

## Recommendations for a risk based bond expenditure review process

- Adopt a risk based bond expenditure oversight policy. Identify the areas with the highest observed risk and devote CGOBOC audit and reporting resources to the high-risk areas first. If you understand the operating environment for City construction projects you can identify the potential risks.
  - i. **High-risk areas.**
    1. Project construction costs are often awarded to the low-cost bidder so the City is paying market rate for construction costs. Contractors game the low-cost bidding process with a low bid and work at recovering project profit margins through excessive change orders.
    2. The City of San Francisco does not have a City-wide policy for processing construction change orders and CSA construction audits have found weak processing controls over project change orders.
      - a. You might want to ask the Controller why there is no City-wide policy or set of procedures for processing construction change orders.
      - b. Each bond expenditure audit should include testing of controls over project change orders.
        - i. The \$887 million S. F. General Hospital rebuild had 607 change orders.
        - ii. The \$244 million Public Safety Building had 389 Charge Orders.
          1. A CSA construction audit found that DPW did not document charge orders over \$20,000 as required by department policy.
          2. A CSA construction audit found that DPW did not prepare the required independent cost estimates for change orders over \$20,000 and lacked negotiating leverage when the contractor submitted revised costs.
        - iii. Smaller projects like the North Beach and Bayview Branch libraries which cost about \$14 million had 116 and 102 change orders.
    3. Manage project change order risk by reporting and monitoring project change orders by change order type.
      - a. Project sponsor change orders- project sponsor changes the project scope of work. Project sponsor change orders for the

Public Safety Building physical security were issued when a new sheriff wanted changes to the existing project specifications. What was the cost of these project sponsor change orders? Were these change orders visible to CGOBOC?

- b. Error and omission change orders- contractor change orders that address DPW design errors or project specification that were omitted from the bid package. Is DPW limiting these type of change orders to 3% of project cost, their internal goal?
  - c. Unforeseen site or building condition change orders do occur especially when renovating old buildings.
  - d. Change orders due to a change in regulatory requirements.
4. Project architecture and design, project soft costs are not purchased through a low-cost bidding process, City departments are required to use DPW and DPW lacks an incentive to control these costs.
- a. Project management, construction management and design costs for curb ramps in the RRSS audit report were 29% of total project cost. Cumming's cost management department opined the cost should be 50% lower, 11-14% of total cost.
  - b. Design costs for the ESER project were \$30.6 million or 16.1% of total project cost. Cumming's cost management department opined that the costs should be 8-10% of total project cost. **If design costs were 8-10 % of total project cost the savings would be between \$11.6 million and \$15.3 million for design costs only!**
    - i. How much did DPW overcharge the project for project management and construction management?
  - c. An independent outside audit that focuses solely on DPW architecture and engineering fees should be scheduled soon since all general obligation bond funded projects incur project management, construction management and design costs and the Cumming construction audits found that DPW costs should be 50% lower.

- d. In the ESER audit \$100,000 of Microsoft project management software was charged to the project. The audit report said the charge was abated and charged to DPW. Was this reported as an audit finding?
5. Bond Pre-authorization costs
- a. The current process allows for pre-bond costs to be reimbursed with no approval from entities outside of Public Works. This policy needs to be changed.
  - b. In the ESER audit, Cumming found that \$550,000 of expenditures originally expended on the Justice Facilities Improvement Program were reimbursed with ESER funds and charged to pre-bond reimbursement.
    - i. Finding #2 in the 2011 Road Repaving and Street Safety Bond highlights \$1.6 million of Bureau of Urban Forestry labor that was transferred to the project. Cumming stated, "Since the bond program essentially provided supplemental funding to scope of work already being performed by Public Works, pre-bond expenditures should be monitored and approved by entities outside of Public Works to ensure they are being used for their intended purpose". This finding appears to state that DPW administrative costs were reimbursed with bond funds which is not allowable.
    - ii. Reimbursement Guidelines were established under the 2014 ESER GO bond. CGOBOC should review the 2014 ESER GO Bond Pre-Bond Reimbursement Guidelines to ensure that they are adequate.
    - iii. Why are these guidelines not applied to all GO Bond funded projects?
6. Manage changes in project scope through better reporting. The road repaving and street Safety audit report disclosed that there was an 8% reduction in the number of blocks of road repaved. Why was this necessary and how was the project scope reduction implemented? The citizens of San Francisco are entitled to this information.

7. Manage the transfer of project cost or bond funding between projects, this happens frequently with Recreation and Parks projects.
  - a. This needs to be more fully disclosed. Why can't excess bond funds remain unspent?
  - b. Why should excess bond funds be transferred to other projects that were not approved by the citizens of S. F.?
  
8. CGOBOC needs to be proactive in establishing management reports that highlight potential construction project risk.
  - a. DPW has an excellent report that captures project key performance indicators (KPIs). All you need to do is request the report for general obligation bond funded projects.
    - i. Construction project delays. DPW has a good report that captures the change in days and the percentage change in elapse time.
    - ii. Changes in project cost amount and the percentage change.
    - iii. Change orders by project.