

SAN FRANCISCO STATE UNIVERSITY
HENSILL HALL RENOVATION PROJECT

Final Report

July 12, 2007

CONSTRUCTION PROJECT EVALUATION
SAN FRANCISCO STATE UNIVERSITY
HENSILL HALL RENOVATION PROJECT

July 12, 2007

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EXECUTIVE SUMMARY

Summary of Findings

Based upon our evaluation, the Hensill Hall Renovation Project at SFSU was administered consistent with our expectations of a project of this size, scope, and complexity, except for certain areas in the contract administration process that could be improved.

Our observations, associated risks, and recommendations are summarized below. Examples of specific action steps are further detailed in the body of this report.

	Observation	Risk	Recommendation
1.	Additional work was performed prior to the execution of an ESA or amendment. Payment for the additional work did not always occur on a timely basis.	Allowing additional work to be performed and approved prior to the formal execution of an ESA may not sufficiently protect SFSU in the event of a dispute, and may create poor relations with design firms, as they must float the cost until the ESA is approved.	In the future, additional work should commence only after an appropriate contractual document has been executed. (Ownership: SFSU)
2.	Detail support for change orders was at times missing or limited.	SFSU may be at risk of overpaying for change order work if detailed quotes and supporting cost documentation is missing, limited or not thoroughly evaluated.	In the future, sufficient supporting documentation should be included with each executed change order. (Ownership: SFSU)
3.	Mark-up was not consistently calculated per Contract General Conditions, including mark-up on mark-up, and no use of the tiered mark-up system.	SFSU may be at risk of overpaying for change order work if mark-up is not accurately calculated per Contract General Conditions.	In the future, CSU standard Contractor Change Order Request Summary and Subcontractor Change Order Request Summary should be completed by the contractor and reviewed to ensure accuracy and compliance with Contract General Conditions. (Ownership: SFSU)
4.	Mark-up was not consistently reduced when extended overhead was charged as directly reimbursable change order costs. Change order mark-up is intended to include overhead and should therefore be reduced. SUAM does not expressly state this requirement.	SFSU may be at risk of overpaying for change order work if overhead costs are not accurately excluded from change order mark-up.	The contract language should be revised to better define items excluded from change order mark-up. In addition, SUAM should be revised to include the requirement for reduced mark-up when extended overhead is charged as a direct change order cost. (Ownership: CPDC)

EXECUTIVE SUMMARY

	Observation	Risk	Recommendation
5.	Additional work was performed prior to the execution of an amendment.	Allowing additional work to be performed and approved prior to the formal execution of an amendment may not sufficiently protect SFSU in the event of a dispute, and may create poor relations with the construction management firms, as they must float the cost until the amendment is approved.	In the future, additional work should commence only after an appropriate contractual document has been executed. (Ownership: SFSU)

INTRODUCTION

Purpose

KPMG LLP (“KPMG”) was retained by California State University’s (“CSU”) Office of the University Auditor on October 29, 2004 to perform an independent project evaluation of San Francisco State University’s (“SFSU”) Hensill Hall Renovation (“Project”).

The overall objective of the construction evaluation was to assess construction management practices for the Project and to substantiate that it was managed in accordance with law, Trustee policy, generally accepted business practices, and industry practices.

To the extent they were uncovered as part of our work, this report provides conclusions and recommendations addressing necessary process improvement and recovery of project costs. Recommendations are listed and numbered sequentially throughout this report.

Scope

While the basic scope of our work matches that required by the RFP and that which KPMG has performed in prior years, we also included additional items that we believe may provide benefit to CSU. KPMG identified specific areas within the scope listed below that present the potential for substantive loss or liability for SFSU’s Hensill Hall Renovation Project. The various scope categories are outlined in CSU’s Request for Proposal, dated July 14, 2004 and KPMG’s proposal, dated July 27, 2004 and contains the following sections:

- Project Background
- Design Cost
- Construction Bid Process
- Construction Change Orders
- Project Management and Inspection Services
- Major Equipment and Materials
- Close-Out Documentation
- Liquidated Damages
- Accounting

Methodology

KPMG’s approach to this engagement incorporates a work plan shared with the University Auditor’s office as outlined in our agreement with CSU. During the course of our work, we expanded on tasks related to scope sections with the greatest potential risk exposure, in our opinion. The work performed by KPMG was conducted in accordance with our aforementioned methodology, but is not limited to, the following tasks:

- Examine financial records, reports, written CSU procedures, CSU contract documents and other material related to the Project and compare current practices and procedures with CSU requirements and best practices in the industry;
- Conduct a preliminary review to determine Project emphasis;
- Interview key individuals involved in the Project;
- Identify significant deficiencies, if any;
- Recommend changes that may result in streamlining the design/construction process, assuring adequate project controls and reducing costs; and
- Prepare a written report of our findings and recommendations.

Exclusions

The services, fees, and delivery schedule for this engagement are based upon the following assumptions, representations, or information supplied by CSU (“Assumptions”).

1. KPMG is not responsible for and will not make management decisions relating to this Project or any other aspect of CSU’s business. CSU shall have responsibility for making all decisions with respect to the management and administration of its real estate and capital projects.
2. CSU management accepts responsibility for the substantive outcomes of this engagement and, therefore, has a responsibility to be in a position in fact and appearance to make an informed judgment on the results of this engagement.
3. Our work under this engagement did not include technical opinions related to engineering, operations, and maintenance.
4. KPMG’s work under this engagement did not include a review, audit, or evaluation of financial statements, tax services, or other services of KPMG not listed in this Statement.
5. We have, and will continue to consider the effect of this engagement on the ongoing, planned, and future audits, as required by *Government Auditing Standards* and have determined that this engagement will not impair KPMG’s independence.

