



November 13, 2019

To: Finance and Administration Committee

From: Darrell E. Johnson, Chief Executive Officer

Janet Sutter, Executive Director
Internal Audit Department

Subject: Oversight Controls and Contract Compliance Related to the Orange Transportation Center Parking Structure Project

Overview

The Internal Audit Department has completed an audit of oversight controls and contract compliance related to the Orange Transportation Center Parking Structure Project. Based on the audit, procurements were handled in accordance with policies and procedures, status monitoring and reporting controls are operating, and consultants are providing services in accordance with their contracts. However, the Internal Audit Department recommends improvements to contract language addressing force account payments, preparation of independent cost estimates, and construction management consultant oversight of change orders. The Internal Audit Department is also making recommendations related to adequate labor timekeeping systems for consultants, as well as procedures to ensure compliance with requirements for federally-funded assets.

Recommendation

Direct staff to implement three recommendations provided in Oversight Controls and Contract Compliance Related to the Orange Transportation Center Parking Structure Project, Internal Audit Report No. 19-508.

Background

The Orange Transportation Center Parking Structure Project is a shared-use parking structure located at Lemon Street and Maple Avenue. There are 608 parking stalls, of which 500 stalls are intended for transit use and the remaining 108 stalls are intended for the City of Orange's general use. The current baseline

estimate for the project is \$33,175,000 and includes the transit and non-transit portions. The project is funded through a mix of local, state, and federal funds.

The Orange County Transportation Authority (OCTA) entered into a time-and-expense contract with Hill International, Inc., for construction management (CM) services with a maximum cumulative payment obligation (maximum) of \$2,126,779. The maximum had increased to \$2,745,380, and the term extended to June 30, 2019, by Amendment No. 7. OCTA entered into a contract with Bomel Construction Company, Inc., for construction of the project with a maximum of \$18,414,300. Contract Change Order (CCO) No. 001 allowed work to proceed on contaminated soil and railroad ties at force account for a not-to-exceed (NTE) amount of \$200,000, CCO No. 001.1 was then issued with an NTE of \$863,000, and CCO 001.2 was finally issued at \$172,640.54, to capture all remaining work, costs, and schedule adjustments. CCO, No. 002 through No. 008 were all executed at lump sum amounts totaling \$779,883.59.

Discussion

Internal Audit identified areas for improvement related to CCO's. Internal Audit recommended that independent cost estimates for CCO's be prepared prior to receipt of contractors' pricing information and that CM's retain documentation evidencing scrutiny of force accounts costs. Internal Audit also recommended, for future contracts, that contract language outlining labor costs paid on force accounts be clarified and enforced. Management responded that it would add requirements related to independent cost estimates to its procedure manual, remind CM's to retain appropriate documentation to support force account costs, and provide clarity to contract provisions.

A sub-consultant to the CM does not utilize an adequate labor timekeeping system; discrepancies were identified in the employee timesheets and job timesheets that accompanied labor billings. Internal Audit recommended that prime and sub-consultants be required to have an adequate labor timekeeping system. Internal Audit also recommended that management remind consultants of the need to request amendments to add staff, labor rates, and other direct costs in a timely fashion. Management agreed to add the requirement for use of an adequate labor timekeeping system to future requests for proposals. Management also agreed to emphasize the need for timely submission of requests for amendment.

Finally, Internal Audit identified a need for procedures to address ongoing monitoring of federally-funded assets. Internal Audit recommended that management develop written procedures, including development and enforcement of operations and maintenance agreements with agencies that take

possession of such assets. Management responded that it is coordinating across all divisions to develop procedures that ensure adequate monitoring and ongoing oversight of federal facilities that are owned and maintained by an OCTA subrecipient.

Summary

Internal Audit made three recommendations for improvements related to CCO's, labor timekeeping systems, and ongoing monitoring of federally-funded assets.

