

<b>FROM</b>	Name & Title Steve Sharkey, Director	Agency Name & Address Department of General Services 800 Abel Wolman Municipal Building	<b>CITY OF BALTIMORE</b> <b>MEMO</b>	
	Subject <b>Report on City Council Resolution 17-0008R – Investigative Hearing – Late Payments to Subcontractors on City Contracts</b>			

**TO:** The Honorable Chairwoman and Members  
 of the Taxation, Finance, and Economic Development Committee  
 Room 409, City Hall  
 100 N. Holliday Street  
 Baltimore, Maryland 21202

**DATE:** March 9, 2017

**Re:** City Council Resolution 17-0008R - Investigative Hearing - Late Payments to  
 Subcontractors on City Contracts

Dear Chairwoman Green Middleton, Vice-Chair Pinkett and Members of the Committee:

The Department of General Services reviewed City Council Resolution 17-0008R - Investigative Hearing - Late Payments of Subcontractors on City Contracts as introduced by Councilman Stokes with the purpose of calling on representatives from the Finance Department, the Office of Civil Rights and Wage Enforcement, the Minority and Women's Business Opportunity Office, and the departments of Public Works, General Services, and Transportation to appear before the City Council to discuss problems with late payments to subcontractors on City contracts, and what steps the City can take to ensure that these problems do not endanger the ability and willingness of subcontractors to work on City projects. The Department of General Services takes this matter extremely seriously.

To clarify, the Department does not pay subcontractors directly. However, DGS has worked diligently to reduce the time it takes to pay the prime contractor, so they are in turn able to pay their subcontractors in a timely manner. In order to more promptly pay contractors DGS examined the vendor payment process.

The Department identified issues pertaining to the prompt payment of its vendors and took a multi-pronged approach to improving its vendor payment process. The DGS Fiscal and Strategic Management Office identified many areas of concern in the process. These included:

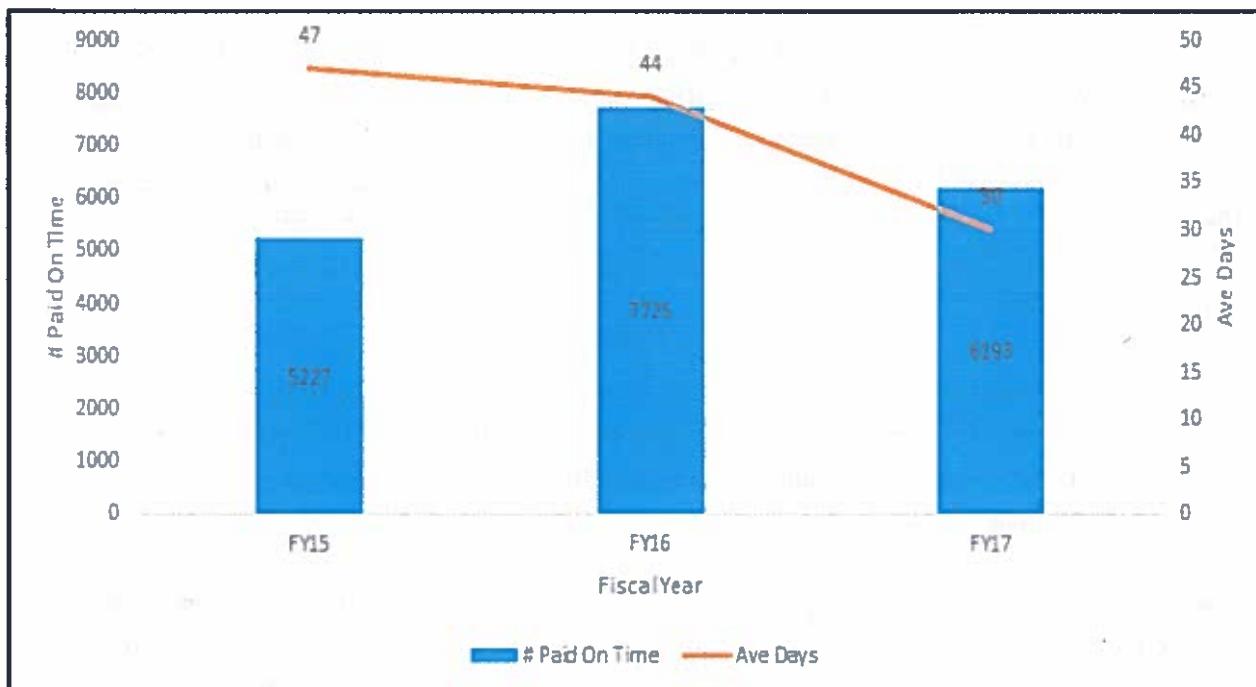
- Paying urgent/emergency work vendors on time (30 days after receipt of invoice),
- A lack of vendor perspectives, specifically to address a lack of a payment process for urgent work,

- Inadequate tracking system which led to a low awareness of invoices coming into the office,
- Trouble monitoring master blanket contracts, specifically when they expire or funds became exhausted, and
- The constant need for change orders prolonging the payment process.

