



City Auditor's Office

Utilities Department Capital Projects – Contract Audit

Report Issued: March 3, 2017

Audit Report No. # 16 A-2



TO: Mayor and Council Members

THRU: Margaret L. Krym, City Auditor 

FROM: Timothy DiSano, Senior Auditor 

DATE: March 3, 2017

SUBJECT: Utilities Department Capital Projects – Contract Audit

Overall our audit report concluded that the Utilities Department Capital Projects were generally properly administered and managed. However, as in most cases some opportunity for improvements exist, this audit disclosed three audit findings and two reportable conditions. As standard practice the audit report provided recommendations and suggestions to address these matters, along with managements responses.

We would like to commend the Utilities Department for being proactive in recognizing areas on their own in need of improvement. During the period of the contracts reviewed the department has implemented two software applications called Canvass and Plan Grid which are utilized to improve documentation, monitoring and storing inspection reports and online drawing specifications. They also have collaborated with the Procurement Division in incorporating best practice guidance recommended by the Engineers Joint Contract Document Committee (EJCDC). The EJCDC guidance provides guidance on all contract requirements pertaining to the construction industry.

We would like to thank the Utilities Department and Procurement personnel for the assistance they extended during this audit engagement. We especially appreciate all their valuable time and efforts spent in providing us the information requested.

Should you have questions or need clarification, please do not hesitate to call the City Auditor's Office at (239) 242-3380 or (239) 242-3308.

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TABLE OF CONTENTS

EXECUTIVE SUMMARY	4
BACKGROUND.....	6
OBJECTIVE.....	6
SCOPE AND METHODOLOGY	7
STATEMENT OF AUDITING STANDARDS.....	7
AUDIT FINDINGS AND RECOMMENDATIONS	8
Finding # 1:	8
Recommendation # 1:	8
Management Response # 1:.....	8
Finding # 2:	9
Recommendation # 2:	10
Management Response # 2:.....	10
Finding # 3:	11
Recommendation # 3:	11
Management Response # 3:.....	12
Reportable Condition # 1:	12
Suggestion Reportable Condition # 1:	12
Management Response Reportable Condition # 1:	12
Reportable Condition # 2:	13
Suggestion Reportable Condition # 2:	13
Management Response Reportable Condition # 2:	13

EXECUTIVE SUMMARY

The City of Cape Coral Auditor's Office 2016 Audit Plan approved by City Council on November 17, 2015, included a Capital Projects Contract Audit of the City's Utilities Department.

The Utilities Capital Projects Contract Audit consisted of reviewing two contracts for compliance to contract specifications, laws, regulations and policies. We also reviewed Department contract administration procedures. These two were:

- Contract "Con-UT14/05/TM" which was to replace approximately 31,000 feet of existing galvanized pipe along specific streets within the City and contract.
- "ITB #13-14/GL" for the rehabilitation of seven specific lift stations positioned around the City.

During these two contract periods the Utilities Department has been actively developing and improving areas of operations such as:

- Implementation of two software applications called Canvass and Plan Grid which are utilized to improve documentation, storing and monitoring of required contract project inspection reports and online drawing specification updating.
- Collaborated with the Procurement Division in incorporating best practice guidance recommended by the Engineers Joint Contract Documents Committee (EJCDC). The EJCDC provides guidance on all contract requirements pertaining to the construction industry.

Based on the audit objectives and procedures performed, we concluded that internal controls were generally functioning effectively to prevent non-compliance with procurement policies, procedures, and applicable governing laws and regulations, contract stipulations, financial reporting, change orders and inspections. However, as in most cases some opportunity for improvement exist, specifically with regards to City Council agenda requests and contract change order approvals.

