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# inside outsourcing

A Year in the Life of City Contracting

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## INTRODUCTION

It is no secret to even a casual observer of local government that the City of New Orleans is facing serious financial problems. Within weeks of taking office, the new administration identified a \$68 million deficit in the general fund. Recently, it increased the projected hole to \$79 million for 2010.<sup>1</sup> In his 2011 budget proposal, the Mayor indicated that it would be necessary to increase City property taxes that go to the operating budget by 24%.<sup>2</sup>

The lion's share of budget overruns and cutbacks has been in the area of personnel. Closing the deficit has required, among other things, the use of one-time revenues, layoffs, furloughs and cuts in pension payments.

Bringing personnel expenditures under control is an essential step in addressing the City's fiscal problems. After all, personnel costs are a major component of government spending. There is, however, another area that significantly affects the City's bottom line: contracting.

It is clearly an area with problems. Over the past few years, individual contracts have come under intense scrutiny. Federal, State and local investigations have documented abuses of selection processes, ineffective performance monitoring and other problems. Mindful of these problems, the new administration has issued a series of executive orders to begin the process of reforming City contracting.

While previous investigations have focused on specific contracts or types of contracts, no study has provided a broad overview of City contracting. In this report, BGR presents information on the extent and characteristics of City contracting in New Orleans during the City's most recent complete fiscal year, 2009. It also discusses problems that surfaced in the course of its review of those contracts.

Among BGR's key findings:

- The City evaded its competitive selection process through excessive expansions of some contracts.
- The City misclassified certain nonprofessional

services as professional services, improperly placing them in a selection process with greater discretion in choosing the winning proposal.

- The City contracted heavily for basic functions that it could have handled more efficiently in-house.
- The City wasted taxpayer money on contracts that failed to deliver the promised results.
- The City wasted money on contracts for projects that never came to fruition.
- The City spent taxpayer money on legal and technical contracts that would have been unnecessary if the City had managed its public records responsibly.
- Despite its crushing fiscal situation, the City directed flexible CDBG funds to privately owned developments when it could have used the money to cover unmet public sector needs in low- and moderate-income neighborhoods.
- The City failed to impose reasonable caps on contracts to provide federally-funded elevation grants, leading to absurdly disproportionate grant awards.

## WHEN DOES CONTRACTING MAKE SENSE?

A threshold question in contracting is whether it makes sense to use an outside contractor. In some cases, such as the procurement of manufactured goods, the answer is obvious. Supplies, materials and equipment are typically procured from outside vendors.

When it comes to the procurement of services, the question becomes more complicated. The City must decide whether it is more beneficial to perform the task in-house or obtain the services from an outside contractor. Reasonable factors that tend to support the decision to contract out include:

- The contract would yield cost savings.
- The contract would improve service quality.
- A contractor would provide skills or expertise that are needed on a limited basis and too costly to retain in-house.
- The contract would allow government to handle significant spikes in workloads.

## SCOPE, METHODOLOGY AND LIMITATIONS

For the purposes of this study, BGR requested all City contracts in effect at any time during 2009. In response, the City made available, and BGR reviewed, approximately 1,000 contract files in the City Attorney's office. BGR also reviewed professional services contracts posted on the City's website. It obtained additional contracts from the City Council and the council's website. In addition, BGR reviewed news articles, reports by State and local oversight entities, and lists generated from various City databases.

Ultimately, BGR gathered and reviewed 822 complete contracts. BGR was unable to determine exactly what percentage of City contracts this represents. That's because the City could not provide a complete list of the contracts in effect during 2009.

BGR's review encompassed contracts to which the City itself was a party; contracts of certain public benefit corporations through which the City operates property;<sup>3</sup> and contracts of attached boards and commissions of the City, such as the Civil Service Commission. It did not include those of unattached boards and commissions, such as the City Planning Commission and Sewerage & Water Board.

BGR did not conduct a systematic review of related procurement documents, selection processes, contract expenditures or performance monitoring. The report does not address problems that such a review might have uncovered.

Because of the various ways in which the City compensates contractors, BGR could not determine the total dollar value of the contracts from the documentation. The contracts and agreements have different bases of compensation. They could be fixed-price or lump-sum payments, reimbursement of expenses up to a dollar cap, or payment on a price-per-unit basis. An accurate tally of the total value would require an analysis of contractual encumbrances and expenditures that was beyond the scope of this study.

## OVERVIEW OF CONTRACTS BY TYPE

Half of the contracts that BGR reviewed were for professional services. Another 22% were grant agreements. The remainder included, among others, contracts for cooperative endeavors; nonprofessional services; facility and public works construction; purchases of equipment, materials and supplies; the lease or use of real property for City purposes; and the lease or use of City-owned real estate for private or other public purposes. Table 1 provides a breakdown of contracts by type.

The contracts BGR reviewed ranged in value from a few thousand dollars to tens of millions of dollars. Among the high-value contracts with private companies were the City's technology services contract with Ciber Inc. (\$46.8 million), its recovery project management contract with MWH Americas Inc. (\$31.7 million paid through October 21, 2010) and its three contracts for residential garbage collection (totaling \$35.9 million in 2009).

For more information on the types of contracts, see the Appendix.

## EVADING THE COMPETITIVE SELECTION PROCESS

Competition is critical to achieving the benefits of contracting in the form of lower prices and better quality for goods and services. Yet the City avoided competition in several ways, such as expanding the scope of work for major contracts to cover unrelated projects and misclassifying nonprofessional services as professional ones.

### Excessive Expansions in Contract Scope

BGR found that the City circumvented the competitive selection process by inappropriately expanding the scope of services and dramatically increasing the dollar value of several large professional services contracts. BGR considered an expansion of scope to be inappropriate if it substantially altered the services to be provided under the original contract or added services unrelated to those specified in the original contract.