Attachment

- A. Oversight Controls and Contract Compliance Related to the Orange Transportation Center Parking Structure Project, Internal Audit Report No. 19-508

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Oversight Controls and Contract Compliance Related to the Orange Transportation Center Parking Structure Project

Internal Audit Report No. 19-508

October 31, 2019



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Conclusion

The Internal Audit Department (Internal Audit) of the Orange County Transportation Authority (OCTA) has completed an audit of oversight controls and contract compliance related to the Orange Transportation Center Parking Structure Project. Based on the audit, procurements were handled in accordance with policies and procedures, status monitoring and reporting controls are operating, and consultants are providing services in accordance with their contracts. However, Internal Audit recommends improvements to contract language addressing force account payments, preparation of independent cost estimates, and construction management consultant oversight of change orders. Internal Audit also recommends that prime and sub-consultants be required to have an adequate labor timekeeping system. Finally, Internal Audit recommends that management develop and implement procedures that outline responsibilities and provide guidelines to ensure compliance with requirements for federally-funded assets.

Background

Orange Transportation Center Parking Structure Project (Project)

The Project is a shared-use parking structure located at Lemon Street and Maple Avenue. The parking structure includes 608 parking stalls, of which 500 stalls, or 82 percent, are intended for transit use. The remaining 108 stalls, or 18 percent, are intended for the City of Orange's (City) general use. The City was the lead on the environmental, design, and right-of-way phases of the Project, and OCTA is the lead on the construction phase. The City pays its fair share of 18 percent of the construction costs of the Project. The City also pays 100 percent for City betterments. The current baseline estimate for the Project is \$33,175,000, and includes the transit and non-transit portions. OCTA is responsible for 73 percent of the design costs and 82 percent of the construction costs. The Project is funded through State Transportation Improvement Program funds, Federal Congestion Mitigation and Air Quality Improvement funds, proceeds from the sale of the Santa Ana Transit Terminal, Measure M2, and City local funds.

Contracts

The City was initially intended to be the lead on the construction phase. Under Cooperative Agreement No. C-6-1004, OCTA assumed the lead for the construction phase and agreed to 82 percent participation of the construction costs up to \$21,553,000.

Effective June 13, 2017, OCTA entered into Agreement No. C-6-1024 with Hill International, Inc. (Hill) for construction management (CM) services for the project. The contract is a time-and-expense contract with a maximum cumulative payment obligation (maximum) originally set at \$2,126,779. The maximum had increased to \$2,745,380, and the term extended to June 30, 2019, by Amendment No. 7. Named sub-consultants

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included AESCO, Inc. (AESCO), DSEArchitecture, LSA Associates, Inc., Coast Surveying, Inc., ATS Consulting, and Kroner Environmental Services, Inc.

Effective July 14, 2017, OCTA entered into Agreement No. C-7-1737 with Bomel Construction Company, Inc. (Bomel) for construction of the Project. The contract maximum was established at \$18,414,300. Contract Change Order (CCO) No. 001 allowed work to proceed on contaminated soil and railroad ties at force account for a not-to-exceed (NTE) amount of \$200,000, with a note that the change order will be part of a larger change order, CCO 001.01, that captures all work. CCO No. 001.1 then was issued with an NTE of \$863,000, and finally CCO 001.2 was issued at \$172,640.54, to capture all remaining work, direct costs, extended field and home overhead costs, and schedule adjustments. CCO Nos. 002, 003, 004, 005, 006, 007, and 008 were all executed at lump sum amounts of \$61,381.44, \$18,882.00, \$127,575.00, \$97,754.00, \$191,295.00, \$87,756.15, and \$195,240, respectively.

Project Status Controls

During the design phase, which was led by the City, the Project Manager (PM) attended periodic meetings. During the construction phase, weekly construction meetings were held on site and attended by Bomel, Hill, City representatives, and OCTA representatives, including the PM and Public Outreach staff. Minutes for the weekly construction meetings were prepared and filed in the project files.

