



August 12, 2020

To: Finance and Administration Committee

From: Darrell E. Johnson, Chief Executive Officer

Janet Sutter, Executive Director
Internal Audit Department

Subject: Oversight Controls and Contract Compliance Related to the Interstate 5 Project: State Route 55 to State Route 57, Internal Audit Report No. 20-510

Overview

The Internal Audit Department of the Orange County Transportation Authority has completed an audit of oversight controls and contract compliance related to the Interstate 5 Project: State Route 55 to State Route 57. The Internal Audit Department found compliance with project management procedures and evidence of project administration, management, and oversight controls, including risk assessment controls. Procurements and amendments were handled in accordance with procurement policies and procedures, contract deliverables were received, and invoices were generally paid in compliance with contract provisions, policies, and procedures. However, the Internal Audit Department made one recommendation to improve review of the construction management consultant's invoices.

Recommendation

Direct staff to implement the recommendation provided in Oversight Controls and Contract Compliance Related to the Interstate 5 Project: State Route 55 to State Route 57, Internal Audit Report No. 20-510.

Background

The project will add a second high-occupancy vehicle (HOV) lane in each direction of Interstate 5 (I-5) from State Route 55 to State Route 57. The HOV lanes will be striped for continuous access, and the existing median barriers between the HOV and general purpose lanes will be removed, except from locations where bridge columns necessitate leaving the barriers in place. The

project also includes demolition of the existing I-5 HOV drop-ramp at Main Street. The current budget is \$38,119,000, and the forecast at completion cost is \$41,488,00. The project is funded with federal dollars, including Congestion Mitigation and Air Quality funds and Measure M2.

Discussion

The Internal Audit Department (Internal Audit) found that staff's review of construction management consultant invoices could be improved with regard to monitoring of labor rate escalation, other direct costs support, and billing of first-tier sub-consultants. Consultant staff billing under labor classifications are supposed to be paid at actual rates, with annual increases limited to the contract escalation rate; however, several staff were invoiced at rate increases exceeding the contract escalation rate, and two staff were invoiced at escalated rates that were higher than their actual pay rates. In addition, the consultant billed certain other direct costs at the unit rates estimated in the contract schedule without providing supporting documentation. The contract states that the unit rates are estimates and that items should be paid at cost with supporting documentation. Finally, two first-tier sub-consultants have been billed by other sub-consultants, as their sub-consultant or as other direct costs, and at rates that do not agree to the contract schedule rates. Internal Audit recommended that management add a step on reviewing labor rate escalation to its invoice review checklist, require cost documentation for invoiced other direct costs, and require the consultant to bill all first-tier sub-consultants based on their contract rate schedules. Management agreed and indicated that items noted in the recommendation are currently being implemented.

Summary

Internal Audit made one recommendation to improve review of the construction management consultant's invoices.

Attachment

- A. Oversight Controls and Contract Compliance Related to the Interstate 5 Project: State Route 55 to State Route 57, Internal Audit Report No. 20-510

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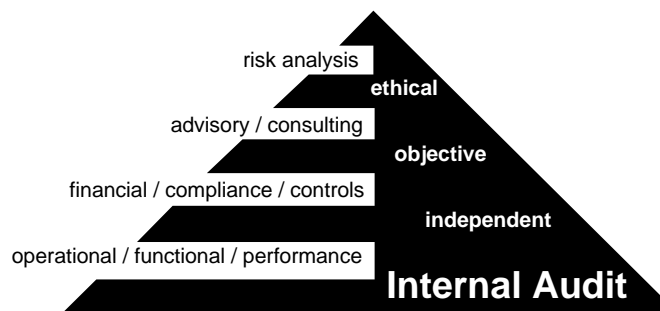
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Oversight Controls and Contract Compliance Related to the Interstate 5 Project: State Route 55 to State Route 57

Internal Audit Report No. 20-510

July 29, 2020



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Conclusion

The Internal Audit Department (Internal Audit) of the Orange County Transportation Authority (OCTA) has completed an audit of oversight controls and contract compliance related to the Interstate 5 (I-5) Project: State Route 55 (SR-55) to State Route 57 (SR-57). Based on the audit, we found compliance with project management procedures and evidence of project administration, management, and oversight controls, including risk assessment controls. Procurements and amendments were handled in accordance with OCTA procurement policies, and procedures and contract deliverables were received. Invoices were generally paid in compliance with contract provisions, policies, and procedures; however, one recommendation was made to improve review of the construction management consultant invoices.

