

CONSTRUCTION
CALIFORNIA STATE UNIVERSITY,
NORTHRIDGE
PERFORMING ARTS CENTER

Audit Report 11-13
November 7, 2011

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ABBREVIATIONS

BOT	Board of Trustees
CM at Risk	Construction Manager at Risk
CPDC	Capital Planning, Design and Construction
CRB	Certification Review Board
CSU	California State University
CSUN	California State University, Northridge
EO	Executive Order
GMP	Guaranteed Maximum Price
OUA	Office of the University Auditor
SUAM	State University Administrative Manual

EXECUTIVE SUMMARY

At its January 2010 meeting, the Board of Trustees directed the Office of the University Auditor (OUA) to review construction activity. Construction auditing had been performed by KPMG since fiscal year 1997/98 with coordination from the OUA. In fiscal year 2008/09, OUA staff began performing construction audits.

We visited the California State University, Northridge campus and the offices of the construction manager and selected subcontractors from May 31, 2011, through June 30, 2011, and audited the Performing Arts Center project focusing on the construction management policies and procedures and internal controls and processes in effect at that time.

Our study and evaluation did not reveal any significant construction management or internal control problems or weaknesses that would be considered pervasive in their effects on construction activity controls. However, we did identify a reportable weakness that is described in the executive summary and body of this report. In our opinion, the operational and administrative controls in effect for the Performing Arts Center project were sufficient to meet the overall audit objective stated below.

As a result of changing conditions and the degree of compliance with procedures, the effectiveness of controls changes over time. Specific limitations that may hinder the effectiveness of an otherwise adequate system of controls include, but are not limited to, resource constraints, faulty judgments, unintentional errors, circumvention by collusion, and management overrides. Establishing controls that would prevent all these limitations would not be cost-effective; moreover, an audit may not always detect these limitations.

The following summary provides management with an overview of condition requiring attention. Areas of review not mentioned in this section were found to be satisfactory. Numbers in brackets [] refer to page numbers in the report.

PRE-CONSTRUCTION AND BID PROCESS [6]

Duties of project staff related to the expanded list of subcontractors were not clearly stated in the State University Administrative Manual and/or the Project Administration Reference Manual.

INTRODUCTION

BACKGROUND

In March 2006, the Board of Trustees (BOT) approved a revised campus master plan for California State University, Northridge (CSUN) that included a proposed performing arts center. Also in March 2006, the BOT approved schematic plans for the CSUN Performing Arts Center project at a cost of \$99,948,000, with funding from a combination of state and non-state sources, including fund-raising, the 2006/07 Governor's budget, and the Higher Education Outlay Bond Fund of 2004.

In February 2008, the campus solicited project bids and selected CW Driver, Inc., as the construction manager. CSUN issued the Notice to Proceed on March 3, 2008, and executed an agreement with the construction manager at a construction cost of \$97,891,587. The campus received a Certificate of Occupancy on December 14, 2010, and filed a Notice of Completion on April 1, 2011.

The Performing Arts Center, designed by Hammel Green and Abrahamson, Inc., features a prominent three-story lobby that provides access to the 1,600-seat main hall from Nordhoff Avenue. The location and massing were designed in concert with the campus master plan goals for the creation of courtyards to support academic use and views into the campus. The building structure is a steel-braced frame with concrete filled metal decks, and the building exterior is finished in a combination of glass curtain walls, metal panels, and tile. The project includes 35 faculty offices and space for theater lighting and sound, scenery design, rehearsal, and production. In addition to the main hall and lobby, the building program includes a 250-seat experimental theater, a tiered lecture hall, the campus radio station, and performance supporting spaces. Sustainable features include a cool roof, an energy management system, and connection to the central plant for heating and cooling. The west-facing lobby has an energy-efficient curtain wall system and a large roof overhang to minimize solar heat gain. Energy-efficient lighting and control systems are used in conjunction with natural lighting.

