

New Castle County
Change Orders and Contractor Payments – Construction Projects
Audit Report

To: Tracy Surlles, Acting General Manager of Special Services
Yvonne Gordon, Chief of Administrative Services
Christopher A. Coons, County Executive
Paul G. Clark, County Council President

Background

New Castle County Code, Chapter 2, Article 5, Section 2.05.303, “Purchasing of Contract Construction”, deals with the purchasing of contract construction by the County’s Department of Special Services. Our audit of the Procurement Function, performed in 2006, evaluated the internal controls over the County’s compliance with that section of the Code, as well as Section 2.05.502 dealing with the procurement of supplies and contractual services (including professional services). The audit of the Procurement Function primarily encompassed the procurement of contract construction, supplies, and contractual services up to the point at which the contract is executed with the vendor.

This audit evaluated the internal controls over change orders on construction contracts, after the contract for a construction project is executed. The audit also analyzed the controls over payments to contractors.

We were informed by Special Services Management that change orders for special services contracts are governed by Chapter 2, Article 5, Section 2.05.303.D.16 of the New Castle County Code.

A change order is requested upon the occurrence of differences between the construction specifications/drawings and actual conditions encountered during the execution of the contract, and when the work required by the change order is within the scope of the contract. The change order can be requested by the owner (i.e., New Castle County), construction manager, architect, contractor, etc. Change orders are the result of elements beyond the contractor’s control, unforeseen conditions, material delivery delays, etc. The project management team reviewing the change order is dependent upon the type of project and where the change order originated. The owner always reviews change order requests and approves for further processing or denies. If the change order is approved by the project manager/administrator, then it is packaged together with any supporting documentation and reviewed and approved by his/her direct manager, the Fiscal Section, and then by the Acting General Manager. Once all approvals have been obtained and documented, the change order is given to the Fiscal Section for input to the Tier Performance System. It will then be reviewed by the PRC (Purchasing Review Committee). The PRC, which meets every week to discuss change order requests, must approve every change order on capital projects.

Some change orders that arise are of an urgent nature, so verbal approval is requested. For a verbal approval, the project manager/administrator will send an e-mail to his/her direct manager (a Division or Section Manager) and to the Acting General Manager, with a "cc" to the Fiscal Section. In the e-mail, there will be an explanation of what the change order is needed for and the amount. The Acting General Manager and Division/Section Manager will ask questions if needed and then approve or deny. If verbal approval is given by Special Services management, the Fiscal Section will send a formal verbal request to the members of the PRC. The PRC will ask questions for clarity if needed and then approve or deny. Once the change order is verbally approved, the project manager/administrator can have the contractor begin the work. The project manager/administrator will then send the change order paperwork to the Fiscal Section to be entered to the Tier Performance System, and the Fiscal Section will send the paperwork to the PRC for formal approval.

The Purchasing Division will process a Change Order (also called an "Advice of Change" on the Tier Performance System) when a department properly authorizes the change to an existing purchase order. We generated a report from the Tier Performance System of all Advices of Change for Fiscal Years 2006 and 2007 (through the end of March). During these two periods, the number and dollar amount of Advices of Change were as follows:

- Fiscal Year 2006: 587 Advices of Change for approximately \$8 million in increases. 168 of these were over \$10,000, 84 (or 50%) of which were originated by the Special Services Department.
- Fiscal Year 2007 (through March 31): 246 Advices of Change for approximately \$6.7 million in increases. 115 of these were over \$10,000, 82 (or 71%) of which were originated by the Special Services Department.

Please note that, as explained later in this report (see comment # 1 on page 6), not all of these Advices of Change actually represented "true" change orders.

Audit Objectives and Results

After performing some preliminary research and after internal discussions, we decided on the following objectives for this audit:

1. Evaluate the controls over construction contract change orders; in particular, the documentation which exists supporting them.
2. Evaluate whether the Purchasing Review Committee (PRC) is reviewing purchase order increases in accordance with policy, and evaluate the quality of the PRC's minutes.
3. Evaluate departmental written policies and procedures for change orders, particularly for construction contracts.
4. Evaluate the Project Cost Reports for the Public Safety Building as well as the use of a Construction Manager and an Owner's Representative for this project.
5. Discuss with the Special Services Department the recent review performed by an outside law firm of the standard language in construction contracts.