**Table 1: City Contracts in Effect During 2009, by Type**

Type of Contract	Contracts Reviewed
Professional services	410
Grants of federal, state and local funds administered by City	183
Other cooperative endeavors (excluding grants)	72
Nonprofessional services	37
Construction of facilities and other public works	30
Equipment, materials and supplies, including lease-purchase agreements	21
Lease or use of real property for City purposes	19
Lease or use of City-owned real estate for private or other public purposes	19
Other	31
<b>Total reviewed</b>	<b>822</b>

*Ciber Inc.* In the summer of 2005, the City hired Ciber Inc. to migrate and maintain the City’s computer applications from a mainframe environment to a web-based platform. The contract set forth a series of related tasks, such as developing and maintaining a system to operate integrated applications and working on GIS technologies. It provided for payment according to a fee schedule subject to a cap of \$5.5 million. The City renewed the original contract, which it referred to as a “Master Services Agreement,” four times.

According to the Legislative Auditor, over time the City assigned Ciber tasks outside the scope of the initial contract. In the wake of the flooding, it asked Ciber to switch its focus from the migration project to restoring and maintaining operations. Given the chaotic and critical circumstances, the redirection on an emergency basis was sensible. However, the City also asked Ciber to perform additional services that cannot be justified on that basis. The Legislative Auditor provided four examples in its report: network services related to the installation of the City’s crime cameras, a new electronic routing system for approving City con-

tracts, a software package related to a short-lived charter school project, and “technology related/program management support services” for the City’s Capital Projects Administration.<sup>4</sup> These four projects totaled more than \$5.9 million.

As a result of contract renewals and expansions, from 2005 to 2009 the cap on the Ciber contract increased more than eight-fold, from \$5.5 million to \$46.8 million. This made it the most expensive professional services contract found in BGR’s review. In renewing, the City transformed the contract from a discreet set of pre-Katrina services to a massive privatization of its information technology services after post-Katrina layoffs in that department. The contract expired at the end of 2009.

*Telecommunications Development Corp.* In October 2009, the City entered into a three-month, \$450,000 contract with Telecommunications Development Corp. to provide project management and personnel services for the City’s technology office. Less than a week into the contract term, the City expanded its scope to include “staff augmentation and project management services” for the City’s Project Delivery Unit, which manages recovery projects. This more than tripled the value to \$1.5 million. In late March and early April 2010, instead of issuing new RFPs or considering moving those services in-house, the City twice amended the contract, extending the term and increasing the cap by more than \$3.5 million.<sup>5</sup> This brought the total to more than 10 times the size of the contract the City signed only several months earlier. The current administration has renegotiated the contract to eliminate the firm’s services to the Project Delivery Unit. The City continues to use some of the company’s services in the technology office.

*Public Financial Management.* In 2007, the City retained Public Financial Management to provide a broad range of financial and management advisory services, including the development and implementation of a new budget model,<sup>6</sup> financial forecasting, revenue evaluation, capital programming and performance reporting. The City extended the contract twice for one-year periods as allowed under the original contract. It also added a wide range of unrelated or loosely related services, including: verifying locations for

residential garbage collection, reviewing pension fund investment procedures, reviewing the functions of the Mayor’s Office of Technology, providing financial advisory services for possible bond issues, and providing forensic reviews and assessments of “operations, vendor and contract relations and finances” upon request. These extra services totaled approximately \$450,000. As a result of these expansions and the renewals, the contract cap increased from \$990,000 to \$3,187,000 as of December 31, 2009.

The previous administration failed to fully implement the budget model, called “Budgeting for Outcomes.” The current one extended the contract so that the firm could assist with the 2011 budget process and full implementation of the model.

By expanding the scope of services in these large professional services contracts, the City failed to explore the potential benefits of fresh competition. In each of these cases, the City avoided the competitive selection process by tapping existing contractors to handle work only loosely related, at best, to their original contracts.

### **Inappropriate Classification as ‘Professional Services’**

The City Charter provides that contracts for “the rendering of any services to the City, other than professional services,” shall be awarded to the lowest responsible bidder.<sup>7</sup> The charter further requires the City to award professional services contracts through competitive selection processes established by the Mayor and the City Council. That process can take into account factors other than price, such as expertise and service quality.

Professional services include both recognized professions, such as law, architecture and accounting, and occupations requiring a high level of training and proficiency, such as information technology.<sup>8</sup> The City avoided going through a bid process by inappropriately designating certain services as professional. These included call center, copying, news clipping and boat towing services.

The largest of these, by far, was the \$5.7 million contract with ACS State & Local Solutions Inc. to provide the system and staffing for the City’s ill-fated 311 call

center. The system drew numerous complaints from citizens who could not get answers to problems they reported. Some difficulties arose from the City’s failure to integrate the 311 system with the computer systems used by many City departments.<sup>9</sup> The City ultimately terminated the contract on June 30, 2009, six months prior to the end of its three-year initial term, and moved the 311 operation in-house. Subsequently, the City selected a different vendor – through a competitive bid process as a nonprofessional services contract – to provide 311 call center services in emergency situations.

Categorizing nonprofessional services as professional services inappropriately removes them from competitive bidding rules that require them to go to the lowest responsible bidder. It allows for the selection of contractors who may not be offering the lowest price, leaving taxpayers to cover the difference.

### **The Threshold for Competitive Selection**

City law does not require a competitive selection process for professional services contracts of \$15,000 or less.<sup>10</sup> Used properly, the exemption for smaller contracts enables the City to avoid a disproportionate investment of time and money in a procurement process. However, it can also provide an opportunity for patronage because of the wide discretion this approach allows.