The audit identified three findings and two reportable conditions. We have provided recommendations and suggestions to address these issues. The findings are listed here:

- Management inadvertently provided City Council with an incorrect agenda request document, which was consequently approved by City Council and awarded a contract not in accordance with accepted submitted bid documentation.
- The Utilities Department accepted a change order in the amount of \$150,146 without City Council's approval.
- Some documentation evidencing inspection activity for Contract "Con-UT14/05/TM" could not be provided. The documentation provided was not sufficient to enable verification of quantities used.

A complete list of the audit findings, reportable conditions, recommendations, suggestions and management responses is outlined in the report.

We discussed the audit findings and reportable conditions with the Utilities Department management and their responses are included. Our conclusions were based on the various audit procedures performed during the audit.

BACKGROUND

The Utilities Department Administration provides for the overall management of the existing Utilities Operations. They are tasked with maintaining the infrastructure to safely provide drinking water, reuse irrigation and sewer service to City residents.

Currently there are several capital improvement and maintenance projects in progress within the Utilities Department.

As of Fiscal Year 2015, the Utilities Department had 212.9 approved positions, with an adopted operating budget of \$126,775,715 in expenditures and an adopted budget of approximately \$15.7 million for capital projects. Within the Utilities Department, there are four main divisions.

1. Administration: Responsible for overall utility operations, utility project management and long range department plans.
2. Water Production: Responsible for producing water that meets or exceeds all safe drinking water, Environmental Protection Agency and Florida Department of Environmental protection standards.
3. Collection and Distribution: Responsible for water, sewer and irrigation operation and maintenance.
4. Water Reclamation: Responsible for processing wastewater, so after treatment the wastewater meets and/or exceeds all standards and requirements established by the Environmental Protection Agency and Florida Department of Environmental protection standards.

Over the last few years, the City has begun to increase capital improvement and maintenance project activity. This follows many years of projects that were placed on hold due to budget constraints. In addition, capital improvement and maintenance project activity is projected to continue over the next several fiscal years.

OBJECTIVE

The objective of this audit was to review the following:

1. If the selected Contracts were properly approved and competitively awarded in accordance with the City's procurement policies, applicable governing laws and regulations.
2. If appropriate City staff/inspectors properly monitored the contracts to ensure the required work was performed in accordance to the stipulations and conditions within the contract.
3. If payments to vendors for invoice payment applications were properly supported, approved and authorized and in accordance with contract term's and condition's.
4. If any applicable change orders were properly supported, approved and authorized.

SCOPE AND METHODOLOGY

The scope of the audit focused on a sample of two Utilities Capital Project Contracts completed and closed out during fiscal year 2015.

The following audit methodologies were used to address our audit objectives:

- Obtaining an understanding of the City's procurement policies and procedure manual.
- Obtaining an understanding of applicable governing laws and regulations.
- Examining two selected Utilities Capital Project Contracts and ITB documentation for compliance with procurement policies, procedures and applicable governing laws and regulations.
- Examining payment application for proper approval and authorization by vendor, utilities and accounts payable staff, contract stipulations, proper and sufficient supporting documentation, and calculation accuracy.
- Examining the final close out package for required supporting documentation per contract stipulations.
- Examining inspections reports for compliance with contract stipulations and department policies and procedures.
- Examining change orders for proper approval & authorization by vendor, utilities and if necessary project engineer, compliance with contract stipulations, proper and sufficient supporting documentation if necessary and calculation accuracy.
- Interviewing key personnel, such as contract administrator, project manager, inspectors, procurement and legal staff.

The audit performed was neither designed nor intended to be a detailed review of every transaction or procedure. Therefore, the opportunities for improvement identified in this report may not be all-inclusive of areas needing improvement. Although we exercised due professional care in the execution of this audit, this should not be interpreted to mean that noncompliance or irregularities do not exist. The deterrence of fraud is the responsibility of Management.

STATEMENT OF AUDITING STANDARDS

We conducted this performance audit in accordance with Generally Accepted Government Auditing Standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

AUDIT FINDINGS AND RECOMMENDATIONS

Finding # 1: Management inadvertently provided City Council with an incorrect agenda request document, which was consequently approved by City Council and awarded a contract not in accordance with accepted submitted bid documentation.