6. Evaluate the controls over contractor payments; in particular, the controls over ensuring that payments made are in accordance with the work completed.

Scope

We conducted our audit in accordance with standards promulgated by the Institute of Internal Auditors and the United States General Accounting Office. Our audit testing encompassed the period July 1, 2005 through May 2nd, 2007. **It should be noted that the majority of this timeframe occurred during the tenure of the former General Manager of Special Services. The Acting General Manager assumed responsibility for her function in March 2007.**

Our testing encompassed six construction projects, two involving buildings and four involving sewers.

Professional auditing standards require that we plan and perform the audit to obtain reasonable assurance whether internal controls are adequate in all material respects. Our audit of internal control included obtaining an understanding of the internal controls over change orders and contractor payments, testing the operating effectiveness of the controls, and performing such other procedures as we considered necessary in the circumstances.

Our evaluation of internal control may reveal three categories of internal control deficiencies. The first two categories are of a much greater magnitude than the third category.

- A Material Weakness is a matter that, in our judgment, could adversely affect New Castle County's ability to accomplish its objectives related to change orders and contractor payments. **There are no Material Weaknesses in this report.**
- A Significant Deficiency is a control exception that is of a lesser magnitude than a material weakness; however, it could potentially have a significant, adverse impact upon the change order and contractor payment functions in the future and, therefore, warrants management's attention. **There are no Significant Deficiencies in this report.**
- Other Reportable Items are opportunities for improvements in the system of internal control. There are five Other Reportable Items in this report, beginning on page 5.

In general, our testing involves audit sampling. We evaluate the results of the tests and use professional judgment, based on the number of exceptions and/or the materiality of such exceptions, whether to include exceptions in the audit report and, if so, in which category to include them. In some cases, we perform additional testing to help us obtain additional audit evidence in making such evaluation and determination.

Because the scope of an audit does not allow us to examine every single function and transaction performed by an area, an audit would not necessarily disclose all matters that might be material weaknesses, significant deficiencies, or other reportable items.

Opinion

In our opinion, during the period July 1, 2005 through May 2, 2007, adequate internal controls existed in all material respects over the change order and contractor payment functions. We do have five comments which are discussed in the Other Reportable Items section of this report.

Overall we believe the Special Services Department (and Purchasing Review Committee) is thorough and diligent in its review and approval of change orders. We believe the people involved in the process take their responsibilities very seriously. We were particularly impressed with the Special Services Fiscal Unit. The comments in this report generally relate to two large building projects: Public Safety Building and Woodlawn Library.

Recognition of Participation and Cooperation

We would like to thank the Acting General Manager of Special Services and the Chief of Administrative Services, and their staffs, in providing cooperation during the course of the audit, and in being receptive to constructive comments and recommendations to strengthen the controls over the change order and contractor payment functions.

Response

The Acting General Manager of Special Services and the Chief of Administrative Services provided the County Auditor with written responses to the comments and recommendations in this report. These responses have been incorporated into the report.

Cc: Jeffrey Bullock, Chief Administrative Officer
Edward Milowicki, Acting Chief Financial Officer
Members of New Castle County Audit Committee
Members of New Castle County Council

Comments and Recommendations Other Reportable Items

Audit Objective #1: Evaluate the controls over contract change orders; in particular, the documentation which exists supporting them.

Comment # 1: Re-evaluate the term “change order” and ensure change orders are processed in accordance with management’s policies and procedures.

We selected for testing those capital projects that had five or more change orders over \$10,000 during the period July 1, 2005 through May 2, 2007. We reviewed the documentation supporting the change order, whether the change order was properly approved, and whether (if applicable) the work was postponed until the necessary approvals were obtained. A summary of the projects we tested can be seen in the following chart.