Background

I-5 Project: SR-55 to SR-57

The project will add a second high-occupancy vehicle (HOV) lane in each direction of the I-5 from the SR-55 to the SR-57. The HOV lanes will be striped for continuous access, and the existing median barriers between the HOV and general-purpose lanes will be removed, except from locations where bridge columns necessitate leaving the barriers in place. The project also includes demolition of the existing I-5 HOV drop-ramp at Main Street.

The current budget is \$38,119,000, and the forecast at completion cost is \$41,488,00. The project is funded with federal dollars, including Congestion Mitigation and Air Quality (CMAQ) funds, and OC Go (i.e., Measure M). OCTA was the lead agency during the environmental and design phases, and the California Department of Transportation (Caltrans) is the lead agency during construction.

Contracts

OCTA has the following agreements related to the I-5 Project from SR-55 to SR-57:

- Agreement No. C-0-1785 with AECOM Technical Services, Inc., to develop an approved Project Report and Environmental Document (PR/ED), paid on a firm-fixed price basis with an amended maximum obligation of \$1,477,235;
- Agreement No. C-4-1778 with T.Y. Lin International, to prepare plans, specifications, and estimates (PS&E), paid on a firm-fixed price basis with an amended maximum obligation of \$3,765,988;
- Agreement No. 7-1834 with TRC Engineers, Inc. (formerly Caltrop Corporation, a TRC Company), to provide construction management (CM) support services, paid on a specified rate of compensation basis with a maximum obligation of \$3,508,520;

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- Agreement No. C-5-3207 with Hill International, Inc., to assist in developing and implementing a public communications and community outreach plan, paid on a time-and-expense basis with a maximum obligation of \$401,362.
- Agreement No. C-1-2728 with Caltrans, to outline the terms and conditions of cooperation to provide independent quality assessment;
- Agreement No. C-4-1841 with Caltrans, to assign responsibilities for PS&E and right-of-way support;
- Agreement No. C-7-1817 with Caltrans, to assign obligations and responsibilities to complete construction;
- Agreement No. C-6-1574 with Southern California Regional Rail Authority, to establish terms, conditions, and funding responsibilities toward completion of services for PS&E; and
- Agreement No. C-7-2031 with City of Santa Ana, to define terms, conditions, and funding responsibilities for completion of final design and construction.

Project Administration, Oversight, and Monitoring

The Program Management Procedures serve to effectively manage and monitor capital projects, identify responsibilities, and address project schedules and budgets, and Project Management Plans. Risks related to the project are identified, monitored, and documented in the risk assessment registers of the Project Management Plan.

During the environmental and design phases, monthly Project Development Team (PDT) meetings were held. During the construction phase, weekly status meetings are held in the field office, with some attendees calling in through Skype due to the coronavirus (COVID-19). During monthly meetings with Caltrans, the project manager (PM) receives monthly construction progress reports for the I-5 Project: SR-55 to SR-57. The Project Controls section prepares monthly status reports and schedules for all active capital projects, and posts these documents to the intranet.

The Capital Programs Division provides quarterly progress reports on the Capital Action Plan performance metrics to the Board of Directors (Board). Quarterly Measure M2 progress reports are also provided to the Board. These reports include reporting of the I-5 Project: SR-55 to SR-57.

Procurements are governed by the Contracts Administration and Materials Management (CAMM) Department's procurement policies and procedures, and CAMM maintains evidence of procurement compliance in the agreement files. When consultants request amendments to their contracts, the PM determines if their request is based on additional work outside of original projections.

The PM reviews the design and CM consultant invoices to determine if billings reflect services received and are within budget before approving the invoices. The Project

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Controls staff reviews consultant invoices using an invoice review checklist. For the design consultant invoices, a Project Controls staff checks if the percentage completion does not exceed 100 percent and the values are consistent with the task pricing. For the CM consultant invoices, the Project Controls staff checks if the labor rates are consistent with the contract, invoiced labor hours are adequately supported, and other direct costs (ODC) are based on contract rate schedules and adequately supported. The public communications consultant invoices are reviewed by the contract PM in External Affairs, who determines if billed labor rates are based on the contracts, labor hours are reasonable, and ODC are supported with receipts or other documentation.