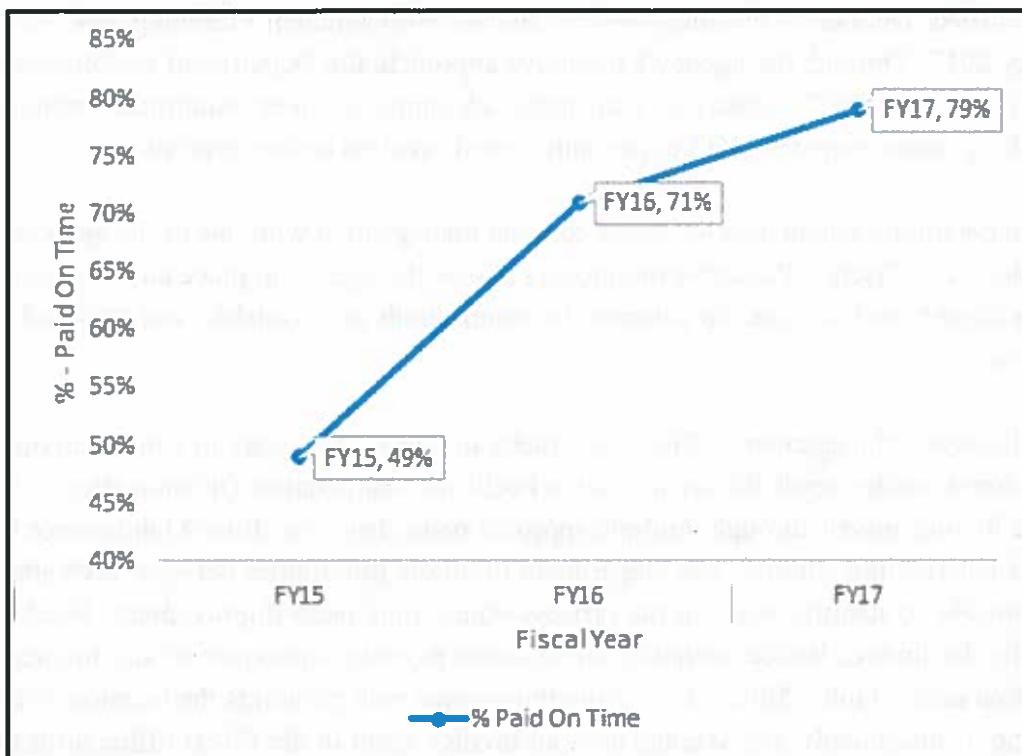
After identifying areas in need of attention and improvement, DGS sought to rectify the situation and improve prompt vendor payments. The Department initiated an urgent work vendor payment process pilot program with great success. These successes included:

- Reduced vendor payment times from average 47 days in FY15 to 30 days currently. (See Exhibit A)
- Increased on-time payments from 49% in FY15 to 79% in FY17. (See Exhibit B)
- Collaborated with Finance & Mayor's Office to develop new procedures, pilot programs
- Revised the AM Manual through Board of Estimates
- Shift from one-size fits all (goods model) to agency-needs tailor fit policies. [pre-review & change order rule changes]
- Cross agency retraining on invoice receipting

Exhibit A.



## Exhibit B.



The Fiscal and Strategic Management Office held four days of Lean Government Training to map out current invoice tracking process, identify steps in the process that prolong the payment process, and to identify solutions that improve the payment process, which includes developing new workflows.

DGS encountered numerous challenges along the way, which included collaborating with multiple agencies, determining initial master blanket funds for urgent work to help reduce the need for change orders, and getting the vendors on board, i.e. sending aging reports on schedule, convincing the vendors and the agencies to send the invoices electronically.

To overcome these challenges and improve the vendor payment times, DGS instituted a four-pronged approach to prevent lapses in service and pay the vendors within 30 days by (1) performing contract management, (2) tracking invoices, (3) incorporating vendor input related to fast-tracking urgent work, and (4) developing policy changes. Contract management allows DGS to prevent an interruption in provided services and ensure prompt vendor payment. The Department focuses on contracts nearing expiration (6 months out) and/or those having spent 75% of the contracted amount. With contracts 6 months from expiration, DGS either determines if the agency is going to renew the contract, exercise any options inherent in the original contract or prepare specifications and requisitions for bid before the contract expires.