Project	Total # of COs > \$10K	Total \$ of COs > \$10K	# of "true" COs	Total \$ of "true" COs	% of project budget
Public Safety Building	44	\$5,678,958	40	\$3,545,688	7.24%
Woodlawn Library	18	\$949,003	18	\$949,003	11.28%
Southern Sewer Project (1)	6	\$3,502,917	3	\$174,964	0.18%
Stormwater Basin Renovation (2)	8	\$280,250	8	\$280,250	3.59%
Stormwater Mitigation (3)	11	\$1,517,850	11	\$1,517,850	8.89%
Stoney Creek Pump Station (4)	6	\$1,588,185	6	\$1,588,185	10.69%
Totals	93	\$13,517,163	86	\$8,055,940	

Notes:

(1) Two of the "true" change orders (totaling \$155,000) were for legal services which are not required to be reviewed by the PRC.

(2) One of the COs was a \$200,000 contract amendment which was approved by County Council and represented 71% of the total change orders for the project.

(3) All the COs were contract amendments which were approved by County Council.

(4) Two of the COs (totaling \$660,000) were for legal settlements reached with a contractor because of damages due to contract delays upon finding contaminated soil - an unforeseen condition.

We were informed by Special Services Management that change orders for special services contracts are governed by Chapter 2, Article 5, Section 2.05.303.D.16 of the New Castle County Code. **The additional work must be within the scope of the original contract and “... will only be allowed when there is a difference between the construction specifications and drawings and the actual conditions encountered during the execution of the contract.”**

We found during our testing that not all of the change order transactions (a “CO” on the Purchasing System) were “true” change orders based on the language in the above paragraph. That is, in some cases, a change order transaction was utilized in the following situations:

- To process an addition to the original purchase order to increase the purchase order to the actual contract amount.
- For the Public Safety Building Project, we learned that the project number was changed to transfer the project from the Special Services Department to the Public Safety Department. In doing so, the remaining amounts on all existing purchase orders were transferred from the old project number to the new project number; these transfers were made by processing a change order to the new project number.
- In addition, there were some situations in which there was a change order to process a contract amendment which was not within the scope of the original contract. Although these are technically “change orders”, they are not typical of the definition of change orders as provided to us by Special Services management (i.e., for work that falls within the scope of the original contract). It should be noted that some of these contract amendments were approved by County Council.

Of the \$13,517,163 in change orders over \$10,000 processed between July 1, 2005 and May 2, 2007 for the six projects, \$5,461,223 (or 40%) of these “change orders” actually represented one of the first two situations above. Although these observations do not have an impact upon the amount of dollars actually approved for particular projects, it does significantly misrepresent to an independent observer the amount of County dollars approved for projects that were due to “true” change orders. Thus, the amount of “true” change orders over \$10,000 processed between July 1, 2005 and May 2, 2007 for these six projects was at the most \$8,055,940. (We do not have a dollar figure for the third situation above; however, we know, based on the above chart, that there was at least \$1,717,580 in contract amendments approved by County Council.)

Public Safety Building:

The County engaged an outside Construction Manager (Gilbane Building Company) and Owner’s Representative (Remington Group Inc.) to help manage the project. Also, Tevebaugh Associates was the Architect for the project and was involved in many management decisions. The Acting General Manager of Special Services informed us that weekly meetings were held with Gilbane, Remington, and Tevebaugh to monitor and assess the status of the project.

There were several change orders in which work was performed before the change order was created and/or was approved by the PRC (Purchasing Review Committee). It should be noted that the Acting General Manager of Special Services informed us that items may have been verbally approved by her or the prior General Manager of Special Services during the weekly meetings with Gilbane, Remington, and Tevebaugh.

Administrative Services Policy #42, "Purchasing Review Committee, Emergency Purchases, and Legal Review", established the PRC. The PRC is composed of the Chief of Administrative Services, the Chief Purchasing Agent, a representative from the Law Department, a representative from the Office of Finance, and a representative from an operating department. The policy states that the PRC "... will hear and respond to requests for contract/project amendments/change orders, add-ons, and overruns." The policy does not provide a dollar threshold for requests nor does it exclude any particular requests; however, we were informed by both Special Services and Administrative Services managements that every change order on capital projects must be approved or denied by the PRC. We were also informed by Special Services management that, if necessary, verbal approval may be obtained from the individual members of the PRC prior to obtaining the PRC's formal, written approval. When verbal approvals are obtained, these are reflected in e-mails from the PRC members and these e-mails are retained by the Special Services Fiscal Unit.

