The School District of Lee County, Florida
Internal Audit Report: Facility Construction

July 30, 2020

RSM

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TRANSMITTAL LETTER

July 30, 2020

Mary Fischer
Board Chair
The School Board of Lee County, Florida
2885 Colonial Blvd.
Ft. Myers, FL 33966

Pursuant to our approved Statement of Work dated September 23, 2019, with the School Board of Lee County, FL, we hereby present our internal audit report of the facility construction function. Our report is organized in the following sections:

Executive Summary	This provides a high-level overview and summary of the observations noted in our internal audit of the facility construction function within the Facility Development & Programming Department.
Background	This provides an overview of the facility construction function, as well as relevant background information.
Objectives and Approach	The internal audit objectives and focus are expanded upon in this section as well as a review of the various phases of our approach and the results of our audit procedures.
Observations Matrix	This section includes a description of the observations noted during our internal audit and recommended actions.

We would like to thank the staff and all those involved in assisting us with this internal audit.

Respectfully Submitted,

RSM US LLP

RSM US LLP

EXECUTIVE SUMMARY

Background

In 2018, the School District of Lee County (District) created a ten-year plan to construct ten (10) new schools in order to accommodate the exponential growth of full-time equivalent students. The construction of these ten (10) schools, along with various renovation and capital improvement projects, are managed by the Facility Development & Programming Department (FDP). As part of the District's Operations Department, Facility Development & Programming is responsible for planning, coordinating, and executing capital projects in a timely and cost-effective manner. FDP is involved throughout the life cycle of a capital project, often working with Procurement Services to develop a scope of work, project budget, and vendor solicitation package at the beginning of the process. FDP oversees the daily operations and accounting of a project, and coordinates with Construction Managers and vendors to ensure projects are being completed according to scope, on schedule and within budget.

Working to facilitate the construction of District facilities, FDP consists of the following: 1 Executive Director, 1 Director of Construction Projects Management, 4 Facility Engineers, 1 Accountant, and 1 Secretary. FDP has reported completion of sixteen (16) total projects in the last two (2) years, totaling $20,253,878 in final contract costs and $505,291 in project savings. As of May 2020, six (6) projects are either in progress or in the closeout process, including two (2) new school construction projects.

Objectives and Scope

The objective of this internal audit was to assess the design and effectiveness of the internal control structure as it relates to facility construction and whether the system of controls is adequate and appropriate for promoting and encouraging the achievement of management's objectives. Procedures included:

- Evaluation of the design of key processes and controls identified during walkthroughs through industry benchmarking, best practices and comparable client experience.
- Review and testing of source documents (procurement packages, invoices, change orders, vendor performance monitoring documents, closeout packages) for a sample of ongoing and recently completed construction projects.
- Development of recommendations for process and control modification / addition / deletion for any design gaps or non-compliance issues identified during our analysis and testing.

The results of our procedures were shared with the District's construction project management team(s) as they were identified, and have been summarized in the pages that follow.

Overall Summary / Highlights

The individuals dedicated to the facility construction function within the Facility Development & Programming Department have established a control environment appropriate to mitigate many of the risks common to construction projects. The team has accomplished this with checklists and review procedures consistent with common industry practices. During our testing we noted observations related to the completeness of supporting documentation for invoices, negotiation of fixed cost components, and the composition of the request for qualifications selection committee.

Internal audits provide insight into an organization's culture, policies, and procedures and aids the board and management oversight by verifying internal controls such as operating effectiveness, risk mitigation, and compliance with relevant laws/regulations/policies. The observations detailed in the pages that follow represent only the instances where exceptions were noted, and do not detail the instances where testing resulted in no reportable observations.

Fieldwork was performed November 2019 through April 2020.

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Observations	3
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We would like to thank all District team members who assisted us throughout our procedures.

EXECUTIVE SUMMARY (CONTINUED)

Observations Summary

Below is a summary listing of the observations that were identified during this internal audit. Detailed observations are included in the observations matrix section of the report.

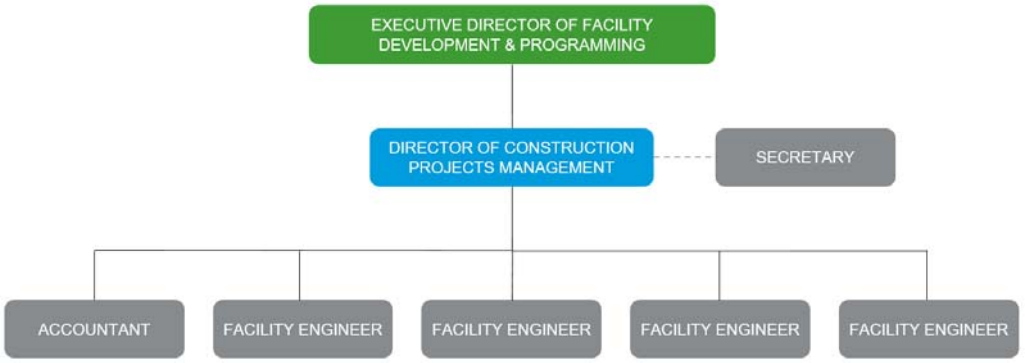
Summary of Observations
Observations
1. Pay Application Support and Record Retention Through our detailed testing of construction pay applications (invoices), we noted inconsistency in the level of documentation that was readily available to support amounts invoiced by construction contractors.
2. Negotiation of Fixed-Cost Components During our detailed testing of construction pay applications (invoices), and in conversations with Management, we noted the District sometimes negotiates with contractors to treat certain costs as lump sum, and to establish certain rates within Construction Manager at Risk (CMAR) agreements. Although these items are negotiated, Management does not maintain documentation supporting the reasonableness and methodology for determining the amount of these components, and did not modify contract language to more clearly reflect the treatment of these items.
3. Composition of Request for Qualifications (RFQ) Selection Committee Through our testing of project procurements, we noted that the current process of forming a Request For Qualifications (RFQ) Selection Committee does not require diversity in the committee.
Process Improvement Opportunities
1. Program and Project Management Software Through our testing and walkthroughs with process owners, we noted that the District currently processes all construction related documents in hard-copy form. Pay applications, change orders, contingency usages and other documents are provided to Project Managers for review, and are then scanned for electronic retention, and filed in cabinets in the office.
2. Vendor Monitoring During our walkthroughs and testing of the closeout process, we noted that although the District evaluates construction contractors after a project is complete, the results of the evaluation are not considered during procurement and assignment of future projects.

