CONSTRUCTION
CALIFORNIA STATE UNIVERSITY,
STANISLAUS

SCIENCE I RENOVATION AND SEISMIC RETROFIT

Audit Report 14-11
December 15, 2014

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ABBREVIATIONS

AVP    Associate Vice President
BOT    Board of Trustees
CA     Construction Administrator
CPDC   Capital Planning, Design and Construction
CRB    Certification Review Board
CSU    California State University
CSUS   California State University, Stanislaus
EO     Executive Order
ICSUAM Integrated California State University Administrative Manual
OAAS   Office of Audit and Advisory Services
SRSR   Science I Renovation and Seismic Retrofit
EXECUTIVE SUMMARY

At its January 2014 meeting, the Board of Trustees directed the Office of Audit and Advisory Services (OAAS) to review construction activity. Construction auditing had been performed by KPMG since fiscal year 1997/98 with coordination from the OAAS. In fiscal year 2008/09, OAAS staff began performing construction audits.

We visited the California State University, Stanislaus campus and the offices of the general contractor and selected subcontractors from July 28, 2014, through August 29, 2014, and audited the Science I Renovation and Seismic Retrofit (SRSR) project focusing on the construction management policies and procedures and internal controls and processes in effect at that time.

In our opinion, the fiscal, operational, and administrative controls in effect for the SRSR project were sufficient to meet the objectives stated in the “Purpose” section of this report.

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 conditions 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 [7]

The campus did not ensure that the general contractor included all required trade subcontractors on its final expanded list of subcontractors.

CHANGE ORDER ADMINISTRATION [8]

Administration of trade subcontractor labor rates and associated labor burden needed improvement. Specifically, there was no process to document and approve updated hourly labor rates.

PROJECT COMPLETION AND CLOSEOUT [9]

The campus did not obtain the signature of the inspector of record on the project closeout checklist and the certificate of completion.
INTRODUCTION

BACKGROUND

In January 2008, California State University, Stanislaus (CSUS) executed an agreement with the architectural firm of RSK Associates to develop a conceptual design and schematic plans for the Science I Renovation and Seismic Retrofit (SRSR) project. In May 2008, the chancellor’s office Capital Planning, Design and Construction (CPDC) department approved schematic plans for the SRSR project at a project cost of $18,164,000, with funding from the sale of lease revenue bonds.

In July 2011, the campus solicited project bids and selected Acme Construction Company, Inc., as the general contractor. The campus executed an agreement with Acme Construction Company, Inc., on December 31, 2011, at a cost of $10,141,000, and issued the Notice to Proceed on January 3, 2012, with a completion date of November 2, 2013. The campus filed the Notice of Completion on November 22, 2013.

The Science I Building reopened for classes on January 27, 2014, following its renovation and seismic retrofit. The SRSR project included a complete interior remodel that added eight new classrooms and an open computer lab. The building now houses the departments of mathematics, philosophy, and modern languages, as well as the School of Nursing. A number of energy-efficiency measures were also included, such as the installation of photovoltaic solar panels on the roof that provide enough energy to meet all building needs except for heating, ventilation, and air conditioning, and skylights and additional windows that provide more natural light, thereby reducing energy costs.

The CSUS campus managed the SRSR project, and it chose the Design-Bid-Build delivery method. In this method, the design and construction aspects are contracted for separately, and the project is usually awarded to the lowest bid by a qualified general contractor. The architect/engineer (A/E) develops a schematic design, works with other professionals to complete drawings and specifications, and coordinates the bid documents. The project is advertised and bids are requested for various general contractors, who in turn bid out subcomponents of the project to multiple subcontractors and compile a complete bid for submission. The A/E participates in bid review and selection. During the construction phase, the A/E reviews work progress and issues site instructions, change orders, and other documentation necessary to the construction process; and the general contractor manages the construction process and daily activity on the construction site and often provides work with its own forces. The university remains responsible for project inspection and testing, and for generally administering the project.

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
Board of Trustees (BOT); the campus manages capital projects via a process consistent with the provisions of the Integrated California State University Administrative Manual (ICSUAM); 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 that impact the plan. Certification is continuous unless a 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 ICSUAM guidelines; and the use of systemwide standardized architectural, engineering, and other professional appointment contract forms.

The ICSUAM, in part, contains an overview of all CPDC policies and procedures associated with the capital outlay process. ICSUAM §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. ICSUAM §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.
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 SRSR 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 ICSUAM.
- Professional appointments are in accordance with statutory requirements, BOT policy, and the ICSUAM; 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 ICSUAM, 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 ICSUAM.
- 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 ICSUAM.
- Group II equipment is properly managed and accounted for, purchased materials meet specifications required by construction documents and drawings, and all required inspections and tests are timely and properly performed and adequately documented.
INTRODUCTION

- 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 whether fiscal, 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 SRSR project with an emphasis on compliance with the CSU *Construction Management Procedures Manual*, ICSUAM 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 CAMPUS RESPONSES

PRE-CONSTRUCTION AND BID PROCESS

The campus did not ensure that the general contractor included all required trade subcontractors on its final expanded list of subcontractors.