As an example, we reviewed one item from the Public Safety Building Project (change order # 013915) where we saw an 11/01/05 letter from the contractor to Gilbane proposing a quote of \$71,029.90 for work involved due to new drawings. We saw a 12/10/05 Notice to Proceed from Gilbane to Special Services, signed by Gilbane, Tevebaugh, and Remington on 12/07/05, stating to go ahead and proceed with the work. We also saw a 1/09/06 e-mail from Gilbane to the contractor giving the contractor approval to proceed. The change order for the work was created on 1/25/06 and was signed by Gilbane (1/26/06), Tevebaugh (2/02/06), Remington (2/01/06), and by the Acting Chief of Special Services (2/08/06). However, the change order was not approved by the PRC until 2/16/06, it was not entered to the Purchasing System until 5/04/06 (indicating that it was late being given to the Special Services Fiscal Unit), and we did not see any e-mails indicating that verbal approvals were given by the members of the PRC. Thus, it appears that the work was performed prior to the change order being approved by the PRC.

As discussed in the first paragraph, the Acting General Manager of Special Services informed us that (1) weekly meetings were held with both Gilbane and Remington to monitor and assess the status of the project and (2) either she or the prior General Manager of Special Services often provided verbal approvals at these meetings. However, when approval is given to a contractor to proceed with work prior to the date the PRC reviews the Change Order, it is too late for the PRC to object to the work should it have concerns. We did not see any evidence/documentation indicating that the people involved in these weekly meetings had the authority to authorize the final approval of these change orders without the consent of the PRC.

Woodlawn Library

We were informed by the prior General Manager of Special Services that, due to unusual circumstances not mentioned in this report, the original Project Manager was late in processing several change order requests.

There were several change orders presented at the 8/17/06 PRC meeting. These change orders were for 20 items that were submitted by the contractors during the February through June 2006 timeframe. Our review of documentation during our contractor payment testing revealed that the work on many of these change orders was performed prior to 8/17/06. Neither the Special Services Fiscal area nor the PRC was aware of these items because the Special Services Project Manager had not made these areas aware of the change orders. Thus, these change orders were approved by the Special Services Project Manager (and apparently by the outside Construction Manager) prior to the PRC reviewing and approving them.

Recommendations:

1. Special Services management discuss with Administrative Services management the possibility of using a code other than “CO” for the types of situations where the item is not a “true” change order.
2. If there are projects involving an outside Construction Manager and/or Owner’s Representative, Special Services work with the PRC to develop special procedures (if necessary) for the PRC’s role in the project.

Response from Special Services Department Management

- The Special Services Department will follow through with the first recommendation.
- The Special Services Department will follow through with the second recommendation. However, please note that for most projects, the PRC’s role will be consistent with past practice and existing policies. This comment appears to be based primarily on the Public Safety Building Project, which was unusual due to its magnitude and due to the fact that the County retained both a Construction Manager and an Owner’s Representative. The need for retaining both a Construction Manager and an Owner’s Representative was due to both project complexity and staffing restrictions (no in-house project manager). While the department does not foresee a future project similar to the Public Safety Building, it would certainly work with the PRC to develop special procedures if a similar situation did arise.

Response from Administrative Services Management

Administrative Services will work with Special Services to expand and clarify the definition of a change order.

Audit Objective #2: Evaluate whether the Purchasing Review Committee (PRC) is reviewing purchase order increases in accordance with policy, and evaluate the quality of the PRC's minutes.

Administrative Services Policy #42, "Purchasing Review Committee, Emergency Purchases, and Legal Review", established the Purchasing Review Committee (PRC). The PRC is composed of the Chief of Administrative Services, the Chief Purchasing Agent, a representative from the Law Department, a representative from the Office of Finance, and a representative from an operating department. The policy states that the PRC "... will hear and respond to requests for contract/project amendments/change orders, add-ons, and overruns." The policy does not provide a dollar threshold for requests nor does it exclude any particular requests; however, we were informed by Special Services and Administrative Services managements that every change order on capital projects must be approved by the PRC. We were also informed by Special Services management that, if necessary, verbal approval may be obtained from the individual members of the PRC prior to obtaining the PRC's formal, written approval. When verbal approvals are obtained, these are reflected in e-mails from the PRC members and these e-mails are retained by the Special Services Fiscal Unit.