BACKGROUND

Overview

In 2018, the School District of Lee County created a ten-year plan to construct ten (10) new schools in order to accommodate the exponential growth of full-time equivalent students. The construction of these ten (10) schools, along with various renovation and capital improvement projects, are managed by the Facility Development & Programming Department (FDP). As part of the District's Operations Department, Facility Development & Programming is responsible for planning, coordinating, and executing capital projects in a timely and cost-effective manner. FDP is involved throughout the life cycle of a capital project, often working with the Budget Department to create a project budget, and Procurement Services to develop a scope of work and vendor solicitation package at the beginning of the process. FDP oversees the daily operations and accounting of a project and coordinates with Construction Managers and vendors to ensure projects are being completed according to scope, on schedule, and within budget.

Working to facilitate the construction of District facilities, the Facility Development & Programming Department consists of the following: 1 Executive Director, 1 Director of Construction Projects Management, 4 Facility Engineers, 1 Accountant, and 1 Secretary.



Current Projects*

As of May 2020, six (6) projects are either in progress or in the closeout process, including two (2) new school construction projects. According to the District's fiscal year (FY) 2020 Final Budget, $380,022,223 is budgeted for the construction of five (5) new schools, one (1) addition to an existing school, and two (2) rebuilds.

School Name	Project Description	Project Type	Contract Amount	Estimated Completion Date	Project Status
Harns Marsh Middle School	Covered Walkway	CCNA	$ 412,997	06/15/2020	In Close Out
Oak Hammock Middle School	Covered Walkway	CCNA	$ 314,064	06/15/2020	In Close Out
Transportation East - Buckingham	Berm & Drainage	CCNA	$ 57,475	06/15/2020	In Close Out
Heights Elementary School	ADA Playground	CCNA	$ 174,842	06/15/2020	In Close Out
MMM High School	New Construction	CMAR	$ 81,223,943	03/1/2021	In Progress
MM Middle School	New Construction	CMAR	$ 1,328,500	07/15/2021	In Progress

**information in this section is unaudited and was provided by Facilities Development & Programming*

BACKGROUND (CONTINUED)

Overview (continued)

Completed Projects*

Sixteen (16) projects have been completed in the last two (2) years, totaling $20,253,878 in final contract costs. In total, $505,291 was returned to the District in the form of project savings.

School Name	Project Description	Completion Date	Original Budget	DMP Tax Savings	Total Project Savings	Final Cost
Lehigh Acres Middle School	Portable Deployment	07/31/2018	$ 266,081	N/A	$ 74,770	$ 191,311
North Fort Myers Academy for the Arts	HVAC	09/05/2018	$ 2,390,700	$ 17,787	$ 17,787	$ 2,372,913
Diplomat Elementary School	Antennae Removal	05/09/2019	$ 81,536	N/A	$ 12,500	$ 69,036
Three Oaks Middle School	Kitchen Renovation	07/25/2019	$ 626,049	N/A	$ 7,306	$ 618,743
Lehigh Senior High School	Kitchen Renovation	07/25/2019	$ 353,087	N/A	$ 1,745	$ 351,342
Oak Hammock Middle School	Portable Deployment	07/31/2019	$ 81,809	N/A	$ 467	$ 81,342
Harns Marsh Middle School	Portable Deployment	07/31/2019	$ 222,993	N/A	N/A	$ 222,993
East Lee County High School	Kitchen Renovation	07/31/2019	$ 435,293	N/A	$ 27,792	$ 407,501
Harns Marsh Elementary School	Kitchen Renovation	07/31/2019	$ 405,546	N/A	$ 74,356	$ 331,190
Treeline Elementary School	Kitchen Renovation	07/31/2019	$ 261,998	N/A	$ 19,739	$ 242,259
Sunshine Elementary School	Covered Walkway	12/18/2019	$ 168,214	N/A	$ 15,463	$ 152,751
Bonita Springs Elementary	Covered Walkway	12/24/2019	$ 87,145	N/A	$ 1,686	$ 85,459
J. Colin English Elementary School	Covered Walkway	01/24/2020	$ 170,131	N/A	$ 12,000	$ 158,131
Lehigh Senior High School	Addition & Renovation	02/12/2020	$ 10,581,649	$ 67,705	$ 174,318	$ 10,407,331
Ida S. Baker High School	HVAC (Phase II)	02/12/2020	$ 4,184,127	$ 57,245	$ 65,362	$ 4,118,765
Dunbar Community School	HVAC	03/05/2020	$ 442,811	N/A	N/A	$ 442,811

**information in this section is unaudited and was provided by Facility Development & Programming*

Construction Manager at Risk (CMAR)

The District primarily utilizes the Construction Manager at Risk (CMAR) contracting methodology for construction projects. CMAR contracts are structured to compensate the Construction Manager for actual costs incurred during construction, plus a fee/profit. The CMAR delivery method is a collaborative process, as it typically allows for the procurement of a Construction Manager during the design phase to provide insights on constructability of designs in real time, and to help identify potential cost savings through value engineering. This differs from the traditional hard bid methodology of contracting that requires a design to be 100% completed prior to soliciting bids for construction work.