Hill, as the CM, submitted daily reports, weekly reports, and monthly progress reports to the PM. The reports identify percentage completion, number of requests for information, and overall status of construction. During construction, the PM communicated with Hill on a daily basis.

Invoice Review

For the Hill invoices, the PM reviewed the hours billed and compared the billed hours to what she saw on-site. The PM relied on the project management consultant to review the rates and reconcile the hours billed to timesheets.

Hill prepared the construction Application and Certificate for Payment, after reaching an agreement with Bomel. The signed Application and Certificate for Payment was then submitted to the PM, who checked the completion status and made inquiries of Hill as needed to confirm status. The PM then relied on the project management consultant to review the values and mathematical accuracy of the signed Application and Certificate for Payment.

Invoices were reviewed and signed by the PM or the Division Director, based on payment authorization level. Accounts Payable reviewed invoices for proper signature authority prior to processing payment.

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Objectives, Scope, and Methodology

The objectives were to evaluate the procurements, amendments, and change orders for compliance with policies and procedures and/or contract terms, assess project administration and oversight controls, and evaluate contract compliance.

According to generally accepted government auditing standards, internal control is the system of processes that an entity's oversight body, management, and other personnel implement to provide reasonable assurance that the organization will achieve its operational, reporting, and compliance objectives. The five components are control environment, risk assessment, control activities, information and communication, and monitoring.¹

The methodology consisted of testing compliance with selected procurement policies and procedures including vendor protest policies, testing amendments and change orders for compliance with contract terms and policies and procedures, testing for evidence of weekly construction meetings and project status reporting to the Board of Directors, and testing invoices for compliance with policies and contract terms.

The scope is limited to the Project and the related OCTA contracts. The scope excludes the design, environmental, and right-of-way phases, as these phases were led by the City.

The scope included all weekly construction meetings, all amendments and CCO's, and all invoices paid through May 2019. The scope also included Measure M2 progress reports beginning with the quarter ending December 2015, and the Capital Action Plan Performance Metrics reports beginning the first quarter of fiscal year 2015-16. The scope included certain project controls, which were selected with a bias toward those that are significant to the Project. Since the sample is non-statistical, any conclusions are limited to the sample items tested.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

¹ See U.S. Government Accountability Office publication, "Standards for Internal Control in the Federal Government," available at <http://www.gao.gov/products/GAO-14-704G>, for more information.

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Audit Comments, Recommendations, and Management Responses

Cost Estimates and CM Oversight

Cost estimates for CCO work were not prepared independent of the contractor's price proposals. Policy requires cost estimates be prepared by the PM and/or CM prior to receipt of the construction contractor's price proposals; however, for several of the CCO's, the cost estimates were prepared after receipt of contractor proposals.

The CM is responsible for reviewing CCO documentation on OCTA's behalf; however, Internal Audit identified opportunities for improvement in the CM's process. The CCO files did not include documentation to support all force account costs paid to the construction contractor; specifically, labor rate calculations, reconciliation of subcontractor labor hours, and a few extra work tickets. This documentation should be validated by the CM and retained in the files.

Upon request, the CM provided force account labor rate calculations; however, the calculations were inconsistent with contract language. The contract provides that labor be compensated at actual wages paid plus 20 percent, and allows a 17 percent labor surcharge as compensation for payments imposed by state and federal laws. The actual labor rates calculated and charged by the contractors included the basic wage rate, fringe benefits, and payroll insurance and taxes, with the 20 percent markup and 17 percent labor surcharge. While it is unclear if fringe benefits are considered actual wages paid and therefore allowable, the contractor's inclusion of payroll insurance and tax costs is clearly unreasonable, as the 17 percent labor surcharge covers these costs. Finally, credits from the contractor for work not performed as a result of CCO's, did not include the standard markups applied to labor and equipment. Also, credits provided reflected equipment rental rates that were lower than the rates charged for equipment under force account. There is no evidence that the CM reviewed the labor rate calculations against the contract or questioned the pricing on the credits; while these amounts do not represent a high percentage of the CCO cost, the CM should be reviewing all cost elements for reasonableness and accuracy.

