

DRAFT 7.13.21

School Board of Manatee County
Construction Audit Report
June 25, 2021





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June 25, 2021

Audit Committee and School Board of
Manatee County
215 Manatee Ave. W.
Bradenton, FL 34205

Re: Construction Audit Report

Pursuant to the approved 2020/2021 internal audit plan, we hereby submit the Construction Audit Report. We will be presenting this report to the Audit Committee at the next scheduled meeting on July 7, 2021.

Our report is organized in the following sections:

Executive Summary	This provides a summary of the observations and testing results related to our Construction Audit.
Background	This provides an overview of the Construction Services Department.
Objectives, Scope, and Methodology	The audit objectives and focus are expanded upon in this section as well as period of review and areas evaluated in our review.
Testing	This section documents the testing performed and results of the areas reviewed during the audit.

We would like to thank all those involved in assisting the Internal Auditors in connection with the Construction Audit.

Respectfully Submitted,

Carr, Riggs & Ingram, LLC
Internal Auditors

The Construction Audit was included in the 2020/2021 Internal Audit Plan. Construction received a Medium Score during the five year Internal Audit Risk Assessment conducted in 2020. We interviewed personnel, conducted walkthroughs, obtained documents and reports, and performed testing to determine whether the Department of Construction Services functions are operating effectively, efficiently and with appropriate internal controls and in compliance with applicable laws, rules, and regulations.

Over the last six (6) months the Department of Construction Services has undergone and will continue to experience a number of key changes. These include personnel changes, transition of project procurement, use of new contracts, and implementation of a tool to track project progress. Therefore, we evaluated risk as it pertains to areas outside of the changes occurring within the Department of Construction Services and developed a program that addressed the following functions:

- Policies and Procedures
- Pay Applications
- Unforeseen Conditions
- Change Orders
- Closeout
- Key Performance Indicators

Overall the specific operating controls evaluated during this audit (noted above) as it relates to the Construction Services Department is rated as **Satisfactory**. We did identify areas that should be addressed to enhance the control environment around the Department of Construction Services. The specific test steps, exceptions, recommendations, and Management Responses can be found at Appendix A. The following is a summary of the areas that should be addressed:

- Policies and Procedures for the Construction Services Department are captured in the Department of Construction Services Procedure Manual. The Procedure Manual is robust and contains a number of key processes, which include both general information and guidance for construction processes. We were able to rely on a number of these procedures throughout our review. However, during the course of our Audit there were procedures communicated by Management that were in process of being updated and not yet fully implemented. There were also procedures identified through review that could be enhanced to reflect current processes and provide additional guidance to employees (see page 5). *Moderate*
- All Budget Transfers reviewed were properly approved by applicable parties. For closed projects, unspent balances were transferred to the Unforeseen Conditions Fund and returned to the District. However, there were some noted exceptions that resulted in the recommendation to create a cumulative log to track Unforeseen Conditions and also provide additional guidance and documentation for those situations that qualify for the use of Unforeseen Conditions (see page 8). *Moderate*
- Pay Applications were properly approved by the Department Director, Project Director, Construction Manager and when applicable Architect/Engineer, and were also paid in a timely manner from date of receipt. The Contract Management Verification form was signed off by the Department Director. The District's Pay Application Cover Sheet and Continuation Sheet were used for each Pay Application and figures were properly calculated and correctly reflect contract, amendments, and change order amounts. We did note an exception in regards to four (4) Pay Applications in which Auto Allowance was billed as a lump sum (see page 6). *Low*