We found that three trade subcontractors who were paid in excess of one-half of one percent of the base contract were not included on the final expanded list of subcontractors provided to the campus, as required by the Public Contract Code and the Contract General Conditions. The total value of the three trade subcontracts was $232,514.

Public Contract Code §4104 and §4110 state that the specifications prepared for the work or the general conditions under which bids will be received shall set forth that the prime contractor will provide the name and location of each subcontractor who will perform work or labor or render services to the prime contractor in an amount in excess of one-half of one percent of the prime contractor’s total bid. A prime contractor violating any of the provisions of this chapter (the Subletting and Subcontracting Fair Practices Act, Public Contract Code §4100 et seq.) violates his or her contract and the awarding authority may exercise options, including cancelling the contract or assessing the prime contractor a penalty in an amount of not more than ten percent of the amount of the subcontract involved.

The Contract General Conditions for Design-Bid-Build Projects §4.04.c 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 subcontracts are still outstanding at the time of submittal, a follow-up request will be made. If any listed firms have been substituted without approval by 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 (AVP) of capital planning and facilities management stated that an updated subcontractor list was requested twice during the project, but the lists did not accurately reflect the dollar amounts of the contracts between the general contractor and subcontractors.

The absence of a complete and accurate expanded list of subcontractors results in noncompliance with the Subletting and Subcontracting Fair Practices Act and increases the risk that violations of the act will not be detected.

Recommendation 1

We recommend that the campus:

a. Reiterate to staff and future general contractors that the expanded list of subcontractors must be complete and accurate.
b. Consider assessing a penalty of not more than $23,251 to the general contractor for violation of the Public Contract Code and Contract General Conditions.

**Campus Response**

The campus will provide training to staff and future general contractors that the expanded list of subcontractors must be complete and accurate. The campus has considered the recommendation to assess a penalty for the violation of the Public Contract Code and General Conditions. After further analysis and consultation, the campus feels the contractor acted in good faith, and the omission of the three trade subcontractors from the final expanded list was merely an oversight, not an intentional disregard for the requirements of the contract code. Therefore, the campus has chosen not to assess the penalty to the general contractor.

Expected date of completion: February 28, 2015

**CHANGE ORDER ADMINISTRATION**

Administration of trade subcontractor labor rates and associated labor burden needed improvement.

We reviewed hourly labor rates and the associated labor burden charged by two trade subcontractors for a sample of change orders, and we found that one trade subcontractor charged inflated labor rates on seven separate change order requests. After further review, we found that the project manager who reviewed the change orders accepted the higher labor rates due to an increased prevailing wage rate change. However, there was no process to document and approve updated hourly labor rates.

The *Contract General Conditions for Design-Bid-Build Projects* §6.01.b (1) states that the contractor shall submit a fully detailed breakdown of the cost of every labor classification to be utilized on a proposed change on the hourly labor rate worksheet. The unit cost of labor shall be an accurate accounting of actual costs being paid.

The AVP of capital planning and facilities management stated that the project manager on site did review the wage rates and did not feel they were excessive due to possible increased insurance premiums and wage increases (per a Construction Employers Association notification) since the time of bid.

Insufficient review of hourly labor rates and the associated labor burden charged to the project may result in increased project costs.

**Recommendation 2**

We recommend that the campus document and approve updated hourly labor rates.
Campus Response

The campus will document and approve updated hourly labor rates going forward on construction projects.

Expected date of completion: February 28, 2015

PROJECT COMPLETION AND CLOSEOUT

The campus did not obtain the signature of the inspector of record on the project closeout checklist and the certificate of completion.

Integrated California State University Administrative Manual §9830.03, Contract Completion and Acceptance of Construction, states that both the design professional and the project manager/construction inspector are required to submit a statement in writing to the construction administrator that the project complies with all plans, specifications, and change orders. The campus also is required to submit a written statement that the facility is in compliance with the contract documents and that it is free from apparent defects. When the project is judged 100 percent complete, the construction administrator so certifies and then instructs the contractor to submit a 100 percent completion payment request and the record drawings completed during the progress of the work, along with all remaining turnover items.

The California State University Project Administration Reference Manual §5.05 states that the construction administrator (CA) will prepare all appropriate documents at completion and execute the legal requirements. Both the project manager/construction inspector and the design professional shall state in writing to the CA that to the best of their knowledge the contractor has complied with the terms of the contract. The project closeout checklist must be completed by the project manager/construction inspector (as applicable) and submitted to the CA with the recommendation to accept the project and file a Notice of Completion.