The CSUN campus managed the Performing Arts Center project, and it chose the Construction Manager at Risk (CM at Risk) with Guaranteed Maximum Price (GMP) delivery method. In this method, a construction management firm chosen by a competitive bidding process provides all or significant portions of design and construction administrative services and takes part in establishing the GMP. The CM at Risk acts as the general contractor during construction, assumes the risk of subcontracting the work, and guarantees completion of the project. The liability for the success in completing the project on time and in budget lies with the construction manager, and not with the university. Further, there is a potential for cost savings should the project be completed below the GMP.

Executive Order (EO) 672, *Delegation of Capital Outlay Management Authority and Responsibility*, dated July 25, 1997, delegates to campus presidents the authority to manage directly state and non-state funded capital outlay projects. The chancellor's office issues this delegated authority to the campus subject to its compliance with the capital outlay certification procedure. To comply, the campus submits a request for Delegation of Capital Outlay Management Authority to the Certification Review Board (CRB) for review. Then the executive vice chancellor and chief financial officer in the chancellor's office must approve the request. The campus president is responsible for ensuring that he or she exercises delegated authority in compliance with applicable statutes, regulations, and policies of the BOT; the campus manages capital projects via a process consistent with the provisions of the State

University Administrative Manual (SUAM); and the campus has in place appropriate internal controls and processes to ensure that responsibilities are carried out in a manner consistent with the campus capital outlay management plan submitted with the request for delegated authority.

The certification procedure required by EO 672 includes submission of a capital outlay management plan, which defines the campus organizational and operational structure and expenditure authority, and serves as the campus policies and procedures for the administration of construction activities. Updated plans are to be submitted when campus operational structure changes are made which impact the plan. Certification is continuous unless a Capital Planning, Design and Construction (CPDC) post-project performance review determines that problems were caused by campus negligence, in which case the CRB may recommend that the campus be placed on probation. The CRB may ultimately recommend that certification be withdrawn if identified operational/management deficiencies are not remedied.

For those campuses that are not certified, the chancellor's office may execute a Memorandum of Delegation for a capital outlay project, which delegates administration, including construction management, to the campus. The CPDC construction management unit may also perform construction administration and management.

EO 666, *Delegation of Professional Appointments Related to Capital Outlay Projects and Campus Physical Development*, dated March 7, 1997, delegates the authority to each campus president or designee to make all professional appointments relative to capital outlay projects and campus physical development. Further, the campus president or designee is responsible for ensuring compliance with all applicable statutes and regulations, BOT policies, and SUAM guidelines; and the use of systemwide standardized architectural, engineering, and other professional appointment contract forms.

The SUAM, in part, contains an overview of all CPDC policies and procedures associated with the capital outlay process. SUAM §9700 through §9843, *Construction Management for Public Works Contracts*, describe the requirements for preparing and administering public works contracts under the provisions of Public Contract Code §10700 *et seq.* SUAM §9200 through §9212, *Professional Services for Campus Development*, describe the requirements for developing and administering professional services agreements with service providers such as architects and engineers and for testing services and project-related studies.

The California State University (CSU) *Construction Management Procedures Manual* contains the CSU construction management policies and procedures that apply to a project, and each construction administrator, project manager, inspector of record, campus representative, and design professional is required to use this manual as appropriate during the construction administration of a project.

PURPOSE

The overall audit objective was to ascertain the effectiveness of construction management policies and procedures and internal controls and processes related to the administration of construction activities and, specifically, the Performing Arts Center project.

Within the overall audit objective, specific goals included determining whether:

- ▶ Delegated authority to manage capital outlay projects exists, and the campus capital outlay management plan is current for campus-managed projects.
- ▶ Project development is in accordance with statutory and CSU policy requirements, including required BOT and CPDC approvals.
- ▶ Administration and management of the project provide effective internal controls and processes consistent with the campus capital outlay management plan and the SUAM.
- ▶ Professional appointments are in accordance with statutory requirements, BOT policy, and the SUAM; and systemwide standardized professional appointment contract forms are used, approved by the Office of General Counsel, and fully executed prior to performance of work.
- ▶ Extra services are appropriate, authorized, and separately tracked; and an evaluation is performed for each professional service provided.
- ▶ The bidding process is rigidly controlled, performed in accordance with statutory requirements and the SUAM, and incorporates the contract documents maintained on the CPDC website.
- ▶ Contract documents are complete, routed to the Office of General Counsel as appropriate, and timely executed; required contract bonds and insurance are received; and a Notice to Proceed is issued.
- ▶ Subcontractors are adequately monitored, and requests for subcontractor substitutions are handled in accordance with statutory requirements and the SUAM.
- ▶ Operational and administrative controls ensure maintenance of financial accountability and completion of the project within the approved scope, schedule, and budget.
- ▶ Contract and service agreement payments are adequately supported, appropriately approved, and timely paid; and retention is handled in accordance with statutory requirements and the SUAM.
- ▶ Equipment is procured in the most economical method; purchased materials meet specifications required by construction documents and drawings; and all required inspections and tests are timely and properly performed and adequately documented.