BACKGROUND (CONTINUED)

Construction Manager at Risk (CMAR) (continued)

The CMAR delivery method can be effective to reduce costs, create efficiencies, and improve effectiveness. The benefits of utilizing a CMAR, also come with certain associated risks when appropriate oversight is not established/maintained, such as overpaying or inappropriately paying for potentially complex areas of the cost of work, including:

- Labor and labor burden
- Self-performed work and/or related parties
- Insurance and bonds
- General conditions/requirements
- Overhead, profit, fees
- Subcontractor costs

While these risks are associated with a CMAR, the delivery method also provides greater transparency/tools to address these risks and manage the project overall. The CMAR delivery method is a best practice in construction project management.

Procurement

The District has a centralized Procurement Services Department that oversees all aspects of the District's procurement process. The District's objective is to purchase the highest quality goods and services at the lowest possible price, while maintaining compliance with School Board policies, as well as Federal and State requirements. The Procurement Services Department is responsible for managing the vendor solicitation process and coordinating with other departments to procure the goods and services necessary for the District to operate effectively.

In 2016, construction-related procurement was performed in-house by the Facility Development & Programming Department. The District's procurement function has since been restructured and centralized under Procurement Services, a sub-department of Business Services. Despite this organizational restructuring, Facility Development & Programming has remained involved in the procurement process for construction-related solicitations.

The following graphic represents the process followed for construction procurement:

Procurement Services works with FDP to develop a Request for Qualifications (RFQ) package and assist in the competitive bidding process. Procurement Services utilizes an RFQ template with standardized contract language for every solicitation, whether it is for a general contractor, architect, or building official. The standardized contract language comprises the majority of the package; however, FDP provides the scope of work and any construction-specific details such as bonding and licensing requirements. Once FDP provides the necessary information, Procurement Services assembles the package and advertises the solicitation to the public. After all RFQ submissions have been received at the bid closing date, the "Selection Committee", including representatives from Facility Development & Programming, will convene to evaluate the submittals and assign each firm a score. Each Committee Member or "evaluator" completes a standard evaluation form that outlines the required qualifications and selection criteria.

BACKGROUND (CONTINUED)

Procurement (continued)

Examples of selection criteria considered during the evaluation of proposing vendors include:

- Past experience and client references
- Project approach and resources
- Financials, litigations, and safety
- Workload
- District projects and distance to site

Using the calculated score from the evaluation sheet, each submitting firm is ranked and a "short list" is created of the top ranked firms. Firms that have been selected for the Short List move on to oral presentations where they are again evaluated, scored, and ranked in order from the highest to lowest. The final rankings from the oral presentations are presented to the School Board for approval, and FDP begins the negotiation process before the firm is awarded the contract. Facility Development & Programming serves as a subject matter expert during this process and works alongside Procurement Services during the negotiation meetings. If the District cannot come to an agreement with the highest ranked vendor, that vendor is removed from the list and the negotiation process is repeated with the next highest ranked vendor. Following award of the contract, Facility Development & Programming submits a requisition for a purchase order to Procurement Services. Procurement will then validate the requisition and create a purchase order for the contract, and FDP will issue a Notice to Proceed ("NTP") to the vendor.

The RFQ Selection Committee

The composition of the Selection Committee (Committee) varies depending on the scope of work of an RFQ; however, the Committee must be comprised of a minimum of five (5) and up to a maximum of twelve (12) District personnel. The RFQ Selection Committee's composition requirements are the same for a Continuing Contract for Professional Services (CCNA), Construction Manager at Risk (CMAR), Architectural, MEP, and Roofing Consultant Services, and Building Official Services solicitation. A representative from FDP is typically assigned to the Committee for all capital construction projects. In December 2019, Procurement Services implemented a process to assist in determining which department representatives should be included on the Committee for a given solicitation. A shared online document was created to streamline the process and help Procurement Services receive Committee recommendations more efficiently. This live spreadsheet allows representatives from each department to input their name under their respective departments or teams (i.e. Maintenance, FDP, Planning, Business Services, School Safety, Academic Services, IT, and Legal). The spreadsheet provides the project name, category (Construction Manager, Roofing Consultant, Building Official, MEP, etc.), evaluation dates, times, and locations.

As the spreadsheet is completed, Procurement Services sends a meeting invite to each name on the list. Prior to this change, emails were sent by Procurement to the various department heads requesting specific personnel or positions (i.e. Zone Supervisor) for the Committee, often requiring back-and-forth communication and coordination between Procurement and the various departments.

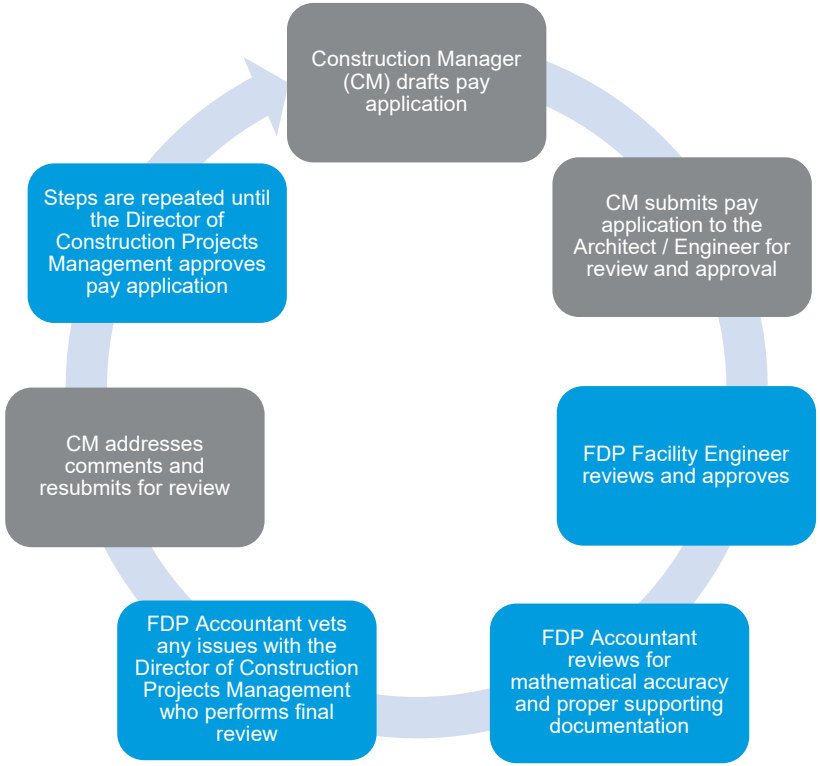
Continuing Services Contracts (CCNA)