PROJECT BACKGROUND

The Project involved construction of a new service yard in addition to the renovation work which included remodeling to meet ADA requirements, seismic retrofitting, HVAC and electrical upgrades, hazardous material abatement, elevator modifications and remodel of some laboratories and lecture rooms.

During the week of May 21, 2007, KPMG conducted fieldwork at the SFSU campus, and reviewed records from the following entities involved with the Project:

Contractors	Pacific Engineer Builders, Inc. and Swinerton Builders
Architect	MBT Architecture
Construction Management	Van Pelt Construction Services
Project Management and Administration	SFSU's Office of Capital Planning, Design and Construction

Follow-up discussions to clarify issues and supplement supporting documentation were conducted through the completion of this report.

Delivery Methodology

The Project was delivered using a design-bid-build, lump sum contract delivery methodology.

Timeline

Design was initiated after an agreement for architectural services was entered into on March 10, 1998 between MBT Associates ("MBT") and SFSU. The initial design, encompassing schematic and preliminary design development services, was managed by the Chancellor's Office CPDC. On October 20, 1998 the design contract with MBT was formally delegated to the SFSU campus.

As the design was substantially complete, a request for construction bids was issued on November 24, 1999. After a complicated bid process, which involved a bid withdrawal and several bid protests, Pacific Engineer Builders, Inc. ("PEBI") was awarded the construction contract. As a result of a lengthy process to resolve the bid protests, the contract with PEBI was not executed until April 3, 2000. Construction subsequently began on June 23, 2000 with the issuance of the Notice to Proceed.

During construction, it became apparent to SFSU that PEBI was not able to deliver the Project in accordance with its contractual obligation. As a result, SFSU terminated PEBI pursuant to Public Contract Code Section 10845 on April 8, 2002 due to defaults not remedied in a timely manner.

PEBI's surety, American Manufacturers Mutual Insurance Company ("American"), was notified and as a result of negotiations, a Project completion agreement was entered into on July 10, 2002 between American and CSU. This agreement allowed PEBI to finalize a portion of the ongoing work to a point where a new contractor could take over, and allowed the surety to be in a position to retain a completion contractor.

American went through a competitive selection process in August of 2002 to retain a completion contractor. Swinerton Builders ("Swinerton") was the successful bidder.

The completion agreement set a milestone date for physical completion of the takeover work to October 18, 2002. As of November 15, 2002 the takeover work was not completed and on December 24, 2002 SFSU put the surety on formal notice that the lack of progress was not acceptable.

The final payment for PEBI's work was made in January 2003. About this time, American's parent company, Kemper Insurance Company ("Kemper"), was in a state of insolvency. As a result of Kemper's financial instability, American was prevented from entering into any new contractual obligations. Instead the arrangement was made for SFSU to enter into contract with Swinerton directly and American would reimburse SFSU for the cost of the completion work in excess of what it would have cost under the original agreement with PEBI.

A construction contract was executed between SFSU and Swinerton on September 18, 2003. Swinerton began construction on September 29, 2003 when the Notice to Proceed was issued. The Project was subsequently progressing to SFSU's satisfaction.

On February 25, 2004 the city streets surrounding Hensill Hall were subject to a combined sewage overflow due to heavy rains and clogged city sewers. The excess water intruded Hensill Hall causing severe damage and delaying the Project by an estimated 315 days. Repair work was incorporated into the existing design, construction, and construction management contracts but was accounted for and paid for separate from the original Project scope of work.

Beneficial occupancy was accepted on a floor by floor basis starting December 1, 2004. On September 23, 2005 the formal Notice of Completion was issued for the entire Project with minor exceptions. The Certificate of Completion was issued on November 29, 2005 and a Certificate of Occupancy for all remodeled floors was issued on December 1, 2005.

Project Costs

The Capital Outlay Estimate form 2-7 dated June 1, 2000 allocates funds of \$18,555,000 for construction work and \$840,000 for Group II Equipment.

This budget did not contain preliminary design development services and working drawing phases of the architectural and engineering services amounting to \$915,000. The funding for this work was handled under a separate Allocation Order. Additional funds were obtained from American and the remainder by SFSU.

At the time of KPMG's fieldwork SFSU had incurred \$26,498,036 in costs on the Project. A summary of Project costs, including an amount of \$393,120 paid by the Chancellor's Office for initial design services, is summarized below:

Description	Budget (2-7)	Actual	Variance (Budget - Actual)
Design Development	\$915,000	\$925,292	(\$10,292)
Construction	\$15,370,000	\$21,776,342	(\$6,406,342)
Architect and Engineering	393,435	813,894	(420,459)
Contract Management	1,220,068	1,373,711	(153,643)
Contingency	1,220,067		1,220,067
Required Additional Services	115,000	539,655	(424,655)
CSU Fee	236,430	387,230	(150,800)
Group II Equipment	840,000	681,911	158,089
Subtotal	\$20,310,000	\$26,498,036	(\$6,188,036)
Surety Proceeds	4,565,000		4,565,000
Additional Construction budget - Campus	1,583,006		1,583,006
Total	\$26,458,006	\$26,498,036	(\$40,030)

KPMG noted a discrepancy in the surety funds obtained from American. SFSU represented the surety proceeds amount as \$4,780,000. However, only \$4,565,000 could be verified and reconciled against actual check copy. As a result of this discrepancy, KPMG is showing a potential cost overrun on the Project, while SFSU is showing a slight budget surplus.

