



EXAMINATION REPORT

**SOUTH CAROLINA DEPARTMENT of TRANSPORTATION'S
INTERNAL PROCUREMENT OPERATIONS
With REGARD to the DEPARTMENT'S EXEMPTIONS
from the
CONSOLIDATED PROCUREMENT CODE**

**Office of Audit & Certification
Division of Procurement Services
August 22, 2018**

TABLE OF CONTENTS

	<u>PAGE</u>
Transmittal Letter	1
Introduction.....	2
Understanding the Exemption	4
Historical Observations	6
Scope.....	12
Results of Examination.....	14
Recommendations.....	15
Conclusion	16
SCDOT's Response to Audit Report.....	17

HENRY MCMASTER, CHAIR
GOVERNOR
CURTIS M. LOFTIS, JR.
STATE TREASURER
RICHARD ECKSTROM, CPA
COMPTROLLER GENERAL



HUGH K. LEATHERMAN, SR.
CHAIRMAN, SENATE FINANCE COMMITTEE
W. BRIAN WHITE
CHAIRMAN, HOUSE WAYS AND MEANS COMMITTEE
GRANT GILLESPIE
EXECUTIVE DIRECTOR

THE DIVISION OF PROCUREMENT SERVICES

DELBERT H. SINGLETON, JR.
DIVISION DIRECTOR
(803) 734-8018

JOHN ST. C. WHITE
MATERIALS MANAGEMENT OFFICE
(803) 737-0600
FAX: (803) 737-0639

October 15, 2018

Delbert H. Singleton, Jr., Esq.
Director, Division of Procurement Services
State Fiscal Accountability Authority
1200 Senate Street, Suite 600
Columbia, SC 29201

Re: South Carolina Department of Transportation (DOT)
Examination of the Department's Exemption from the Procurement Code
July 1, 2017 to June 30, 2018

Dear Mr. Singleton:

We have examined DOT's internal procurement operations, as required by S.C. Code Ann. §57-1-490, to ensure that the Department has acted properly with regard to the Department's exemptions contained in Section 11-35-710. The examination covered the period from July 1, 2017 through June 30, 2018.

The examination found that DOT acted properly in the application of its exemptions. However, we made one recommendation to the Legislature regarding DOT's exemptions. No administrative penalties are warranted.

Sincerely,

John St. C. White
Materials Management Officer and State Engineer

INTRODUCTION

Since its initial enactment, the South Carolina Consolidated Procurement Code has expressly exempted broad categories of DOT's procurements, from all aspects of the Procurement Code. Those exemptions appear in §11-35-710(1) and have remained virtually unchanged since its initial enactment. Twenty-five years after granting these exemptions, the General Assembly asked the South Carolina Legislative Audit Council (LAC) to audit DOT's management of its resources. The LAC performed that audit and issued its report in November 2006. The following legislative session, the General Assembly enacted §57-1-490, a law requiring a more specific annual audit of DOT's use of its Procurement Code exemptions. An excerpt from that law states:

The Materials Management Office of the Department of Administration¹ annually must audit the department's internal procurement operation to ensure that the department has acted properly with regard to the department's exemptions contained in Section 11-35-710. The audit must be performed in accordance with applicable state law, including, but not limited to, administrative penalties for violations found as a result of the audit. The results of the audit must be made available by October fifteenth to the Department of Transportation, the Department of Transportation's chief internal auditor, the Governor, the chairmen of the Senate Finance and Transportation Committees, and the chairmen of the House of Representatives Ways and Means and Education and Public Works Committees. The cost and expenses of the audit must be paid by the department out of its funds.²

This report represents the eleventh annual audit under this law by the Materials Management Office.

Section 11-35-710(1) provides DOT the following exemptions from all aspects of the procurement requirements of Title 11, Chapter 35:

the construction, maintenance, and repair of bridges, highways, and roads; vehicle and road equipment maintenance and repair; and other emergency type parts or equipment utilized by the Department of Transportation or the Department of Public Safety;

¹ Act 121 of 2014 (SC Restructuring Act of 2014) abolished the Budget and Control Board and established the Department of Administration and the State Fiscal Accountability Authority effective July 1, 2015. The Act placed the Materials Management Office in the State Fiscal Accountability Authority.