For projects that have a total project cost of less than $2 million, the District utilizes Continuing Services Contracts to perform smaller capital projects. For continuing contracts, the District issues an RFQ and awards contracts to multiple firms under a single solicitation. For example, ten (10) firms can be awarded and kept under contract for a three (3) year period. During that time, the District can use these firms to perform small capital projects without going through the procurement process. Firms are picked for individual projects based on their position on the overall vendor list. Once the District uses each vendor once, the vendor returns to the bottom of the list and the process is repeated. If a firm cannot perform the work required for a given project, the District moves on to the next firm on the list.

BACKGROUND (CONTINUED)

Payment Applications & Invoice Review Process

A payment application or "pay application" is a detailed invoice submitted by a contractor to the owner (the District) for the purposes of receiving payment for completed work during a particular time period. Due to the complexity and cost of larger construction projects, a traditional single-page invoice does not provide a sufficient amount of detail to support the project costs claimed by the contractor. A payment application serves as the contractor's request for payment and also the architect's certification of the work completed by the contractor. The District utilizes the standard AIA (The American Institute of Architects) certified payment application, which includes a cover page (the Application and Certificate for Payment) as well as a continuation sheet (the Schedule of Values), which provides a detailed accounting of the work completed on a given project.



In order for a payment application to be approved by the owner, the contractor is required to provide documentation to support invoiced costs; however, the documentation required depends on the type of contract (i.e. Lump Sum vs Guaranteed Maximum Price or "GMP"). Examples of supporting documentation include:

- Labor reports and timesheets for supervision or labor costs
- Invoices or receipts for general conditions costs (i.e. jobsite trailers, small tools, dumpsters, construction management software, etc.)
- Subcontractor payment applications or invoices for work completed by subcontractors
- Lien waivers

Together, the AIA payment application and supporting documentation provided by the contractor form a payment application package. Each month, Facility Development & Programming reviews each of these packages as they are received from contractors. Before a pay application is approved and paid, FDP is responsible for reviewing the contractor's payment application package for completion, accuracy, and proper supporting documentation. The payment application process begins when the contractor creates a draft of a pay application, often referred to as a "pencil draw", which FDP expects to receive by the 25th day of each month. Prior to the finalization of a payment application, the Facility Engineer and/or Architect will often conduct a "site walk" or meeting to discuss the contents of the application. The purpose of this meeting is to walkthrough the progress made on the project and determine the percentage of completion for various line items included in the schedule of values. After the site walk has been completed and the payment application has been drafted, it is reviewed and approved by the Architect, who is a District agent independent of the contractor. Facility Development & Programming performs three (3) layers of review before an application is approved and processed. The Facility Engineer first performs a high-level review based on his or her unique knowledge of the daily operations of a project.

BACKGROUND (CONTINUED)

Payment Applications & Invoice Review Process (continued)

The second review is performed by the FDP Accountant, who utilizes a "Checklist for Payment Applications" to assist in the review process. The checklist is used to standardize the review process and ensure the payment application is reviewed properly and consistently. The checklist outlines eighteen (18) key review steps and five (5) administrative procedures related to the approval, processing, and filing of the payment application. While the checklist is completed and used as a guide, it does not encompass the entire review process. In general, the Accountant is reviewing for:

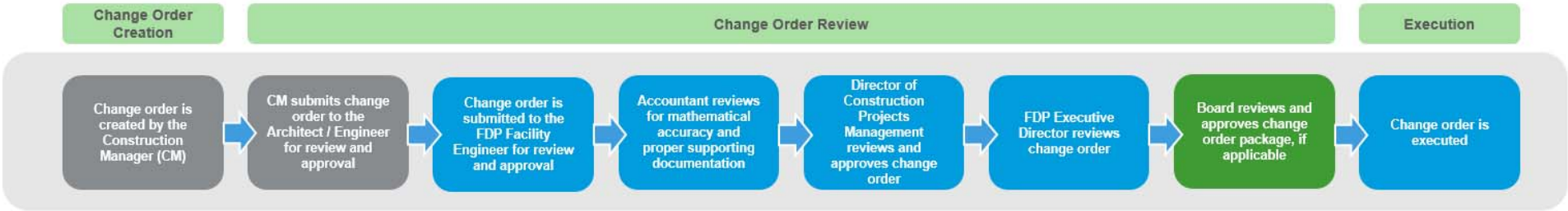
- Completion (the payment application includes all necessary line items and descriptions)
- Proper approvals or signatures (Construction Manager and Architect, if applicable)
- Mathematical accuracy (line items on the cover page and schedule of values are correct)
- Proper supporting documentation (labor reports, timesheets, vendor invoices, subcontractor invoices, lien waivers, etc.)