DESIGN COSTS

MBT Architecture (“MBT”) was selected to perform design services for the Project. A standard Project Architect/Engineering Agreement was executed between SFSU and MBT on April 6, 1998 in the amount of \$1,191,273. The initial schematic and preliminary design development phases were managed by the Chancellor’s Office CPDC prior to the remainder of the agreement being delegated to SFSU on October 20, 1998.

21 changes were made to the agreement including 5 amendments and 16 extra service agreements (“ESA’s”). The total value of the changes was \$470,688 bringing the total contract value to \$1,661,961. The contractual obligations for design services are represented in the following table:

Description	Date	Total
Schematic Design (19%)	4/6/1998	\$ 226,342
Preliminary (14%)	4/6/1998	166,778
Construction Documents (38.19%)	4/6/1998	454,947
Bidding (4.02%)	4/6/1998	47,889
Construction Phase (24.79%)	4/6/1998	295,317
Base Agreement Subtotal		\$ 1,191,273
Amendment #1 - Evaluate misplaced soil anchors and redesign toilet rooms	3/2/2001	\$19,205
Amendment #2 - Structural engineering for the substitution of mechanical units	10/3/2001	7,400
Amendment #3 - Professional services for site meetings	12/5/2001	41,000
Amendment #4 - Review cold room controls substitution	11/26/2002	4,870
Amendment #5 - Additional Construction Administration services	8/23/2003	100,000
Extra Services Agreement #6 - Additional mechanical engineering services	9/29/2003	6,600
Extra Services Agreement #7 - Additional electrical engineering services	9/24/2003	1,928
Extra Services Agreement #8 - Design services for the temperature control	2/12/2004	1,320
Extra Services Agreement #9 - Additional project meeting attendance	12/8/2003	16,640
Extra Services Agreement #10 - Construction and Post Construction Phase services	1/5/2004	107,439
Extra Services Agreement #11 - Additional electrical engineering services	1/20/2004	3,124
Extra Services Agreement #12 - Design services for replacement of chilled water riser	6/23/2004	10,450
Extra Services Agreement #13 - Mechanical engineering services for fire sprinkler	11/19/2004	3,454
Extra Services Agreement #14 - Architectural and Engineering for roll up door	11/19/2004	1,672
Extra Services Agreement #15 - Structural engineering services for CMU walls	11/19/2004	5,500
Extra Services Agreement #16 - Additional contract administration services	12/6/2004	85,000
Extra Services Agreement #17 - Amend ESA#8 to add additional services	12/6/2004	660
Extra Services Agreement #18 - Mechanical coordination	12/6/2004	4,400
Extra Services Agreement #19 - Phase I adjustment due to PEBI termination	12/6/2004	35,010
Extra Services Agreement #20 - Revision of the Seawater system	1/20/2005	10,430
Extra Services Agreement #21 - Upgrade of Alcohol Storage room	1/20/2005	4,586
Total Adjustments to the Agreement		\$ 470,688
Total Agreement		\$ 1,661,961

KPMG reviewed the agreement, amendments, ESA’s and invoices and discovered certain discrepancies in the contract administration process.

A total of \$74,937 in additional design services were invoiced prior to the execution of an amendment or ESA. Per the description on the invoices, work was also performed prior to the execution of an ESA. Additionally, \$26,605 of the amount was authorized for payment prior to the formal authorization of an amendment, however no evidence of a payment made to MBT was observed.

Contract	Date of ESA	Invoiced		Approved	
		Prior to ESA	Prior to ESA	Prior to ESA	Prior to ESA
Amendment 1	3/2/2001	\$ 19,205	\$ 19,205	\$ 19,205	\$ 19,205
Amendment 2	10/3/2001	7,400	7,400	7,400	7,400
Amendment 3	12/5/2001	30,070	-	-	-
Amendment 4	11/26/2002	3,896	-	-	-
ESA 13	11/19/2004	3,454	-	-	-
ESA 14	11/19/2004	1,672	-	-	-
ESA 15	11/19/2004	5,500	-	-	-
ESA 17	12/6/2004	660	-	-	-
ESA 18	12/6/2004	3,080	-	-	-
Total		\$ 74,937	\$ 26,605		

MBT routinely waited several months after work was performed to receive payment due to the delay in execution of amendments and ESA's. Since an amendment or ESA typically was not issued until MBT's services had been rendered, the actual costs of the work should have been known at the time the amendment or ESA was executed. However, the amendments or ESA's were in most cases executed for the original MBT proposed amounts, which may have resulted in unnecessary costs to SFSU. Although most ESA's and amendments stated a not-to-exceed compensation structure, they were actually compensated on a fixed fee basis, reflective of the original MBT proposed amount.

Observation:

Additional work was performed prior to the execution of an ESA. Payment for the additional work did not always occur on a timely basis.

Risk:

Allowing additional work to be performed and approved prior to the formal execution of an ESA may not sufficiently protect SFSU in the event of a dispute, and may create poor relations with design firms, as they must float the cost until the ESA is approved.

Recommendation:

1. In the future, additional work should commence only after an appropriate contractual document has been executed.

(Ownership: SFSU)

Campus Response:

1. We concur. In the future, campus projects that require additional work will commence only after an appropriate contract has been approved. A memo will be issued by the Vice President for Administration and Finance/CFO to the Associate Vice President of Capital Planning, Design and Construction reiterating the recommendation.