- ▶ Change orders are appropriately approved, supported, accurately priced, and sufficiently tracked; and construction allowances and contingency balances are adequately administered and controlled.
- ▶ Project completion is adequately administered, including completion of pre-final/final inspections, punch list items, project closeout checklist, and Notice of Completion; preservation of project files, equipment manuals/warranties, and spare parts/materials; and resolution of any liquidated damages.

SCOPE AND METHODOLOGY

The scope of audit included, but was not limited to, the review of design budgets and costs; the bid and award process; invoice processing and payment; change orders; construction management, architectural, and engineering services; use of major equipment/materials; the closeout process; administration of liquidated damages; and overall project cost accounting and reporting. This included any transactions or activity performed by the campus, construction management firm, and trade subcontractors.

Our study and evaluation were conducted in accordance with the *International Standards for the Professional Practice of Internal Auditing* issued by the Institute of Internal Auditors, and included the audit tests we considered necessary in determining that operational and administrative controls are in place and operative. This review emphasized, but was not limited to, compliance with state and federal laws, BOT policies, and Office of the Chancellor and campus policies, letters, and directives.

We focused primarily on the operational and administrative controls in effect for the Performing Arts Center project with an emphasis on compliance with the CSU *Construction Management Procedures Manual*, SUAM policies and procedures associated with the capital outlay process, the campus capital outlay management plan, and construction contract general conditions. We evaluated the effectiveness of construction management policies and procedures and adequacy of internal controls and processes, and sought opportunities for improvement to further the success of CSU's capital outlay program.

Specifically, we reviewed and tested:

- ▶ Delegation of construction management authority.
- ▶ Review and approval of project design, budget, and funding.
- ▶ Professional services agreements and any extra services changes.
- ▶ Administration of the bid and award process.
- ▶ Contract execution and required contract bonds and insurance.
- ▶ Subcontractors and subcontractor substitutions.
- ▶ Contract and service agreement payment processing.
- ▶ Procurement of major equipment and materials.
- ▶ Performance of required inspections and tests.
- ▶ Review, approval, and tracking of change orders.
- ▶ Direct labor and associated burden.
- ▶ Construction management and overall project cost accounting and reporting.
- ▶ Construction allowances and contingency balances.
- ▶ Administration of the project closeout process and resolution of any liquidated damages.

OBSERVATIONS, RECOMMENDATIONS, AND MANAGEMENT RESPONSES

PRE-CONSTRUCTION AND BID PROCESS

Duties of project staff related to the expanded list of subcontractors were not clearly stated in the State University Administrative Manual and/or the Project Administration Reference Manual.

We found that the campus review of the expanded list of subcontractors did not identify a trade subcontractor with a contract value in excess of one-half of one percent of the Guaranteed Maximum Price (GMP) construction agreement. The total value of the trade subcontract was \$625,000.

Executive Order (EO) 672, *Delegation of Capital Outlay Management Authority and Responsibility*, dated July 25, 1997, states, in part, that the campus is responsible for ensuring appropriate internal controls and processes on the campus are in place to ensure that responsibilities are carried out in a manner consistent with the campus management plan submitted with the request for delegation. EO 672 further states that the campus shall maintain financial accountability for each project.