Contract "ITB #13-14/GL" was for a total construction cost of \$1,650,089. The total cost included \$1,150,736 to rehabilitate seven specific lift stations; City controlled contingency cost of \$115,074 (10%); and City controlled allowance totaling \$384,280.

The audit revealed that when the agenda item was sent to the City Council for approval, Department staff inadvertently included a second contingency of \$165,009 (10% of \$1,650,089). As a result, the total contingency was increased to \$280,083. Therefore, the Council approved contract amount totaled \$1,815,098. This error could have been caused by the layout of the bid document, which required all the vendors to include a notation of a contingency as part of their bid submission.

At close out, spending on this contract for the seven specific lift stations totaled \$1,625,620, which was less than the original approved bid plus the first 10% contingency amount.

The remaining portion of the approved contingency of \$165,000 was not spent on the seven specific lift stations defined within the approved project scope and remained available for Utilities Department use.

Recommendation # 1:

We recommend that the contingency amounts should be calculated and approved by authorized City staff and not be included as a part of the vendor bid submission. Additionally, someone in the Utilities Department, who is familiar with the project, should review and approve the agenda item prior to submission. Their review should be documented with a signature or initials indicating approval.

Management Response # 1:

Utilities response:

The remedy to prevent this from recurring follows: (1) Utilities will work jointly with Financial Services to assure that contingency is not included as a bid item in the future. (2) Utilities has integrated EJCDC document templates for use in setting up ITB, RFP, RFQ, etc. documents which will eliminate any and all outside interference or influence on the department's mechanisms of project procurement submittals. (3) Since this contract, the Utilities Department has added personnel to assist with review of project bid information.

Procurement response:

In reference to the “city contingency” wording included as part of the bid documents: Finance/Procurement will continue to review the bid documents in coordination with Utilities to ensure that any and all language not related to the items required for the project such as “city contingency” are not part of the official bid form. Currently the “city contingency” language do not appear in any of the bid forms. In addition, EJCDC documents, which are templates for infrastructure projects, are being utilized and reviewed by Utilities and Procurement. In reference to the agenda submission and/or wording: the draft agenda item and all backup are forwarded to the department for review prior to the department electronic approval of said agenda in NOVUS.

Finding # 2: The Utilities Department accepted a change order in the amount of \$150,146 without City Council’s approval.

The audit revealed that the Utilities Department approved a change order in the amount of \$150,145 without the proper approval of City Council as required by City Ordinance 11-11. This change order added an additional lift station, which was not one of the original seven specific lift stations defined in the approved project scope of contract “ITB #13-14/GL”. The change order utilized the remaining second contingency amount mentioned in finding #1. This additional lift station was an expansion of the originally defined and approved contracted scope of work. The contract specifically identified seven lift stations by number and the added additional lift station was not identified in the original contract documents.

Since the department had an additional approved contingency amount they accepted an additional lift station for rehabilitation, which was not included in the originally approved contract and therefore the additional lift station expanded the originally defined and approved contracted scope of work and expended funds without the proper authorization.

Ordinance 11-11, 2-146(g) Contract Amendments defines contingency amounts as contract amendments and states: “At the time of contract approval, the City Council may approve “a contract amendment” amount for funding the cost of potential changes due to unforeseen circumstances. These funds may also be used to enhance the project. The City Manager or designee is authorized to approve and execute change orders within the limits of funds available in the “contract amendment”. Change orders that exceed the pre-approved amount require City Council approval”.

The City of Cape Coral procurement policies and procedures manual indicates that the City Manager shall have the authority to approve and execute all procurement related contracts and amendments, etc. up to \$50,000 or less. However, staff could not provide any documentation to indicate that the change order was submitted to the City Manager for approval.