² 2007 Act No. 114, §5 (codified in S.C. Code Ann. §57-1-490(B))

INTRODUCTION

Section 57-1-490(B) requires that the Materials Management Office (MMO) audit DOT "to ensure that the department has acted properly with regard to the department's exemptions contained in §11-35-710." Such an audit must begin with an understanding of the exemptions' meanings.

We conducted an examination of DOT's internal procurement operations as required by S.C. Code Ann. §57-1-490, to ensure that the department has acted properly with regard to the department's exemptions contained in §11-35-710.

The management of DOT is responsible for establishing and maintaining a system of internal controls over procurement operations to ensure proper application of the exemption. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of control procedures. The objectives of internal control relate to (1) financial reporting, (2) operations, and (3) compliance. Ensuring that the department acts properly with regard to the department's exemptions contained in §11-35-710 is a subset of those objectives. Management designs internal controls to provide reasonable assurance that unauthorized acquisition, use, or disposition of assets will be prevented or timely detected and corrected.

Because of inherent limitations in any system of internal controls, errors or irregularities may occur and not be detected. Projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the degree of compliance with the procedures may deteriorate.

Our review and evaluation of the system of internal control over internal procurement operations, as well as our examination of relevant procurement policies and procedures, were conducted with professional care. However, because of the nature of audit testing, they would not necessarily disclose all weaknesses in the system.

UNDERSTANDING the EXEMPTION

On its face, the statute contains a number of exemptions. The second and third exemptions, for equipment maintenance, and emergency-type parts and equipment, have received relatively little attention over the years. These exemptions are unambiguous and have been applied fairly consistently. In contrast, the exemption for "the construction, maintenance, and repair of bridges, highways, and roads" has been the subject of interpretation. Of primary concern is the meaning of the phrase "construction, maintenance, and repair of bridges, highways, and roads," and what each word encompasses.

To understand the standard we apply for evaluating DOT's application of the exemption to contracts, we refer to the first DOT exemption audit report dated October 15, 2008³. Understanding DOT's exemption for construction, maintenance, and repair of bridges, highways, and roads however, requires an understanding of the terms used in the wording of the statute.

Section 11-35-710(1) provides DOT an exemption for "the construction, maintenance, and repair of bridges, highways, and roads". The exemption must be read in conjunction with the definitions provided by the Procurement Code. The following four definitions are relevant.

"Construction" means the process of building, altering, repairing, remodeling, improving, or demolishing a public infrastructure facility, including any public structure, public building, or other public improvements of any kind to real property. It does not include the routine operation, routine repair, or routine maintenance of an existing public infrastructure facility, including structures, buildings, or real property."⁴

"Services" means the furnishing of labor, time, or effort by a contractor not required to deliver a specific end product, other than reports which are merely incidental to required performance. This term includes consultant services other than architectural, engineering, land surveying, construction management, and related services. This term does not include employment agreements or services as defined in §11-35-310(1)(d).

"Architect-engineer and land surveying services" are those professional services associated with the practice of architecture, professional engineering, land surveying, landscape architecture, and interior design pertaining to construction, as defined by the laws of this State, as well as incidental services that members of these professions and those in their employ may logically or justifiably perform, including studies, investigations,

³ The October 15, 2008, DOT Exemption Report is available on the web at: <https://procurement.sc.gov/files/DOT08.pdf>. Our discussion of the definition of construction titled "CONSTRUCTION INCLUDES DESIGN" begins on page 14 of that report.

⁴ §11-35-310(7) In 2008, the definition of construction was amended. 2008 Act No. 174.

UNDERSTANDING the EXEMPTION

surveys, evaluations, consultations, planning, programming conceptual designs, plans and specifications, cost estimates, inspections, shop drawing reviews, sample recommendations, preparation of operating and maintenance manuals, and other related services.

"Construction management services" are those professional services associated with a system in which the using agency directly contracts with a professional construction manager to provide that group of management activities required to plan, schedule, coordinate, and manage the design and construction plan of a state project in a manner that contributes to the control of time, cost, and quality of construction as specified in the construction management contract.

Read together, these definitions clearly distinguish construction services from non-construction services, both those related to construction and those not. Narrowly looking at these definitions, one might conclude DOT's exemption for construction does not extend to any construction related professional services because the term construction does not include architectural and engineering, construction management, and land surveying services. However, as explained in the October 15, 2008 audit report, MMO applies a broader definition of construction to DOT's exemption. MMO concluded the exemption includes construction related professional design services, as defined by law. Further, the exemption applies to contractual services for maintenance and repair of bridges, highways, and roads. However, the exemption does not apply to procurements of materials and supplies used by in-house personnel for such activities.

