITB-5 and ITB-6 for technical evaluation only on 10 September 2003 and 18 September 2003 respectively whereas those bids were opened on 28 August 2003.
- (b) The Local Committee on Contracts (LCC) recommended award of contract relating to ITB-5 on 2 October 2003 but the Procurement Section issued the purchase order only on 14 October 2003.
- (c) Requisition No- SUP-5 for office supplies was raised on 22 July 2003 and was approved only on 18 September 2003, so the approval process took about two months. The due date for delivery was 22 October 2003 as per requisition. The Procurement Section sent the ITB (ITB-14) only on 30 September 2003 -- it took 12 days for inviting bids and provided only 9 days to bidders for submission of their bids.
- (d) The bids for ITB-14 were opened only on 17 October 2003, however the bid opening date as per ITB was 8 October 2003.
- (e) The bids pertaining to ITB-4, ITB-5 and ITB-6 were opened only on 28 August 2003, however the bid opening date as per ITB was 25 August 2003.

Recommendation 6

OIOS recommends that the UNMISSET Administration advise requisitioning sections to raise requisitions at least three months in advance to facilitate a competitive and effective bidding process (AP2004/682/03/006).

28. *UNMISSET did not accept recommendation 6 and stated that given the 6 months mandates that UNMISSET has been working under, it is neither practical nor feasible to strictly impose such a long lead-time. The Mission was of the view that bidders have been given reasonable response times in conformity with Annex D-20 of the Procurement Manual and with respect the nature of the types of commodities being tendered. Based on the Mission's response, OIOS has withdrawn recommendation 6.*

29. Rule 105.13 (c) of the Financial Rules and Regulations states that where the advice of review committee (LCC or Headquarters Contracts Committee) is required, no final action leading to award or amendment of a procurement contract may be taken before such advice is received. OIOS found that the Mission is getting service from contractors without finalizing the cost for the revised scope of work. In such cases, the Mission finalizes the cost through negotiation. In OIOS' opinion, it is prudent to finalize the cost before commencement of the new contract period. The reason is that the Mission will have time to go for fresh bidding if negotiation could not be achieved at a reasonable cost. Otherwise, the contractor would be in an advantageous position since it would be known that the Mission is not going to exercise alternative action (fresh bidding) and this might lead to higher cost. In such a situation, the Mission does not have sufficient time to exercise alternative action and might face difficulty to achieve economy in the award of contract. Some instances are described below:

- (a) UNMISSET had a contract with Eurest Support Service for the supply of rations, which expired on 30 June 2004. The Mission was in favour of extending the same contract for another year with a revised scope of work including services for catering, supply and disposal of water bottles. In a communication dated 10 April 2004, the Procurement Division at UN Headquarters agreed in principle, provided that the terms were most favorable to the Organization. The Mission sent a proposal to the Procurement Division on 24 May 2004 for extending the contract. But the Procurement Division informed only on 10 August 2004 that the contract could not be extended. Furthermore, it stated that the new catering arrangements have nothing in common with the expired contract. Moreover, all elements, including pricing were completely different. The Procurement Division also suggested entering into a catering contract through direct negotiation and presenting the case to HCC through the LCC. Since July 2004 the contractor is providing services in accordance with the revised scope of work based on the Mission's instruction but the contract is yet to be finalized.
- (b) The Mission had a contract with Seanap International at a weekly fixed price rate for the disposal of used petroleum, oil and lubricants (POL) and medical waste. The contractor sold its interest in this contract to another contractor "Aneater t/a Waste master" effective from 18 March 2004 and the Mission entered into a contract with the new contractor for the remaining period of contract till 30 June 2004. The previous contract was awarded in July 2002. There is reduced volume of work due to downsizing of the Mission. The contractor is providing services without finalizing the revised contract amount.

Recommendation 7

OIOS recommends that the UNMISSET Procurement Section finalize the revised cost for change in the scope of work before commencement of the new contract period to avoid uncertainty about the cost (AP2004/682/03/007).

30. *UNMISSET accepted recommendation 7 and stated that in the two cases cited by OIOS, at the time of audit the determination of the revised cost due to the changes in the scope of work was either in the process of being finalized in one case or was already finalized in the other case. In*

view of the Mission's response that the revised cost is still under process of finalization, the recommendation will remain open in the OIOS database until the revised cost is finalized and authorized.

D. Administration of contracts

31. Section 9.9.14 of the Procurement Manual states, "Solicitation Document may include a clause for stipulation of liquidated damages to ensure timely contract performance". The Mission did not include liquidated damages clause in the contracts entered through ITB. Only few systems contracts for the supply of construction material have such a provision. It is also to be noted that the Mission awarded contracts to those vendors who committed to deliver in a short period, normally one month. But then, when the vendors failed to deliver within that stipulated time, they are not penalized. Thus, the rationale for awarding the contracts was also not fulfilled.

Recommendation 8

OIOS recommends that the UNMISSET Procurement Section ensure that a clause for liquidated damages is included in all contracts and apply the provision in cases of late delivery (AP2004/682/03/008).

32. *UNMISSET accepted recommendation 8 and stated that it has now included a standard clause for liquidation damages in its purchase orders and contracts. However, application of liquidated demands upon the vendor/contractor would have to be examined on the merits of each individual case.* In view of the action taken by the Mission, OIOS has closed the recommendation in its database.

33. Section 15.2 of the Procurement Manual requires that the Procurement Officer in cooperation with the Requisitioning Section should ensure adequate vendor performance in accordance with Section 7.11 of the Manual. The Procurement Section had generally complied with this requirement in cases where the contract period was extended, but in other cases, performance evaluation was not being made after the completion of contract.

Recommendation 9

OIOS recommends that the UNMISSET Procurement Section ensure that performance evaluation of contractors is conducted in all cases and a copy is kept in the contract file (AP2004/682/03/009).

34. *UNMISSET accepted recommendation 9 and stated that it has proceeded to complete vendor/contractor performance evaluations of all cases for FY 2004-2005.* In view of the Mission's response, OIOS has closed recommendation 9 in its database.

VI. ACKNOWLEDGEMENT

35. We wish to express our appreciation to the Management and staff of UNMISSET for the assistance and cooperation extended to the auditor during this assignment.

Copy to: Mr. Jean-Marie Guéhenno, Under-Secretary-General for Peacekeeping Operations
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