Errors or omissions that are identified during the review process are communicated and vetted with the Director of Construction Projects Management who performs the final review. Once the payment application is reviewed and approved by the Director of Construction Projects Management, it is sent to Finance for processing and payment. If it does not pass the review process, FDP provides comments to the contractor and returns the payment application. The process is repeated until the payment application is approved by Facility Development & Programming.

Change Order Process

Change management is a critical component in keeping capital projects in scope, on schedule, and within budget. Owners and contractors must have systems in place to adapt and deal with the various issues that arise during the construction process. Proper planning and change management controls can mitigate the risk of having to alter a contract or scope of work mid-way through a large capital construction project. In the event that a change must be made, both the contractor and owner must come to an agreement on those changes, and a formal document must be provided that details the proposed changes. A "change order" is used to document this agreement, as an official addition to the contract documents. A change order should include a description or justification for the proposed change, and supporting documentation such as vendor invoices and labor and materials breakdowns. Examples of change orders include additive and deductive changes to the original contract amount, time extensions or reductions to the project schedule, and the addition or deletion of certain scope items.

The following graphic depicts the change order process utilized by FDP:



BACKGROUND (CONTINUED)

Change Order Process (continued)

The change order process often begins with a meeting between Facility Development & Programming, the contractor, and/or architect, if applicable. As the need for a change order is identified, the contents of the change order will be discussed by the relevant parties prior to the creation of the change order document. Once the potential change has been vetted with the necessary parties, the contractor creates the change order. Before the change order is submitted to Facility Development & Programming, the architect must review the proposed changes and provide a signature on the change order document. The change is order then provided to the FDP Facility Engineer, who performs a first level review. The second layer of review is an in-depth examination of the contents of the change order, conducted by the FDP Accountant. Similar to the payment application review process, the Accountant reviews the change order for the following:

- Completion (the change order is sequentially numbered and includes all necessary line items and descriptions)
- Proper approvals or signatures
- Mathematical accuracy (contract amounts, labor and materials, overhead and profit, and sales tax)
- Proper supporting documentation (vendor invoices, purchase orders, etc.)

A "Change Order Checklist" is used by FDP as a guide to assist with the review process. If errors or omissions are identified at any point in the review process, findings will be vetted with the Director of Construction Projects Management and the change order will returned to the contractor for revision. Once the Facility Engineer and Accountant perform their reviews, the Director of Construction Projects Management performs a third review. Depending on the content of the change order, the Director of Construction Projects Management will often re-perform the procedures completed by the Accountant and assign checkmarks to reviewed items. School Board and Superintendent approval are obtained for additive change orders that increase the total project cost and/or GMP. After a change order has been approved by FDP, it is included on the contractor's next application for payment, and paid through the monthly review process.

Direct Materials Purchases & Project Savings

In general, Facility Development & Programming should aim to minimize additive change orders, as they require additional capital funds that were not originally budgeted and can cause delays in construction. However, change orders can also be used as a tool to save the District money as potential savings are identified. Change orders can be issued to deduct tax savings made possible by Direct Materials Purchases ("DMP"). As a government entity, the District can take advantage of tax-exempt status by purchasing goods and services directly from a supplier. An owner direct purchasing program allows the District to coordinate with a contractor to issue a change order to reduce the contract amount for materials purchased by the District, and associated taxes. As part of the planning process, FDP calculates the anticipated tax savings at the beginning of each project.

During construction, the Facility Engineer assigned to the project will review invoices and identify opportunities for potential tax savings. During our review of change orders, we noted that Facility Development & Programming is actively using direct materials purchases to reduce project costs. In addition to deductive change orders for direct materials purchases and schedule reductions, a change order can be issued at the end of a project if it is completed under budget and project savings are credited back to the District.

Vendor Performance Monitoring

Vendor performance monitoring is an ongoing process that involves the continuous evaluation of firms conducting business with the District. A successful vendor-monitoring program ensures that contractors are performing work that aligns with the District's values, standards, and terms of agreement. Vendor performance management is typically a function of an organization's Purchasing or Procurement Division, but is applicable to the daily operations of Facility Development & Programming. Monitoring procedures can include progress and performance reporting, the use of final evaluation forms, formal and informal meetings with contractors, and construction site visits. Facility Engineers are in regular communication with contractors and frequently visit construction sites to assess the current state of their projects.

BACKGROUND (CONTINUED)

Vendor Performance Monitoring (continued)

FDP also uses a "Construction Manager Evaluation Form" which is completed at the conclusion of a project by the Facility Engineer and incorporated into the project's closeout file. The evaluation form includes a list of eighteen (18) performance measures in which the Construction Manager is evaluated. Each line item is assigned a score based on a numbered ranking system (1-4) and the Construction Manager's final score is the average of each of the eighteen (18) elements. Examples of performance measures include:

- The accuracy and completeness of the firm's pay applications and other documents
- The firm's success at minimizing the number of change orders
- The firm's ability to complete the project on schedule
- The firm's success at completing the project within the contract price

The form is not received by Procurement Services and does not have an impact on a contractor's ability to be awarded future contracts with the District. All vendors who submit a bid for a project are evaluated based on their bid package or oral presentation only. A vendor performance-monitoring program would allow the District to differentiate high performing firms from low performing firms and factor vendor performance into future decision-making. Although the District has vendor performance monitoring procedures in place, a full-cycle program has not been implemented. Refer to Process Improvement #2 for further detail.

Project Closeout

The project closeout phase is a critical step in the construction management life cycle. Before a project can be closed, Facility Development & Programming must validate that all project components and records are satisfactorily complete. This requires the coordination between the Architect, Engineer, and Construction Manager to obtain the requisite documents needed to close out a project (i.e. Certificate of Final Completion, Certificate of Final Inspection, Certificate of Occupancy, etc.) and prepare the construction site for occupancy/use, and turnover to maintenance. A final accounting must also be performed to confirm that all contractors have been paid in accordance with their contract.