BGR found that 94 contracts – nearly 25% of all professional services contracts reviewed – did not go through a competitive process because they had contract caps below the \$15,000 threshold. The dollar value of more than half of these 94 fell at \$15,000 or within \$1,000 of that amount. The bunching of contracts at dollar values so close to the cap raises questions as to whether the City used the exemption to avoid putting contracts out for competitive selection.<sup>11</sup>

### **QUESTIONS OF INEFFICIENCY AND WASTE**

Skirting the proper contracting procedures is not the only practice that has led to wasted resources. Other practices, such as using contractors for recurring functions that would be better handled by in-house personnel, also play a role.

## Contracting for Recurring Functions

City policy applicable to the executive branch on professional services contracts states that contracts “shall not be made for readily available skills or jobs more appropriately assigned to a permanent position.” It adds that “only unique or specialized skills that are not available as positions in the classified or unclassified service may be considered for contracts.”<sup>12</sup>

Despite the policy, the previous administration basically turned the operation of its technology office over to contractors. It also hired contractors to assist the finance department with routine tasks.

In addition, the City Council has for years relied almost exclusively on outside consultants for utility regulation.

*Utility Regulation.* The City Council relies almost exclusively on private attorneys, engineers, accountants and other consultants to carry out its responsibility to regulate the local electric and gas utilities. The utilities pay the cost of regulation and ultimately recoup it from ratepayers.

In January 2005, the council entered into new contracts with its five principal advisors, some of whom had worked with the City Council since the 1980s. It renewed those contracts through 2009. It then issued a new request for proposals, and rehired the same principal advisors for 2010. From 2005 to 2009, the two largest contracts had increased significantly both in hourly rates and contract caps, as shown in Table 2. Each annual renewal increased the total contract cap through 2009; the new contracts for 2010 started with a new cap.

For fiscal 2009, the consultants billed the council a total of \$5.8 million. The Louisiana Public Service Commission, which regulates utilities for the other 63 parishes in the state, incurred \$4.7 million of legal and consulting costs related to its regulation of electric and gas utilities in that same period. It passed the costs on to the regulated utilities for payment.

A key difference between the regulatory approaches of the City Council and the Public Service Commission is that the Commission maintains a significant in-house staff. The City Council has only one staff position in

**Table 2: Principal Advisors to City Council in Utility Regulatory Matters**

Contractor	Top hourly rate			Contract cap, 2005-2009			
	2005 Original	2009 Extension	2010 New Contract	2005 Original	2009 Extension	Total Cap Through 2009	2010 New Contract
Sonnenschein, Nath & Rosenthal LLP (1)	\$400	\$495	\$495	\$2,500,000	\$3,300,000	\$16,130,000	\$3,000,000
Legend Consulting Group Ltd.	295	325	325	1,650,000	1,950,000	9,250,000	1,905,000
Wilkerson and Henry LLC (2)	275	275	275	600,000	600,000	3,000,000	792,000
Bruno and Tervalon LLP	180	180	180	200,000	250,000	1,250,000	250,000
Paillet, Meunier & LeBlanc LLP	180	180	180	200,000	250,000	1,150,000	250,000
<b>Totals</b>				<b>\$5,150,000</b>	<b>\$6,350,000</b>	<b>\$30,780,000</b>	<b>\$6,197,000</b>

(1) The contract originated with Sullivan & Worchester LLP and was assigned effective March 27, 2008 to Sonnenschein, Nath & Rosenthal LLP, as authorized by City Council Motion M-08-170. The assignment followed the move of the City Council’s principal attorney at Sullivan & Worchester to Sonnenschein. In 2010, the name of the Sonnenschein firm changed to SNR Denton.

(2) On August 12, 2010, the City Council approved an amendment to reduce the maximum compensation for this firm from \$807,000 to \$792,000 for 2010.

Source: Professional services contracts between the City of New Orleans and the listed contractors

its regulatory office. The Commission maintains 13 offices and has a total staff of 98. Seventy-six of these work on utility regulation. The Commission and its staff regulate – in addition to gas and electricity – other utilities such as certain telecommunications and water and wastewater systems. The in-house operations of the Commission relating to utilities cost \$7.5 million in 2009. The Commission could not provide a breakdown of costs for the gas and electric component alone.

The cost of regulation in New Orleans appears disproportionate to the cost of regulation in the rest of the state. The City Council has not studied whether alternatives, such as building in-house regulatory capacity, would allow it to reduce its regulatory costs while protecting ratepayers. In early 2009, the council issued a request for proposals for consultants to study its regulatory approach and received one proposal with a price tag of \$130,000. According to a news report, some council members balked at the cost and the lack of other proposals, and the council did not pursue the study.<sup>13</sup> However, the sheer size of the regulatory cost makes a good case for investigating alternative approaches to the council's utility regulation.

*Finance Department.* A smaller instance of using contractors for recurring functions occurred in 2009. The City entered into a \$175,000 professional services contract with an accounting firm to assist the finance department in the preparation of the City's comprehensive annual financial report. The services included a number of basic tasks, such as balancing the general ledger and performing cash reconciliations, which should have been performed in-house. The Finance Department has been operating with reduced staffing since Hurricane Katrina, and has entered into contracts for assistance in its annual reporting ever since the storm. According to the department, it has struggled to attract and retain experienced personnel. The City extended the contract in 2010 and anticipates continuing the outside assistance in 2011.