- All Pay Applications reviewed during our testing contained an itemized breakdown of hours worked for each of the employees that were included in the billing. There were some pay applications that also contained system payroll records to support the itemized hours. As a best practice, additional documentation, such as system payroll records, should be obtained for all Pay Applications to support labor costs submitted in Pay Applications. It should be noted that the updated CM Contract contains additional language in regards to labor costs which includes the District's right to audit the CMs Payroll (see page 7). *Best Practice*
- Through discussion with Management, as a best practice, the Construction Services Department would benefit from implementing a checklist for Pay Application Reviews. This would memorialize the review performed based on the Construction Manager Contract Pay Procedure. Any additional enhancements to the Procedures should be captured on the checklist. The checklist should provide for the ability to document the employee that performed the various steps and ability to add notes and references. The checklist should also capture and document any discrepancies in the Pay Application and how the discrepancies were resolved (see page 7). *Best Practice*
- As Management has already identified the need of Key Performance Indicators (KPIs), a best practice recommendation will be for Management to continue the pursuit of developing KPIs. KPIs would allow for reporting to the Board on key construction measurements (cost of projects, volume of activity performed) and could help identify the need for additional staff based on volume and project sizes (see page 11). *Best Practice*

Critical	Such an issue would be expected to receive immediate attention from Management, but must not exceed 30 days to remedy from the final Audit Report date.
High	Such an issue would be expected to receive urgent corrective action by Management, and must be completed within 60 days of final Audit Report date.
Moderate	Such an issue would be expected to receive corrective action from Management, and must be completed within 90 days of final Audit Report date.
Low	Such an issue does not warrant immediate attention but requires corrective action by Management, and must be completed within 120 days of final Audit Report date.

APPENDIX A

BACKGROUND

The Department of Construction Services is located at the Matzke Support Center and consists of a total of 12 employees, including the Director. The Director was recently hired in May of 2021 after the former Director departed in February of 2021. The Director of the Construction Services Department reports directly to the Deputy Superintendent of Operations. The Department of Construction Services employees are responsible for building new facilities, renovating existing facilities, insuring compliance with concurrency, site acquisition and disposal, and maintaining the building drawings and As-Built documentation.

The Department has also undergone changes in processes that will have an impact on new projects. Selection of Construction Managers for projects is now driven by the Procurement Department with involvement of the Department of Construction Services. Selection of Architecture/Engineers and Construction Managers for smaller projects will be made by the Construction Services Department based on Board approval of the continuing contract list. Larger projects will go through a construction RFQ conducted by the Procurement Department. The Construction Manager (CM) Agreement and Architect/Engineer Agreement were updated and will be used on upcoming projects. Additionally, the Department is moving to Smartsheet to keep the District apprised of work being done on projects.

OBJECTIVE

The main purpose of the review was to determine whether certain functions of the Construction Department are operating effectively, efficiently and with appropriate internal controls and in compliance with applicable laws, rules, and regulations.

Due to the transition of the procurement function out of the Department of Construction Services, we did not include the procurement process as part of our review. The Procurement Department now encompasses conducting construction RFQs for the selection of firms. Procurement of construction will be reviewed during the Procurement Audit by the In-House Board Internal Auditor during 2021-2022.

SCOPE

Our audit scope included review of the Construction Services Department activities from July 1, 2020 through May 30, 2021.

METHODOLOGY

We evaluated the Construction Services Department to determine the risk with associated functions. We interviewed management, reviewed available policies and procedures, and previously issued reports and the Districtwide Risk Assessment to develop the audit program. During our review we tested the following areas within the Construction Services Department:

- Policies and Procedures
- Pay Applications
- Unforeseen Conditions
- Change Orders
- Closeout
- Key Performance Indicators

TESTING

Policies and Procedures

Policies and Procedures for the Construction Services Department are captured in the Department of Construction Services Procedure Manual. The Procedure Manual is robust and contains a number of key processes, which include both general information (organizational chart, job descriptions, and office procedures) and those directly for construction processes, such as plans room procedures, project procedures, planning, and project forms.

Management did communicate at the start of the Audit that there are sections of the Procedure Manual that are currently a work in progress. There were some procedures that were updated or in the process of being finalized that have not yet been fully implemented. The Department also recently moved from a network folder that contained all department documents, including the Procedure Manual, to a SharePoint site. This transition resulted in some issues with the Procedure Manual in regards to links and forms. Through our testing we did identify some opportunities to update certain procedures to enhance controls and provide additional guidance to the Department of Construction Services employees.