To facilitate the closeout process, Facility Development & Programming uses a "Checklist for Final Project Close Out". The checklist includes a listing of required closeout documents and brief instructions regarding where certain documents should be submitted and how many copies should be received. This checklist is the responsibility of the Facility Engineer who verifies the receipt of closeout documents from the Architect, Civil Engineer, and Construction Manager. There are fields designated for the Facility Engineer, Director of Construction Projects Management, and Secretary to provide checkmarks indicating that they have confirmed the receipt of the documents and procedures have been followed. Once all checklist items are completed, the construction site is then turned over to the Maintenance Department who takes ownership of the property.

OBJECTIVES AND APPROACH

Objectives

The objective of this internal audit was to assess the design and effectiveness of the internal control structure as it relates to facility construction and whether the system of controls is adequate and appropriate for promoting and encouraging the achievement of management's objectives.

Approach

Our approach to the audit execution consisted of the following phases:

Understanding and Documentation of the Process

To gain an understanding of the key personnel, processes, risks, and controls, we performed the following:

- Conducted an entrance conference with senior and executive management from Facility Development & Programming (FDP) to discuss the scope and objectives of the audit work, obtain preliminary data, and establish working arrangements.
- Conducted interviews with representatives from Facility Development & Programming to obtain an understanding of the District's operating policies and procedures, monitoring functions, contractual arrangements, and key documents; and
- Performed walkthroughs of the processes to validate our understanding.

Evaluation of the Process and Controls Design and Testing of Operating Effectiveness

The purpose of this phase was to evaluate the design of the key process and controls and test compliance and internal controls for operating effectiveness based on our understanding of the processes obtained during the first phase. We utilized sampling and other auditing techniques to meet our audit objectives outlined above. We conducted the following testing, and other procedures as deemed necessary.

- Evaluated the design of key processes and controls identified during walkthroughs through industry benchmarking, best practices and comparable client experience.
- Reviewed and tested source documents (procurement packages, invoices, change orders, monitoring documents, closeout packages) for a sample of ongoing and recently completed construction projects.
  - Reviewed sample RFQ procurement packages to assess involvement of FDP and composition of selection committee
  - Tested sample invoices for proper approval, supporting documentation (invoices / receipts as applicable, prime contractor lien releases, subcontractor invoices, and subcontractor lien releases), calculation of retainage, and mathematical accuracy.
  - Tested sample change orders and usage of contingency for proper approval, supporting documentation (invoices and quotes, level of detail for rates/quantities calculations) overhead and profit calculations, and mathematical accuracy
  - Tested sample direct materials purchases for appropriate tax savings calculations and incorporation into the pay application
  - Tested sample project closeout packages for appropriate completion of the FDP checklist, and collection of documents (certificate of completion, certificate of final inspection, final lien release)
  - Tested sample projects for the completion of vendor monitoring/evaluation forms
- Developed recommendations for process and control modification / addition / deletion for any design gaps or non-compliance issues identified during our analysis and testing

Reporting

We summarized and reviewed the results of this internal audit with appropriate members of Management, the Superintendent and the Lee County School Board.

OBSERVATIONS MATRIX

Observation	1. Pay Application Support and Record Retention
Description	Through our detailed testing of construction pay applications (invoices), we noted inconsistency in the level of documentation that was readily available to support amounts invoiced by construction contractors. Specifically, we noted that complete supporting records were not maintained in the final pay application files for the following: <u>General Conditions Costs</u> • In four (4) pay applications for one (1) project, documentation was not provided for more than $165,000 of general conditions costs during our initial review of the pay application packages. Upon collection of further supporting documentation, it was determined that the missing information was related to labor and supervision costs. An itemized spreadsheet was provided by the Construction Manager, as well as a labor report providing the total hours for the period; however, individual timesheets were not provided. • In one (1) pay application, an invoice internally generated by the contractor was provided as support for a Wi-Fi device. Upon collection of further supporting documentation, it was revealed that costs were being invoiced at $132 per month, while the actual cost incurred was only $84. <u>Subcontractor Costs</u> • In one (1) pay application, supporting documentation for a subcontracted component totaling more than $16,400 consisted of an email from the prime contractor, rather than an invoice supporting actual costs billed by the subcontractor. • In one (1) pay application, no retainage was withheld from the prime contractor; however, the prime contractor withheld 10% from a subcontractor. We understand the contact included a “pay when paid” clause, which requires the prime contractor to pass along payment to subcontractor when received from the District. If the District did not hold retainage from the prime contractor, retainage should not have been held from the subcontractor. In most cases, appropriate records were subsequently obtained from contractors after our inquiries, and after we shared the results of our initial review of invoices. Construction Manager at Risk (CMAR) contracts typically require that supporting documentation accompany pay applications, for all costs incurred by the contractor, to support amounts invoiced. Supporting documentation consists of a variety of documents including but not limited to: subcontractor invoices, lien releases from subcontractors acknowledging that payment from the prime has been received, invoices from materials suppliers, equipment rental invoices, prime contractor timesheets showing actual hours worked, payroll documents supporting actual rates paid to contractor employees, insurance invoices, and bond invoices. The District’s construction contracts contain language that requires the full suite of supporting documentation with each pay application. In order for the District to fully recognize the benefits of cost transparency afforded by using CMAR agreements, all documentation supporting costs actually incurred should be collected and reviewed before approving and paying an invoice. This practice helps deter overbillings from the contractor, and provides a complete record for the district of project costs.

