October 2, 2015

Dr. Elliot Hirshman, President  
San Diego State University  
5500 Campanile Drive  
San Diego, CA 92182

Dear Dr. Hirshman:

Subject: Audit Report 15-11, Storm/Nasatir Halls Renovation, San Diego State University

We have completed an audit of the Storm/Nasatir Halls Renovation construction project as part of our 2015 Audit Plan, and the final report is attached for your reference. The audit was conducted in accordance with the Institute of Internal Auditors' *International Standards for the Professional Practice of Internal Auditing*.

I have reviewed the management response and have concluded that it appropriately addresses our recommendation. The management response has been incorporated into the final audit report, which has been posted to the Office of Audit and Advisory Services’ website. We will follow-up on the implementation of corrective actions outlined in the response and determine whether additional action is required.

Any observations not included in this report were discussed with your staff at the informal exit conference and may be subject to follow-up.

I wish to express my appreciation for the cooperation extended by the campus personnel over the course of this review.

Sincerely,

Larry Mandel  
Vice Chancellor and Chief Audit Officer

c: Timothy P. White, Chancellor
CONSTRUCTION

San Diego State University

STORM/NASATIR HALLS RENOVATION

Audit Report 15-11
September 1, 2015
EXECUTIVE SUMMARY

OBJECTIVE

The objectives of the audit were to ascertain the effectiveness of construction management policies and procedures related to the fiscal, operational, and administrative controls over construction activities, determine the adequacy of internal controls and processes, identify cost recovery opportunities, and ensure compliance with relevant governmental regulations, Trustee policy, Office of the Chancellor directives, and campus procedures.

CONCLUSION

Based upon the results of the work performed within the scope of the audit, the fiscal, operational, and administrative controls in effect for the Storm/Nasatir Halls Renovation project were sufficient to meet the objectives of this audit. Our audit procedures did identify an opportunity to improve controls over the approval of extra service authorization (ESA) letters and change orders.

Specific observations, recommendations, and management responses are detailed in the remainder of this report.
1. EXTRA SERVICE AND CHANGE ORDER APPROVAL

**OBSERVATION**

ESA letters and change orders for the Storm/Nasatir Halls Renovation project were not always approved in accordance with the capital outlay management plan.

We reviewed 33 ESA letters and 14 change orders, and we found that:

- Four ESA letters totaling $661,849 were not signed by the appropriate personnel as specified in the campus outlay management plan.

- One change order totaling $1,041,081 was not approved by the vice president of business and financial affairs.

- One change order totaling $74,950 was not signed by the campus fiscal manager.

The absence of proper approval of ESA letters and change orders increases the risk of errors, misunderstandings, and miscommunication regarding rights and responsibilities and may result in unwarranted changes and excess charges.

**RECOMMENDATION**

We recommend that the campus reiterate to staff that ESA letters and change orders must be approved in accordance with the campus capital outlay management plan.

**MANAGEMENT RESPONSE**

The campus will notify staff, by October 31, 2015, that ESA letters and change orders must be approved in accordance with the campus capital outlay management plan.
SAN DIEGO STATE UNIVERSITY – STORM/NASATIR HALLS RENOVATION

GENERAL INFORMATION

BACKGROUND

In March 2008, the Board of Trustees (BOT) approved schematic plans for the Storm/Nasatir Halls Renovation project at a cost of $58,197,000, with state funding from the State Capital Outlay Budget and non-state funding from Continuing Education Reserve Funds and through Aztec Shops, a recognized campus auxiliary organization.

In November 2007, the campus executed an agreement with the architectural firm LPA, Inc. for services related and incidental to the design and construction of the Storm/Nasatir Halls Renovation project. It also executed an agreement with the construction manager (CM), C.W. Driver, Inc., for preconstruction services that included design and bid phase services. In June 2012, the campus executed a guaranteed maximum price (GMP) agreement with the CM for construction phase services at a construction cost of $54,374,244, and issued a Notice to Proceed on June 27, 2012, with a completion date of August 28, 2014. The State Fire Marshal granted a Certificate of Occupancy on January 3, 2014, and the campus filed a Notice of Completion on September 4, 2014.

The Storm/Nasatir Halls Renovation project consisted of renovations to the existing 137,700-square-foot Storm/Nasatir Building Complex and construction of new space to house two new lecture halls with 275 and 475 seats, faculty offices, and a small food service facility/convenience store. The renovations included new and upgraded classroom technologies and academic and research laboratories. The project addressed deficiencies in the existing buildings by providing new code-compliant heating, ventilation and air-conditioning systems, new lighting and ceiling systems, telephone and data system upgrades, security system upgrades, and electrical system corrections. Architecturally, the renovations provided new windows and an exterior finish to improve the building’s energy efficiency, as well as new elevators, ramps, site work, and door operators to assure wheelchair access.

The San Diego State University (SDSU) campus managed the Storm/Nasatir Halls Renovation project, and it chose the CM at Risk with 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 CM, and not with the university. Further, there is a potential for cost savings should the project be completed below the GMP.

Campus presidents have delegated 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 BOT policies; 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 aforementioned certification procedure 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 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.

Each campus president (or designee) also has delegated authority to make all professional appointments relative to capital outlay projects and campus physical development in accordance with applicable statutes, regulations, BOT policies, and ICSUAM provisions; and must ensure the use of systemwide standardized architectural, engineering, and other professional appointment contract forms. Further, each construction administrator, project manager, inspector of record, campus representative, and design professional is required to use the California State University (CSU) Construction Management Procedures Manual, which contains the CSU construction management policies and procedures that apply to a project.

SCOPE

We visited the SDSU campus and the offices of the CM and selected subcontractors from April 27, 2015, through May 29, 2015. Our audit and evaluation included the audit tests we considered necessary in determining whether fiscal, operational, and administrative controls for the Storm/Nasatir Halls Renovation project were in place and operative.

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, pricing, and tracking of change orders.
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.

Our testing and methodology was designed to provide a review of key operational and administrative controls, which included detailed testing on a limited number of CM and selected subcontractor transactions. Our review did not examine all aspects of financial controls or encompass all financial transactions for every contractor and subcontractor.

CRITERIA

Our audit was based upon standards as set forth in CSU Board of Trustee policies; Office of the Chancellor policies, letters, and directives; campus procedures; and other sound administrative practices. This audit was conducted in conformance with the Institute of Internal Auditors’ *International Standards for the Professional Practice of Internal Auditing*.

This review emphasized, but was not limited to, compliance with:

- Executive Order (EO) 672, *Delegation of Capital Outlay Management Authority and Responsibility*
- EO 666, *Delegation of Professional Appointments Related to Capital Outlay Projects and Campus Physical Development*
- ICSUAM §9000 through §9005, *Capital Outlay and Public Works Contracts*
- ICSUAM §9200 through §9212, *Professional Services for Campus Development*
- ICSUAM §9700 through §9843, *Construction Management for Public Works Contracts*
- CSU *Construction Management Procedures Manual*
- CSU *Administration of University Property - Equipment Procedures*
- *Contract General Conditions for CM at Risk with Guaranteed Maximum Price Projects*
- Public Contract Code Chapter 2.5, *CSU Contract Law*
- Public Contract Code §4100 et seq., *Subletting and Subcontracting Fair Practices Act*
- Government Code §13402 and §13403

AUDIT TEAM

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Senior Auditor: Jamarr Johnson