Department of Construction Services Procedure Manual (DCS-1) Moderate

Condition: During the course of our Audit there were a few procedures communicated by Management that were not yet fully implemented. There were also procedures identified through review that could be enhanced to reflect current processes and provide additional guidance to employees. Below are examples of these procedures:

- Construction Manager Contract Negotiations Procedure- The procedure was updated but not yet implemented. The procedure provides key guidance in the negotiation of General Conditions with the Construction Manager. During the AG Post Audit Review (PAR) the process outlined in this procedure was in place to complete the General Negotiations Worksheet and Labor Burden Worksheet. Based on recommendations from the AG PAR, Management was in the process of updating the procedures at the time the former Department Director resigned and the process has not yet been updated and finalized.
- Construction Manager Contract Pay Procedure – The procedure is used to review Pay Applications of Construction Managers for accuracy and timeliness of Payment. The procedure is adequate but could be enhanced by incorporating the process of the site walkthroughs by the Project Director and subsequent review of the Pay Application with the Construction Manager. The Pay Application process could also be enhanced through the implementation of a Pay Application checklist.
- Budget Transfers Procedure – The procedure is used to provide guidance for reallocating funds within a Construction Manager's Guaranteed Maximum Price Budget. The Unforeseen Conditions section could be enhanced to provide parameters on the use of Unforeseen Conditions.

Impact: Guidance on key processes might not be available or properly reflect current practices which could lead employees to miss key documents or executing steps.

Criteria: Procedures documented provide guidance to perform various key controls to ensure key information is obtained and reviewed.

Policies and Procedures (Continued)

Cause: Procedures were not yet fully implemented or do not fully reflect current practices.

Recommendation: Management should evaluate the processes documented in the Procedure Manual and implement any procedures that have been or are in the process of being finalized. Management should also consider enhancing procedures based on recommendations in this audit. Due to the turnover in the Department and changes in processes, such as procurement and implementation of Smartsheet, updated procedures would serve as valuable reference materials for new employees as well as ongoing guidance for existing employees.

Management Response: *The Director of Construction Services and the Chief Operations Officer are committed to bringing the Department of Construction Services Procedures Manual up to date to reflect the current Construction Management Agreement, the current Architect/Engineer Agreement, and any newly established procedures to insure appropriate project controls. Areas to be assessed include, but are not limited to, the protocols for the use of Share Point to archive critical project documents, appropriately revising the General Negotiations and Labor Burden Worksheets to reflect the most recent Construction Manager Agreement, Pay Application review procedures that enhance the accuracy in the assessment of field conditions and use of resources, and the establishment of enhanced internal controls through Smartsheet applications.*

Pay Applications

Pay Applications for payments to Construction Managers are presented and approved monthly. The Pay Applications contain the current state of the project at the time the project is billed. The Construction Manager Contract Pay Procedure documents the Pay Application review process. As noted in the Policies and Procedures section, the Procedure should be enhanced to capture the entire Pay Application Review process which includes the site walkthrough performed by the Project Director.

There were 12 projects that had substantial completion or were in-process with significant work completed for a total budget of \$39,086,565 during the 2020/2021 school year. We selected seven (7) of these projects for review for a total of \$34,453,110. We selected 1 project that had substantial completion in May 2020 since we wanted to include representation of all Project Directors in our sample. From the seven (7) projects, we selected 15 total pay applications. We obtained the Pay Applications as well as other supporting documentation, such as contracts, amendments, and change orders.

Pay Applications were properly approved by the Department Director, Project Director, Construction Manager and when applicable Architect/Engineer, and were also paid in a timely manner from date of receipt. The Contract Management Verification form was signed off by the Department Director. The District's Pay Application Cover Sheet and Continuation Sheet were used for each Pay Application and figures were properly calculated and correctly reflected contract, amendment, and change order amounts. In reviewing supporting documentation in the Pay Application, we noted the following exceptions and suggestions for best practices:

Pay Applications – Lump Sum (DSC -2) Low

Condition: There were four (4) Pay Applications in which Auto Allowance was billed as a lump sum.