HISTORICAL OBSERVATIONS

Prior audits of DOT's exemption, as well as our study of its history, the Procurement Code, and the applicable federal laws leads to the following observations.

Oversight and Uniform State Procurement Policy

Just two years after the ABA issued its original Model Procurement Code for State and Local Government, the General Assembly enacted South Carolina's Consolidated Procurement Code.⁵ While the Model Code strongly favors the centralization of procurement policy and authority, it includes optional, alternate text by which the legislature can delegate to the relevant purchasing agency the authority for certain types of procurements, subject to all the procurement code's purchasing procedures. Of the four areas expressly contemplated⁶, the ABA's revisions to the Model Code in 2000 reiterate this option, though the wording was revised, as follows, to reflect developments in the intervening twenty years: "the design, construction, maintenance, operation, and private finance of bridge[s], [and] highway[s]..."⁷ Despite providing this alternate option, the ABA's commentary makes clear its continued recommendation for centralized procurement authority and uniform procurement procedures:

[These categories] represent examples of types of procurements which a legislature may see fit to exempt from centralized procurement. These types of procurements would then remain with the Purchasing Agencies which require these supplies, services, or construction. However, *centralized responsibility for procurement is preferred, and procurement functions vested in the Chief Procurement Officer can always be delegated to other agencies or officials.* Again, experience has shown that a cohesive and integrated procurement system rather than one which is fragmented or diffused, will promote efficiency and economy and will best conserve the taxpayers' monies.⁸

⁵ "The General Assembly finds that: (1) it adopted a modified version of the 1979 ABA Model Procurement Code for State and Local Governments when it enacted 1981 Act No. 148. Since then, the ABA has revised its recommended model by adopting the 2000 ABA Model Procurement Code for State and Local Governments, which it developed in cooperation with, among others, the National Association of State Procurement Officials, the National Institute of Governmental Purchasing, the American Consulting Engineers Council, the Design Professionals Coalition, the Council on the Federal Procurement of A/E Services, the Engineers Joint Contracts Document Committee, and the National Society of Professional Engineers." 2008 Act. No. 174, § 1.

⁶ ABA Section of Urban, State and Local Government Law, Model Procurement Code for State and Local Governments § 2-303 (1979).

⁷ American Bar Association, 2000 ABA Model Procurement Code for State and Local Governments § 2-303 (2000).

⁸ ABA Section of Urban, State and Local Government Law, Model Procurement Code for State and Local Governments § 2-303 commentary (1979) (emphasis added).

HISTORICAL OBSERVATIONS

Consistent with this recommendation, South Carolina has adopted a strong, centralized approach to public procurement. Authority and policy are centralized in the State Fiscal Accountability Authority (SFAA), with purchasing authority delegated back to purchasing agencies consistent with their capabilities. DOT's exemption is a major exception to this basic policy.⁹

Policy Behind Exemption and Conflicts with Federal Laws

The reason for granting DOT an exemption for "construction, maintenance, and repair of bridges, highways, and roads" is unknown. Apparently, those involved assumed that the exemption "was to relieve [DOT] of the necessity of following two different sets of procurement procedures since the federal government requirements also apply to highway and road construction."¹⁰

Even if the assumption is correct, the justification is flawed for several reasons. First, federal law contemplates, in part, that state laws can govern.¹¹ Second, the federal laws that do apply often contemplate expressly that states will have their own rules that govern, in addition, or as a gap-filler for, the federal rules.¹² Third, the federal law does not provide participating contractors with a practical and effective avenue of relief. Unlike the Consolidated Procurement Code, which

⁹ With two exceptions, the only other entities that have been granted such sweeping exemptions are quasi-governmental authorities, entities frequently given special treatment by the law. Specifically, the State Ports Authority, the Public Service Authority (Santee Cooper), the South Carolina Research Authority, the Medical University Hospital Authority, the Jobs-Economic Development Authority (JEDA), Midlands Authority, Midlands Technical College Enterprise Authority, Trident Technical College Enterprise Campus Authority, Venture Capital Authority, and the Edisto Development Authority all have exemptions. *See, generally*, S.C. Code Ann. § 11-35-710. The exceptions are the Division of Public Railways of the Department of Commerce and non-construction procurements by higher education using certain athletic, student, and canteen funds. S.C. Code Ann. § 11-35-710(4)&(6).