*The Office of Technology.* The City's reliance on outside contractors to staff its technology office increased dramatically after the City laid off approximately 40 IT personnel, or 75% of its staff, following Hurricane Katrina.<sup>14</sup> It tapped a contractor, Ciber, to furnish staff. The company's staffing level increased from 30 to more

than 100 during the initial years of the recovery, before declining.<sup>15</sup>

As Ciber's work was reduced, the City turned to other contractors to provide staff for the office. This continued well into 2010. In the case of a contract with Telecommunications Development Corp., which began in October 2009, the City's inspector general identified nearly \$1 million in potential cost savings if the work were done by City personnel instead of contract workers.<sup>16</sup> Currently, the City's own staff remains at less than half of the pre-storm level.

In times of unusually high workloads, it may make sense to pursue contract staffing, rather than hiring new personnel. But the long-term dependence on contractors to meet recurring needs, such as annual financial reports, point to a management problem. Similarly, while reliance on existing contractors to meet critical needs in an emergency may be sensible, chronic reliance on them for staffing is problematic. The practice violates the City's own policy of not hiring contractors for work that should be assigned to permanent employees.

### The IT Debacle

In the preceding section, BGR flagged one problem in the IT arena: the City's extensive use of outside contractors to staff its technology office. The technology contracts also presented another problem – the expenditure of enormous sums on systems that continue to suffer from a lack of integration and functionality.

Using several technology contracts, the City sought to execute two key initiatives: the migration of its applications and systems from a mainframe environment to a web-based platform, and the enhancement and integration of its financial system. The migration project began prior to Hurricane Katrina under Ciber. Following the storm, Ciber completed a portion of the migration project,<sup>17</sup> but the City turned the remainder of the task over to another contractor. Subsequently, the City replaced it with two other firms, but never gave them authorization to proceed.<sup>18</sup> While some progress has been made, the migration was never completed.

In 2006, the City installed a new financial system. It contracted with Microsoft Corp., the provider of the

system, to make upgrades, fix bugs and improve the system's integration with the City's revenue, purchasing and other systems. Microsoft began this effort in late 2006, and continued through January 2009. Other contractors succeeded Microsoft in working on the financial system. However, the lack of integration among the various systems continues to pose problems. Multiple audits and a review by the current Mayor's transition team have portrayed the segregated systems as a major problem undermining the City's financial management. According to the Legislative Auditor, as of December 2009 only a limited amount of data had been migrated to the new systems; the majority of the City's accounting and purchasing data still resided in the older mainframe system.<sup>19</sup>

Overall, the City authorized almost \$70 million combined on the five contracts. While the contracts included staffing the day-to-day operations of the technology office, as described above, it is clear that the City also spent massive amounts on systems that nevertheless remain troubled. In 2009, City consultants estimated the City would have to spend an additional \$30 million to upgrade its IT system and create a unified software platform for purchasing, accounting, budgeting and contract administration.<sup>20</sup>

### Projects that Went Nowhere

In several cases, BGR found that the City obtained services from contractors for projects and then abandoned them, scaled them back or received little for its investment. BGR did not undertake a systematic audit of contracts for such instances, but rather happened upon these in the course of its review.<sup>21</sup>

*Architectural Services.* In its pursuit of hundreds of recovery projects, the previous City administration sought designs for capital projects for which it lacked construction funding.<sup>22</sup> The current administration has moved to re-evaluate all projects and scale back the overall slate.

For example, the Nagin administration changed the scope of work on a complex of storm-damaged Parks & Parkways buildings from repair to reconstruction, despite the fact that FEMA had not declared the property eligible for reconstruction. The estimated cost

## SHORTCHANGING CONTRACTS THAT WORKED

City budget constraints have limited the use of contractors in an area where the benefits clearly exceed the costs: sales tax auditing. In 2009, the City had in place 12 contracts with accounting firms to audit sales and use taxes collected by the city. Each contract provided for payment at an hourly rate, subject to a maximum of \$150,000. The City did not fully fund the audit program. In fact, it made available only \$225,000, for 115 audits, despite the fact that the benefits of these contracts far exceeded the costs: The auditors identified more than \$4.8 million of unpaid sales and use taxes, resulting in collections of \$2.1 million. The current administration has requested increased funding for sales tax audits in its proposed 2011 budget.

soared from \$1.6 million to \$8.9 million, causing the architect's fee to increase as well. The current administration subsequently changed the project back to renovations, with an estimated cost of \$2.5 million to \$3.1 million. Because the architect's fee was based primarily on the estimated project cost, the City paid approximately \$513,000 on the contract, multiple times what the City would have paid if the project had been scoped properly.

*The little-known website.* The City procured website design services for a website that few knew existed and which is no longer publicly available. In 2008, the City entered into a nearly \$100,000 professional services contract for website design and other services for the City's former Office of Recovery and Development Administration.<sup>23</sup> It included nearly \$88,000 for website design, plus another \$10,000 annually for technical support, e-mail marketing software and statistical tracking software. According to the City, the project was funded by a private grant. Ultimately, the City paid the firm approximately \$88,000. But now, only two years after the contract took effect, the website is not publicly accessible. Those trying to visit the website today are immediately redirected to the City's main website.

*The dialogue that never happened.* In 2009, City officials hired consultants to help prepare a series of public

meetings on race relations, for which it hoped to obtain grant funding. The City paid \$30,500 for three consultants to conduct preliminary interviews with community leaders and other citizens and to perform extensive planning for a series of meetings.<sup>24</sup> Ultimately, the City held two meetings. It abandoned the effort after it failed to obtain funding for additional meetings.

*The unpublished guide.* The City hired a company to prepare print-ready design files for a still-unpublished citizen's guide to City services. The City paid \$15,000 for the design, using funds provided by a private grant. Though the contractor delivered the designed product, the City never published the guide.

