

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

January 3, 2023

Dr. Lynn Mahoney, President
San Francisco State University
1600 Holloway Avenue
San Francisco, CA 94132

Dear Dr. Mahoney:

**Subject: Audit Report 22-51, Construction – Creative Arts Replacement Building,
San Francisco State University**

We have completed an audit of the *Creative Arts Replacement Building* construction project as part of our 2022-2023 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 will be 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: Jolene Koester, Interim Chancellor
Lateefah Simon, Chair, Committee on Audit
Yammilette Rodriguez, Vice Chair, Committee on Audit

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CONSTRUCTION

San Francisco State University

Creative Arts Replacement Building

Audit Report 22-51
January 3, 2023

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 Creative Arts Replacement Building as of September 9, 2022, taken as a whole, provided reasonable assurance that risks were being managed and objectives were met.

Our review found that improvements were needed in the final accounting of project costs and the process used to track project allowances.

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

OBSERVATIONS, RECOMMENDATIONS, AND RESPONSES

1. FINAL ACCOUNTING OF PROJECT COSTS

OBSERVATION

The general contractor did not submit a final accounting of project costs for the Creative Arts Replacement Building project in a timely manner.

Specifically, we found that the general contractor did not provide sufficient documentation demonstrating that the total cost of the project equaled or exceeded the final guaranteed maximum price (GMP) of the two related construction agreements. The documentation should include, but not be limited to, all actual subcontractor costs, direct material and labor provided by the general contractor, and a reconciliation of contractual fees paid by the campus.

Submittal of a final accounting of actual project costs by the general contractor decreases the risk that the campus' payments will exceed actual construction costs (up to the GMP) and that any errors and irregularities will not be detected.

RECOMMENDATION

We recommend that the campus require the general contractor to submit a final accounting of project costs for the Creative Arts Replacement Building project that encompasses both GMP construction agreements, and perform a verification of the costs. If the total actual cost is less than construction agreements, the campus should notify Capital Planning, Design and Construction at the chancellor's office and request that the difference be returned to the campus.

MANAGEMENT RESPONSE

We concur. The general contractor did not submit a final accounting of project costs for the Creative Arts Replacement Building project in a timely manner that encompasses both GMP Construction agreements or perform a verification of the costs. The campus will request the final accounting of project costs for the Creative Arts Replacement Building project. If the actual cost is less than construction agreements, the campus will notify Capital Planning, Design and Construction at the chancellor's office and request that the difference be returned to the campus.

This will be completed by May 30, 2023.

2. ALLOWANCES

OBSERVATION

Administration of allowances for the Creative Arts Replacement Building project needed improvement.

We found that the general requirements identified in the two project GMPs as an allowance were not separately tracked for usage during construction of the project.

In addition, we noted that the campus and the general contractor negotiated a global settlement in change order six, in which each party agreed that \$85,747 in allowance costs would be converted to the contractor's project contingency for use on the project. We found that these allowance costs were not transferred to and accounted for on the project contingency log and were not credited back to the campus as unused allowances at the end of the project. The general contractor stated that although they made an error in not transferring the costs to the project contingency log, the costs would have been claimed as offset against contractor write-down negotiated in the global settlement, and therefore, there was no fiscal impact to the project.

Proper tracking and approval of project allowances decreases the risk that errors and irregularities will not be detected.

RECOMMENDATION

We recommend that the campus:

- a. Provide refresher training to relevant personnel regarding the administration of allowance costs, such as tracking and monitoring the usage of all allowances, including general requirements allowances, through an allowance log or other mechanism that allows for easy identification and review of allowance drawdowns, as well as appropriate authorization, use, and documentation.
- b. Review the \$85,747 in allowance costs noted above to determine whether the campus should pursue recovery of any part of these costs, document this determination, and, if applicable, document the resulting recovery.

MANAGEMENT RESPONSE

We concur. The campus will:

- a. Provide refresher training for relevant personnel regarding the administration of allowance costs, such as tracking and monitoring the usage of all allowances, including general requirements allowances, through an allowance log or other mechanism that allows for easy identification and review of allowance drawdowns, as well as appropriate authorization, use, and documentation.
- b. Review the \$85,747 in allowance costs noted above to determine whether the campus should pursue recovery of any part of these costs, document this determination, and, if applicable, document the resulting recovery.

This will be completed by May 30, 2023.

GENERAL INFORMATION

BACKGROUND

In May 2017, the Board of Trustees (BOT) approved schematic plans for the Creative Arts Replacement Building project at a cost of \$81,144,000, with funding from campus designated capital reserves and systemwide revenue bonds.

In November 2016, the campus executed an agreement with the architectural firm Mark Cavagnero Associates for services related and incidental to the design and construction of the Creative Arts Replacement Building project. It also executed an agreement with the construction manager (CM), McCarthy Building Companies, Inc., for preconstruction services that included design and bid phase services. In July and August 2018, respectively, the campus executed two GMP agreements for separate phases of the project with the CM for construction phase services at a total construction cost of \$58,981,907. Additionally, the campus issued two separate Notices to Proceed on July 19, 2018, and August 14, 2018, which correspond to each of the two executed construction agreements. The campus filed a Notice of Completion on April 30, 2021. The total project costs were \$72,397,496 at the time of completion.

The Creative Arts Replacement Building is the first of four buildings planned to replace the prior Creative Arts Building. The four-story, 76,000-square-foot building houses the entire Broadcast and Electronic Communication Arts (BECA) program, interdisciplinary lecture and active learning classrooms, and administrative offices for the College of Liberal and Creative Arts. The facility was designed for innovative communication, collaboration, and engagement. The BECA portion of the building is a flexible learning and production environment for teaching electronic media capture, editing, and broadcast. The ground floor includes the television studios and adjacent instructional control rooms. The newsroom is located at the southeast corner of the building, leveraging the high traffic and high visibility of the Holloway Avenue and Font Boulevard corner of the campus. The audio recording live room and related spaces are located on the ground floor, where it is most economical to achieve a high level of acoustical isolation. Video editing, audio production spaces, and interdisciplinary lecture classrooms occupy the second level, and the third level houses BECA audio demonstration and video editing classrooms and faculty offices. The project was designed to achieve a Leadership in Energy and Environmental Design (LEED) platinum 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 San Francisco State University (SFSU) campus managed the Creative Arts Replacement Building 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.

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 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 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

We performed fieldwork from July 25, 2022, through September 9, 2022. Our audit and evaluation included the audit tests we considered necessary in determining whether operational, administrative, and financial controls for the Creative Arts Replacement Building 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.
- Professional services agreements and any extra services changes.
- Administration of the bid and award process.
- Contract execution and required contract bonds and insurance.

- Plan reviews and permitting in accordance with CSU requirements.
- Construction management and accounting, including allowance and contingency tracking and invoicing and payment applications.
- Review, approval, pricing, and tracking of change orders.
- Subcontractor administration.
- Close-out 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 construction manager 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 CM at Risk with Guaranteed Maximum Price Projects*

AUDIT TEAM

Assistant Vice Chancellor: Wendee Shinsato
Senior Auditor: Jamarr Johnson