OBSERVATIONS MATRIX (CONTINUED)

Observation	1. Pay Application Support and Record Retention (continued)
Description	Management indicated that cost recovery audits are conducted by a third-party at the conclusion of each project with construction costs in excess of $2,000,000 and that limited procedures are performed by the District's Internal Audit Department, under Business Services, for projects between $200,000 and $2,000,000. Considering these audits occur at project completion, based on our experience, even when contract language clearly supports recovery of funds from the contractor, this often requires legal intervention and compromise, where the District may only recover a portion of the overbillings. By collecting documentation prior to the payment of invoices (and project closeout), the District can identify and correct overbillings in real time, rather than relying on an audit after project completion.
Recommendation	The District has an established pay application checklist that includes eighteen (18) steps related to the format and mathematical roll forward, but it does not include a step to validate that supporting documentation is attached and was reviewed. We recommend the District modify the existing checklist to include detailed review of the pay application supporting documentation. This should include review of all costs included in the pay application, to validate that a corresponding vendor, supplier, or provider invoice was included in the supporting package and agrees to the amount charged by the contractor. Refer to the Process Improvement Opportunity #1, regarding electronic upload of the pay application package. Given that Facility Development & Programming has one (1) accountant performing the initial review of the supporting documentation included in the pay application package, we understand that a more detailed review of the costs requires additional efforts by the District. In consideration of the time and resources required to perform this review, we also recommend the District conduct an analysis to determine if additional administrative assistance or temporary help may be warranted at the end of the month when pay applications are submitted.
Management's Action Plan	**Response:** Facility Construction will inform all Construction Management firms of the new policies pertaining to monthly payment application approvals on all contracts moving forward. The LCSD payment application check-off process sheet will have an added step to verify back up materials are included in the application submission. The Construction Management firms must provide full and complete invoicing back up materials to support each and every payment line item request. Specific attention to General Condition's billings and CMAR staffing hours and contracted rates will be a focal point. Construction Managers engaged will be made fully aware that their payment applications will be rejected should the appropriate back up material not be provided with the payment application submission to the School District of Lee County. **Responsible Party:** Director of Construction Projects Management **Estimated Completion Date:** Complete

OBSERVATIONS MATRIX (CONTINUED)

Observation	2. Negotiation of Fixed-Cost Components
Description	During our detailed testing of construction pay applications (invoices), and in conversations with Management, we noted the District sometimes negotiates with contractors to treat certain costs as lump sum, and to establish certain rates within Construction Manager at Risk (CMAR) agreements. Although these items are negotiated, Management does not maintain documentation supporting the reasonableness and methodology for determining the amount of these components, and did not modify contract language to more clearly reflect the treatment of these items. Specifically, we noted instances where the District agreed to: • Labor rates for construction manager employees • Insurance rates for general liability, builder's risk, subcontractor default • Rates for a performance and payment bond • Rates for contractor software By design, CMAR agreements provide transparency of costs versus construction manager profits, by establishing a guaranteed maximum price (GMP) that includes actual costs, plus a percentage fee (profit). The contract templates utilized by the District contain provisions that require detailed support of actual costs for all items within the GMP. While fixing components of a GMP can reduce administrative burden related to invoice review, this practice removes transparency of costs from the negotiated components. While negotiations to fix certain components are commonplace, best practices include documenting the agreement in writing with the contractor, and documenting methodologies employed by the District for determining the reasonableness of fixed amounts. Contract disputes may arise if the contract requires certain supporting documents, but alternative arrangements were agreed verbally. This can be especially problematic in the event of turnover, on either the District or contractor team, as new parties to the project may not have a record of prior verbal agreements.
Recommendation	When Management agrees to fix certain components of a CMAR agreement, we recommend the District document the following: • Insertion of language, or a formal amendment to the contract, specifying which portions are fixed, and amounts. • Pre-audits to support the reasonableness of fixed components, including documents reviewed to validate actual costs, historical cost comparisons, independent estimates, etc.
Management's Action Plan	**Response:** The District agrees that any process related to the negotiation of costs and/or fees involving construction contracts should be formalized and documented both within the actual contract and through supporting documentation. We will create a process to include Procurement, Construction, Maintenance, and/or any other relevant department to formally document cost agreements for our construction contracts moving forward. **Responsible Party:** Director of Construction Projects Management, Director of Procurement Services **Estimated Completion Date:** June 30, 2021

OBSERVATIONS MATRIX (CONTINUED)

Observation	3. Composition of Request for Qualifications (RFQ) Selection Committee
Description	Through our testing of project procurements, we noted that the current process of forming an RFQ Selection Committee does not require diversity in the Committee. The purpose of forming a committee for the award of a project to a vendor is to increase transparency and objectivity in the selection process. Key to achieving both goals is the establishment of a diverse, well balanced, and qualified committee. The Committee formed to select the vendor for the Lehigh Senior High School Addition and Renovation ($10.5M) was comprised of five (5) District personnel, with three (3) from Facility Development and Programming (FDP), and two (2) from Maintenance Services. While the involvement of both FDP and Maintenance is critical to assessing qualifications of prospective bidders, the committee did not include representation from other key project stakeholders, which may have included Business Services, School Development, School Administration, and/or Technology. The procurement exhibit for Construction Management Services RFQs specifies that the committee shall be comprised of between five (5) and twelve (12) members, and further specifies which departments/representatives are approved to participate in the committee. Our understanding is that Procurement and FDP solicit other departments, who may provide committee members as available; however, there is no requirement in the current policy/procedure to diversify the committee members. As a result, the committee that selected the Lehigh SHS vendor included a majority from FDP. This increases the risk of conflicts of interest (whether real or perceived) during the selection process, as FDP personnel are likely to have prior established relationships with proposing construction vendors. The committee for the MMM High School project contained members from FDP, Maintenance, Business Services, and Technology. Through further discussions with Management, we also understand the process of identifying committee members was updated in November 2019, and has resulted in more diverse committees. Refer to Management's response below for further detail.
Recommendation	We recommend the District modify procedures for the RFQ Selection Committee to require a greater level of diversity. Procurement should solicit input from various Departments when modifying the procedure, and may consider the following options: • Simple modification of the committee composition to include a requirement that the committee contain members from a minimum of four (4) Departments. • Alternatively, the District may specifically define the committee, requiring each relevant Department to assign a member.
Management's Action Plan	**Response:** Procurement agrees with the recommendation. • The Lehigh Senior High School Renovation and Additions RFQ was released in 2017 and was the fourth Construction RFQ issued utilizing the newly implemented procurement process for construction services. We have recently completed our forty-first Construction RFQ this Spring of 2020. During the period 2017-2019, Procurement implemented an update to the process for requesting evaluation committee members from departments to ensure diverse department representation on evaluation committees.

