



Seattle Public Schools Office of Internal Audit

Internal Audit Report Construction Management Practices

Issue Date: December 5, 2017



Internal Audit Report

Construction Management Practices

Introduction and Background

In accordance with the fiscal year 2018 capital audit plan, we have completed an audit of the district's construction management practices. Construction related audits are designed to strengthen financial controls around some of the district's largest expenditures and make recommendations that increase effectiveness, efficiency, and accountability.

Project Delivery Methods

For public owners in Washington State, there are three project delivery options available for large public works projects, design-bid-build (DBB), general contractor/construction manager (GCCM), and design-build (DB). Job order contracting (JOC), which is designed to speed up work using an on-call contractor, is also an alternative method, but it is used for small projects.

The legislature first authorized GCCM in 1991. At that time, GCCM was reserved for the Department of Corrections to accelerate the construction of prisons due to overcrowding. Beginning in 1994, additional state agencies, cities, counties, ports, public utility districts, and hospital districts were also authorized; school districts were authorized to use alternative public works procedures in 2000.

To deliver its large construction projects, Seattle Public Schools primarily uses DBB, which remains very effective for public and private projects. The district currently has three GCCM projects in design or construction that are estimated to cost approximately \$178 million over the next three years.

GCCM as an Alternative Competitive Process

If a project meets certain criteria, a public body may use an alternative project delivery method. A project review committee was created in 2007 under the purview of the state's Capital Projects Advisory Review Board (CPARB) to review and approve public body applications for the utilization of GCCM. The committee approves projects that meet strict state guidelines and certifies entities to use GCCM for three years if they have sufficient experience and staff who can successfully manage projects using the alternative procedures.

State law requires that one or more of the following be met for a public body to use GCCM:

- (1) Implementation of the project involves complex scheduling, phasing, or coordination;
- (2) The project involves construction at an occupied facility which must continue to operate during construction;
- (3) The involvement of the general contractor/construction manager during the design stage is critical to the success of the project;
- (4) The project encompasses a complex or technical work environment;
- (5) The project requires specialized work on a building that has historic significance; or
- (6) The project is, and the public body elects to procure the project as, a heavy civil construction project.

In a GCCM project, the owner contracts with an architect/engineer for project design and separately selects a GCCM as general contractor, before design is complete. The GCCM is selected based on a combination of qualifications, experience, and price. After the owner has selected the GCCM, they enter

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into a preconstruction services contract where the contractor assists with equipment selection, estimating, scheduling, etc. As the design is developed, the GCCM works with the designer to help control costs and ensure constructability.

Per state law, when construction documents are 90 percent complete, the owner negotiates the maximum allowable construction cost (MACC) with the GCCM, who assumes the risk for construction at a guaranteed price. Once the MACC is negotiated, a GCCM contract for construction is executed.

The GCCM process is designed to ensure that traditional public contracting goals such as fair competition are maintained. Although the construction contract for a GCCM project is negotiated, the construction subcontracts, which represent the largest single cost component, are still competitively bid and awarded to the lowest bidder on a lump sum basis. Additionally, if a public body cannot negotiate a satisfactory MACC with the selected firm, the public body may terminate negotiations and negotiate with the firm that received the next highest score during the selection process.

GCCM Subcontractor Procurement

Work by subcontractors can be as much as 80 to 90 percent of the total project scope of work. Subcontractors on GCCM projects are usually selected through a competitive process that awards the contract to the responsible bidder with the lowest responsive bid. However, the law allows an alternative process for early selection of mechanical and electrical subcontractors when the value of the subcontract is anticipated to exceed three million dollars. This is similar to the process for selecting a GCCM. This alternative process has been available to public bodies in Washington since 2010. However, the district used it for the first time recently. That specific procurement and the accrual of costs associated with it will be audited separately.