*Crime camera maintenance.* In September 2009, the City entered into a nonprofessional services contract for maintenance and repair of its network of crime surveillance cameras. According to the City's inspector general, the firm was paid nearly \$400,000, but its work did not improve the reliability of the system. The inspector general's report found that fewer than one in five of the cameras were functioning.<sup>25</sup>

While the amounts wasted in some of these efforts are small relative to the City's financial needs, they are a matter of concern in a city with serious budgetary problems.

### Mismanagement of Public Records

The City incurred significant costs for outside attorneys and other consultants as a result of officials' failure to properly retain and provide public records. In one case, a local reporter sued the City for violations of the public records law after the then-Mayor's administration failed to deliver his e-mails and calendar.<sup>26</sup> The lawsuit generated several contracts: a \$15,000 contract for legal advice; an \$8,500 contract for a technology trade association to recover missing e-mails from the City's computer systems; and later a \$15,000 contract with another tech firm to review the first one's work and test for additional e-mails.<sup>27</sup> After the lawsuit was settled, the City entered into another contract with the latter firm to update the City's policies and procedures for retaining e-mails as public records and redacting portions exempt from disclosure. That contract was capped at \$50,000.<sup>28</sup>

Another public records dispute proved more costly. In December 2008, a private attorney sought e-mail records of four City Council members, their staff members and one official from the City's Office of Recovery & Development Administration. Before either the City Attorney or the City Council's attorney had reviewed the e-mail records for privileged material, the City's sanitation director released the requested records to the private attorney. In March 2009, the City Council sued the attorney to block the further release of the records.<sup>29</sup> The City administration also intervened in the lawsuit.

The episode resulted in several legal contracts. Shortly after the initial lawsuit was filed, the City administration retained Beveridge & Diamond under a \$15,000 contract for legal advice. After the appeals court verdict, it again hired Beveridge & Diamond, this time under a \$200,000 contract, for additional representation and legal services.<sup>30</sup> The City Council paid approximately \$60,000 to its special counsel, Herman, Herman, Katz & Cotlar LLP, to cover the costs of the litigation, plus the subsequent review and redaction of council members' e-mail records.<sup>31</sup>

All in all, the City spent approximately \$330,000 on legal and technical costs that resulted from the improper handling of public records.

### QUESTIONABLE SPENDING DECISIONS

For a City operating in a fiscal crisis, every dollar counts. However, in some cases, the City contracted in a manner more in keeping with a time of plenitude. In other cases, recovery dollars could have been distributed more effectively.

#### CDBG Funds

One of the most flexible sources of government funding that the City receives is Community Development Block Grants (CDBG) from the U.S. Department of Housing and Urban Development (HUD).<sup>32</sup> Under federal law and regulation, CDBG funds may be used for a wide variety of activities, including infrastructure, housing, social services, code enforcement, public facilities and certain economic development activities. At least 70% of the funding must be used to serve low- and

moderate-income persons.

The City uses a portion of the CDBG funds it receives to pay for public sector activities, such as code enforcement and blight remediation. It distributes the rest through contracts with private sector entities.

BGR was able to obtain 37 such CDBG contracts in effect during 2009. Under them, the City distributed grant funds totaling \$7.6 million to 30 private, nonprofit organizations and a private developer.

Of that amount, the City distributed \$1.9 million in CDBG funds for social services provided by 23 different nonprofit organizations. The services included child care, assistance to the elderly, educational programs and youth services targeted to persons and families with low or moderate incomes. Individual grants ranged from \$32,000 to \$150,000, with an average award of approximately \$70,000.

Seven other grants funded four homebuyer assistance programs and three home repair programs. Together, these programs received allocations totaling \$2 million in CDBG funds.

The City also directed \$3.7 million in CDBG funds to rental housing development. These included \$3.5 million for the acquisition of property for two affordable housing projects. It provided \$2 million of the \$3 million purchase price to help a nonprofit acquire 29 condominiums in Venus Gardens in Central City. The nonprofit agreed to rent the units to low- and moderate-income households, including artists, who meet income eligibility requirements.<sup>33</sup> Venus Gardens had been developed in the late 1990s – in part with a \$600,000 loan from the City.<sup>34</sup>

The City also provided a private developer with \$1.5 million to purchase vacant land for a new mixed-income housing development on Esplanade Avenue. The total purchase price for the land was \$1.9 million. The City's CDBG grant award to the project supplemented significant federal tax credits and other CDBG funds funneled through the State.

Without question, many of the CDBG awards to private enterprises support worthy endeavors. Some of them

may take the place of services that the City would otherwise need to provide. However, the City could have spent part of the \$7.6 million it directed to private entities to meet obligations to citizens for which the City lacks adequate funding.

CDBG funds can be used to pay for or expand on various projects and services that the City is currently struggling to provide, such as recreation facilities and enhanced services in low- or moderate-income areas.<sup>35</sup> They can also be used to address blight or drainage deficiencies in such areas.

The administration is taking steps in that direction. For 2011, it has proposed directing \$2 million of CDBG funds to the newly formed New Orleans Recreation Development Commission. The 2011 proposed budget also expands its annual allocation of CDBG funds for code enforcement.

The City is currently in the midst of preparing its 2011-13 consolidated plan for the use of CDBG funds. As part of the review, it should rethink the approach it has taken in recent years and consider using more of the funds to meet the responsibilities of City government. The City has presented a draft of the plan for public comment until November 12.

### Grants to Elevate Flood-Prone Homes

In the course of its review, BGR examined grants made under the federal Hazard Mitigation Grant Program to pay for the elevation of single-family homes susceptible to flooding. The goal of the grant program is to reduce future flood insurance claims on those properties.

