

City of Cape Coral City Auditor's Office
 Outsourced Audit of Utilities Expansion (Kessler International)
 July 2006

	Finding	Recommendation	Response
1.	Some documentation to monitor project costs was incomplete, disorganized, and not available for audit.	1. Maintain documentation sufficient to support project costs in an organized fashion and have it readily available for review.	1. Concur with the recommendation but only partially concur with the finding. City documents could have been better organized, however, no guidelines have ever been issued to the Expansion Team relating to what documents would be required for auditing purposes. The City and the Construction Manager (CM) were preparing documents for an audit similar to the previous Townsend Audit. However this investigation took an entirely different direction and the materials requested were very different from the previous audit. The City staff will meet with the City Auditor's Office to develop guidelines to ensure that the critical and essential documents necessary to the audit process are organized and stored in a manner acceptable to the Auditors Office.
2.	There was no public advertising to obtain bids.	2. Construction bids should be publicly advertised.	2. Do not concur with both the finding and the recommendation. The delivery method for the Utility Expansion Program is Construction Manager at Risk. This method was carefully evaluated and selected by staff and approved by City Council. Under this delivery method a construction team was selected through the Request for Proposal (RFP) process and approved by City Council. A contract was put together with the input and guidance of the City Attorney's Office and outside counsel. No general advertising of bids is

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			<p>required in this contract. The Construction Manager (CM) provides a Guaranteed Maximum Price (GMP) for the various work authorizations necessary to complete the entire five-year program. To accomplish this, the Construction Manager (CM) takes quotes and bids from the various subcontractors identified in the Request for Proposal (RFP). The City and the Construction Manager (CM) agreed that the Construction Manager (CM) would receive sealed bids from underground utility contractors since these underground utility contractors would be providing the major portion of the work for the projects. To provide fair and open competition among the team members, sealed bids would be appropriate.</p>
3.	Kessler found that some subcontractors had minimum requirements waived.	3. Adhere to minimum qualifications for subcontractors or document mitigating factors for waiving the requirements.	<p>3. Concur with the recommendation but do not concur with the finding. Although we had no contractual relationship with the subcontractors and were not privy to the details of their requirements we have been assured by the Construction Manager that all of the subcontractors met the minimum requirements. Our contract is with the Construction Manager and our concern is that they provide the proper insurances and adhere to the contract requirements. City staff has already implemented procedures to ensure that the</p>

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			<p>subcontractors meet their subcontract insurance requirements because it is an item used in the prequalification process.</p>
4.	<p>Bid openings were not open to the public.</p>	<p>4. Use public bidding, sealed bids, and public bid opening procedures to award contracts to contractors and subcontractors.</p>	<p>4. Partially Concur with the recommendation but do not concur with the finding. Sealed bids are appropriate and are already being accomplished. This recommendation would change the City's choice of delivery method. As discussed in Item 2, this recommended process is not required per the master contract. City representatives are always present at the sealed bid openings to ensure the process was fair and proper. The City and Construction Manager have discussed advertising for underground utility contractors in future contracts and then adding qualified subcontractors to the team. Also, if it is the desire of City Council, we can arrange to hold bid openings at City Hall so the public could attend.</p>
5.	<p>The CM increased its employees' billable rates to the City without City Council approval on projects that exceeded the Work Authorization expected end date.</p>	<p>5. The City should only pay costs for a work authorization at rates that have been approved by Council.</p>	<p>5. Concur with the recommendation but do not concur with the finding. Staff reviews all labor hours and labor rates with each invoice submittal and has insured that the rates have been properly charged. Every work authorization was submitted to City Council and approved. The package sent to Council includes all the detail of projected labor rates and detail for the entire Guaranteed Maximum Price proposal. Where a</p>

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			<p>projects contract time covered more than one fiscal year there was a rate for the current fiscal year and a projected rate for the next fiscal year. In addition, the Tier One work authorization for each fiscal year included an hourly billing rate schedule that covered personnel from all three tiers. This billing rate schedule was approved by Council with the approval of each of the Tier One work authorizations. The Master Contract may be silent on increasing the labor rates in Tier Two and Tier Three, but the actions of the proposals and approvals were clear.</p>
6.	<p>The City allowed lump sum bids from subcontractors within the gross maximum price contract with the CM.</p>	<p>6. Limit the number of lump sum bids awarded to subcontractors, focusing on actual costs with a not to exceed limit.</p>	<p>6. Do not concur with both the finding and the recommendation. This issue was briefed to City Council along with guidelines set forth by the American Society of Civil Engineers in Engineering Report 45. We are not aware of any national or local standards that discourage lump sum bids. There are many different pricing options available to owners and contractors. Where clear and concise scopes of work are present the Lump Sum pricing format is a highly utilized practice. Many of our projects incorporate different pricing schedules within the work authorization and there are valid reasons for the use of each method. The negotiated lump sum method is most appropriate and most efficient for design services. In addition,</p>