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Objectives, Scope, and Methodology

The objectives were to assess project administration and oversight internal controls, and evaluate contract compliance with the contracts for design, CM, and public communications.

According to generally accepted government auditing standards, internal control is the system of processes that an entity's oversight body, management, and other personnel implement to provide reasonable assurance that the organization will achieve its operational, reporting, and compliance objectives. The five components are control environment, risk assessment, control activities, information and communication, and monitoring.¹ The components and principles that were evaluated as part of this audit are:

- Control Environment
 - OCTA demonstrates a commitment to attract, develop, and retain competent individuals in alignment with objectives.
- Risk Assessment
 - OCTA identifies risks to the achievement of its objectives across the entity, and analyzes risks as a basis for determining how the risks should be managed.
- Control Activities
 - OCTA selects and develops control activities that contribute to the mitigation of risks to the achievement of objectives to acceptable levels.
- Information and Communication
 - OCTA obtains or generates and uses relevant, quality information to support the functioning of internal control.
- Monitoring
 - OCTA evaluates and communicates internal control deficiencies in a timely manner to those parties responsible for taking corrective action, including senior management and the Board, as appropriate.

The methodology consisted of testing procurements and amendments for compliance with selected procurement policies and procedures, testing receipt of selected contract deliverables, testing the monthly Project Controls status reports and quarterly reports to the Board for evidence of project status reporting to management and the Board, assessing invoice review procedures and testing invoices paid for contract compliance and evidence of controls, and testing certain project management documentation, including a Project Management Plan and risk assessment register, for compliance with procedures. The methodology also included testing evidence of project administration and oversight controls, including review of the minutes for the PDT and construction status meetings, and receipt of Caltrans monthly construction progress reports.

¹ See U.S. Government Accountability Office publication, "Standards for Internal Control in the Federal Government," available at <http://www.gao.gov/products/GAO-14-704G>, for more information.

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The scope is limited to the I-5 Project: SR-55 to SR-57, and included the procurements and amendments for the design, CM, and public communications contracts, and excluded the PR/ED contract. The scope included all invoices paid from inception and all status meetings. The scope also included select contract deliverables for the design and public communications contracts and selected requirements from the Program Management Procedures. The scope also included status reporting presented or posted in the last two years. The judgmental sample of status reporting was selected to provide coverage of the more recent activity. Since the sample is non-statistical, any conclusions are limited to the sample items tested.

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.

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Construction Management Invoice Review

Consultant personnel billing under labor classifications are subject to a maximum 2.5 percent annual escalation rate per the contract. Several sub-consultant personnel billing under labor classifications were invoiced at rate increases exceeding the 2.5 percent contract escalation rate. Additionally, the consultant billed two inspectors for two weeks and four months, respectively, at escalated rates that were not supported by current payroll registers (i.e., the inspectors had not actually received pay increases), resulting in \$1,903 in over-billings.

Every month, the consultant bills \$1,768 for two copy machines, high speed internet, server, software, desk phones, and desk phone lines, at unit rates estimated in the contract Schedule II-ODC Schedule (Schedule II), without supporting documentation. Schedule II states that the unit rates reflected are estimates and that costs will be reimbursed at actual cost upon submission of supporting documentation. Without supporting documentation, OCTA staff cannot determine whether these items are being billed at actual cost.

Finally, there are two first-tier sub-consultants that have been billed by other sub-consultants as a second-tier sub-consultant, or as an ODC, at rates that do not match the contract schedule rates. These two sub-consultants have contract schedules that establish rates for their personnel; however, these rates were not used when other sub-consultants billed one as a second-tier sub-consultant and billed another one as an ODC.

Recommendation 1:

Internal Audit recommends that management add a step to review labor rate escalation in its invoice review checklist. Internal Audit also recommends that management require cost documentation for ODC, and request the consultant to bill all first-tier sub-consultants based on their contract rate schedules.

Management Response:

Management agrees with the recommendation, and items noted in the recommendation are currently being implemented. The invoice review checklist has been revised to add an additional step to include labor rate escalation review. Invoiced labor rate escalation is currently being reviewed.

Management had previously identified the first-tier sub-consultant billing issue, and this was corrected with the consultant's April 2020 invoice. There was no increased cost to OCTA based on the previous sub-consultant billings.

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Management will be seeking recovery of the \$1,903 in over billings due to the incorrect application of the contract's 2.5 percent annual labor escalation factor.