¹⁰ Letter from Zeigler to Mabry of 7/10/97, and Letter from Probst to Fusco of 5/24/01.

¹¹ See discussion in text below under heading "Unregulated Procurements". *See, also*, 23 C.F.R. § 636.110 (2008) ("You may use your own procedures for the solicitation and receipt of proposals and information ..."). Title 23, Part 636 of the CFR contains the FHWA's policies and procedures for approving, and the contracting procedures for conducting, all design-build projects funded under title 23 of the U.S. Code. 23 C.F.R. § 636.101 (2008). *See, generally*, 23 U.S.C. 112(b)(3)(A) ("A State transportation department or local transportation agency may award a design-build contract for a qualified project described in subparagraph (C) using any procurement process permitted by applicable State and local law.").

¹² *E.g.*, 23 C.F.R. 636.119(a) (2007) ("In order for a project being developed under a public-private agreement to be eligible for Federal-aid funding . . . the contracting agency must have awarded the contract to the public-private entity through a competitive process that complies with applicable State and local laws."). Also see discussion in text above under heading "Unregulated Procurements".

HISTORICAL OBSERVATIONS

provides an inexpensive and speedy administrative review process, contractors concerned with the integrity of a highway contract must go to court and seek an injunction.¹³

These reasons aside, the Consolidated Procurement Code expressly provides for conflicts between federal and state rules -- by requiring agencies to comply with any applicable federal law.¹⁴

Even if the Consolidated Procurement Code applied to all highway and road construction, the SFAA's role in construction procurements is relatively narrow. The SFAA's Chief Procurement Officer for Construction (CPO) does not enter into contracts for other state entities and is not a party to those contracts. Likewise, the CPO does not issue procurements, select contractors, make awards, or handle day-to-day administration of agency contracts. Rather, the CPO provides oversight, auditing, certain procurement-related approvals (e.g., use of pre-qualification), policy, and a quasi-judicial administrative review process for procurement protests and contract disputes.

Unregulated Procurements

Grouped by which *laws* dictate procedures governing how a public contract is awarded, DOT's procurements can be divided into four groups:

- Awards governed by state procurement code laws.
- Awards governed by federal procurement laws.
- Awards governed by a mix of federal and state procurement laws.
- Awards not governed by any law dictating how the contract is awarded.¹⁵

Of primary concern are awards not governed by any law dictating how contracts are awarded.

A review of applicable federal rules explains. In the federal regulations that dictate the

¹³ See, e.g., *Clark Construction Co. v. Pena*, 895 F. Supp. 1483 (M.D. Ala. 1995).

¹⁴ *S.C. Code Ann.* § 11-35-40(3).

¹⁵ MMO understands that DOT has internal procedures for such contracts. However, such internal procedures do not provide the safeguards provided by law. While some state statutes govern, these laws say *very* little regarding how the contracts must be awarded and primarily serve as a grant of authority to contract. E.g., S.C. Code Ann. §§ 57-3-200 (grant of authority), 57-5-1620 (requiring advertising and award to lowest qualified bidder), 57-5-1625 (authorizing design-build and the use of evaluation criteria), 57-5-1630 (creating limits on post-award change orders), and 57-5-1650 (authorizing pre-qualification of DOT contractors).

HISTORICAL OBSERVATIONS

procurement rules for contracts involving federal grant money, the default rule is that states must use their own procurement procedures.¹⁶ This default rule yields to any program-specific, federal statutory requirements.¹⁷ For example, federal law establishes certain aspects of the procurement process to be used for entering into a federal-aid, design-build highway construction contract.¹⁸ In the absence of any program-specific federal statutory requirements, federal regulations do not dictate how states award federally funded public contracts. If state law does not provide any procurement rules such as we find from DOT's procurement code exemption found in §11-35-710(1), there are none.¹⁹ Stated differently, no significant,²⁰ enforceable laws govern how DOT awards public contracts that fall within the scope of DOT's procurement code exemption that is not governed by a program-specific federal statutory requirement.²¹ Examples would include DOT road construction projects that use no federal funds, such as primary or secondary roads.