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			<p>the Lump Sum method provided the City with a simplified accounting and payment schedule which reduces the amount of paperwork that has to be reviewed with each invoice. We strongly disagree with the suggestion that we should not use lump sum line items under a unit price contract. The Florida Department of Transportation (FDOT) pays for some of the same items we do using a lump sum price. This also, is normal, standard industry practice in Southwest Florida.</p>
7.	<p>The negotiated CM labor billing rates were computed using costs specifically excluded in the "Cost of Work" according to the CM Agreement.</p>	<p>7. Ensure that negotiated billing rates are computed in accordance with the terms of the CM Agreement and recoup past overcharges paid.</p>	<p>7. Concur with the recommendation but do not concur with the finding. The labor rates were established and reviewed in the beginning of the project and inflationary adjustments of those rates in the subsequent years were reviewed by staff and approved by City Council during the yearly Tier 1 approval process. Staff checked the increase to ensure they did not exceed a labor price index issued by a leading national agency. These rates were then presented to City Council and approved at or near the beginning of every fiscal year.</p>
8.	<p>The City did not provide any documentation that cost estimates for construction prepared by the CM were reviewed or analyzed for reasonableness by City personnel.</p>	<p>8. City staff should review and document the reasonableness of cost estimates prepared by the CM.</p>	<p>8. Do not concur with the finding or the recommendation. The City, as any owner, usually relies on the design engineer to provide estimates of cost. City staff does review the engineer's</p>

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			<p>estimates which are included in the Council Agenda Package. These packages are reviewed and signed by staff and forwarded to City Council. Montgomery Watson Harza Americas (MWA) was the design engineer, and as a member of the expansion team, they provided preliminary cost estimates. These estimates proved to be very accurate when compared to the final cost of the work. Estimates are only provided as a guideline to prepare for future costs and are not part of the costs we pay. We pay based on bids and actual work completed.</p>
9.	<p>Charges to the City for Tier 2 (Design) included a 6% administrative fee charged by MWA on all subcontracts and a 6% handling fee charged by the CM (KBR)</p>	<p>9. Determine whether this double charging of administrative fees is in compliance with the contract, discontinue the practice if necessary and recoup any past overcharges paid.</p>	<p>9. Concur with the recommendation but do not concur with the finding. The City was not double charged an administrative fee. All charges for the Tier Two (design) work authorization were done in accordance with the Master Contract and per the terms of each individual work authorization. There was no double billing. In general practice, contractors are allowed to mark-up their subs quotes in order to cover their responsibility for their subs performance. There is nothing in the Master Contract that prohibits the contractors from marking up their second tier subcontractors, nor should there be. The contractors are responsible for the performance of their second tier subs. At the outset of the program it was</p>

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			<p>agreed that the Construction Manager would not be allowed to charge the 6% administrative fee on the Engineer's (MWA) 6% administrative fee. After the assignment of the contract from Kellogg Brown & Root (KBR) to Montgomery Watson Harza Constructors (MWHC), it was further agreed that the MWHC would not add a 6% administrative fee for any of the direct MWA work or its administrative fees.</p>
10.	<p>After KBR declined to obtain required bonds, MWHC became the CM and entered into a "Separate Agreement" with KBR. This practice may be in violation of Florida Statute 287.</p>	<p>10. Review the legality of the "Separate Agreement" between MWHC and KBR and if needed take steps to come into compliance with FS 287.</p>	<p>10. Concur with the recommendation but do not concur with the finding. The assignment of the Kellogg Brown & Root (KBR) contract to Montgomery Watson Harza Constructors (MWHC) was reviewed by the City Attorney's Office and approved by the City Council. This finding refers to a separate agreement between MWHC and KBR to which the City is not a party to. We have asked the City Attorney's Office to review this finding.</p>
11.	<p>Based upon the "Separate Agreement" between MWHC and KBR, MWHC added two employees to the project when they assumed the role of CM for construction and charged them to the City. According to the "Partial Assignment & Contract Amendment" language, all costs incurred as a direct result of the Assignment were to be bourn by KBR/MWHC.</p>	<p>11. If the additional employees are found by the City Attorney's Office to be outside of eligible costs due to contract language, discontinue payment and recoup past costs paid.</p>	<p>11. Concur with the recommendation but do not concur with the finding. The City does concur that if the City Attorney's Office finds that the added employees were in violation of the contract, we should recoup those costs. The City does not feel that is the case. We have documents that were sent from Montgomery Watson Harza</p>

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			<p>Constructors (MWHC) to the City at the time of the assignment indicating their intent to add two employees. One of the employees filled a position that has been vacated by a previous Kellogg Brown & Root project engineer, and the other position was scheduled to be added at some time in the future per the Construction Managers staffing plan. The staffing plan showed that as the program moved forward, staffing would increase due to the number and size of projects. Unnecessary costs associated with the added employees were not incurred.</p>
12.	<p>KBR used temporary agency labor and billed them to the City as their employees rather than as a subcontractor causing the City to incur additional costs.</p>	<p>12. Discontinue paying labor rates for subcontracted labor. The overcharges for the temporary agency labor should be recouped.</p>	<p>12. Partially concur with the finding and do not concur with the recommendation. The City agrees that temporary employees should not be billed using the same labor rates as regular (full-time) employees and adjustments will be made in future projects. Part of the issue is that temporary labor was not addressed in the Master Contract. The City disagrees with the concept of billing the temporary employees as "subcontractors." The Construction Manager (CM) provides overhead and support (such as: office space, telephone, electric, etc.) while a subcontractor is fully independent and functioning. The recommendation would be to have a separate labor multiplier for temporary employees and we will work with our</p>

