

City of Milwaukee Employees' Retirement System (ERS)

Vendor Management Audit Report

JANUARY 30, 2009

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EXECUTIVE SUMMARY

Background and Scope

As part of the annual audit plan, Jefferson Wells completed an audit of the Vendor Management process at ERS.

The objective of the Vendor Management audit was to determine whether ERS has implemented a Vendor Management process that assesses the risk of its vendor relationships, and requires appropriate efforts to monitor and mitigate those risks.

A comprehensive vendor management program generally includes an assessment of risks to identify your needs, the importance and criticality of the function, and the necessary controls and reporting processes over the activity. Based on the risk level, the program should define the need for, and extent of the following activities:

- Due diligence efforts to identify and select a vendor including assessing the vendor's competence and stability, both financially and operationally, as well as its ability to provide the contracted services over the life of the contract.
- Use of a written contract that states the duties, obligations, and responsibilities of the vendor and ensures that the vendor maintains adequate internal controls over activities.
- Ongoing oversight (including policies and controls) and periodic reviews of vendor performance, including assessments of costs, contract compliance, and service levels.

Fieldwork was completed from January 20, 2009 through January 30, 2009. The audit included the following activities:

- Determined if a vendor management process has been implemented to address the components of a sound vendor management program as listed above.
- Verified that the selection of vendors for outsourced services is performed in accordance with the organization's vendor management policies and procedures.
- Performed an assessment of the vendor management control structure.
- Developed audit work papers for the review of the vendor management controls and processes.

Conclusion

This report reflects the results of the Jefferson Wells Vendor Management audit. The techniques used to identify these results included interviews, observations, and review of documentation.

Based on the results of our review, ERS has implemented certain elements of a comprehensive vendor management program including the following:

- City of Milwaukee Board Rules and Regulations – requires the Board to review all ERS contracts.
- Professional Services Contract Checklist – defines the core items a contract should include.
- Statement of Investment Policy – defines the selection and review process of investment managers.
- Standard Contract for Services – contract for non-investment manager vendors.
- Standard Statement of Work – consulting agreement to define contractor roles and responsibilities.
- Use of a Request for Proposal process – used on an as needed basis for a new vendor.

Other aspects of a vendor management program are performed, however, are not consistent, formalized and documented. For example, a review process exists to annually review the performance of investment managers; however, other vendors are not formally reviewed periodically, and are not formally risk rated to indicate the need for an annual review or lack thereof.

ERS would benefit from additional enhancements and formalization of its vendor management program. The program should provide direction and guidance on each of the components listed in the background section above. Guidance should be provided on how to risk rate third party arrangements, and what additional steps are needed based on the risk rating.

Additional details regarding this finding, along with a recommendation for improvement is provided later in this report.

PROCEDURES PERFORMED

The following procedures were performed during the internal audit.

- Analyzed the top 25 highest paid vendors in fiscal years 2007 and 2008.
- Verified whether a risk analysis was performed on each vendor assessing the importance and criticality of the function to be provided, along with appropriate due diligence efforts to determine the competence, both financially and operationally, of the vendor prior to use.
- Reviewed management's use of written contracts that state the duties and obligations of each party. Conducted a review of a sample of current contracts to ensure they were current and that they were reviewed by the city attorney's office.
- Reviewed management's ongoing oversight and monitoring of vendors including performance levels, compliance, costs, etc.

ISSUE, RECOMMENDATIONS & MANAGEMENT'S RESPONSE

Vendor Management Program

A formal, documented "Vendor Management Program" does not exist. Although components of a program are in place, (i.e., contracts are used and existed for all tested vendors) procedures for assessing the risk of a third party arrangement, performing due diligence to identify and select a vendor, ensuring controls are in place to oversee the vendor's performance and management's ongoing monitoring and oversight of vendor performance are not performed consistently.

Recommendation:

Management should develop a formal Vendor Management Program that provides specific guidance on the following:

An assessment of risks to identify needs, the importance and criticality of the function, and the necessary controls and reporting processes over the activity. Based on the risk level, the program should define the need for, and extent and circumstances requiring the following activities.

- Due diligence efforts to identify and select a vendor including assessing the vendor's competence and stability, both financially and operationally, as well as its ability to provide the services over the life of the contract.
- Use of a written contract that states the duties, obligations, and responsibilities of the vendor and ensures that the vendor maintains adequate internal controls over activities.
- Ongoing oversight (including policies and controls) and periodic reviews (generally annually) of vendor performance, including assessments of costs, contract compliance, and service levels.

For each vendor, documentation should be maintained of all of these activities, or why, based on risk assessment results, the activity is considered unnecessary.

Management Response:

As indicated above, ERS management has many pieces in place to adequately address a vendor management program. A more formalized approach would be beneficial to the organization and institutionalize the knowledge of the current management team.

Responsible Party: Deputy Director

Implementation Date: December 2009