Even when federal law dictates certain procedures for DOT procurement, significant aspects of those procurements either remain unregulated or expressly contemplate that some state law will dictate the appropriate procurement process.²² For example, the federal regulations governing the

¹⁶ *Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments*, 49 C.F.R. §18.1 & §18.36(a) (2007) (often called the "Common Rule") ("When procuring property and services under a grant, a State will follow the same policies and procedures it uses for procurements from its non-Federal funds."). *See, generally, City of Cleveland v. Ohio*, 508 F.3d 827 (6th Cir. 2007).

¹⁷ 49 C.F.R. §18.4(a) (2007) ("[This 'Common Rule' applies] to all grants and sub-grants to governments, except where inconsistent with Federal statutes or with regulations authorized in accordance with the exception provision of §18.6 . . .").

¹⁸ 23 C.F.R. 636.104 (2007). Federal regulations also provide a limited set of rules regarding the award of low bid, federal-aid highway construction work. 23 C.F.R. Part 635. In large measure, these rules are consistent with, but much more limited than, the rules provided for in the Consolidated Procurement Code.

¹⁹ *See* 49 C.F.R. §18.36(a) (2007).

²⁰ While some state statutes govern, these laws say *very* little regarding how the contracts must be awarded and primarily serve as a grant of authority to contract. *E.g.*, S.C. Code Ann. §§ 57-3-200 (grant of authority), 57-5-1620 (requiring advertising and award to lowest qualified bidder), 57-5-1625 (authorizing design-build and the use of evaluation criteria), 57-5-1630 (creating limits on post-award change orders), and 57-5-1650 (authorizing pre-qualification of DOT contractors). MMO understands that DOT has internal procedures for such contracts. However, such internal procedures do not provide the safeguards provided by laws.

²¹ *See, generally, FHWA Policy Memorandum, Procurement of Federal-aid Construction Projects* (June 26, 2008) (explaining relationship between the "common rule" and the program-specific statutes and regulations), and FHWA Policy Memorandum, *Procurement of Transportation Enhancement Projects* (November 12, 1996). FHWA Policy Memoranda are available at <http://www.fhwa.dot.gov/legsregs/elecdirs.htm>.

²² *E.g.*, 23 C.F.R. 636.119(a) (2008) ("In order for a project being developed under a public-private agreement to be eligible for Federal-aid funding (including traditional Federal-aid funds, direct loans, loan guarantees, lines of credit,

HISTORICAL OBSERVATIONS

award of federal-aid, design-build highway construction contracts expressly provide for states to use their own procedures for the advertisement, solicitation, receipt, evaluation, and award of proposals.²³ Federal regulations also provide some rules regarding the award of low bid, federal-aid highway construction work; however, these rules are, in large measure, consistent with, but much more limited than, the rules provided for in the Consolidated Procurement Code.²⁴

or some other form of credit assistance), the contracting agency must have awarded the contract to the public-private entity through a competitive process that complies with applicable State and local laws." (emphasis added), 23 C.F.R. §635.110(f) (2008) (allowing states to use their own qualification or prequalification procedure for any phase of a design-build procurement).

²³ 23 C.F.R. §635.113(c)(1) (2008) (providing for the state to use its own process for handling proposals and information; reviewing and evaluating proposals; allowing the submission, modification, revision and withdrawal of proposals; and announcing awards), 23 C.F.R. §636.110 (2008) ("You may use your own procedures for the solicitation and receipt of proposals and information ...").

²⁴ 23 C.F.R. Part 635

HISTORICAL OBSERVATIONS

Unresolved Ambiguities

In 1994, the Attorney General's Office observed that §11-35-710(1) "is not artfully drafted and ... is susceptible to various interpretations."²⁵ Years of administrative interpretation has yet to resolve the ambiguity inherent in DOT's procurement code exemption.

Allowing this ambiguity to continue has real costs. First, the agencies involved have spent considerable time addressing this issue. Second, private businesses seeking to contract with the state make assumptions on such matters at their own risk, as the courts have long saddled business with the risk of knowing whether or not the agency they do business with has the proper authority.²⁶ Third, a lack of clarity in procurement laws can lead to expensive litigation, with consequences for all involved.²⁷ Only legislative action can fully conclude this matter.²⁸

²⁵ S.C. Att'y Gen. Op. No. 94-9, dated January 14, 1994, at 2.

²⁶ E.g., *Service Management, Inc. v. State Health and Human Services Finance Commission*, 298 S.C. 234, 379 S.E.2d 442 (Ct. App. 1989) ("Finally, parties entering into agreements with the state assume the risk of ascertaining that he who purports to act for the state stays within the bounds of his authority.").