SUAM 9210 provides guidance for the execution of agreements for professional services, and section 9201.3 provides guidance specifically for ESA's. Section 9201.3 states Extra Service Authorization letters are to be used to facilitate additional services, and the use of amendments to design agreements is not appropriate to authorize extra services. It appears amendments were erroneously used at the beginning of the Project; however, this practice was later corrected.

Recommendation:

None

CONSTRUCTION BID PROCESS

The initial construction bid process began with the release of the notice to contractors on November 24, 1999. Bids from C. Overaa & Co, Vahdani Construction Company, S.J. Amoroso Company, Arntz Builders, Dennis J. Amoroso Construction Company, and PEBI were opened on January 25, 2000.

C. Overaa & Co. withdrew their proposal due to a bid assembly error, leaving Vahdani Construction Company as the apparent low bidder. However, bid protest letters were submitted by S.J. Amoroso Company and PEBI stating that Vahdani was non-responsive. S.J. Amoroso Company also stated PEBI was non-responsive. PEBI stated that S.J. Amoroso was non-responsive. ISEC, a subcontractor, submitted a protest stating PEBI was non-responsive. After an investigation of the bid protests, SFSU determined that Vahdani was indeed non-responsive and rejected Vahdani's bid. PEBI was determined to be the lowest responsive and responsible bidder. A Petition for Writ of Mandate was filed in San Francisco Superior Court (*Amoroso v. San Francisco State University, Case No. 31137*). The court denied the petitioner's request, ruling in favor of SFSU on May 8, 2000.

Due to the lengthy process of resolving the bid protests, the contract with PEBI was not executed until May 15, 2000. Construction began on June 23, 2000 with the issuance of the Notice to Proceed.

As construction progressed, it became apparent to SFSU that PEBI was not able to deliver the Project in accordance with the contractual terms and conditions. SFSU terminated PEBI pursuant to Public Contract Code Section 10845 on April 8, 2002 due to defaults not remedied in a timely manner.

PEBI's surety, American Manufacturers Mutual Insurance Company ("American"), was notified, and as a result of negotiations, a Project completion agreement was entered into on July 10, 2002 between American and the Trustees of CSU. This agreement allowed PEBI to finalize a portion of the ongoing work to a point where a new contractor could take over, and allowed the surety to be in a position to retain a completion contractor.

An invitation for offers for a completion contractor was issued on August 9, 2002 by Sage Associates, as construction management representatives for American. Competitive bids were received from Swinerton Builders, S.J. Amoroso and BRCO. Swinerton was declared the successful bidder.

American's parent company, Kemper Insurance Company ("Kemper"), was in a state of insolvency and as a result, American was prevented by Kemper from entering into any new contractual obligations. Instead, the arrangement was made for SFSU to enter into contract with Swinerton directly and American would reimburse SFSU for the cost of the completion work in excess of what it would have cost under the original agreement with PEBI.

Although the procurement process for retaining Swinerton was not managed by SFSU, the process was competitive. No protests were received for awarding the contract to Swinerton.

It was noted in discussions with SFSU that Project specific pre-qualification experience were not required by the bidders. CSU has a process whereby technical qualifications, specific to the Project, can be required in addition to CSU's general pre-qualification requirements. This mechanism will help preclude contractors without sufficient experience to bid. SFSU expressed that a major reason PEBI failed to be perform and had to be terminated was their lack of experience with projects of this similar size and complexity and lack of experience in the type of renovation work performed. Although PEBI was generally qualified by CSU, additional technical requirements may have prevented an unqualified contractor from being awarded the work. Since this Project was awarded, CPDC has established additional pre-qualification criteria.

Subcontractor Compliance

Per the Contract General Conditions section 2.06-(b) subcontractors who perform work in excess of 'one-half of one percent' of the bid amount must be listed on an expanded listing of subcontractors. In this case, one-half of one percent of Swinerton's bid totaled \$48,481. No irregularities were noted during testing.

Inquiry of SFSU and Swinerton revealed no evidence of subcontractor substitution on the Project.

CONSTRUCTION CHANGE ORDERS

Although two contractors were used for the Project, PEBI and Swinerton, KPMG was only able to access and review Swinerton's internal change order records. The contractor's own records comprise an important part in the process of evaluating change orders. However, KPMG reviewed PEBI's change orders as available at SFSU and performed limited testing on these records for completeness.

- PEBI's had an initial contract value of \$15,080,000 and a total of seven change orders representing \$784,653 in additional cost, prior to being terminated. The final total contract value for PEBI was \$15,864,653, prior to termination.
- Swinerton had an initial contract value \$9,696,100 and a total of 26 change orders representing \$1,749,284 in additional cost increasing Swinerton's total contract value to \$11,445,384.