The *Contract General Conditions for Construction Manager at Risk with Guaranteed Maximum Price Projects* §4.04.b states that when requested by the construction administrator, the contractor shall submit a subcontractor status report, which will be compared with the expanded list of subcontractors. If any subcontractors are still outstanding at the time of submittal, a follow-up request will be made. Further, if any firms are substituted without approval of the Trustees in accordance with Section 4107(a) of the Public Contract Code, or if subcontractors are added and perform work in excess of one-half of one percent of base contract, penalties are applicable per Section 4110 of the Public Contract Code.

The associate vice president for facilities development and operations stated that the campus was unaware that the construction manager had contracted directly with the metal panel subcontractor, rather than including them as a sub-tier within the larger sheet metal subcontract. However, he stated that both subcontractors were clearly identified by the construction manager as project participants in the final GMP submittal, and that the construction manager's decision to contract this scope directly was made with the concurrence of the listed sheet metal subcontractor. Finally, he stated that the construction manager's decision benefited the campus and the California State University by lowering the overall contract value of the scope of the work in question.

Failure to develop, document, and communicate procedures compromises internal controls and increases the risk that violations of the GMP construction agreement will not be detected.

Recommendation 1

We recommend that the chancellor's office Capital Planning, Design and Construction department revise the State University Administrative Manual (SUAM) and/or the Project Administration Reference Manual to more clearly state the duties of the contractor and project staff to ensure the expanded list of subcontractors reflects the workers on site.

Management Response

We agree. We are modifying SUAM and the Contract General Conditions to effect compliance with the Subletting and Subcontracting Fair Practices Act. This will be a topic for our webinar training program early in 2012.

APPENDIX A: PERSONNEL CONTACTED

Name

Title

Office of the Chancellor

Benjamin F. Quillian

Elvyra San Juan

Executive Vice Chancellor and Chief Financial Officer

Assistant Vice Chancellor,

Capital Planning, Design and Construction

California State University, Northridge

Harold Hellenbrand

Jolene Koester

Colin Donahue

Howard Lutwak

Tom McCarron

Ken Rosenthal

Interim President

President (At time of review)

Associate Vice President for Facilities Development and Operations

Director, Internal Audit

Vice President, Administration and Finance and

Chief Financial Officer

Manager of Construction Services



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

www.calstate.edu

Benjamin F. Quillian
Executive Vice Chancellor and
Chief Financial Officer

562-951-4600
Fax 562-951-4971
bquillian@calstate.edu

MEMORANDUM

DATE: December 15, 2011

TO: Larry Mandel
University Auditor

FROM: Benjamin F. Quillian *B.F.*
Executive Vice Chancellor and Chief Financial Officer

SUBJECT: Audit Report Number 11-13
Performing Arts Center
California State University, Northridge

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DEC 15 2011

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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 Capital Planning, Design and Construction (CPDC) staff, and have attached our response to the auditors' findings and recommendation to CPDC.

BFQ:ESJ:bn

Attachment

c: Elvyra F. San Juan, Assistant Vice Chancellor
Larry Piper, Chief of Facilities Planning
Thomas Kennedy, Chief of Architecture and Engineering
James Sowerbrower, Chief of Construction Management

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

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THE CALIFORNIA STATE UNIVERSITY
OFFICE OF THE CHANCELLOR



BAKERSFIELD

CHANNEL ISLANDS

January 12, 2012

CHICO

MEMORANDUM

DOMINGUEZ HILLS

EAST BAY

TO: Mr. Larry Mandel
University Auditor

FRESNO

FULLERTON

FROM: Charles B. Reed
Chancellor

HUMBOLDT

SUBJECT: Draft Final Report 11-13 on the *Performing Arts Center*,
California State University, Northridge

LONG BEACH

LOS ANGELES

In response to your memorandum of January 12, 2012, I accept the response as submitted with the draft final report on the *Performing Arts Center*, California State University, Northridge.

MARITIME ACADEMY

MONTEREY BAY

CBR/amd

NORTHRIDGE

POMONA

SACRAMENTO

SAN BERNARDINO

SAN DIEGO

SAN FRANCISCO

SAN JOSÉ

SAN LUIS OBISPO

SAN MARCOS

SONOMA

STANISLAUS