

Audit and Advisory Services
401 Golden Shore
Long Beach, CA 90802-4210

December 8, 2020

Dr. Jeffrey D. Armstrong, President
California Polytechnic State University, San Luis Obispo
1 Grand Avenue
San Luis Obispo, CA 93407

Dear Dr. Armstrong:

**Subject: Audit Report 20-62, Student Housing South,
California Polytechnic State University, San Luis Obispo**

We have completed an audit of the *Student Housing South* construction project as part of our 2020-2021 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 recommendations. The management response has been incorporated into the final audit report, which has been posted to 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,



Vlad Marinescu
Vice Chancellor and Chief Audit Officer

c: Timothy P. White, Chancellor
Adam Day, Chair, Committee on Audit
Jane W. Carney, Vice Chair, Committee on Audit

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CONSTRUCTION

**California Polytechnic State University,
San Luis Obispo**

Student Housing South

Audit Report 20-62
October 16, 2020

EXECUTIVE SUMMARY

OBJECTIVE

The objectives of the audit were to ascertain the effectiveness of operational, administrative, and financial controls related to construction activities; identify cost recovery opportunities; and ensure compliance with relevant governmental regulations, Trustee policy, Office of the Chancellor (CO) directives, construction contract general conditions, and campus procedures.

CONCLUSION

Based upon the results of the work performed within the scope of the audit, except for the weaknesses described below, the operational, administrative, and financial controls for the Student Housing South project as of September 4, 2020, taken as a whole, provided reasonable assurance that risks were being managed and objectives were met.

However, the review did identify opportunities for improvement in the campus permitting process, review and approval of change orders, maintenance of conflict-of-interest statements, and the project closeout process.

Specific observations, recommendations, and management responses are detailed in the remainder of this report.

OBSERVATIONS, RECOMMENDATIONS, AND RESPONSES

1. CAMPUS BUILDING PERMITS

OBSERVATION

The campus could not provide evidence that the campus deputy building official issued a campus building permit for the structural foundation and structural vertical phases of the Student Housing South project, as required by the California Building Code. Campus management indicated that they believe the permit was issued, but it could not be located during the audit.

We did note that all appropriate plan check approvals, such as approvals from the State Fire Marshall (SFM) and the Division of the State Architect, were obtained prior to the start of construction for these phases.

Obtaining appropriate building permits before beginning work on a project reduces the risk of noncompliance with state regulations and reduces the probability of rework and increased project costs.

RECOMMENDATION

We recommend that the campus remind appropriate personnel that a building permit issued by the campus deputy building official is required prior to the start of construction and should be maintained for future projects.

MANAGEMENT RESPONSE

We concur and will remind appropriate personnel that a building permit issued by the campus deputy building official is required prior to the start of construction. We will incorporate a process to ensure that this occurs. We will also determine the appropriate person(s) responsible for maintaining the building permits for future projects.

Anticipated implementation date: April 16, 2021

2. CONFLICT OF INTEREST

OBSERVATION

The campus did not retain conflict-of-interest and confidentiality statements for committee members involved in the selection process of the general contractor for the Student Housing South project, as required by Integrated California State University Administrative Manual (ICSUAM) §5402.00, *Formal Solicitation for Services*.

Maintaining conflict-of-interest and confidentiality statements for selection committee members reduces the risk of noncompliance with the formal solicitation process and the potential for perceived or actual conflicts of interest.

RECOMMENDATION

We recommend that the campus implement a process to retain conflict-of-interest and confidentiality statements for selection committee members for future projects.

MANAGEMENT RESPONSE

We concur and will implement a process to retain conflict-of-interest and confidentiality statements for selection committee members for future projects.

Anticipated implementation date: April 16, 2021

3. CHANGE ORDER APPROVAL

OBSERVATION

Change orders for the Student Housing South project were not always approved in accordance with the capital outlay management plan.

We reviewed 20 prime contract change orders and found that two change orders valued at greater than \$200,000 each were not approved by the vice president for administration and finance.

Proper approval of change orders decreases the risk of unwarranted changes and excess charges.

RECOMMENDATION

We recommend that the campus remind appropriate staff that change orders must be approved in accordance with the capital outlay management plan.