The following table summarizes the Project change orders between SFSU and Swinerton:

Change Order	Description	Date	Amount
1	Repair of non-functioning drains, relocation of conduit on floors 5 & 6	2/10/2004	\$ 129,033
2	Temporary fire alarm system on floors 1-5, relocation of conduit floor 4	3/30/2004	60,025
3	Additional control points for Building Management System, Fire caulk	6/5/2004	103,727
4	Installation of various items at seawater vault, ceiling partition offset	6/15/2004	64,466
5	Adjustments to HVAC system for existing conditions, work on sterilizers	8/25/2004	259,522
6	Compensable time extension of 31 days	8/26/2004	119,688
7	Delete exterior storage buildings, credit for deleted site work, testing	8/26/2004	(563,485)
8	Installation of new isolation valves, various plumbing and electrical	8/26/2004	166,212
9	Door relocation for ADA compliance, replaced plugged plumbing	10/8/2004	159,831
10	Beneficial Occupancy for the 4th floor	3/1/2005	-
11	Beneficial Occupancy for the 5th floor	3/1/2005	-
12	Beneficial Occupancy for the 6th floor	3/1/2005	-
13	Replace VCT flooring, disposal difference for hazardous ceiling waste	3/2/2005	75,067
14	Hensill Hall Optional standby power addition	2/21/2005	205,824
15	Calibration of the "Belimo" valves, bring 208 receptacles to code	6/10/2005	82,748
16	Relocation of five doors, isolation valves and piping, conduit relocation	3/18/2005	69,454
17	Extended project completion date (non-compensable)	2/21/2005	-
18	Additional door and frame modifications, elevator repair	3/17/2005	52,893
19	Replace fan coil units, provide new chilled water supply	7/5/2005	196,105
20	New switch for Thornton Hall Standby power	7/5/2005	36,608
21	Modifications to doors and frames, repair electrical conduit on floors 3-6	7/5/2005	75,664
22	Revision to fire/life safety system, painting floors 1-3, drip trays	10/7/2005	129,253
23	Revised bathroom layout, install 3 FDSR's, abate membrane (cold room)	10/7/2005	41,820
24	Alcohol storage room, sea water changes, concrete pad and access doors	11/6/2005	93,113
25	Modifications to ductwork, plumbing and electrical, air balance, VCT	12/15/2005	102,579
26	Time extension and extended overhead, re-insulate pipes, full settlement	1/23/2006	89,137
Totals			\$ 1,749,284

In certain cases the supporting documentation included with the change orders did not contain detail quotes or estimates from the subcontractors, or a detail of lump sum contractor charges as would be expected. Some, but not all of the missing documentation was provided by SFSU after inquiry. In addition, change orders extending time to both PEBI and Swinerton did not state how the time extensions were determined. As a result, KPMG could not verify its reasonableness.

Observation:

Detail support for change orders was at times missing or limited.

Risk:

SFSU may be at risk of overpaying for change order work if detailed quotes and supporting cost documentation is missing, limited or not thoroughly evaluated.

Recommendation:

2. In the future, sufficient supporting documentation should be included with each executed change order.

(Ownership: SFSU)

Campus Response:

2. We concur. In the future, sufficient supporting documentation will be included with each executed change order. A memo will be issued by the Vice President for Administration and Finance/CFO to the Associate Vice President of Capital Planning, Design and Construction reiterating the recommendation.

KPMG sampled nine change order line items for testing. The samples were selected to represent large dollar amounts, a variety of change orders, and include both additive and deductive changes. The samples represent \$1,061,430 in total changes comprised of \$650,113 in additive changes, and \$411,317 in deductive changes.

Mark-up testing was performed on the selected samples and revealed that mark-up was not always calculated correctly. Two instances were noted where mark-up was calculated on mark-up which is not permitted per Contract General Conditions section 6.01c (4), and three instances were found when the tiered mark-up system as defined in Contract General Conditions section 6.01c (5) was not used. This tiered system permits 15% mark-up on the first \$50,000 of direct costs and 10% mark-up on the balance over \$50,000. Of the samples selected, the tiered system was never used for contractor direct costs exceeding \$50,000 representing a potentially greater error. These errors may not have occurred had the CSU

standard Change Order Request form been used. The total dollar amount of mark-up variance due to these two mark-up errors contained in the selected sample totaled \$5,192.

Observation:

Mark-up was not consistently calculated per Contract General Conditions, including mark-up on mark-up, and no use of the tiered mark-up system.

Risk:

SFSU may be at risk of overpaying for change order work if mark-up is not accurately calculated per Contract General Conditions.

Recommendation:

3. In the future, CSU standard Contractor Change Order Request Summary and Subcontractor Change Order Request Summary should be completed by the contractor and reviewed to ensure accuracy and compliance with Contract General Conditions.

(Ownership: SFSU)

Campus Response:

3. We concur. In the future, the CSU standard Contractor Change Order Request Summary and Subcontractor Change Order Request Summary will request the contractor to complete and be reviewed by appropriate campus personnel to ensure accuracy and compliance with Contract General Conditions. A memo will be issued by the Vice President for Administration and Finance/CFO to the Associate Vice President of Capital Planning, Design and Construction reiterating the recommendation.

General Conditions 6.01c(4) states that mark-up includes, “all incidental overhead support costs and profit.” Incidental costs include site overhead including facilities and utilities, bonds, small tools and other miscellaneous support costs, among others. Some of the change orders line item samples contained costs that could be classified as incidental overhead support costs including utilities, debris boxes, toilets, and general clean up. The Contract General Conditions do not expressly state incidental clean-up as covered by the mark-up, nor is it expressly stated as directly reimbursable. Since mark-up is defined to include incidental costs it would also not be permissible to allow the full mark-up to be charged on the incidental overhead costs. CPDC generally recommend that mark-up be reduced to no more than 9% when overhead is charged as a direct cost, however SUAM does not expressly state this requirement.

Observation:

Mark-up was not consistently reduced when extended overhead was charged as directly reimbursable change order costs. Change order mark-up is intended to include overhead and should therefore be reduced. SUAM does not expressly state this requirement.

Risk:

SFSU may be at risk of overpaying for change order work if overhead costs are not accurately excluded from change order mark-up.