²⁷ E.g., *Sloan v. Department of Transp.*, 365 S.C. 299, 618 S.E.2d 876 (2005) (interpreting DOT's authority to conduct competitive sealed proposals), *Sloan v. Department of Transp.*, 2008 WL 3890145, Op. No. 26534 (S.C. filed August 25, 2008) (Shearouse Adv. St. No. 33, at 73) (interpreting the scope of DOT's authority to conduct emergency procurements).

²⁸ See, generally, Letter from Representative E.B. McLeod, Jr. to Ron Joye, Department of Transportation dated 3/30/94 (implicitly recognizing the need for legislative action and requesting an explanation of DOT's procurement processes and a side by side comparison of those processes with those required by the Consolidated Procurement Code) (copy attached). To date, our state courts have had little opportunity to address this issue. See, generally, *Sloan v. Department of Transp.*, 2008 WL 3890145, Op. No. 26534 (S.C. filed August 25, 2008) (Shearouse Adv. St. No. 33, at 73) ("Contracts for the construction, maintenance, and repair of highways and roads are specifically exempted from the South Carolina Consolidated Procurement Code (Procurement Code). See S.C. Code Ann. §11-35-710 (Supp. 2007). The procurement of construction contracts for the state highway system is governed by [§57-5-1620].").

SCOPE

We conducted our examination to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We conducted an on-site review from August 1 through August 22, 2018. Our examination included testing, on a sample basis, evidence about DOT's internal procurement operations with regard to compliance with the exemptions in §11-35-710 (1), for the period July 1, 2017 through June 30, 2018, the audit period, and performing other procedures we considered necessary in the circumstances. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The scope of our procedures was limited to ensuring that the department acted properly in the application of the exemption, and did not include an examination of the procurement methodology used. (MMO audits DOT's procurement methodology in another audit.)

Our testing was limited to contracts awarded under DOT's exemption during the audit period as follows:

Population Attribute	Population		Sample		Audit Coverage (percent of Population)	
	Count	\$ Amount (millions)	Count	\$ Amount (millions)	Count	\$ Amount
1. Road Construction Contracts	290	949	42	371	14%	39%
2. Architect-Engineer and Land Surveying Services	49	68	18	19	37%	28%
3. DOT Listing of Exempt POs and Solicitations	179	12	18	1.7	10%	14%
4. DOT PO Expenditures in SCEIS	10,202	144	96	22	1%	15%
DOT Direct Pay Expenditures in SCEIS ²⁹	2,498	904	23	77	1%	8%
5. DOT Capital Improvements	89	3.5	9	0.172	10%	5%

²⁹ The total Direct Pay expenditure amount, \$904 million, substantially exceeded expenditures by PO, \$144 million, because it included payments for construction projects which were paid from certificates of completion, and did not require a PO.

SCOPE

1. Road Construction Contracts

DOT Construction provided listings of Exempt solicitations issued during the audit period. We tested road construction contracts awarded, with no exceptions.

2. Architect-Engineer and Land Surveying Services

DOT Engineering provided listings of Exempt solicitations issued during the audit period. We tested consultant and design related professional services contracts awarded, with no exceptions.

3. DOT Listings of Exempt Purchase Orders (POs) and Solicitations

DOT Procurement provided listings of Exempt POs and solicitations issued during the audit period. These lists were tested for accuracy and completeness. We then tested POs and solicitations determined to have been treated as exempt, with no exceptions.

4. DOT Expenditures in SCEIS

We extracted listings of POs and Direct Pays from SCEIS for the audit period to ensure that exempt transactions provided in step 3 had been properly identified. We filtered the populations to eliminate obvious non-exempt transactions to ensure effective testing.

Examples of transactions eliminated from the population include: expenditures to governmental agencies, travel reimbursements, legal services, membership and registration fees, electricity, freight express delivery, utilities, and education and training.

This process reduced the PO population from 25,199 to 10,202 transactions. The Direct Pay population was reduced from 30,453 to 2,498 transactions.

We tested PO's and Direct Pays from the remaining population by analyzing selected transactions to validate their proper treatment as Exempt transactions. To ensure the completeness of DOT's listing of Exempt PO and Direct Pay transactions in step 3, we verified that the tested transactions had been properly identified and reported as Exempt by DOT. We found no exceptions.

5. DOT Capital Improvements

We tested capital improvement projects to determine that DOT acted properly with regard to the exemption, with no exceptions.