MANAGEMENT RESPONSE

We concur and will remind appropriate staff that change orders must be approved in accordance with the capital outlay management plan. We will document any changes to personnel or approved deviations/exceptions that affect the capital outlay management plan.

Anticipated implementation date: April 16, 2021

4. PROJECT CLOSEOUT

OBSERVATION

Project closeout administration needed improvement.

We reviewed campus closeout documentation and found that:

- The campus did not complete the project closeout checklist for the Student Housing South project, as required by the California State University Project Administration Reference Manual. This checklist is a tool that ensures that essential tasks are completed prior to the major project closeout phases of occupancy, filing of the notice of completion, and the release of retention funds. For example, this includes completing all necessary inspections, performing final cleaning activities, receiving necessary warranties and manuals, and resolving all claims on the project.
- The campus could not provide evidence that it obtained State Fire Marshal approval before issuing a limited temporary occupancy certificate for resident advisors and student development coordinators. The SFM approval occurred one week after the occupancy certificate was issued.
- The campus deputy building official did not sign the certification of completion, which verifies and acknowledges that the construction project is complete and a notification of completion can be filed with the county. However, the certification of completion was signed by the architect, project manager, and inspector.

Completion of the final project closing procedures helps to ensure that all required items have been completed prior to occupancy, notice of completion, and release of retention, and that there are no outstanding or unfinished items at the end of the project.

RECOMMENDATION

We recommend that the campus review the project closeout checklist and verify that all required items were completed for the Student Housing South project, and remind staff of appropriate final project closing procedures as discussed above for future projects.

MANAGEMENT RESPONSE

We concur and will review the project closeout checklist and verify that all required items were completed for the Student Housing South project, and we will remind staff of appropriate final project closing procedures as discussed above for future projects.

We will document and retain any approved deviations/exceptions from the project closeout checklist.

Anticipated implementation date: April 16, 2021

5. BIDDING AND CONTRACTING PROCESS

OBSERVATION

The campus did not obtain Disabled Veteran Business Enterprise (DVBE) participation documentation from the general contractor showing evidence that the participation goal was met or a good-faith effort was made to reach the goal.

Specifically, we were unable to obtain evidence that three of the seven subcontractors that the general contractor claimed for DVBE participation were appropriately certified.

Obtaining DVBE participation documentation from the general contractor decreases the risk of noncompliance with DVBE requirements.

RECOMMENDATION

We recommend that the campus communicate to staff that DVBE participation documentation provided by the general contractor should include evidence that each subcontractor claimed as a DVBE was certified and appropriate to apply toward the DVBE participation goal.

MANAGEMENT RESPONSE

We concur and will communicate to appropriate staff that DVBE participation documentation provided by the general contractor should include evidence that each subcontractor claimed as a DVBE was certified and appropriate to apply toward the DVBE participation goal. We will incorporate a process to ensure that this occurs for future projects.

Anticipated implementation date: April 16, 2021

6. CERTIFIED PAYROLL RECORDS

OBSERVATION

The campus did not maintain certified payroll records for the general contractor and each trade subcontractor, which prevented the verification of wage rates submitted for change order work.

State University Administrative Manual (SUAM) §9824.01 states that the campus shall request a minimum of the first week’s certified payroll records from the general contractor and a minimum of the first week’s certified payroll records from each subcontractor of any tier.

Requesting and maintaining certified payroll records allows for the verification of wage rates submitted for change order work, to ensure that labor costs charged to the campus are appropriate.

RECOMMENDATION

We recommend that the campus remind staff that certified payroll records for the general contractor and each subcontractor are required to be requested and maintained, and that these records should be used to verify wage rates submitted for change order work.

MANAGEMENT RESPONSE

We concur and will remind staff that certified payroll records for the general contractor and each subcontractor are required to be requested and maintained per State University

Administrative Manual (SUAM) §9824.01, and that these records should be used to verify wage rates submitted for change order work. We will also determine the appropriate person(s) responsible for maintaining the building permits and incorporate a process to ensure that this occurs for future projects.

Anticipated implementation date: April 16, 2021

GENERAL INFORMATION

BACKGROUND

In November 2014, the Board of Trustees (BOT) approved schematic plans for the Student Housing South project at a cost of \$198,863,000, with funding from systemwide revenue bonds and a housing program reserve contribution of \$10,000,000. The bonds will be repaid from housing revenue.