The median cost for the 28 elevation projects reviewed by BGR was \$276,246.<sup>36</sup> The largest grants to elevate homes exceeded, by large amounts in some cases, the appraised value of the properties as recorded on the 2010 tax roll. The awards also exceeded the values on the pre-Katrina tax roll.

FEMA funds 75% of elevation costs under the Hazard Mitigation Grant Program, and the State provides the balance.<sup>37</sup> The Mayor's Office of Homeland Security and Emergency Preparedness serves as the local administrator in New Orleans. In that role, it pools and

**Table 3: Ten Largest Elevation Awards**

House Location	Grant Award (1)	Value of Properties From 2010 Tax Rolls
4100 Block of Cleveland Avenue	\$622,773	\$245,000
200 Block of Audubon Boulevard	488,018	411,200
2400 Block of Nashville Avenue	449,839	327,600
4500 Block of Fort Macomb Road	446,057	416,100
300 Block of Audubon Street	445,774	350,000
2600 Block of Jefferson Avenue	329,330	325,000
3500 Block of Somerset Drive	295,924	146,400
3500 Block of Rue Nichole	263,980	175,000
3500 Block of Rue Michelle	262,681	178,300
4100 Block of MacArthur Boulevard	257,295	92,000

(1) The homeowner receives the grant funds on a cost-reimbursement basis.

Sources: Homeowner contracts with the City of New Orleans; Orleans Parish Board of Assessors, property records database, [www.nolaassessor.com](http://www.nolaassessor.com), accessed October 14, 2010.

submits applications to FEMA on behalf of homeowners interested in participating. The application must demonstrate a positive benefit-to-cost ratio for the pool as a whole, meaning that anticipated savings from the avoidance of future flood insurance claims exceeds the cost of the elevation.

A variety of factors conspire to create situations in which the elevation grant exceeds the home's value. First, FEMA imposes no caps on the cost of elevation projects. Second, it does not require a positive benefit-to-cost ratio for individual properties. Third, in evaluating proposals it does not consider whether the elevation expense is reasonable in the context of the value of the home. Fourth, it does not compare the cost of elevation to other forms of remediation, such as reconstruction.

The substantial elevation grants result mainly from the peculiarities of the federal laws and regulations governing the program. This should concern federal taxpayers. The City could, however, have set reasonable limits on payouts to homeowners. For instance, Jefferson Parish uses a maximum cost limit of \$75 per square foot for its elevation projects. The State imposes a cap of \$100,000 per project for grants made through the Road Home Program.

## CONCLUSION

The effectiveness of City contracting often hinges on how the City limits problems, inefficiencies and abuses. BGR's review of hundreds of City contracts active during 2009 found a host of problems related to the avoidance of competitive selection of contractors, mismanagement of resources and questionable spending priorities. In a time of financial crisis, such as the one under which New Orleans currently labors, getting contracting right becomes all the more important.

The City avoided competition for contracts in a number of ways, foreclosing its potential benefits in cost savings or improved services. It approved significant scope expansions for some professional service contracts and bypassed the public bid process by misclassifying some contracts as professional services.

Questions of inefficiency and waste arose in both large and small contracts. The City's information technology contracts cost tens of millions of dollars, but its systems still lack sufficient integration and functionality. The cost of the City Council's almost exclusive use of private contractors to regulate local utilities appears disproportionate compared to the cost of utility regulation in the rest of the state. The City also paid for design plans it will not use, spent money on projects

that went nowhere, and paid legal and consultant fees to resolve problems arising from its mismanagement of public records.

As the City deals with budget crises and continues to reform its contracting practices, these findings highlight important areas for improvement and vigilance against waste and abuse.

To overcome the current fiscal crisis, the City must spend available funds in a manner commensurate with the current state of affairs. City government is challenged with serious needs in arenas for which it is responsible, at a time of fiscal scarcity. Righting the ship will demand strict fiscal discipline. It will demand contracting only when necessary, for the best price possible, with the best possible return on the public's investment. The City cannot afford contracting for functions that could be more efficiently handled in-house.

The City must take full advantage of competitive selection processes. It cannot afford to use contract expansions or improper classification of services to skirt competitive selection. The City must ensure that taxpayers get the expected results from the contracts their dollars pay for.

## RECOMMENDATIONS

The current administration was not in charge during the time period reviewed. However, it has an opportunity to address the City's contracting problems. In many respects, it could do so simply by adhering to existing policies and procedures. In other cases, it will be necessary to rethink the City's approach to contracting.

BGR makes the following recommendations to provide general guidance for improving contracting decisions and procedures, and specific suggestions relative to certain contracts reviewed in this report.

### Improving Contracting Decisions

The administration should establish a process for determining whether to proceed with a procurement.

- As a first step in considering whether to proceed

with a contract, the City should determine whether a service is necessary (or highly desirable) for the effective operation of, or service delivery by, City government. The City should make such evaluations in the context of competing priorities and budgetary limitations.

- Once a clear case for the service has been established, the City should determine whether it would be more advantageous to provide the service in-house or seek an outside contractor. This determination should include an analysis of whether outsourcing would:
  - Be more cost-effective, taking into account not just the contract price, but also the costs of contract administration and monitoring, any one-time conversion costs, and other costs. Offsetting revenues derived from the service, if any, should also be considered.
  - Provide higher-quality service.
  - Provide needed skills and expertise that are too costly to retain in-house.
  - Assist in meeting temporary spikes in workload, if applicable.

The City Council should establish similar processes for procurements it initiates.

### Improving Contracting Procedures

The City administration should bolster its written procedures for contracting to address certain problems identified in this report.