OBSERVATIONS MATRIX (CONTINUED)

Observation	3. Composition of Request for Qualifications (RFQ) Selection Committee (continued)
Management's Action Plan	**Response (continued):** • Starting with RFQ's released in November 2019, a GoogleSheet is shared with Chiefs, Executive Directors, and Directors of divisions/departments identified in the RFQ process manual as eligible for participating on the evaluation team. They are requested to input staff from their departments to be on the evaluation committee. This new process has helped streamline the selection of evaluation committee members as well as allowed a quick visual of the evaluation team's diversity. If instances occur where there is lack of diversity on the evaluation team, the Director of Procurement can request additional evaluators to achieve needed department diversity. This new process has resulted in evaluation teams with up to four non-FDP department representatives and an average of 4.6 departments participating in the last 12 Construction RFQs. • Since implementation of our new selection process, Procurement has received feedback from Construction Contractors that too many non-construction staff are evaluating construction related RFQ's. Procurement's response to the Public is that we will attempt to have a minimum of 50% participation from Construction, Maintenance and Planning Departments. • Procurement believes that the observed lack of department diversity has been rectified with the implementation of our Construction RFQ Selection sheet. We can further the commitment to the department diversity of our evaluation committee by implementing the recommendation of a minimum of four Departments represented on evaluation committees. **<u>Action Item</u>** Further the commitment to department diversity of our evaluation committee by ensuring that each evaluation committee has a balanced composition of members from the Operations Division, and other departments as necessary dependent on project type **Responsible Party:** Director of Procurement Services **Estimated Completion Date:** July 2020

PROCESS IMPROVEMENT OPPORTUNITIES

1. Program and Project Management Software

Through our testing and walkthroughs with process owners, we noted that the District currently processes all construction related documents in hard-copy form. Pay applications, change orders, contingency usages and other documents are provided to Project Managers for review, and are then scanned for electronic retention, and filed in cabinets in the office.

The manual nature of processing these items increases the risk of undetected errors, missing/lost documentation, and untimely submission and review. Further, the absence of a central source of record for program and project documents and data severely limits Management's ability to monitor several key performance indicators related to the District's construction portfolio.

Considering the size and volume of upcoming projects that the District has planned over the next ten (10) years, a program and project management software could greatly benefit the District, through increases in efficiency and the ability to conduct more advanced data analysis.

Several software packages are available that offer program wide, as well as project specific functionality. From a project management perspective, software can allow the District to setup a detailed project budget, track actual expenses, and provide a platform for vendors and contractors to upload invoices electronically. More advanced packages provide automated workflows for invoices, change orders, and other key project documents that will automatically route documents through a pre-determined approval path. In addition, the ability to upload these items electronically provides the District with data that can be used for efficient analysis and reporting.

From the program management perspective, the data collected from individual projects can be combined for analysis that would allow Management to easily monitor the progress of all projects and the program as a whole. Data can be used to define key performance indicators for continuous monitoring that can provide valuable insights regarding historical budget vs actual, records of historical costs, year over year analysis, average change order costs and frequency, and can be used to identify emerging trends.

Implementation of a program management software to aid in the electronic collection and retention of key project documents, would provide enhancements / benefits to the existing process outlined above.

PROCESS IMPROVEMENT OPPORTUNITIES (CONTINUED)

2. Vendor Monitoring

During our walkthroughs and testing of the closeout process, we noted that although the District evaluates construction contractors after a project is complete, the results of the evaluation are not considered during procurement and assignment of future projects.

The evaluation form is completed by the project manager at the conclusion of each project, and includes eighteen (18) components to evaluate of contractor expertise, responsiveness, cost sensitivity, and quality of work.

For smaller projects (under $2 million), the District utilizes a pool of vendors on a rotational basis, that were procured on continuing contracts. Through conversations with Management, we noted that these vendors are assigned to projects systematically (next on the list), and that past performance and/or similar experience to the project's specific scope is not considered.

If prior experience and performance are not considered, a project may be assigned to a poor-performing vendor, or a vendor not suited to the specific scope of the project. This can lead to lower quality of work received by the district, and overall increased costs through the additional project management and oversight required by District employees.

Procurement Services is also actively monitoring State Legislature, as a bill has recently been proposed to increase the maximum limit for continuing contracts (CCNA) from $2 million to $4 million, which could affect current procedures for continuing contracts. If passed, the ability for the District to award larger projects under CCNA will increase the need for the District to consider experience and performance in vendor selection.

Implementing a more robust process for the assignment of projects to vendors on continuing contracts to further enhance vendor monitoring. The process could include consideration of past performance, experience with the similar scopes, and other measurable components. Since equitable distribution of contracts and transparency should still be a consideration, the methodology for selection of vendors for each project should be clearly documented. As an example, a scoring rubric could be utilized that considers performance metrics, prior awarded projects, and scope-specific experience. Utilizing a rubric would help to maintain a consistent approach, and add objectivity and transparency to the process for selection.

We have provided example Standard Operating Procedures from a Florida School District to Procurement for review/consideration.

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