Comment # 2: Re-evaluate Purchasing Review Committee (PRC) policies and procedures and composition of PRC.

Our testing of change orders on capital projects revealed:

- There were 24 of 92 change orders, for a total of \$3,028,100, (a percentage of 26% and 42%, respectively, of the number and dollar amount of change orders we tested) where the approval of the PRC was not documented in written minutes. However, the approval of the Law Department representative on the PRC was documented on the hard copy of the Advice of Change. We were informed by the Purchasing Manager that formal minutes are only prepared if the Administrative Assistant in the Purchasing Division attends the meeting; during the timeframe of the audit, there were several meetings she was unable to attend. Regardless of whether or not there are written minutes, the Law Department representative on the PRC initials the hard copy of the Advice of Change as evidence that the PRC approved the change order.

We believe it is important to have written minutes that record the discussions of the Committee members.

- Our review of the PRC minutes indicated that the minutes do not usually reflect the reasoning behind why the PRC approved the change order. That is, how did the PRC ascertain that the work was within the scope of the original contract and was due to a difference between the construction specifications / drawings and the actual conditions encountered during the execution of the contract?

Examples:

- Although there was discussion in three PRC meetings about a \$147,674.28 change order for Woodlawn Library, there was no indication in the minutes as to why the PRC finally decided to approve it. (Note: The PRC minutes indicate that this was a controversial change order.) Nor did we see the actual change order itself; all we saw was the advice of change signed by the Chief of Special Services.
- A change order for \$10,000 in the 6/01/06 PRC minutes did not contain any reasoning as to why the PRC approved the change order, the minutes referred to the incorrect purchase order number, there was nobody from Special Services at the PRC meeting, and the only document from the Special Services Department was an e-mail from an engineer stating “Please increase PO121610 by \$10,000 for environmental testing services at Stoney Creek Pump Station.” (Given that the Company’s name is Environmental Testing, it is pretty obvious that they’d be performing environmental testing.)
- A change order for \$230,000 was not in the PRC minutes. (As mentioned above, minutes are not taken when the Purchasing Division Administrative Assistant is not able to attend.) We obtained an Indemnification, Hold Harmless and Settlement Agreement from the Special Services Department which indicated the County had negotiated a \$230,000 settlement with the contractor due to claims being made against the contractor by subcontractors. Since there was no indication in the agreement as to how the \$230,000 was derived, we find it difficult that the PRC could approve the amount (which they did by signing the Advice of Change).

Given the dollar materiality of many of the change orders, we believe it is important to document why the PRC approved the change order in case anyone were to question the approval at a later point in time. We realize that the Special Services Department usually provides documentation as to why the change order is being requested; however, this documentation in and of itself does not explain how the PRC makes its decision.

Recommendations:

1. If the Administrative Assistant in the Purchasing Division is unable to attend a PRC meeting, the PRC obtain the services of an Administrative Assistant in another division to take the minutes. These minutes should document how the PRC reached its decision that the contractor was entitled to the change order. (Note: Administrative Services has decided on an alternative to this recommendation. See below.)
2. The PRC evaluate and clarify the procedure which states that the PRC “... will hear and respond to requests for contract/project amendments/change orders, add-ons, and overruns.” That is, is it really the intent of the PRC to review every single change amendment, change order, add-on, and overrun? Also, do users reading the policy really understand what each of these terms mean? The current policy does not provide a dollar threshold for requests nor does it exclude any

- particular requests; however, we have already been told by the Purchasing Manager and the Chief of Administrative Services that the PRC only reviews items for capital projects.
3. Management inform County Council that they are welcome to attend a PRC meeting if they have questions on the role and responsibilities of the PRC.

Response from Administrative Services Management

Written minutes will be discontinued and replaced with the following: Purchasing will see that all correspondence and notes regarding the approval of a change order will be scanned and attached to the appropriate purchase order. All information pertaining to each change order will be available via the online document in Tier.

Audit Objective #3: Evaluate departmental written policies and procedures for change orders, particularly for construction contracts.