GCCM Self-Performed Work

GCCM firms were initially prohibited from performing any of the actual construction work on a project for which they are prime contractor. Due to subsequent changes to state laws, today they are allowed to bid on one or more subcontract work packages; this is referred to as self-performed work. Typical self-performed trades include site preparation, concrete footings, floors and walls, wall framing, drywall finish, trim and finish. To help ensure fair competition, state law places a 30 percent limit on the amount of work a GCCM can self-perform.

Audit Objectives

This audit focuses on identified high-risk aspects of the GCCM method. Subsequent GCCM related audits will further expand on these topics. Consistent with our common practice for capital audits, this audit also examines whether the district has incorporated into its procedures recent changes to public works laws, and it suggests the use of best practices where applicable.

The objectives of the audit are as follows:

1. To determine whether the district has complied with recent changes to public works statutes and whether a process exists to verify and document new procedures.



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2. To evaluate the district's GCCM process, to include subcontractor procurement, procurement and limitations on GCCM self-performed work, and general compliance with the intent of the law.
3. To offer best practices for use of GCCM and monitoring of project costs.

Audit Approach and Methodology

To accomplish the objectives, we performed the following procedures:

- Identified high-risk elements of the GCCM contracting method.
- Reviewed construction manager contract provisions applicable to audit objectives.
- Reviewed 2017 public works legislation.
- Studied a selection of Seattle Public Schools' GCCM applications and project review committee presentations.
- Examined existing statutes pertaining to the alternative project delivery methods.
- Interviewed capital and contracting services staff concerning GCCM project procedures and revisions to contract documents.
- Reviewed contract files and revised district public works contract documents.
- Reviewed studies for Washington GCCM projects.
- Researched best practices for applicable audit objectives.

Roles and Responsibilities

District management is responsible for establishing effective internal controls and complying with state laws and district policies. Internal Audit's responsibility is to test those controls, assess the district's current practices, and make recommendations for improvement. The district has a dedicated audit response function to resolve findings once audits are complete and provide status updates to the Audit and Finance Committee.

Results and Conclusions

The district has mostly complied with new public works legislation; this report contains two exceptions to that conclusion. Based on our review, the district's GCCM practices appear consistent with the intent of the laws that govern them. The audit identifies an opportunity to increase accountability as it pertains to subcontractor responsibility, recommends the district improve controls over the verification of GCCM limits on self-performed work, and offers opportunities to improve construction management practices overall.

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Findings and Recommendations

1) Compliance with New Public Works Statutes

In the 2017 regular session, the state legislature passed three bills pertaining to public works matters that directly affect Seattle Public Schools. In this audit, we determined whether the district has complied with the new legislation. Where the statutes may not provide clear direction, we determined whether the steps taken by the district align with recommended best practices.

We found the district has complied with all applicable changes except those contained in Senate Bill 5301, which added a new item to the mandatory bidder responsibility criteria. These criteria define what it means to be a responsible bidder and ensures public works contracts are awarded only to qualified bidders.

Senate Bill 5301, which applies to all projects with bid openings on or after July 23, 2017, is meant to ensure public owners do not award contracts to firms that have violated state minimum wage laws. Through a sworn statement, bidders certify under penalty of perjury that in the three-year period prior to the bid solicitation date, they have not violated minimum wage laws, as determined by a court or by the Department of Labor and Industries.

The district has updated its procedures for verifying bidder responsibility, incorporated the appropriate language into its instructions to bidders, and revised its bid form to include a sworn statement from the bidder. The sworn statement, however, does not include the place of execution. Furthermore, the district has not implemented controls to ensure a sworn statement is submitted for projects not procured through public bidding.

Recommendation

In accordance with RCW 9A.72.085, we recommend the district add the place of execution to the signature block of the sworn statement. We recommend the district create a separate sworn statement to be used for projects not procured via public bids. Consistent with other audit recommendations that may have legal implications, we recommend the district consult with legal counsel about these changes.