In June 2014, the campus solicited project bids and selected Webcor Construction, LP as the design-builder. The campus executed a design and construction agreement with Webcor Construction, LP on January 13, 2015, at a cost of \$165,000,000 and issued the Notice to Proceed for the design phase on January 14, 2015. The final project cost, after all change orders had been processed, was \$172,750,000. The campus filed the Notice of Completion on January 7, 2020.

The Student Housing South project is a new residential community for first-year students located at the Grand Avenue entrance to campus and across the street from the existing freshman residence halls. The project consists of seven residence hall buildings that are three to five stories tall. They contain a total of 1,475 beds and include large open spaces for outdoor activities and community/retail spaces for a small café, community room, game room, mail room, welcome center, and office/workspaces. Each floor of the residence hall buildings accommodates 50 beds, with 21 double rooms, two quad rooms, a community kitchen, laundry facilities, and a shared study space. In addition, the residence halls can accommodate 29 residence advisors and two coordinators of student development. The adjacent parking garage is a separate four-story concrete structure and houses equipment to heat the Student Housing South facilities. Sustainable site measures include a pedestrian-oriented design that features a walking pathway to the campus, green space, and a site designed to maximize the low-impact development concept of stormwater retention. Sustainable building features include water-saving fixtures, high-efficiency windows, a central heating plant with co-generation, and solar panels. The project was designed to achieve a Leadership in Energy and Environmental Design (LEED) gold certification. LEED is a third-party certification program begun in 1999 by the United States Green Building Council and is a nationally accepted benchmark for the sustainable “green” design, construction, and operation of buildings.

The California Polytechnic State University, San Luis Obispo campus managed the Student Housing South project, and it chose the Design-Build delivery method. In this method, the design and construction aspects are contracted with a single design-builder (general contractor) who has full responsibility for finalizing and implementing a design that meets or exceeds California State University (CSU) performance expectations. The design-build entity is responsible for the adequacy of design and any construction defects, which allows the CSU to avoid these types of claims and limits errors and omissions change orders. Further, the design-build approach shortens project completion by overlapping the design and construction project phases. This approach also minimizes the university’s need to schedule and coordinate the overall project, although clear specifications of CSU performance requirements and high-quality inspection of work in progress are required to fully realize the benefits of this approach.

Campus presidents have been delegated the authority to directly manage 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 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 campus capital outlay management plan 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.

Each campus president (or designee) also has been 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 CSU Construction Management Project Administration Reference Manual, which contains the CSU construction management policies and procedures that apply to a project.

SCOPE

Our audit and evaluation included the audit tests we considered necessary in determining whether operational, administrative, and financial controls for the Student Housing South project are in place and operative. The audit focused on procedures in effect during the planning and construction of the project.

Specifically, we reviewed and tested:

- Delegation of construction management authority.
- Review and approval of project design, budget, and funding.
- Administration of the bid and award process.
- Contract execution and required contract bonds and insurance.
- Construction management and accounting, including invoicing and payment applications.

- Review, approval, pricing, and tracking of change orders.
- Subcontractor administration.
- Closeout processes, including completion of required inspections and certifications.

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, which was designed to provide a review of key operational, administrative, and financial controls, included interviews, walkthroughs, and detailed testing on a limited number of design-builder and 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 federal and state regulations and guidance; Trustee policy; Office of the Chancellor directives; and campus (and auxiliary, if applicable) procedures; as well as sound administrative practices and consideration of the potential impact of significant risks. 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:

- 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
- Executive Order (EO) 666, *Delegation of Professional Appointments Related to Capital Outlay Projects and Campus Physical Development*
- EO 672, *Delegation of Capital Outlay Management Authority and Responsibility*
- ICSUAM §9000 through §9005, *Capital Outlay and Public Works Contracts*
- ICSUAM §9200 through §9212, *Professional Services for Campus Development*
- ICSUAM §9230 through §9237, *Project Plan Development for Major Capital Construction Projects*
- ICSUAM §9700 through §9843, *Construction Management for Public Works Contracts*
- CSU *Construction Management Project Administration Reference Manual*
- *Contract General Conditions for Design-Build Projects*

AUDIT TEAM

Director: Wendee Shinsato
 Senior Auditor: Jamarr Johnson