Impact: Payment could occur for charges that were not incurred or supported.

Pay Applications (Continued)

Criteria: As cost-plus contracts with a Guaranteed Maximum Price (GMP), all charges in the respective payment application, unless otherwise specified in the contract documents, are reimbursed at actual cost and are to be fully supported with payroll documentation, vendor invoices, sub pay applications and/or other third-party receipts.

Cause: The contract documents did not specify the ability to bill charges as a lump sum.

Recommendation: For any project not completed that is being billed as a lump sum, as well as those projects closed under the right to audit clause, the District should request support for any previous lump sum charges.

The District's updated CM Contract does have additional language for reimbursable expenses, which include auto allowances. Any items that will be billed as a lump sum going forward should be clearly stated in future contracts.

***Management Response:** The Director of Construction Services and the Chief Operations Officer will review the procedure associated with Pay Application review. In addition to enhancing the review process of the Project Director, the role of the Design Professional will also be assessed to ensure they are providing a thorough review in compliance with the revised Architect/Engineer Agreement. The presentation of General Condition costs and requirements for itemized statements will be assessed to ensure the format is consistent across projects and Construction Managers. Initial steps have already been taken in the revised Construction Manager Agreement to be utilized on upcoming 2021-22 projects which clarifies the General Condition content and format in the Guaranteed Maximum Price Amendment and subsequent Pay Applications.*

Best Practice Recommendation: All Pay Applications reviewed during our testing contained an itemized breakdown of hours worked for each of the employees that were included in the billing. There were some pay applications that also contained system payroll records to support the itemized hours. As a best practice, additional documentation, such as system payroll records, should be obtained for all Pay Applications to support labor costs submitted in Pay Applications. It should be noted that the updated CM Contract contains additional language in regards to labor costs which includes the District's right to audit the CMs Payroll.

***Management Response:** See Exhibit A – The Director of Construction Services and the Chief Operations Officer will determine the potential for a process to review the Construction Manager's system payroll records as part of the monthly Pay Application certification. Similarity of format across Construction Managers and the level of intelligible detail provided will be assessed. Note that this assessment will include a review of staff resources and expertise required to undertake this field accounting review against the Project Directors primary function of overseeing construction to ensure that a building structure meets all established life safety criteria.*

Best Practice Recommendation: Through discussion with Management, as a best practice, the Construction Services Department would benefit from implementing a checklist for Pay Application Reviews. This would memorialize the review performed based on the Construction Manager Contract Pay Procedure. Any additional enhancements to the Procedures should be captured on the checklist. The checklist should provide for the ability to document the employee that performed the various steps and ability to add notes and references. The checklist should also capture and document if there are any discrepancies in the Pay Application and how the discrepancies were resolved.

Pay Applications (Continued)

***Management Response:** The Director of Construction Services and Project Directors will work to develop a detailed checklist for Pay Applications which allows for the accurate tracking of General Conditions expenditures, confirms the accuracy of Change Order processing, accurately tracks the expenditures of the Unforeseen Conditions Fund, and tracking of errors when identified to correction.*

Unforeseen Conditions

The Budget Transfer Procedure contains the process for reallocation of funds within a Construction Manager's Guaranteed Maximum Price Budget, which includes Unforeseen Conditions. Within the project, funds can be moved from one line item to another through Budget Transfers. The Budget Transfer/Unforeseen Condition Form is completed for these transfers. If there are funds remaining in a line item these will be transferred to supplement the cost of other line items. There could also be a trade that a subcontractor would typically perform work but it ended up being performed by another subcontractor or it made sense to move it to another line item. Again, the movement from one line item to the other does not change the value of the contract. The Project Manager, Architect (when applicable), and Construction Manager must sign the Budget Transfer/Unforeseen Condition Form.

An Unforeseen Condition is a budgeted line item that allows for situations in which additional funds are needed for a typical cost within the project. The GMP will have the established amount which appears in the Amendments and is updated if an additional amount is needed with any subsequent Amendments. For example, during excavation there is an old dump site, requiring the need to mitigate the debris. The use of Unforeseen Conditions is a Project team decision to determine why the expense was not included in the scope and the cost to remediate the issue. The Continuation Sheet for each Pay Application serves as the main tracking of ongoing Unforeseen Conditions.