2) Subcontractor Responsibility Requirements

State law requires that public works contracts be awarded only to “responsible” bidders and defines the mandatory responsibility criteria. We found that the district verifies mandatory bidder responsibility criteria before awarding public works contracts and maintains documentation to demonstrate this.

As it pertains to *subcontractors*, RCW 39.06.020 states in part:

A public works contractor must verify responsibility criteria for each first tier subcontractor, and a subcontractor of any tier that hires other subcontractors must verify responsibility criteria for each of its subcontractors. Verification shall include that each subcontractor, at the time of subcontract execution, meets the responsibility criteria listed in RCW 39.04.350 (1) and possesses an electrical contractor license, if required or an elevator contractor license, if required.

The requirement to verify bidder responsibility, along with the criteria itself, must be included in every public works contract and subcontract. The district incorporates the appropriate language into its contracts but does not have a process to ensure that its contractors include this language in subcontracts.

Recommendation

We recommend the district ensure that its contractors are including appropriate bidder responsibility language in their subcontracts.

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3) Verification of GCCM Limits on Self-Performed Work

State law allows a GCCM to compete for subcontract work as long as the work is routinely performed by the GCCM; the bid opening is managed by the public body and is in compliance with statutes; and notification of the GCCM's intent to bid is included in the public solicitation of bids for the bid package. There are, however, limits on the amount of subcontract work a GCCM can perform on a project, and the district is responsible for accounting for these dollars. RCW 39.10.390(3) states:

The value of subcontract work performed and equipment and materials supplied by the general contractor/construction manager may not exceed thirty percent of the negotiated maximum allowable construction cost, unless procured as a heavy civil construction project under this chapter. Negotiated support services performed by the general contractor/construction manager shall not be considered subcontract work for purposes of this subsection.

The district does not track the amount and percentage of GCCM self-performed work to verify compliance with this limitation.

Recommendation

We recommend the district monitor the amount and percentage of GCCM self-performed work and maintain this documentation for audit purposes.

The Capital Projects Advisory Review Board (CPARB) is set to resume collecting project data from all public bodies in Washington State that use either GCCM or design build alternative public works project delivery methods; this data will include subcontracting information.

For all of its active GCCM projects, we recommend the district obtain subcontractor awards and payments to satisfy CPARB's data collection requirements.

4) GCCM Certification

The legislature first authorized the use of alternative project delivery methods in 1991. Public bodies in Washington state that wish to use GCCM must go before the project review committee for approval of an individual project or, if the public body has demonstrated the ability to successfully deliver projects using GCCM, for a three-year certification to use this method.

The district has been approved to use GCCM for individual projects many times. The district currently has three GCCM projects in design or under construction and appears to have sufficient procedures for determining when GCCM is appropriate.

Recommendation

We recommend the district apply for certification to use GCCM contracting procedures. Under its authority, the project review committee will determine whether the district has the experience and qualifications to decide which projects are appropriate for GCCM, whether the district has the capacity to properly discharge this alternative contracting procedure, and whether the district has adequately resolved audit findings on previous public works projects.

5) Construction Manager Equitable Adjustment

The district has agreed that one of its construction managers is entitled to an equitable adjustment for a change in services if the construction manager provides assistance to the district in support of an audit by an external party.

Construction project records are currently maintained in the district's e-Builder project management system. District staff have direct access to construction, accounting, and other records and should be able to fulfill document requests during an audit without significant assistance from the construction manager. Any records available to the construction manager should also be accessible by district personnel. Furthermore, it is the responsibility of the district, not the construction manager, to provide documentation and to review and respond to preliminary or final audit conclusions. These activities are part of the normal course of business for a public entity, and firms doing business with public owners should be aware of this.

Recommendation

Consistent with contracting practices for other public entities in Washington State, we recommend the district not agree to an equitable adjustment if a construction manager assists in providing access to records in support of a third party audit. We recommend district staff with knowledge of the subject matter obtain records and respond to audit findings.



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Management Response

We are reviewing your comments and will be discussing with other departments what actions we can take to implement the recommendations.