The AVP of capital planning and facilities management stated that the inspector of record had left the project shortly before the project closeout checklist and certificate of completion were filled out, and therefore his signature was not obtained.

The absence of required signatures for the project closeout checklist and certification of completion increases the risk of misunderstandings and miscommunication regarding rights and responsibilities.

Recommendation 3

We recommend that the campus obtain the inspector of record signature for the project closeout checklist and certificate of completion.
Campus Response

The campus will provide training to the appropriate staff for project closeout and certificate of completion procedures.

Expected date of completion: February 28, 2015
### APPENDIX A:
### PERSONNEL CONTACTED

<table>
<thead>
<tr>
<th>Name</th>
<th>Title</th>
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<tbody>
<tr>
<td><strong>Office of the Chancellor</strong></td>
<td></td>
</tr>
<tr>
<td>Elvyra San Juan</td>
<td>Assistant Vice Chancellor, Capital Planning, Design and Construction</td>
</tr>
<tr>
<td><strong>California State University, Stanislaus</strong></td>
<td></td>
</tr>
<tr>
<td>Joseph F. Sheley</td>
<td>President</td>
</tr>
<tr>
<td>Julie Benevedes</td>
<td>Assistant Vice President of Financial Services and Executive-In-Charge of Business and Finance</td>
</tr>
<tr>
<td>Debra Da Rosa</td>
<td>Buyer III Lead</td>
</tr>
<tr>
<td>Briquel Hutton</td>
<td>Director of Audit Services</td>
</tr>
<tr>
<td>Russell Giambelluca</td>
<td>Vice President for Business and Finance (At time of review)</td>
</tr>
<tr>
<td>Regan Linderman</td>
<td>Controller</td>
</tr>
<tr>
<td>Melody Maffei</td>
<td>Associate Vice President of Capital Planning and Facilities Management</td>
</tr>
</tbody>
</table>
January 14, 2015

Larry Mandel, Vice Chancellor and Chief Audit Officer
The California State University
Office of Audit and Advisory Services
401 Golden Shore, 4th Floor
Long Beach, CA 90802-4210

RE: Science I Renovation and Seismic Retrofit Audit Report 14-11

Dear Mr. Mandel,

Enclosed please find the campus responses to the Science I Renovation and Seismic Retrofit Audit Report (14-11) for California State University, Stanislaus.

If you have any questions please do not hesitate to contact myself or Brieul Hutton, Director of Audit Services at (209) 664-6783.

Sincerely,

Julie Benevides
Interim Vice President, Business and Finance

JB/bh
Enclosures: 1

cc: Joseph F. Sheley, President
CONSTRUCTION
CALIFORNIA STATE UNIVERSITY,
STANISLAUS

SCIENCE I RENOVATION AND SEISMIC RETROFIT

Audit Report 14-11

PRE-CONSTRUCTION AND BID PROCESS

Recommendation 1

We recommend that the campus:

a. Reiterate to staff and future general contractors that the expanded list of subcontractors must be complete and accurate.

b. Consider assessing a penalty of not more than $23,251 to the general contractor for violation of the Public Contract Code and Contract General Conditions.

Campus Response

The campus will provide training to staff and future general contractors that the expanded list of subcontractors must be complete and accurate. The campus has considered the recommendation to assess a penalty for the violation of the Public Contract Code and General Conditions. After further analysis and consultation, the campus feels the contractor acted in good faith and the omission of the three trade subcontractors from the final expanded list was merely an oversight, not an intentional disregard for the requirements of the contract code. Therefore, the campus has chosen not to assess the penalty to the general contractor.

Expected Date of Completion: February 28, 2015

CHANGE ORDER ADMINISTRATION

Recommendation 2

We recommend that the campus document and approve updated hourly labor rates.

Campus Response

The campus will document and approve updated hourly labor rates going forward on construction projects.

Expected Date of Completion: February 28, 2015
PROJECT COMPLETION AND CLOSEOUT

Recommendation 3

We recommend that the campus obtain the inspector of record signature for the project closeout checklist and certificate of completion.

Campus Response

The campus will provide training to the appropriate staff for project closeout and certificate of completion procedures.

Expected Date of Completion: February 28, 2015
January 23, 2015

MEMORANDUM

TO: Mr. Larry Mandel
   Vice Chancellor and Chief Audit Officer

FROM: Timothy P. White
      Chancellor

SUBJECT: Draft Final Report 14-11 on the
         Science I Renovation and Seismic Retrofit,
         California State University, Stanislaus

In response to your memorandum of January 23, 2015, I accept the response
as submitted with the draft final report on the Science I Renovation and Seismic
Retrofit, California State University, Stanislaus.

TPW/amd