



April 5, 2009

Hon. William C. Thompson, Jr.
Comptroller of the City of New York
1 Centre Street
New York, NY 10007

Joel I. Klein
Chancellor
New York City Department
of Education

52 Chambers Street
New York, NY 10007

Dear Comptroller Thompson:

I am writing in response to your April 1 letter regarding the Department of Education's use of requirements contracts. Unfortunately, your office's analysis is marred by distortions and misrepresentations. Based on the numbers in your materials, your office failed to conduct a careful reading of the contracts and to verify basic contract information—even citing as a “particularly stunning example” of DOE “mismanagement” a contract that was entered into while you were President of the Board of Education.

I direct you to the following examples of incorrect or misleading allegations in the contracts highlighted in your letter:

- Xerox Corporation:

The figure you give for the contract's original amount, \$1 million, is incorrect. The Xerox contract was actually registered for **\$31 million**. We originally registered the contract for \$20 million in 2002, and later extended it twice, once by \$10 million and a second time by \$1 million. It appears that you cite the amount of this last extension as if it were the entire registration amount. The accurate estimate is still less than the amount actually expended, but as we explain below this fact in itself is neither problematic nor atypical in a requirements contract.

For the record, a review of the original Xerox contract documents shows that the original estimate was reached through a standard process. Procurement for the Xerox and T&G Industries contracts began before the start of mayoral control (the contracts went into effect on August 1, 2002). The Board of Education provided vendors bidding on this RFP (including T&G Industries) with a comprehensive inventory of the Department's copy machines; the number and types of machines guided the unit pricing proposed by the vendors, ultimately resulting in a contract estimate.



- T&G Industries:

The figure you give for the contract's original amount, \$1 million, was actually registered for **\$31 million**. Like the Xerox contract, it was originally registered at \$20 million and twice extended, once by \$10 million and again by \$1 million. It appears that, as with the Xerox contract, you cited the amount of the last extension as if it were the entire registration amount.

- Hewlett-Packard:

The Hewlett-Packard contract is a state contract that provides Microsoft software licenses for schools and central offices. The state, not the DOE, selected the vendor and set the rates. In other words, the DOE estimate could not have had an effect on pricing. With regard to the estimate, it should be noted that we had little basis for estimating vendor expenditures when the contract began in 2005—this was the first time we procured software licenses centrally; previously, schools paid for them on their own. A replacement contract is with your office now and has a two-year estimate of \$12 million, which is in line with the roughly \$6 million annual expenditures against the former contract listed in your chart.

- Meizner:

This contract with a software reseller was first competitively bid in June 1999—when you were President of the Board of Education and prior to this administration. With renewals, the contract lasted for 10 years. At the time the contract was initially estimated, it was the agency's practice to provide estimates based on *annual* spending rather than on the full term of the contract. The \$135,000 estimate that appears in your table represents the expected spend for one year; the actual estimate for the entire contract is 10 times that amount, or **\$1.35 million**. It is also worth noting that when the Department negotiated the last renewal—for three years starting in 2007—we reached terms that ensured us a minimum 20% discount off publisher's list prices.

- Creative Media:

This contract was bid originally in 2002. At that time, as noted above, the agency's practice was to provide estimates for *annual* rather than for the full-term contract amounts. The annual estimate was \$589,000, which is the number that appears in your chart. We registered each renewal (provided for in the base contract) for



additional amounts that your office appears to have missed. The sum of the subsequent renewals, i.e., the contract's actual "original amount," is about **\$3 million**.

Your letter also raises questions about 127 "entities" that obtained contracts with the Department with "little or no competition" on which we spent \$525 million. We examined the list you compiled and found that 85 percent of the expenditures listed went to state-approved providers of services to pre-school children with disabilities. As with contracts for Supplementary Education Services, which also appear on your list and about which you have criticized us in the past, *we are required by law to contract with any state-approved provider*. Because the state alone has the authority to review and approve programs and sites and to set rates, the Board of Education while you were Board President sensibly determined that the city did not need to perform its customary procurement process before contracting with any state-approved provider. We arrive at these contracts after the State Education Department sets tuition rates and vendors estimate costs for their services based on the size of the student register they are contracting to provide services for. This population has been growing, so it is not uncommon that registers have gone up during the five-year duration of these contracts.

In general, your analysis mischaracterizes the Department's requirements contracting process. Requirements contracts are structured on a per unit price basis, meaning that schools and departments only pay for the units they purchase at the unit price fixed in the contract. In some of the examples your office listed, schools decided they wanted to purchase more services and goods than we originally estimated. These expenditures are not examples of cost overruns and do not add costs to taxpayers; they simply reflect increased demand, which the schools pay for out of their budgets.

You make two further charges that I wish to respond to. First, you contend that the DOE fails to negotiate the best prices in cases where expenditures exceed estimates. In fact, we analyze and estimate the potential volume that could be associated with each contract and provide our best estimate to potential vendors. The estimates sometimes fall below actual expenditures, especially in times of dramatic budget changes; since 2002, the Department's budget has increased by \$8 billion. In the early years of such growth, it may be difficult to estimate the volume of potential purchases. There could be a few contracts—among the thousands the Department signs each year—where our best estimates proved to be low relative to the price we could have negotiated on a volume discount. But we are not aware of any suboptimal pricing, and you have not presented evidence to suggest otherwise. Additionally, given the size of our district and the competitive nature of our bidding process, we believe we already receive vendors' lowest possible prices even on the contracts where a volume discount could have applied.



Finally, your suggestion that low estimates on contracts provide “an inaccurate picture” of our expenditures appears to misapprehend the way our budget works. The DOE does not use contract estimates, which are set in varying years, as indicators of planned expenditures. School budgets and the overall DOE budget are the comprehensive financial documents that provide a “picture” of planned expenditures for a given year. These budgets change each year depending on the amount of funding the Department receives from the city, state, and federal governments. No district, including New York City, continuously revises contract estimates based on year-to-year budget fluctuations. As budgets shift, schools and Department offices adjust spending against requirements contracts accordingly. To determine how much money the Department plans to spend on pre-kindergarten services for the current year, one should consult this year’s budget rather than the estimate made when the contract was signed, which could have been several years earlier.

These mischaracterizations and distortions add little to public understanding of DOE procurement issues. Our offices have worked closely together in the past. I hope that practice continues into the future, and that you will contact us to verify contract and purchasing information to ensure the public is properly informed.

Sincerely,

A handwritten signature in black ink that reads "Joel I. Klein".

Joel I. Klein
Chancellor