Comment # 3: Develop written policies and procedures for initiation, approval, and processing of change orders.

Overall, we believe that the Special Services and Administrative Services Departments need to develop better policies and procedures for the initiation, approval, and processing of change orders. The lack of comprehensive, documented policies and procedures increases the risk that change order activity may not be managed in the best interest of New Castle County. We reviewed several publications on construction contracts, as well as the purchasing manuals for a few municipalities, and have several suggestions for improving the existing policies and procedures regarding change orders. We believe the Administrative Services Department should establish an enterprise policy for change order management and that each individual department (particularly Special Services) that manages contracts should have its own written policies and procedures. The departmental policies and procedures should include sufficient detail for project managers and staff to properly administer change orders in accordance with management's directives.

Existing Written Documentation on Change Orders

We looked in the County Code and County policies and procedures for language concerning change orders and found the following:

- A. New Castle County Code, Chapter 2, Article 5, Section 2.05.303, "Purchasing of Contract Construction", deals with the purchasing of contract construction by the County's Department of Special Services. This section contains the following language (2.05.303, D.16) regarding add-ons and overruns on Special Services contracts:

- “The County Executive may establish administrative policies to limit the allowable add-ons and overruns on special services contracts exceeding fifty thousand dollars (\$50,000.00) as originally executed. Such add-ons and overruns will only be allowed to account for differences between the construction specifications and drawings and actual conditions encountered during the execution of the contract.” Except for items B and C below, we did not see any written policies and procedures relating to change orders.
 - “In no case shall additional work be added to a special services contract exceeding fifty thousand dollars (\$50,000.00), as originally executed, which is not within the scope of the original special services contract. The Law Department shall determine if work is within the scope of the original special services contract. If it is not, the additional work must be contracted for pursuant to subsection (D) (1) of this Section.” (which deals with competitive bidding on contract construction)
 - “When contracts are let for less than fifty thousand dollars (\$50,000) but due to add-ons and overruns exceed that limit, the excess must be bid unless otherwise determined by the County Executive.”
- B New Castle County Purchasing Manual, Section XV., Part B: “In order to amend a Purchase Order, an Advice of Change must be sent to Purchasing.” The Manual then goes into a detailed process for processing an Advice of Change on the Purchasing System. We did not see any other procedures in this Manual for change orders.
- C Administrative Services Policy #42, “Purchasing Review Committee, Emergency Purchases, and Legal Review”: This policy, addressed earlier in this report, provides the following definitions:
- “Add-ons and overruns are expenditures that exceed the original encumbered amount.”
 - “A change order, as defined for this Policy, is any change or amendment to a purchase order that is within the scope of the work, dollar amounts, or both.”

Recommendations:

We recommend that the Special Services and Administrative Services Departments develop additional written policies and procedures for the initiation, approval, and processing of change orders. These policies and procedures should address the following items:

1. Definitions of “change order”, “add-on”, and “overrun.” For example, does a change order include a change in the scope of the original contract, or is a different term used for this?
2. A standard change order form for all County departments to use. Our testing within Special Services revealed that there is more than one form being used for a change order.
3. The general information a contractor is required to submit when submitting a change order for approval.
4. The documentation required by the Purchasing Review Committee (PRC) when reviewing a change order request.

5. The general methodology the authorized individuals follow when deciding whether or not to approve a change order. (e.g., in Special Services, does the individual independently verify the reasonableness of any unit prices used?)
6. How the Law Department, per County Code, determines and documents if the change order is "... within the scope of the original special services contract." A representative of the Law Department is on the PRC, so this is where we assume this process is occurring.
7. A requirement that work should not proceed on the project until the change order has been properly approved. (Note: If there are situations where work can proceed upon verbal approval, these situations should be specified in the policies and procedures.)

Response from Special Services Department Management

The Special Services Department concurs with this recommendation.

Audit Objective #4: Evaluate the Project Cost Reports for the Public Safety Building as well as the use of a Construction Manager and an Owner's Representative for this project.

Comment # 4: Evaluate, in the future, possible duplication in contracts.