Even if the work on this additional lift station was considered an emergency it still would have required City Council authorization. City Ordinance 11-11, 2-144 Procurement Procedures states, 15 (d) states: “Emergency purchases: The procurement manager may make or authorize others to make emergency purchases of supplies, services or construction items

when there exists a threat to public health, welfare or safety provided that the emergency purchase shall be made with the competition as is practicable under the circumstances. The director of the affected department shall notify the procurement manager, who shall authorize the purchase of the needed item(s) or service. The department director shall send a requisition to the procurement division within 24hrs of the notification to the procurement division, together with a written explanation of the basis for the emergency purchase. The City Manager shall approve all emergency requisition in excess of \$20,000. Any emergency purchase in excess of \$50,000 must be approved by the City Council either before or as soon as practicable after the purchase”.

Any deviation from strict compliance with procurement policies and procedures and procurement ordinances weakens governance controls.

Recommendation # 2:

We recommend that the Utilities Department seek City Council approval of contract change orders that expand the original project scope and are greater than \$50,000 to be in compliance with City Ordinance 11-11 and contract stipulations.

Management Response # 2:

In this situation, if Finding# 1 did not happen then Finding# 2 would not have happened.

Since the use of the funds and the resulting change order executed was for a project or need that was very similar in nature, staff thought it was appropriate to utilize remaining funds to rehab one additional plant lift station since the contractor was already mobilized. In this instance, a critical wastewater plant lift station required immediate rehabilitation. Health and safety issues were at risk of being compromised and staff utilized remaining funds to accomplish the lift station rehabilitation work. Staff actually recognized a project savings for mobilization costs by the contractor. The budget for this additional lift station rehabilitation was originally included in the FY-12' Council approved CIP budget. Also the lift station had a City Manager approved engineering and design contract that was approved in April of 2013. This wastewater plant lift station wet well coating was single sourced and vetted through procurement via inter-office memorandum. Moving forward, City staff's goal is to safeguard change-orders so similar instances will always receive proper approval in compliance with current city policy and ordinances. The Utilities Department has implemented a secondary approval process for project change orders to eliminate this risk.

Finding # 3: Some documentation evidencing inspection activity for Contract “Con-UT14/05/TM” could not be provided. The documentation provided was not sufficient to enable verification of quantities used.

Review of documentation for Contract “Con-UT14/05/TM” revealed that the Utilities Department was missing some documentation evidencing inspection activity as follows.

- In one case, the department was not able to provide the EXCEL spreadsheet, “Inspector’s Street Grid” of agreed final material quantities, which is developed from the inspector’s field notes.
- In another case, we were unable to obtain the inspectors field notes, which are used to develop the EXCEL spreadsheet, “Inspector’s Street Grid” of agreed final material quantities.

Department staff indicated that during management of this contract, they had a computer hardware failure and these documents were lost and unrecoverable. They had not sufficiently backed up this project inspection data.

The department process for tracking and verifying usage of materials began with data from inspector field notes, which fed into the Inspector’s Street Grid spreadsheet. This spreadsheet listed rows as individual bid items. Payment applications provided by the contractor also listed rows as individual bid items. With the missing documentation it was not possible to trace actual material usage from field notes to an Inspector Street Grid and then to a corresponding payment application.

Best practice dictates that project inspections be performed daily and be evidenced in writing with supporting documentation such as photos. Also, they are required to be retained in compliance with record retention policies.

Without sufficient documentation of inspections, the City is unable to assure compliance with contract/project specification and conditions. Also without sufficient backup and storage of records the City is not in compliance with the State of Florida General Records Schedule GS1-SL for State and Local Government, item #136 Project File: Capital Improvement requires documentation for capital improvement projects and/or sent out for bid, shall be kept on file for 10 fiscal years after completion of the project. Also Item #340 Disbursement Records: Detail, requires documentation specific to expenditures or transfers of agency moneys for the procurement of commodities, services and other purposes, shall be kept on file for 5 fiscal years.