Recommendation:

4. The contract language should be revised to better define items excluded from change order mark-up. In addition, SUAM should be revised to include the requirement for reduced mark-up when extended overhead is charged as a direct change order cost.

(Ownership: CPDC)

Management Response:

4. We agree. We have modified the Contract General Conditions via the Supplementary General Conditions and the Change Order Procedures in SUAM, and have posted these revised documents to the Construction Management website.

Change Order Report Analysis

CSU has historically considered change order costs incurred due to errors and omissions by the architect of up to 3% of the initial award construction cost as falling within the architect's 'standard of care'. However, the MBT agreement as executed does not contain any language defining 'standard of care', but states errors and omissions insurance shall be secured commensurate with the magnitude of the Project.

Since this Project used two contractors, SFSU provided two change order logs, one each for PEBI and Swinerton that reflected the initiating source of each change. A total of \$735,298 in change order costs between the two contractors was attributable to error in or omission from the contract documents. SFSU did not consistently identify whether a change was attributable to an error or an omission.

The CSU practice is to consider the monetary impact of omissions as 20%. The following table weights the known omissions at 20% of their dollar value:

Class	Type of change	Amount	% of Total CO	% of Original Contract
4.1	Error in or omission from the contract documents	\$ 706,225	28.5%	4.7%
4.2	Unforeseeable job site condition	751,686	30.4%	5.0%
4.3	Change in the requirements of a regulatory agency	607,581	24.5%	4.0%
4.4	Change originated by the University	379,235	15.3%	2.5%
4.5	Changes in specified work due to the unavailability of specified materials	36,406	1.5%	0.2%
4.6	Other	(4,447)	-0.2%	0.0%
Total Change Orders		\$ 2,476,686	100.0%	16.4%
Original Contract Amount		\$ 15,080,000		
Total		\$ 17,556,686		

KPMG used PEBI’s original contract amount to establish the basis for the errors and omissions calculation, since this represents the contract value at time of bid. Based on the information provided, change orders attributable to errors and omissions are calculated to 4.68% of the original contract amount which is greater than the 3% that fall under the CSU’s acceptable levels of ‘standard of care’. The total dollar amount attributable to errors and omissions is \$706,225, considering known omissions at 20%.

Subsequent to fieldwork, SFSU completed a detail analysis of errors and omissions where it was concluded that the acceptable levels of standard of care had not been exceeded, as summarized in the table below. Due to the complexity of this Project, it is not possible to accurately establish a representative percentage of errors and omissions. SFSU and CPDC concluded that no recourse against MBT is warranted.

PEBI Base Contract	\$ 9,597,346		
CO - Error @ 100%	\$ 156,629	100%	\$ 156,629
CO - Omission @ 20%	\$ 89,022	20%	17,804
Total - CO - E&O - PEBI			\$ 174,433
E & O Change Order Percentage - PEBI			1.82%
Swinerton PEBI Base Contract	\$ 9,696,100		
CO - Error @ 100%	\$ 221,597	100%	\$ 221,597
CO - Omission @ 20%	\$ 127,587	20%	25,517
Total - CO - E&O - PEBI			\$ 247,114
E & O Change Order Percentage - Swinerton			2.55%

Recommendation:

None

CONSTRUCTION MANAGEMENT SERVICES

Van Pelt Construction Services (“Van Pelt”) entered into a standard CSU Service Agreement with SFSU on August 30, 2000 to provide construction management services for the Project. The contract consists of a not-to-exceed base contract agreement in the amount of \$525,120 and seven amendments totaling \$860,591 for a total contract value of \$1,385,711. Additional amendments were created for services related to the effects of the water intrusion event of Hensill Hall renovation but are not part of the renovation Project.

The contract and Project relevant amendments are outlined below:

Description	Date	Amount
Base Contract	8/30/2000	\$ 525,120
Amendment 1 - Schedule Review Services	8/15/2001	12,000
Amendment 2 - Extend service period	8/22/2002	175,000
Amendment 2 - Extend service period	2/11/2003	200,000
Amendment 4 - Extend service period	12/10/2003	176,000
Amendment 6 - CM and litigation support	10/15/2004	132,000
Amendment 8 - Extend service period	3/3/2005	66,000
Amendment 10 - Extend service period	10/24/2005	87,591
Total		\$ 1,373,711

The invoices from Van Pelt contained appropriate approval prior to payment, and were recorded accurately in the accounting system. However, three invoices in the amount of \$72,000 encompassed work for which an amendment had not yet been executed at the time the work was rendered and the invoice presented. No instances of payment to Van Pelt prior to execution of an amendment were noted.

Observation:

Additional work was performed prior to the execution of an amendment.

Risk:

Allowing additional work to be performed and approved prior to the formal execution of an amendment may not sufficiently protect SFSU in the event of a dispute, and may create poor relations with the construction management firm as they must float the cost until the adjustment is approved.

Recommendation:

5. In the future, additional work should commence only after an appropriate contractual document has been executed.

(Ownership: SFSU)

Campus Response:

5. We concur. In the future, additional work will commence only after an appropriate contractual document has been executed. A memo will be issued by the Vice President for Administration and Finance/CFO to the Associate Vice President of Capital Planning, Design and Construction reiterating the recommendation.

MAJOR EQUIPMENT/MATERIALS REVIEW

KPMG selected and reviewed a sample of materials and equipment based on construction cost and accessibility to the installed items. As this Project was a functional facility at the time of KPMG's fieldwork, consideration was given to equipment and materials located in occupied areas in order not to interrupt any student or faculty activities.