RESULTS of EXAMINATION

DOT's exemption from the Procurement Code applies to procurements for construction, maintenance, and repair of bridges, highways, and roads; vehicle and road equipment maintenance and repair; and other emergency-type parts or equipment. In 2007, the General Assembly enacted a law that requires MMO to audit DOT annually with regard to DOT's application of the exemption.

Our testing of DOT's internal procurement operation of procurement transactions for the period July 1, 2017 through June 30, 2018 was performed to ensure DOT acted properly with regard to its exemption. DOT's application of the exemption from the Procurement Code resulted in over \$1 billion in contracts awarded during the audit period.

Based on this examination, we believe DOT acted properly in applying the exemption.

RECOMMENDATION

As noted in the 'Historical Observations' Section of this report, §11-35-710(1) "is not artfully drafted and... is susceptible to various interpretations."³⁰ However, the chart on page 12 demonstrates the magnitude of the exemption's application.

As a result, MMO makes the following recommendations consistent with South Carolina's history of centralizing procurement policy and authority in the State Fiscal Accountability Authority:

General Assembly

1. Repeal DOT's existing exemptions, as provided by SC Code Ann. §11-35-710(1), to make the Consolidated Procurement Code applicable to all DOT procurements.

State Fiscal Accountability Authority

2. After the exemptions are repealed, pursuant to §11-35-1210, grant DOT unlimited certification in the area of bridge, highway and road construction projects. Also, pursuant to §11-35-1210, grant DOT unlimited certification in certain defined areas specifically related to highway construction and for which DOT has considerable expertise and staff.

Until the exemptions are repealed, no action is required by the State Fiscal Accountability Authority.

Chief Procurement Officers

3. After the exemptions are repealed, pursuant to §11-35-840, all three Chief Procurement Officers should delegate their authority to resolve contract and breach of contract controversies, under §11-35-4230 and §11-35-4320, to the State Highway Engineer or other appropriate DOT official.

These recommendations are interrelated and intended to be adopted together as a coordinated approach to addressing the challenges of the exemptions.

³⁰ S.C. Att'y Gen. Op. No. 94-9, dated January 14, 1994, at 2.

CONCLUSION

South Carolina Code of Laws §57-1-490(B) requires the Materials Management Office to annually audit the South Carolina Department of Transportation's internal procurement operation to ensure that the department has acted properly with regard to its exemption contained in §11-35-710(1). The audit must be performed in accordance with applicable state law, including, but not limited to, administrative penalties for violations found as a result of the audit. The results of the audit must be made available by October fifteenth to the Department of Transportation Commission, the Department of Transportation's chief internal auditor, the Governor, the chairmen of the Senate Finance and Transportation Committees, and the chairmen of the House of Representatives Ways and Means and Education and Public Works committees.

Our audit concluded that DOT acted properly with regard to the exemptions contained in §11-35-710(1). No administrative penalties are warranted.



Judith Nevergoll, CPA
Audit Manager



D. Crawford Milling, CPA, CGMA
Director of Audit & Certification

October 15, 2018

Mr. D. Crawford Milling, CPA, CGMA
Director of Audit & Certification
Division of Procurement Services
1201 Main Street, Suite 600
Columbia, SC 29201

RE: SCDOT Procurement Code Exemption Audit

Dear Mr. Milling:

Thank you for the October 12, 2018 draft audit of the South Carolina Department of Transportation's (SCDOT) legislative procurement exemptions in compliance with state law Section 57-1-490 (B). SCDOT is again pleased that no exceptions were noted and a determination the agency acted properly with regard to South Carolina state law (11-35-710 (1)) is cited. Staff is committed to continued cooperation with the Materials Management Office (MMO) of the State Fiscal Accountability Authority.

SCDOT does not concur with a recommendation to eliminate the exemption provided in state law. SCDOT follows South Carolina Code of Laws Sections 57-5-1620 and 57-5-1625 in the award of construction contracts. Agency staff will continue to work with MMO to strengthen policies and procedures ensuring the highest levels of integrity and transparency.

Thank you again, for your assistance and guidance in this process. Should there be additional questions or a need of further information, please do not hesitate to contact me directly.

Regards,



Brian W. Keys, P.E.
Deputy Secretary for Finance and Administration

BWK:clb

cc: J. Darrin Player, Chief Procurement Officer
Judith Nevergoll, Audit Manager, MMO