DGS also examines contract burn rates and prepares timely change orders as necessary. Last August, DGS identified that a drain cleaning service contract with Mitchell Plumbing was set to expire in February 2017. Through the agency's proactive approach, the Department established a new contract by January 2017, ensuring that drain cleaning services continued without interruption. Looking ahead prepared DGS to pay anticipated invoices before expiration.

This focus on process improvement also bolstered contract management with one of the agency's urgent work vendors, J.F. Fischer. Proactive monitoring allows the agency to place any necessary change orders for urgent work services in advance, to ensure funds are available, and the vendor can be paid on time.

The Fiscal and Strategic Management Office also tracks invoices from start to finish. Invoice tracking begins when a vendor sends the invoice to the Facilities Maintenance Division after work is completed. The invoice travels through multiple approval paths, from Facilities Maintenance to Fiscal, before it is entered into Citibuy. The Department monitors timeframes between each step, and the overall process to identify steps in the process which may need improvement. Weekly monitoring permits the invoice tracker to notify an accounts payable supervisor of any invoices which have not been entered into Citibuy. Following the invoice path pinpoints the location of an invoice at any time. Consequently, the average days an invoice spent in the Fiscal office prior to entry into Citibuy dropped from 9 days in FY15 to 2 days in FY17.

Additionally, the Department of General Services, in collaboration with vendors, the Bureau of Purchases and the Bureau of Accounting and Payroll Services (BAPS), identified opportunities to streamline our vendor work order processing times to more quickly serve the needs of vendors. Previously, the City maintained a one-size-fits-all policy. The Department made the case for a different process for urgent time and material invoices. During this process, it was important to incorporate the perspective of the vendors which had been previously neglected. By focusing on the perspective of the vendors, DGS is able to identify which steps produced actual value.

Finally, the Fiscal and Strategic Management Office recognized the importance of altering existing policies to further improve prompt vendor payment. The team pinpointed policy criteria for identifying standard and abnormal price variances for completed work for time and material invoices. The policy change was necessary to bring the organization in-line with standard practices and to improve performance in vendor invoice payment processing.

Change orders were previously required for time and material service invoices exceeding vendor estimates, no matter the amount; this process can add up to 30 days to the vendor payment process timeline. Working with BAPS and Purchases, DGS developed a process for streamlining or eliminating change order tasks based on approved standard rules and an analysis of change order and invoicing activity. This expedites the invoice review and payment process by establishing a

new threshold of 10% variance for time and material service invoices, i.e. if the final invoice is greater than the original vendor estimate and the difference between the final and the estimate is equal to or less than 10% a change order is not required to receipt the invoice.

These four process changes combined have helped DGS avoid lapses in service and achieve a greater amount of success paying vendors within 30 days. The Department believes that this model could be adopted by other City agencies.

For capital projects, the Charter requires that the contractor provide a payment bond with its bid, which is intended to ensure payment to any subcontractor that performs work on the project. The Department of General Services' Major Projects Division makes copies of those payment bonds available to subcontractors upon request. While a claim on a payment bond must be initiated by the subcontractor seeking payment, the Major Projects Division will provide any and information necessary in the evaluation of a subcontractor's claim. In addition to seeking payment under the payment bond, a subcontractor may also file a claim for payment in court. In either case, the subcontractor must be able to prove that they are entitled to payment based on proper performance of the work required. For example, there may be an instance where the quality of a subcontractor's work is such that the prime has determined the subcontractor must be removed from the project and is therefore not entitled to payment, even though the subcontractor may take the position that they performed work. The Department is rarely privy to the relationship between a prime contractor and its subcontractor and is cannot determine what the "deal" between a prime and its subcontractor really is. The prime may have legitimate reasons for not paying its subcontractor, but there is no way for the Department to know that.

Prompt payment has further downstream impacts, as contractors can produce more timely payments to their own subcontractors. For subcontractors working on capital projects, the Major Projects Division can provide a copy of the payment bond and will cooperate with the claim investigation, should a claim be made by a subcontractor. DGS' approaches can reduce problems with late payments to subcontractors on City contracts. These steps will help ensure that these problems do not endanger the ability and willingness of subcontractors to work on City projects. By improving the vendor payment process and recourse ability of the subcontractors, DGS is supporting small and local businesses as well as their ability to survive and contract with the City of Baltimore.



STEVE SHARKEY  
DIRECTOR

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