Using the same seven (7) projects from the Pay Application Review in Section B – Pay Application, we obtained the last Pay Application and extracted the Continuation Sheet to review all Budget Transfers that involved Pay Applications. We reviewed the Notes column in the Continuation Sheet for those Budget Transfers listed on the Unforeseen Condition to identify the Budget Transfers and then traced the totals on those forms. We obtained the Budget Transfer/Unforeseen Conditions forms and reviewed for proper approval and support. We also verified that the amount on the Continuation Sheet and Forms matched that in the contracts and amendments. For all Budget Transfers reviewed, they were properly approved by applicable parties. For closed projects, unspent balances were transferred to the Unforeseen Conditions Fund and returned to the District. Based on our testing, we noted the following exception:

Unforeseen Conditions (DCS-3) Moderate

Condition: Out of the seven (7) projects reviewed we had the following exceptions:

- There were three (3) projects in which the Budget Transfers used for Unforeseen Conditions were not documented on the Pay Application Continuation Sheet.
- Although there were invoices to support the use of Unforeseen Conditions, there were three (3) instances in which additional support would have been beneficial to explain the reason the expense qualified and the decision to use Unforeseen Funds.

Unforeseen Conditions (Continued)

Impact:

- The ability to identify the exact Budget Transfer forms used to document the use of Unforeseen Funds could be difficult.
- Unforeseen Funds could be used for items that were not properly budgeted or should not be considered truly unforeseen.

Criteria:

- The District tracks use of Unforeseen Conditions through Budget Transfer Forms and references the transfers on the Pay Application Continuation Sheet.
- The Budget Transfer Procedure notes that supporting documentation should be attached to the Budget Transfer/Unforeseen Conditions Form.

Cause:

- The requirement for additional documentation, such as meeting minutes and discussions by the necessary parties on why the situation qualified for the use of Unforeseen Conditions, is not included in the Budget Transfer Procedure.
- The Budget Transfer Procedure does not contain parameters or general guidance on what type of expenses should qualify for the use of Unforeseen Conditions and additional documentation to support how the decision was made.

Recommendation:

- The Department should consider creating a cumulative log to track Unforeseen Conditions. In addition to ensuring that use is tracked on the Continuation Sheet, this would provide an overview of the funds as they are spent throughout the project with descriptions for each use. A reviewer could then go into a Budget Transfer Form if additional information is needed. Reference to tracking of Unforeseen Conditions, in both a Continuation Sheet and possible log, should be documented in the Budget Transfer Procedures.
- The Department should consider adding additional guidance and necessary documentation of support for Unforeseen Conditions. This would provide scenarios that are appropriate for the use of Unforeseen Conditions as well as to memorialize the reason that the situation qualified for the use of Unforeseen Condition Funds.

Management Response: *The Director of Construction Services and the Chief Operations Officer will evaluate the process associated with the expenditures of the Unforeseen Conditions Fund. The process if accurate executed should be supported by the creation of a Request for Information (RFI) from the Construction Manager (CM), response with direction (Architect's Supplemental Instruction or like Construction Document modification) by the Design Professional, estimating by the CM, and approval for expenditure by the Project Director. This will need to be tracked through multiple logs and eventually show an adjustment on the Pay Application Continuation Sheet. This process needs to be studied closely and appear in the Construction Management Agreement, Architect/Engineers Agreement, and the Department of Construction Services Procedures Manual including the use of the Budget Transfer Form if deemed appropriate.*

Change Orders

The project cost total is adjusted throughout the Project. The initial Contract Amount is typically based on the initial amount to perform pre-construction type work, such as surveys, inspections, architect and engineering design. Construction Managers are selected based on qualifications. After selection the cost of the full project is negotiated. Amendments are used for additions to the cost of the project. The largest amendment is typically after the GMP is negotiated, however there can be additional increases such as change of scope. The Amendments are provided to and approved by the School Board. Deductions to the contract cost occur through Change Orders. Movement of funds that do not increase or decrease the Contract occur through Budget Transfers.