Recommendation # 3:

- 3.a. We recommend that the Department improve their processes and strengthen controls to ensure that project work inspection documentation is maintained in accordance with the State of Florida general records schedule GS1-S1 for state and local governments.
- 3.b. We recommend that the Department work with the City Information Technology Department to improve electronic data backup procedures to ensure that files or databases will be preserved in the case of equipment failure or other catastrophes.

Management Response # 3:

The department has initiated a few electronic software programs to further enhance the department's ability to provide reliable and accurate inspections and document tracking. Canvass and Plangrid have been in use for a number of months and Aconex Project Management Information Systems (PMIS) software will be up and running in about one year. Both Canvass and Plangrid are cloud based and will provide backup capabilities to the department's Ipad tablets currently being used. This will preserve any and all files and databases in case of local hardware or software failure. Inspectors for the Utilities Department have been in place for a number of years and have the knowledge and capabilities to provide the key project information that is paramount in the successful and smooth operation of the projects that they are tasked with managing.

REPORTABLE CONDITIONS¹

Reportable Condition # 1: A change order was not properly authorized and approved by all responsible parties in advance of work being performed.

The audit reviewed 21 additional change orders to contract ITB #13-14/GL and found one that was not authorized by all responsible parties prior to work being performed. The change order was signed by the contractor on 6/17/2015, however not signed by the City Engineer or City of Cape Coral until 8/25/2016 and 8/25/2016 respectively, long after the contract final payment application on 1/20/2016.

The Utilities Department uses a standard contract change order form for documenting and seeking authorization of each change order. Each Change order seeks approval from the City's Engineer, Contractor and City of Cape Coral in advance by all responsible parties before the work is performed.

Suggestion Reportable Condition # 1:

The Utilities Department should improve management oversight of contract change orders to ensure that they are properly authorized and approved in advance by the responsible parties involved.

Management Response Reportable Condition # 1:

Policy has been initiated in order to eliminate change orders from being approved that are not considered an added value item or to address an unexpected specific project constraint. Management believes this risk will be eliminated from recurring in the future.

¹ Matters coming to the Auditor's attention relating to significant deficiencies in the design or operation of internal control that could adversely affect the organization's ability to fulfill future obligations or satisfaction of liabilities.

Reportable Condition # 2: The PDF images of some vendor payment applications for contract “ITB #13-14/GL” were difficult, and in some cases impossible, to read because of poor scanning quality.

The Audit identified scanned payment applications, that were difficult to read and review because of the quality of the scanned images. We inquired with the Utilities staff regarding an electronic, non-scanned version of the payment application to review. The Utilities staff were unable to produce a non-scanned copy of the payment application. However, they were subsequently able to obtain the documentation from the Contractor as of September 20, 2016.

Without legible payment applications and supporting documentation the department is unable to adequately review & assure compliance with contract terms and conditions. Also the department would not be in compliance with State of Florida general records schedule GS1-S1 without sufficient and legible supporting documentation.

It is required that a contractor submit pay applications in accordance with contract specifications. These pay applications are required to be adequately reviewed and approved by City personnel before each payment. Having these documents in their original electronic format would facilitate such reviews and make the payment approval process more efficient. Subsequent scanning of these records should be done in a manner to ensure they remain legible.

Suggestion Reportable Condition # 2:

The City should improve their processes and strengthen controls to ensure that documentation supporting pay applications is maintained in a format that is legible and in accordance with the State of Florida general records schedule GS1-S1 for state and local governments. We suggest that all documents with supporting calculations for pay applications be received from the vendor in original electronic spreadsheet form to facilitate Department review and verification of calculations.

Management Response Reportable Condition # 2:

The documentation sent via PDF was illegible and the Utilities Department will be sure moving forward to reject any and all pay application documents that are illegible. An electronic copy will be required if necessary to review and verify pay application calculations.