Recommendation 1:

Internal Audit recommends that independent cost estimates be prepared prior to receipt of price and cost information from contractors. Internal Audit also recommends that project management instruct CM's to retain documentation evidencing scrutiny of force account costs, including credits. For future contracts, Internal Audit recommends contract language outlining labor costs paid on force account be clarified and enforced, with consideration for treatment of payroll insurance and taxes.

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Management Response (Capital Programs):

Management agrees with the recommendation. An independent cost estimate (ICE) should be prepared to support proposed CCO's. The extent of the ICE will be based on the circumstance of the change. A fully detailed ICE will then be used by the CM and PM to reconcile and determine the adequacy of any costs provided by the contractor. The CM will be required to document justification or source for individual line items in the ICE. For example, cost of individual items in the ICE may have come from previous CCO's, the projects schedule of values, California Department of Transportation standard rates, or the construction managers' own research. This requirement will be added to the Rail Programs Construction Management Procedures Manual. Construction managers will also be reminded to assure that appropriate documentation is retained to support force account costs paid to, or credits taken from, the contractor.

Management Response (Finance and Administration):

The General Provisions section incorporated as a part of the scope of work for the construction contracts, under "Extra Work and Changes" – states that no more than 17 percent may be added as surcharge to the actual wages. The 17 percent is to constitute full compensation for all other payments, including payments imposed by State and Federal laws. Contracts Administration and Materials Management Department (CAMM) will work with legal counsel on language on how to treat payroll insurance and taxes for force account labor and to provide clarity to the contract provisions.

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Invoice Support

Testing of CM consultant invoices identified the following:

- One sub-consultant, AESCO, does not utilize an adequate labor timekeeping system. Discrepancies were identified between hours recorded on employee timesheets and hours reflected on individual job timesheets that accompanied labor billings.
- Several invoices included overtime and double-time rates, and some other direct costs (ODC), that are not part of the contract.
- Several invoices included one or more staff and/or ODC's that were not part of the contract as of the invoice period. The costs were incurred prior to the effective date of the amendment that eventually added the staff and ODC's.

Recommendation 2:

Internal Audit recommends that prime and sub-consultants be required to have an adequate labor timekeeping system.

Management should remind consultants of the need to request amendments to add staff, labor rates, and ODC's in a timely fashion.

Management Response (Capital Programs):

Management agrees with the recommendation. Capital Programs will work with CAMM to include language be included in the Personnel Qualifications and Responsibilities section of future Request for Proposals to require both prime contractors and subconsultants to have an adequate labor timekeeping system.

A tracking tool is used to monitor use of classifications with respect to name, time, and salary escalation limits. All time and expense contracts which include classification rate schedules now have a tracking spreadsheet inserted into the Project Controls accounts payable tracking file.

Management Response (Finance and Administration):

Through the kick-off meetings and after contract execution and on-going meetings with the PM's, CAMM staff will continue to emphasize the need for timely submission of requests for amendments to any staff/scope or changes to ODC's. The recently conducted Procurement 102 module on Amendments (August 14, 2019) also addressed the significance of submitting information in a timely manner to process amendments.

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Procedures for Ongoing Monitoring of Federally-Funded Assets

At the time of the audit, roles and responsibilities, procedures, and contract templates had not yet been developed to address requirements triggered by the use of federal funds on the Project, including requirements for ongoing maintenance, property management, asset management, Title VI, and civil rights requirements.

Recommendation 3:

Internal Audit recommends management develop and implement written procedures to outline roles and responsibilities of staff tasked with implementing operations and maintenance agreements, and performing ongoing oversight of agencies taking possession of assets built with federal funds.

Management Response (External Affairs):

Management agrees with the recommendation and is coordinating across all divisions within the agency to develop procedures that ensure adequate monitoring and oversight of federal facilities that are owned and maintained by an OCTA subrecipient.