SFSU allowed full and complete access to drawings, specifications, samples and submittals, which were organized and contained sufficient information. The equipment and materials located in the field were compared to submittals approved by the architect and/or engineer and were verified against performance specifications, submittals, and drawings.

The following equipment items and specific model data were approved and visually confirmed as installed on the Project:

Division	Drawing No.	Brand	Model No./ Capacity	Description
15160	M7.01	Bell & Gossett	1531 2BC	Pump
15800	M7.01	Greenheck	VABS36F17-1-10	RE-4 Fan
11530	M7.01	Hamilton Fisher	716-1 712-1	Fume Hood
15700	M7.01	Carel	SD103HO	Steam Humidifier
15800	M7.01	McQuay	Vision	Fan Coil Unit
15400	M7.02	Ventrol	ITF-1, VC40-82/114-12	Air Handling Unit
15700	M7.02	McQuay	FUHN1063AA00	Unit Heater
15680	A1.11	Trane	ALR17ES27-ER10	Chiller
16600	E5.0	Cummings	5000-FEK-4353	Emergency Generator

The equipment and materials observed in the field conformed to the specified requirements, drawings, specifications and submittals, based on a visual inspection of equipment labeling, and comparison to physical materials samples provided and approved by the architect.

Recommendation:

None

CLOSE-OUT PROCESS

On September 23, 2005 SFSU issued a conditional Notice of Completion to Swinerton listing blackboard installation, projection screens and keying as items that remained to be completed. A Certificate of Completion was issued on November 29, 2005 followed by a Certificate of Occupancy issued on December 1, 2005.

KPMG verified the Project close-out requirements established by the Contract General Conditions and SUAM. The CSU standard close-out checklist was not used to track close-out items; however the requirements could still be verified. KPMG reviewed operation and maintenance manuals, warranties, punch list, operating permits, pre-final and final inspections and other relevant Project close-out documentation. Nothing came to KPMG's attention indicating an issue with the close-out process.

Recommendation:

None

LIQUIDATED DAMAGES

The Notice to Proceed to Swinerton establishes the original term of the contract as 224 days with work beginning on September 29, 2003 and to be completed on May 9, 2004. A total of 465 days were added to the Project through the change order process and mathematically extended the expected completion date to August 17, 2005. However, change order No. 17 designates an extended Project completion date to July 24, 2004, which is not correctly calculated based on the number of extra days awarded. Subsequently, change order No. 26, the final change order, awards an additional 84 days bringing the Project completion date to October 4, 2004.

The Notice of Completion was issued on September 23, 2005, which is prior to the contracted completion date. Strictly based on the expressly stated completion date on change order No. 17, liquidated damages do not apply.

Recommendation:

None

ACCOUNTING

Due to the different funding sources, SFSU had to compile the total Project accounting, including budget amounts, encumbrances, and expenditures, at KPMG's request. The Excel workbook provided was not directly generated by the accounting system, but consisted of a 'shadow' system based on both of verbally obtained information (budget amounts) and information obtained from the mainframe accounting system (encumbrances and expenditures).

The Project budget was based on three funding sources:

- The Capital Program
- Surety proceeds obtained from American
- SFSU provided funding

KPMG reconciled the stated capital outlay program budget information to allocation orders, but had difficulty reconciling the stated proceeds from American to an actual check. The amount funded by SFSU was not tracked separately for this Project and therefore, the amount presented as available funding for the purposes of this Project could not be verified. However, all SFSU funded expenditures related to Hensill Hall, both this and other projects were tracked as a whole and could be verified with the mainframe accounting system on a sample basis. The process of obtaining campus funding for these expenditures was described as regular meetings between the Vice President of Capital Planning, Design and Construction and the Vice President for Administration and Finance where Hensill Hall cost projections and additional funding needs were discussed and agreed to.

KPMG reviewed documentation which reconciled the Excel spreadsheets and the main accounting system.

Recommendation:

None



**SAN FRANCISCO
STATE UNIVERSITY**

1600 Holloway Avenue
San Francisco, CA 94132
Tel: 415/338-1381
Fax: 415/338-6210

OFFICE OF THE PRESIDENT

August 14, 2007

Mr. Larry Mandel
University Auditor
The California State University
401 Golden Shore
Long Beach, California 90802-4210

**RECEIVED
UNIVERSITY AUDITOR**

AUG 17 2007

**THE CALIFORNIA STATE
UNIVERSITY**

Dear Mr. Mandel:

We have reviewed the KPMG Audit Report on the Hensill Hall Renovation Construction Project at San Francisco State University. Our responses to the other recommendations are attached. We understand the Chancellor's Office is responsible for responding to recommendation #4.

In addition, we have already taken actions to implement the four (4) recommendations which will be forwarded to you in a separate progress report.

Questions regarding our responses may be directed to Leroy M. Morishita, Vice President for Administration and Finance and CFO, at 415/338-2521 or Franz Lozano, Internal Auditor, at 415/405-3736.

Sincerely,

Robert A. Corrigan
President

FL/MO/id

Attachment

cc: Leroy M. Morishita, Vice President for Administration and Finance and CFO
Simon Lam, Associate Vice President, Capital Planning, Design, & Construction
Roger Fish, Director, Capital Planning, Design, & Construction
Franz Lozano, Internal Auditor
Mark Osborne, Associate Internal Auditor

CONSTRUCTION PROJECT EVALUATION
SAN FRANCISCO STATE UNIVERSITY
HENSILL HALL RENOVATION PROJECT

DESIGN COSTS

Recommendation:

1. In the future, additional work should commence only after an appropriate contractual document has been executed.

(Ownership: SFSU)

Campus Response:

1. We concur. In the future, campus projects that require additional work will commence only after an appropriate contract has been approved. A memo will be issued by the Vice President for Administration & Finance and CFO to the Associate Vice President of Capital Planning, Design and Construction reiterating the recommendation.

