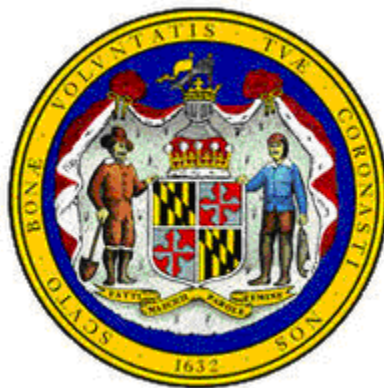


Audit Report

Office of People's Counsel

April 2008



OFFICE OF LEGISLATIVE AUDITS
DEPARTMENT OF LEGISLATIVE SERVICES
MARYLAND GENERAL ASSEMBLY

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Karl S. Aro
Executive Director

DEPARTMENT OF LEGISLATIVE SERVICES
OFFICE OF LEGISLATIVE AUDITS
MARYLAND GENERAL ASSEMBLY

Bruce A. Myers, CPA
Legislative Auditor

April 18, 2008

Senator Verna L. Jones, Co-Chair, Joint Audit Committee
Delegate Steven J. DeBoy, Sr., Co-Chair, Joint Audit Committee
Members of Joint Audit Committee
Annapolis, Maryland

Ladies and Gentlemen:

We have audited the Office of People's Counsel (OPC) for the period beginning May 4, 2005 and ending January 6, 2008.

Our audit disclosed that the OPC did not always obtain the required approvals for consulting services contracts. In addition, certain payments for these services were made even though the labor charges on the invoices differed from the contract rates.

Respectfully submitted,

Bruce A. Myers, CPA
Legislative Auditor

Background Information

Agency Responsibilities

The Office of People's Counsel (OPC) is responsible for protecting the interests of residential and non-commercial users of certain regulated services (such as gas, electricity, and telephone) relating to matters and proceedings before the Public Service Commission and the courts. According to the State's records, OPC expenditures were approximately \$3.2 million during fiscal year 2007.

Change in Method of Appointment

Chapter 5, Laws of Maryland, 2006 Special Session, effective June 23, 2006, altered the method of appointment of the People's Counsel and specified that the People's Counsel be appointed by the Attorney General with the advice and consent of the Senate. Previously, the People's Counsel was appointed by the Governor. The law established a five-year term of office for the People's Counsel beginning July 1, 2006 and also provided that the People's Counsel in office as of June 30, 2006 shall continue to serve at the pleasure of the Attorney General until such time as a successor is appointed. In this regard, on January 17, 2007, the Attorney General appointed a new People's Counsel to serve the remainder of the term.

Findings and Recommendations

Contractual Services

Finding 1

OPC did not always follow State Procurement Regulations for consulting services contracts, and certain payments were not adequately supported.

Analysis

OPC did not always follow State Procurement Regulations for consulting services contracts, and certain payments were not adequately supported. Our test of nine contracts totaling approximately \$711,000, procured during fiscal years 2007 and 2008, and ten related invoices totaling approximately \$238,000, disclosed the following conditions:

- Contracts were not always submitted to responsible State agencies for required approvals. Specifically, Department of Budget and Management (DBM) approval was not obtained for three contracts totaling \$160,000 procured by competitive sealed proposals. In addition, Office of the Attorney General approval was not obtained for three sole source contracts for confidential services totaling \$265,000.
- OPC increased the scope and value of one sole source contract from \$65,000 to \$130,000, but did not receive Office of the Attorney General approval for the modification and did not execute a formal contract amendment. Furthermore, two contracts tested were not signed by the vendors.
- OPC did not document the required sole source justifications for the aforementioned three contracts totaling \$265,000.
- Contractor invoices were paid even though billings were not always in accordance with the terms of the contracts and certain invoice amounts were not adequately supported. Specifically, for five contractor invoices that included labor charges totaling \$77,792, the rates on the invoices differed from those in the respective contracts or there were no labor rate schedules in the contracts. For example, one vendor billed OPC for 118 hours at \$190 per hour even though the highest rate in the contract was only \$175 per hour. We also noted that three invoices, with labor charges totaling \$47,115, were not accompanied by employee time sheets to substantiate the validity of labor hours included in the invoices, as required by the contracts. As a result, there was lack of assurance that all payments were proper.

State Procurement Regulations require that service contracts valued from \$25,000 to \$200,000 be approved by DBM and that sole source contracts and related modifications for confidential services (such as for pending litigation) be approved by the Office of the Attorney General. These Regulations also require that the reasons for sole source procurements be documented in writing.

Recommendation 1

We recommend that OPC comply with the provisions of the State Procurement Regulations. We also recommend that OPC ensure that labor rate schedules are included in its contracts, when appropriate, and that invoice payments are in accordance with the terms of the contract.

Audit Scope, Objectives, and Methodology

We have audited the Office of People's Counsel (OPC) for the period beginning May 4, 2005 and ending January 6, 2008. The audit was conducted in accordance with generally accepted government auditing standards.

As prescribed by State Government Article, Section 2-1221 of the Annotated Code of Maryland, the objectives of this audit were to examine OPC's financial transactions, records and internal controls, and to evaluate its compliance with applicable State laws, rules, and regulations.

In planning and conducting our audit, we focused on the major financial-related areas of operations based on assessments of materiality and risk. Our audit procedures included inquiries of appropriate personnel, inspections of documents and records, and observations of OPC's operations. We also tested transactions and performed other auditing procedures that we considered necessary to achieve our objectives. Data provided in this report for background or informational purposes were deemed reasonable, but were not independently verified.