- The administration should ensure that professional services contracts are properly classified. For any such contract, the City should require a determination by the chief procurement officer that the service meets the definition of a professional service.
- The administration should provide a formal review of any significant proposal by a department to substantially expand the scope of services of a contract, rather than pursue a new competitive selection process. It should notify

the inspector general of any decision to expand the scope of a contract.

- The administration should monitor contractor effectiveness and maintain written evaluations.

For its part, the City Council should notify the inspector general of any decision to expand the scope of a contract. It should also monitor contractor effectiveness and maintain written evaluations.

### **Rethinking Specific Contracts**

The City administration and City Council should rethink their approaches to certain types of contracts that have raised concerns.

- The City Council should seek an independent, comprehensive review of its approach to regulating electric and gas utilities, including whether cost savings could be achieved by balancing the use of outside advisors with a larger in-house staff.
- The City should examine its proposed allocations of future CDBG funds in the context of its budgetary needs in order to determine whether a greater portion of the funds should be used to expand key City services and facilities in low- or moderate-income neighborhoods.
- The City should adopt reasonable caps on elevation costs under its Hazard Mitigation Grant Program.

## APPENDIX: TYPES OF CONTRACTS

*Professional services contracts.* The City contracted for more than 50 types of professional services. Approximately half of the contracts reviewed were architecture and engineering contracts for recovery-related projects. Examples of other types of professional services included legal, accounting and project management.

*Grant agreements.* Through these contracts, the City distributed federal, State and local funds to nonprofit organizations and other private and public recipients. The grants ranged in scope from small economic development and social services grants to multimillion-dollar grants of special post-disaster federal funds for major public projects. A large number of these contracts originated in the Mayor's Office of Community Development and its predecessor, the Mayor's Office of Recovery and Development Administration.

*Other cooperative endeavor agreements.* Approximately 9% of the contracts were cooperative endeavor agreements between the City and other public or private entities.<sup>38</sup> The City enters into such agreements to partner with another entity to achieve a public purpose. Examples of such purposes include economic development projects and intergovernmental endeavors.

*Nonprofessional services contracts.* Five percent of the contracts were for nonprofessional services. Examples of these contracts include garbage collection; electrical, equipment, and heating and air conditioning repairs; demolition; and grounds, tree and building maintenance.

*Real property lease and use agreements.* These contracts, which represented 5% of the contracts reviewed, involved (i) the lease or use by the City of real property owned by others or (ii) the lease or use by others of City-owned real estate. The agreements ranged from office building leases for City operations to leases of City property for movie productions.

*Construction contracts.* Construction contracts made up 4% of all contracts. At the end of 2009, the City was still in the design or pre-design phase of many recovery projects and had gone to bid on only a limited number of construction contracts. The City moved more projects from design to construction in 2010.

*Contracts for equipment, materials and supplies.* Pur-

chases of equipment, materials and supplies through written contracts comprised 3% of the contracts reviewed. The largest contracts were lease-purchase agreements. The vehicles procured through these contracts included ambulances, fire trucks and police cars. This category (and the report) does not include purchases made using a purchase order only.

*Other types of contracts.* The balance of the contracts included various agreements under which the City receives revenues, such as State or private grants to the City; loans of City or City-administered funds; agreements to buy, sell or donate real property; and engineering and construction contracts for certain federally-funded road projects awarded through State-driven selection processes and jointly administered by the City and State.

Approximately 42% of the contracts reviewed related to recovery projects. The vast majority of these were architecture, engineering and construction contracts for public works, and Hazard Mitigation Grant agreements with individual homeowners for elevation or reconstruction projects. Recovery-related projects also included nine grants of disaster recovery funds totaling \$140.4 million.

**Services:** The City contracted with private entities for the performance of 72 types of services. Some provided support services for government operations, such as janitorial, information technology and legal services. Others were for the delivery of public services to citizens. Examples included garbage collection, animal control and the operation of public facilities, such as the Mahalia Jackson Theatre for the Performing Arts.

**Contract Originators:** The two most prolific originators of contracts were the City's Capital Projects Administration (22%) and the Office of Community Development (18%), a sprawling entity that included disaster recovery, economic development, job training, housing, code enforcement, social services and other functions. Other originators of large numbers of contracts included the Department of Public Works (11%), the Department of Health (8%) and the Mayor's Office of Homeland Security (8%). In all, the City Council and 28 City departments, boards, commissions, corporations and offices were originators of the contracts reviewed.

**Contract Recipients:** The City contracted with more than 550 individuals, organizations, companies and other governments.