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			current Program Manager to do so.
13.	Certain employee timesheets and temporary agency invoices were marked as “non-reimb” or “other- un-billable labor”.	13. Supporting documentation should be reviewed prior to payment of invoices. If ambiguous labeling is contained, the City should question the appropriateness of the costs and document any explanations.	13. Concur with the recommendation but do not concur with the finding that we were incorrectly billed. We were supplied with a breakdown of hours worked by position and reviewed that information however individual timesheets are not required. Steps have already been implemented to ensure that all back-up for invoices is provided and reviewed by staff prior to issuing any payments. Staff has requested the Construction Manager to provide an explanation for the timesheet and invoices which were marked as “non-reimb” or “other-un-billable labor”.
14.	Many of the subcontractors did not maintain the required insurance limits as specified in their contracts.	14. The City should require the CM to provide documentation that all subcontractors are insured in the contracted amounts.	14. Concur with the recommendation but do not concur with the finding. The Construction Manager should provide all documentation for insurance from the subcontractors. Although the agreement between the Construction Manager and their subcontractors is not subject to City approval, the issue of insurance is relevant to protecting the credibility of the subcontractor selection process. The City has already taken steps to ensure we have all documentation for insurance on all upcoming projects. The City has had discussions with the Construction Manager concerning an Owners Controlled Insurance Program (OCIP) which would include the Construction

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			Manager and their subcontractors.
15.	<p>Certain position titles included in the Work Authorizations for staff did not coincide with the titles contained on the invoices and/or time sheet summary.</p>	<p>15. The City should compare charged rates to those provided for in the contract and question the charging of positions that are different from the contract. Any discrepancies should be resolved and documented.</p>	<p>15. Concur with the recommendation but do not concur with the finding. The work authorizations titles and invoices should be the same. This is strictly an administrative issue and there has not been any cost impacts due to the title difference. The Construction Manager's timesheets are internal documents they use within their corporate structure, and the individuals' titles may not match the titles listed in the contract. The City will ensure that the titles used in their work authorizations, invoices and timesheets all match.</p>
16.	<p>No documentation was provided that Public Works or the CM ever analyzed the nature of the subcontractors change orders and the amounts charged.</p>	<p>16. Change orders should be reviewed and understood by both the CM and the City. This analysis should be documented.</p>	<p>16. Concur with the recommendation but do not concur with the finding. The City reviews all Project Deviation Notices (PDN's) and Change Orders in detail. There is an established process for review of PDN's and Change Orders. The Construction Manager receives the PDN request from the subcontractor and then negotiates with the sub to attain the lowest cost possible. The Construction Manager then provides the PDN and back, when applicable, to the City for review. If the City does not agree with the PDN for various reasons, such as the cost should not be charged to the City, there is insufficient backup, or the amount is not reasonable, then the PDN is rejected and sent back to the</p>

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			<p>Construction Manager with a letter explaining why it has been rejected. In some cases the Construction Manager can revise and resubmit the request and it will go through the same vetting process. If the PDN is approved, it is notated in the appropriate box on the form, signed by the Utility Extension Manager and sent back to the Construction Manager with a letter of approval. Change Orders are handled in much the same way except that Council approval is required after the Utility Extension Manager has approved the change. Once an approved PDN or Change Order is received by the Construction Manager, they issue a change order to their subcontractor.</p>
17.	<p>The original scope of work for SW3 omitted the installation of meter boxes. Multiple change orders were issued totaling nearly \$400,000 and were charged to SW2. In addition, not all costs charged to the project could be accounted for.</p>	<p>17. All costs should be carefully charged to the correct assessment area. Periodic reconciliations should be done and reviewed to ensure this is occurring. Any discrepancies found should be corrected.</p>	<p>17. Concur with the recommendation but do not concur with the finding. We agree that all costs should be carefully charged to the correct entity, but we disagree with any finding that these controls are not already in place. We have strong controls in place to ensure that the assessment areas and other entities are charged only their appropriate costs. Meter boxes for Southwest Three, additional storm drains, sidewalks, pavement widening, repair work, etc. are tracked separately and not charged to the utility assessments. The other non-assessment related costs are charged to the appropriate Public Works division</p>

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			<p>budgets using purchase orders and proper account strings. The Southwest Three meter boxes were not omitted from that assessment. They were not part of the original scope of work. The City made a change to the design for subsequent projects, which would include the installation of meter boxes as part of a program to eliminate potential cross-connections. Meter boxes were included in the Southwest Two assessment, which followed the Southwest Three project. Since the Southwest Three contract was being closed out, the Southwest Two contract provided a means for the City to have the Southwest Three meter boxes furnished and installed. The boxes, however, were not charged to the Southwest Two assessment. They merely were installed under that contract. The charges for the Southwest Three meter boxes were paid for by the Utilities Division, Water and Sewer Fund.</p>