The County engaged a Construction Manager (Gilbane Building Company) and an Owner's Representative (Remington Group Inc.) for the Public Safety Building Project. Also, Tevebaugh Associates was the architect for the project and was involved in many management decisions. At a County Council meeting dated 7/12/05, the then Chief of Special Services introduced a representative from Remington and explained what their role would be on the project. He said Remington would be reviewing invoices, reviewing change orders, reviewing construction work, and serving as the project manager for New Castle County. One of the County Council members questioned the need to have both a Construction Manager and an Owner's Representative. The Council Member, based upon his experience in the construction industry, said he thought the Construction Manager should already be fulfilling the role the Owners' Representative was hired for. The then General Manager of Special Services said he needed a dedicated resource to New Castle County because none of his internal project managers had the time to devote to this project. He also said he thought the expected cost savings from having Remington negotiate on items during the project should offset the cost the County would incur in hiring Remington.

The actual costs paid to Gilbane and Remington for the Public Safety Building Project (as of 7/15/08) were as follows:

- Gilbane: \$2,778,480 of total purchase order of \$2,823,661.
- Remington: \$892,486 of total purchase order of \$916,500.

We reviewed the contracts for both Gilbane and Remington and found apparent similarities in the work required of each company. Thus, there appears to be duplication of work and we can't help but question whether some of Remington's services were already included in the contract with Gilbane. Examples:

- Budgeting and Reporting:
 - Gilbane: "... prepare preliminary estimates of construction cost ... provide a preliminary evaluation of the Owner's program, schedule, and construction budget requirements ... monitor the approved estimate of construction cost ... show actual costs for activities in progress and estimates for uncompleted tasks by way of comparison with such approved estimate ... develop cash flow reports and forecasts for the Project and advise the Owner and Architect as to variances between actual and budgeted or estimated costs ... maintain accounting records on authorized work performed under unit costs, additional work performed on the basis of actual costs of labor and other materials, and other work requiring accounting records ... shall submit written progress reports ..."
 - Remington: "Prepare an initial project budget ... Review project budget with client and modify as necessary ... Prepare monthly written reports which provide the status of the project: ... Cost Update ..."
- Scheduling:
 - Gilbane: "... shall prepare and periodically update a Project Schedule for the Architect's review and the owner's acceptance ..."
 - Remington: "Develop an initial Project Schedule for all work required to complete the project. This will be an overall Project Schedule and will incorporate the Construction Manager's more detailed schedule ... Update Schedule on a regular basis indicating the progress to-date and projected final completion date."
- Construction:
 - Gilbane: "... shall endeavor to obtain satisfactory performance from each of the Contractors. The Construction Manager shall recommend courses of action to the Owner when requirements of a contract are not being fulfilled."
 - Remington: "Monitor the progress of construction work to determine if work is proceeding in accordance with the contract documents."
- Contractor Change Orders and Payments:
 - Gilbane: "... shall develop and implement procedures for the review and processing of applications by contractors and final payments ... shall review and certify the amounts due the respective contractors ..."
 - Remington: "Review and approve contractors' applications for payment ... Review and negotiate change orders as necessary."
- Meetings:
 - Gilbane: "... shall schedule and conduct meetings to discuss such matters as procedures, progress, and scheduling."
 - Remington: "Coordinate and conduct regular Project Meetings with contractors, designer, and client."

During the project, Remington periodically provided to the Administration and County Council a "Savings and Cost Avoidances" report. The final report provided by

Remington identified “Total Savings to Date” of \$4,439,221. We have the following observations on this report and on Remington itself:

- Remington claims \$1,566,321 in cost savings on the re-bid of six contracts. The identified savings for each contract is the difference between the original lowest bid and the lowest re-bid. A note on the report indicates that “The Project Team pushed for these contracts to be re-bid due to budget constraints ...” Thus, we don’t believe Remington can claim full credit for these costs savings (since the note credits the whole Project Team). Special Services management informed us that these contracts would have been re-bid whether Remington was involved or not because the original bids exceeded the engineers’ estimates.
- Remington takes credit for a \$365,000 grant that was received from the Department of Homeland Security. In reality, this grant was due solely to the efforts of the Public Safety Department. Remington also takes credit for another grant of \$25,000 which also was due solely to the efforts of County personnel.
- For all other items on the “Savings and Cost Avoidances” report, Special Services management informed us that it is difficult to ascertain how much of the savings are directly attributable to Remington’s efforts since the entire Project Team (Gilbane, Remington, Tevebaugh, and Special Services) discussed requests for change orders in their weekly meetings.
- Our observations during the audit revealed that the Fiscal Unit had to spend a great deal of time with the Remington staff person in reconciling Remington’s numbers to New Castle County’s. This appeared to be due to the inexperience of the staff person Remington assigned to the job. As a result, the periodic Project Cost Report provided by Remington to Council was not always ready on a timely basis. We believe that the County should not have had to spend so much time with Remington in reconciling the numbers.

Recommendation:

It is not our intention to minimize the work of the Owner’s Representative or the Construction Manager. Rather, we merely want to point out that (1) the cost savings on the “Savings and Cost Avoidances” report were not entirely attributable to Remington Group, “Savings and Cost Avoidances” report and (2) the County may have been able to save money by (a) specifically assigning work to one or the other of these two companies – not both, or (b) hiring a full-time project manager internally to fulfill Remington’s role.

In the future, we recommend that Special Services management attempt to minimize instances in which contracts for a single project include apparent duplications in the contracts for two or more entities.

Response from Special Services Department Management

The Special Services Department will try to minimize duplications in contracts related to a particular project. As noted above, the Public Safety Building project was unusual and the department does not foresee the need to duplicate the same management structure (construction manager and owner’s representative) on future projects.

Audit Objective #5: Discuss with the Special Services Department the recent review performed by an outside law firm of the standard language in construction contracts.

Comment # 5: Re-evaluate need to have “right to audit” clause in County’s standard contracts.

In our “Audit of the Procurement Function”, report dated 2/12/07, we were informed that the County would be engaging a law firm to assist in reviewing the terms and conditions of the standard County construction contracts, professional services contracts, and goods/materials contracts, and to recommend revisions to such contracts based upon current law and best practices. In that audit, we recommended that the law firm determine whether adding a “right to audit” clause to County contracts would be beneficial in any particular situations. During that audit, we had performed research which indicated that a “right to audit” clause would help to better protect the County’s interests in certain situations. We provided information on “right to audit” clauses to the Chief of Administrative Services and to the Chief of Special Services. For example, a textbook titled “Auditing the Purchasing Function” states that a “right to audit” clause is important if a contract includes any aspect of self-reporting by the vendor where no independent confirmation is practical (e.g., contracts based on cost of labor and materials). The right to audit the vendor should not be limited to using a mutually agreed upon third party; instead, the clause should give the buyer unlimited choice as to who can be chosen as auditor. The audit provision should also, if applicable, include a “flow down” clause that requires the prime contractor to include a right to audit provision in all contracts with subcontractors.

At the time of the Procurement audit, the Chief of Administrative Services and the former General Manager of Special Services did not believe a “right to audit clause” was necessary because:

- Many contracts provide protection to the County by requiring a performance bond.
- Management scrutinizes vendor change orders.

Recommendation:

The law firm performing the Contract Review Project agreed that a “right to audit” clause should be included in the County’s standard contracts and provided the County with suggested language. We recommend that the Special Services Department include this (or similar) language in its standard construction contracts. We also recommend that the Special Services and Administrative Services Departments evaluate, and implement if beneficial, all suggestions provided by the outside law firm.

Response from Special Services Department Management

The Special Services Department plans to implement suggestions provided by the outside law firm. The law firm has assisted the department in updating its standard specifications and special services construction contracts. The firm has also assisted in developing new professional services contracts. The right to audit clause has been added to professional services contracts and will be added to Special Services construction contracts (still in the process of revising the overall format for these contracts).

Audit Objective #6: Evaluate the controls over contractor payments; in particular, the controls over ensuring that payments made are in accordance with the work completed.

We selected a random sample of payments to contractors from the purchase order files relating to the change orders we selected in our change order testing. Each sample item was inspected for the appropriate payment form and for the appropriate signatures. Overall, our testing revealed that internal controls over contractor payments were functioning as intended.

A response to this conclusion is not necessary.