## END NOTES

- 1 Egglar, Bruce, "City on pace to blow budget big time," *The Times-Picayune*, October 1, 2010.
- 2 The proposal seeks to increase these property tax rates by 8.74 mills, a 24% increase over the current 35.91 mills that go to the operating budget.
- 3 BGR's review excluded the French Market Corp. and the Upper Pontalba Building Restoration Corp.
- 4 Louisiana Legislative Auditor, *City of New Orleans Compliance Audit*, May 19, 2010, p. 12. The report analyzed the Ciber contract in depth and cited a number of other problems, including inadequate documentation of services performed.
- 5 Office of the Inspector General, City of New Orleans, *Review of City of New Orleans Contract with Telecommunications Development Corporation*, OIG-I&E-09003(C), August 30, 2010, p. 9.
- 6 For a discussion of the firm's role in the Budgeting for Outcomes process under the previous administration, see: Office of the Inspector General, City of New Orleans, *Review of 2009 Budget Process for City of New Orleans*, OIG-I&E-09002, November 24, 2009, pp. 31-32.
- 7 Home Rule Charter of the City of New Orleans, Section 6-308 (5)(a).
- 8 For this analysis, BGR applied a definition of professional services that includes both recognized professions, such as law, architecture and accounting, and occupations requiring a high level of training and proficiency, such as information technology. This is based on the definition of "professional" in Black's Law Dictionary, as well as the definition of professional service used by the National Institute of Government Purchasing. The institute defines professional services as "services rendered by members of a recognized profession or possessing a special skill. Such services are generally acquired to obtain information, advice, training, or direct assistance." National Institute of Government Purchasing, "NIGP Online Dictionary," 2010, [www.nigp.org/eweb/docs/education/OnlineDict/DictP.htm](http://www.nigp.org/eweb/docs/education/OnlineDict/DictP.htm).
- 9 Krupa, Michelle, "City hotline not up to speed," *The Times-Picayune*, June 2, 2008.
- 10 City of New Orleans, Code of Ordinances, Sec. 2-7.
- 11 The City's Law Department and the Municipal Yacht Harbor Management Corp., a public benefit corporation of the City, were the most frequent originators of contracts just below the threshold, with 20 and 11, respectively.
- 12 City of New Orleans, Chief Administrative Office Policy Memorandum 8(R).
- 13 Egglar, Bruce, "Council members at odds on Entergy regulation contracts," *The Times-Picayune*, October 24, 2009.
- 14 City of New Orleans, 2011 Proposed Operating Budget, p. 51.
- 15 Ciber Inc. Response to the Draft City of New Orleans Audit report, April 21, 2010, included in Louisiana Legislative Auditor, *City of New Orleans Compliance Audit*, op. cit.
- 16 Office of the Inspector General, City of New Orleans, *Review of City of New Orleans Contract with Telecommunications Development Corporation*, op. cit., p. 12.
- 17 Ciber notes that the City directed it to focus on restoring and maintaining the City's IT infrastructure and operations post-Katrina. Ciber Response, op. cit.
- 18 In August 2009, the City hired MSF Global Solutions LLC as the primary vendor on the remainder of the migration project. In addition, in the October 2009 contract with Telecommunications Development Corp., the City directed the firm to assist with mainframe and system migration.
- 19 Louisiana Legislative Auditor, *City of New Orleans Compliance Audit*, op. cit.
- 20 City of New Orleans, *Response to the Draft Report Issued by the Louisiana Legislative Auditor to the City of New Orleans*, April 27, 2010, included in Louisiana Legislative Auditor, *City of New Orleans Compliance Audit*, op. cit.
- 21 The Legislative Auditor documented one project under the Ciber contract, in which the City paid \$1.9 million in 2006 for a computer system for a charter school initiative in the months after Hurricane Katrina. The auditor found that the City never received the software and ultimately dropped the initiative. Louisiana Legislative Auditor, *City of New Orleans Compliance Audit*, op. cit.
- 22 Mayor Mitchell J. Landrieu, State of the City Address, July 8, 2010. Also, Krupa, Michelle, "Mayor extends MWH recovery contract," *The Times-Picayune*, July 1, 2010.
- 23 Agreement for Professional Services between the City of New Orleans and Atlas Advertising, LLC, June 30, 2008. The Office of Recovery & Development Administration was the predecessor to the Office of Community Development.
- 24 Professional services agreements between the City of New Orleans and Allan L. Katz & Associates, AmericaSpeaks and C. Harris Companies, all dated April 1, 2009. Although not required by the contracts, the consultants assisted in writing grant proposals to fund the meetings.
- 25 Office of Inspector General, City of New Orleans, *Follow Up Report: Crime Surveillance Cameras*, OIG-I&E-10-010, October 15, 2010. The contractor was Technology Consortium Group LLC.

26 Lee Zurik v. C. Ray Nagin, et al., CDC 2009-1317, February 5, 2009.

27 The contractors were, respectively, Beveridge & Diamond PC law firm, the Louisiana Technology Council and SunBlock Systems Inc. City records as of October 7, 2010, indicate that no payments have been made on either the Louisiana Technology Council's or SunBlock's contracts.

28 City financial records as of October 7, 2010, indicate the firm was paid \$49,500 on this contract.

29 The Council of the City of New Orleans, et al., v. Tracie Washington, et al., CDC 2009-2279, March 4, 2009.

30 Professional Services Agreement between the City of New Orleans and Beveridge & Diamond, PC, May 14, 2009. City financial records indicate that Beveridge & Diamond was paid approximately \$195,000 of the \$200,000 contract.

31 Payment data was provided by the City Council on November 4, 2010.

32 After the storm, the City received an extraordinary grant to deal with reconstruction and other recovery issues.

33 The purchaser was Efforts of Grace Inc. GCHP-Venus Gardens LLC had converted Venus Gardens into commercial and residential condominiums in 2007. However, it succeeded in selling only one of the 30 residential condominium units prior to the CDBG-funded purchase.

34 The loan was repaid, and the related mortgage was cancelled in 2007.

35 Federal regulations allow the use of CDBG funds for a number of recreation-related purposes: acquiring, building, rebuilding, rehabilitating and installing facilities and improvements (but not repairs, maintenance and operation); increasing recreation services above existing levels, including labor, supplies and materials; making emergency repairs to parks and playgrounds; and planning open space and recreation. The regulations can be found at 24 CFR 570.201(c) and (e); 24 CFR 570.201(f)(1)(i); 24 CFR 570.205(a)(3)(iv); and 24 CFR 570.207(b)(2).

36 BGR analysis of Hazard Mitigation Grant Program data, as of August 19, 2010.

37 The grant program is separate from a similar program that is part of the State's Road Home program.

38 This category does not include cooperative endeavor agreements that involved the distribution of grant funds. BGR included those contracts in the category of Grant Agreements.







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