Reductions to the contract cost occur through Change Orders. The District uses the term Change Order primarily for 2 reasons, Direct Purchase Materials and at the end of the project to adjust the contract amount due to unused funds. Direct Purchase Materials are those that are directly purchased by the School District for tax savings. Each time this occurs, there are two Change Orders, one for the materials and one for the tax savings based on the direct purchase of the materials. This can occur throughout the project and is typically reserved for large purchases, such as lumber, concrete, and electrical. Any Change Order must be approved by the School Board.

During our testing of Pay Applications, we reviewed to ensure that Change Orders were properly completed and supported the adjustments in the Cover Sheet and Continuation Sheet of Pay Applications. We found that all Change Orders were properly approved and reflected in the Pay Applications. The Change Orders are also located in the Project Summaries. During testing of Unforeseen Conditions we reviewed the last Change Order of projects that removed unused funds from the project total. Overall Change Orders were properly documented and tracked.

Project Closeout

Closeout of a project is considered when all final documents are received and a final payment is made. The Project Director performs final sign off on the project. The Department attempts to close out a project as soon as possible. This allows the Department to move on to new projects. Based on discussion with the Department, very few projects remain open for a significant amount of time, and those that do are larger projects or those with many phases.

The Process for Project Close Outs Document is in the Department of Construction Services Procedure Manual. The process discusses the various documents (plans, as-built drawings) and other tasks needed to closeout a project. One of those items is the for the Project Assistant to review content of the project closeout documents using Exhibit C form Construction Manager's (CM) Agreement. This agreement is located in every CM contract. This document contains the items that must be submitted with General Contractor's Request for Final Payment. Once these items are received, the final payment is made to the CM. Of the seven (7) projects reviewed throughout this audit, five (5) were Closed. We reviewed the completed Exhibit C form Construction Manager's (CM) Agreement that contains sign off by the Construction Manager and Project Director for all projects without exception.

Key Performance Indicators

Key Performance Indicators (KPIs) provide an overview of key measurements of a department. KPIs can help facilitate effective and efficient management of the Department and Projects. Through discussion with the new Construction Services Director he has identified the need to establish KPIs for the department. This would involve obtaining and tracking key data on projects. It should be noted that the Department had developed a GMP Cost Comparison Worksheet as part of the CM Negotiation Procedures. The implementation of the worksheet would help capture key data used in KPIs.

Best Practice Recommendation: As Management has already identified the need of KPIs, a best practice recommendation will be for Management to continue the pursuit of developing KPIs. KPIs would allow for reporting to the Board on key construction measurements (cost of projects, volume of activity performed) and could help identify the need for additional staff based on volume and project sizes. Below are some examples of KPIs that the department could establish.

- Cost of new construction per sq. ft.
- Cost of new construction per student station
- Cost of renovation per sq. ft.
- Number of building permits issued by the department
- Number of inspections completed by the department
- Inspection pass rates
- Number of staff compared to total \$ managed

Management Response: *The Director of Construction Services and the Chief Operations Officer will develop Key Performance Indicators (KPI's) which assess project and facility related issues both during construction and post construction:*

- *Construction Cost (\$/Student Stations) District's Position Statewide/Bay Area*
- *Performance of Construction Manager:*
 - *Inspection Pass Rate*
 - *Safety*
 - *Schedule Adherence*
 - *Change Orders*
 - *Percentage of local Sub-Contractors*
 - *Accuracy of Budgeting from Stage 1 through GMP*
- *Building Performance*
 - *Utility Cost/SF*
 - *Maintenance Cost/SF*
 - *Warranty Call Backs*
 - *Customer Satisfaction*
- *SDMC Staffing*
 - *Project Workload*
 - *Staff Satisfaction*
 - *Turnover Rate*

Note that 2021-22 and 2022-23 will be baseline years since much of this data has not been previously collected.