OPC's management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that objectives pertaining to the reliability of financial records, effectiveness and efficiency of operations including safeguarding of assets, and compliance with applicable laws, rules, and regulations are achieved.

Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or compliance with policies and procedures may deteriorate.

Our reports are designed to assist the Maryland General Assembly in exercising its legislative oversight function and to provide constructive recommendations for improving State operations. As a result, our reports generally do not address activities we reviewed that are functioning properly.

This report includes a finding relating to a condition that we consider to be a significant deficiency in the design or operation of internal control that could adversely affect OPC's ability to maintain reliable financial records, operate effectively and efficiently, and/or comply with applicable laws, rules, and regulations. This finding is also considered to be a significant instance of noncompliance with applicable laws, rules, or regulations.

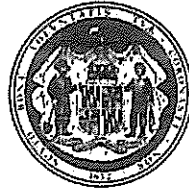
OPC's response to our findings and recommendations is included as an appendix to this report. As prescribed in the State Government Article, Section 2-1224 of the Annotated Code of Maryland, we will advise OPC regarding the results of our review of its response.

PAULA M. CARMODY
PEOPLE'S COUNSEL

APPENDIX
STATE OF MARYLAND

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April 16, 2008

Via Regular Mail and Electronic Delivery

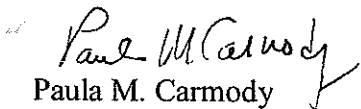
Mr. Bruce A. Myers
Legislative Auditor
Office of Legislative Audits
310 W. Preston Street – Room 1202
Baltimore, Maryland 21201

Dear Mr. Myers:

Enclosed please find the Office of People's Counsel's responses to the draft Legislative Auditor's Report for the period beginning May 4, 2005 and ending January 6, 2008. The Office had already instituted changes to its procedures prior to the audit to address certain concerns identified in the audit, and will continue to take steps to implement the remaining recommendations.

I wish to thank you and your staff for the manner in which the audit was conducted and for the constructive recommendations that were made as a result of the audit. If you have any questions or need additional information, please contact me at 410-767-8162 or the Office Administrator, Seva Diakoparaskevas, at 410-767-8165.

Sincerely,


Paula M. Carmody
People's Counsel

Enclosure

cc: Seva Diakoparaskevas, Administrator, OPC

Maryland Office of People's Counsel
Responses to Findings and Recommendations of Draft Audit Report
Period May 4, 2005 – January 6, 2008

Contractual Services

Finding 1

OPC did not always follow State Procurement Regulations for consulting services contracts and certain payments were not adequately supported.

Recommendation 1

We recommend that OPC comply with the provisions of the State Procurement Regulations. We also recommend that OPC ensure that labor rate schedules are included in its contracts, when appropriate, and that invoice payments are in accordance with the terms of the contract.

OPC Response:

OPC agrees with the finding and related recommendations. The Office had instituted changes in its consultant contracting procedures prior to the audit, and has instituted additional changes in response to the audit discussions.

OPC is an independent agency that represents the interests of residential utility consumers of regulated utility services in matters before the Maryland Public Service Commission, federal agencies and courts. In addition to the People's Counsel and Deputy People's Counsel, who are attorneys, the Office has several experienced attorneys who primarily represent the Office in regulatory litigation. Since the Office does not have technical staff, and must address a wide variety of accounting, economic and engineering issues in electric, gas, telecommunications and private water proceedings, the Office must retain the services of expert consultants to provide technical assistance and expert witness testimony in regulatory proceedings. Therefore, in almost all instances the contracts entered into by the Office are for consultant services on behalf of OPC in regulatory litigation. This was the case for the contracts referenced in the draft audit report.¹ Thus, while the Office agrees that the procurement regulations were not followed in certain instances, there is no doubt that the consultants were retained to provide expert witness services in Public Service Commission proceedings, and that they provided these services, including technical assistance and expert testimony in complex utility cases, subject to supervision by experienced attorneys in the Office. However, the Office understands the importance of proper documentation, and will implement the recommendations.

The Office revised its consultant contract procedures in July 2007, and has further revised these procedures to ensure that the Office is in compliance with State procurement law and regulations by obtaining (1) Attorney General approval for sole

¹ Contracts for consultant services for two Commission proceedings are the subject of many of the audit report's stated concerns.

Maryland Office of People's Counsel
Responses to Findings and Recommendations of Draft Audit Report
Period May 4, 2005 – January 6, 2008

source contracts that require confidentiality, and (2) DBM approval for any other service contracts valued from \$25,000 to \$100,000. As of this date, Office procedures have been modified to accomplish the following:

- Establish a work flow organizational system to establish personnel responsibility for discrete steps in the contracting process;
- Establish a redundant review process to ensure that sole source justifications and appropriate requests for approval are secured prior to submission of contracts to consultants;
- Revise the contract form to ensure that labor rate schedules appear in all consultant contracts;
- Establish a tracking system to ensure that consulting contract approvals (for example, AG approval) and executed contracts are maintained in consultant contract files;
- Maintain all contract- related correspondence and documents in a single consultant contract file;
- Compare all invoice labor rates with contractual labor rates to ensure payments consistent with contract terms; and
- Additional review of time and work description information on invoices by attorneys and procurement officer (Deputy People's Counsel).

Additionally, the Office is finalizing its revision of written procedures to be followed by all personnel involved in the contracting process to incorporate the audit recommendations and suggestions made during the audit process. While the procedural changes are in place already, the Office expects to schedule a meeting with all relevant employees within the next month to review the revised procedures.

AUDIT TEAM

Edward L. Shulder, CPA
Audit Manager

Terry S. Gibson
Senior Auditor