CONSTRUCTION CHANGE ORDERS

Recommendations:

2. In the future, sufficient supporting documentation should be included with each executed change order.

(Ownership: SFSU)

3. In the future, CSU standard Contractor Change Order Request Summary and Subcontractor Change Order Request Summary should be completed by the contractor and reviewed to ensure accuracy and compliance with Contract General Conditions.

(Ownership: SFSU)

Campus Responses:

2. We concur. In the future, sufficient supporting documentation will be included with each executed change order. A memo will be issued by the Vice President for Administration & Finance and CFO to the Associate Vice President of Capital Planning, Design and Construction reiterating the recommendation.
3. We concur. In the future, the CSU standard Contractor Change Order Request Summary and Subcontractor Change Order Request Summary will request the contractor to complete and be reviewed by appropriate campus personnel to ensure accuracy and compliance with Contract General Conditions. A memo will be issued by the Vice President for Administration & Finance and CFO to the Associate Vice President of Capital Planning, Design and Construction reiterating the recommendation.

CONSTRUCTION MANAGEMENT SERVICES

Recommendation:

5. In the future, additional work should commence only after an appropriate contractual document has been executed.

(Ownership: SFSU)

Campus Response:

5. We concur. In the future, additional work will commence only after an appropriate contractual document has been executed. A memo will be issued by the Vice President for Administration & Finance and CFO to the Associate Vice President of Capital Planning, Design and Construction reiterating the recommendation.



Business and Finance
401 Golden Shore, 5th Floor
Long Beach, CA 90802-4210

www.calstate.edu

Richard P. West
Executive Vice Chancellor/CFO

562-951-4600
Fax 562-951-4970
rwest@calstate.edu

MEMORANDUM

Date: August 31, 2007
To: Larry Mandel
University Auditor
From: Richard P. West
Executive Vice Chancellor & Chief Financial Officer
Subject: Audit Report
Hensill Hall Renovation
San Francisco State University

RECEIVED
UNIVERSITY AUDITOR
SEP - 7 2007
THE CALIFORNIA STATE
UNIVERSITY

I am pleased that the overall theme of this audit report continues in a positive vein and that it finds general compliance with established procedures. I have reviewed the report's findings with my Capital Planning, Design and Construction (CPDC) staff, and have attached our response to the auditors' findings and recommendations to CPDC.

RPW:ESJ:bn

Attachments

cc: Ms. Elvyra F. San Juan
Mr. Larry Piper
Mr. Thomas M. Kennedy
Mr. James R. Corsar

CSU Campuses
Bakersfield
Channel Islands
Chico
Dominguez Hills
East Bay

Fresno
Fullerton
Humboldt
Long Beach
Los Angeles
Maritime Academy

Monterey Bay
Northridge
Pomona
Sacramento
San Bernardino
San Diego

San Francisco
San José
San Luis Obispo
San Marcos
Sonoma
Stanislaus

CONSTRUCTION PROJECT EVALUATION
SAN FRANCISCO STATE UNIVERSITY
HENSILL HALL RENOVATION PROJECT

CONSTRUCTION CHANGE ORDERS

Recommendation:

4. The contract language should be revised to better define items excluded from change order mark-up. In addition, SUAM should be revised to include the requirement for reduced mark-up when extended overhead is charged as a direct change order cost.

(Ownership: CPDC)

Management Response:

4. We agree. We have modified the Contract General Conditions via the Supplementary General Conditions and the Change Order Procedures in SUAM, and have posted these revised documents to the Construction Management website.

THE CALIFORNIA STATE UNIVERSITY
OFFICE OF THE CHANCELLOR



BAKERSFIELD

September 19, 2007

CHANNEL ISLANDS

CHICO

MEMORANDUM

DOMINGUEZ HILLS

EAST BAY

TO: Mr. Larry Mandel
University Auditor

FRESNO

FROM: Charles B. Reed
Chancellor

A handwritten signature in black ink that reads "Charles B. Reed".

FULLERTON

HUMBOLDT

SUBJECT: KPMG Draft Final Report on the *Hensill Hall Renovation*
Construction Project at San Francisco State University

LONG BEACH

LOS ANGELES

In response to your memorandum of September 19, 2007, I accept the response as submitted with the draft final report on the *Hensill Hall Renovation* construction project at San Francisco State University.

MARITIME ACADEMY

CBR/jt

MONTEREY BAY

Enclosure

NORTHRIDGE

cc: Ms. Erika Alvord, KPMG

POMONA

Dr. Robert A. Corrigan, President, San Francisco State University

SACRAMENTO

Mr. Franz Lozano, Internal Auditor, San Francisco State University

SAN BERNARDINO

Mr. Leroy M. Morishita, Vice President, Administration and Finance,

San Francisco State University

SAN DIEGO

Ms. Colleen Nickles, Assistant Vice Chancellor, Financial Services

Ms. Elvyra San Juan, Assistant Vice Chancellor, CPDC

SAN FRANCISCO

Mr. Richard P. West, Executive Vice Chancellor and Chief Financial Officer

SAN JOSÉ

SAN LUIS OBISPO

SAN MARCOS

SONOMA

STANISLAUS