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# REVIEW OF CONTRACT MANAGEMENT (PHASE TWO)

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Project # 20160101-2  
January 2017

**Texas Facilities Commission**

*Physical address: 1711 San Jacinto Blvd, Austin, Texas 78701*

*★ Planning and administering facilities in service to the State of Texas ★*

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# Executive Summary

## Overview

Overall, Texas Facilities Commission (TFC) has processes in place to provide reasonable assurance that the agency's contract management goals are accomplished effectively, and in compliance with relevant regulations, policies and procedures. The agency has established comprehensive, repeatable contract/project management processes that utilize formal templates and checklists. Standardized contracts clearly define expectations and requirements, define the scope of work, and emphasize the importance of timely project delivery. In addition, the contracts include specific provisions to ensure state funds are protected, including the option to withhold payment, the right to liquidated damages, and the right to audit. Controls within the project management process include the agency's experienced, credentialed project management team who utilize well-documented procedures, including standardized forms and checklists. Project execution plans (PEPs) assist in ensuring compliance with the project schedule, scope and budget, performance monitoring plan, and key milestones for timely project delivery. Inspections, performed at various stages of project completion including at substantial completion, final completion, and final punch list completion, assist in ensuring that the agency is receiving the required deliverables. The final payment checklist ensures that the contractor submits all the required documentation, including warranty documents, surety release, and mark-up documents, before the final payment.

While the agency recently enhanced its construction contracts with the inclusion of specific language regarding rebates, refunds, discounts and any savings identified by an audit, management has not developed a framework to monitor vendor compliance with these new provisions. Such a framework could include recovery audits. This is particularly important because the agency does not require contractors to provide detailed documentation (i.e. invoices, payroll summaries, etc.) in support of the individual line items within the schedule of values (SOV).

The review found opportunities for regulatory compliance improvement in its vendor performance reporting. The agency has not consistently reported vendor performance (on construction and deferred maintenance contracts) to the Office of the Comptroller, as required by Texas Government Code §2155.089.

### *Implementation of Prior Audit Recommendations*

Implementation of the recommendations from the Review of Contract Management (Phase One), issued in February 2016, is substantially complete. The agency's new procedure, by rule, to identify contracts that require enhanced performance monitoring and the accompanying policy were adopted by the Commission on June 15, 2016 and August 17, 2016, respectively. While there remains room for further improvement, contract management staff has developed a process

for assisting with making sure vendors submit a disclosure of interested parties to the agency at the time they (vendors) sign the contract, as required by Texas Gov't Code, §2252.908.

The agency's contract and project planning processes have improved significantly with a process that requires needs/risk assessments and cost estimates to be part of the supporting documentation for management's recommendation for Commission approval. All of the agency's project managers now meet the state requirement for the CTCM designation. This has significantly improved the agency's compliance with Texas Government Code, §2262.053. However, with 32% (15 out of 47) of the agency's contract managers not meeting the CTCM designation requirement, further improvement is required.

Agency management has enhanced its reporting to the Commission regarding the agency's ongoing construction, deferred maintenance projects, and relevant contracts. Recent enhancements include reporting on executed Guaranteed Maximum Price (GMP) transactions, Change Order Reports showing how management is utilizing its change authority, and Project Status Reports (PSR) showing financial and operational performance (i.e. schedule and time) aspects of the agency's projects. The Project Status Reports are color-coded, highlighting projects that are encountering difficulties.

## **Summary of Management's Response**

*Management concurs with the findings of TFC's Internal Audit Review of Contract Management (Phase II) with the following clarifications. The new contract provisions are intended to ensure that any available and recoverable rebates, savings, refunds or discounts are collected by TFC and the State. There are "best value" delivery methods utilized by TFC for construction that these provisions directly apply to such as the Construction Manager-at-Risk delivery method. For these contracts, FDC and Fiscal will collaborate to assess the risk for recovery of potential savings and devise desk review procedures to ensure that full transparency of costs and potential savings in the areas of higher risk is achieved and savings are collected. For larger construction projects, FDC will coordinate with Internal Audit to obtain recovery audit services either through existing professional service contracts or interagency contracts with SAO or CPA while also ensuring compliance with the General Appropriations Act Article IX Sec. 6.20 Use of Appropriations to Contract for Audits.*

*Conversely, there are competitively bid lump sum contracts and subcontracts where the State should acknowledge that these savings may belong to the contractors and subcontractors. Moreover, the contractors' reliance on obtaining these savings from a track record of good performance or volume purchasing may have played a role in the formulation of their competitive and winning price for the work.*

*The CPA's "one size fits all" system is better suited towards procurement of goods and repeatable services or unit services. It is not suited for performance reporting on complex, unique and one-time services necessary for the design and construction of capital improvements. Additionally,*

*performance reporting on these complex and unique project scopes requires the input of the agency's subject matter experts/contract managers, the project managers. FDC will collaborate with the procurement division to devise an internal reporting mechanism for vendor performance that, for the short term, will translate to the existing CPA system and for the long term, help formulate a better statewide system.*

## **Background**

This report represents the results of the Review of Contract Management (Phase Two). The Office of Internal Audit's *Review of Contract Management (Phase One)* was issued in February 2016. While Phase One was focused on contract planning, contract procurement, and contract formation, Phase Two focused primarily on contract administration and oversight activities, especially those contracts that are managed by project managers within the Facilities, Design, and Construction Division (FDC) of the Texas Facilities Commission. An FDC project is typically comprised of several contracts.

The agency executed approximately 315 contract documents (i.e. 122 contracts and 193 amendments/assignments) valued at approximately \$171 million in Fiscal Year 2016. The volume is expected to continue to increase (to an average of at least \$300 million/year) for the next 5 to 10 years as the agency undertakes the deferred maintenance and new construction work for which it received over \$1 billion in legislative appropriations during the 84th Legislative Session.

## **Closing**

We would like to thank FDC, Procurement, Legal Services, HUB, and Fiscal staff for the cooperation and assistance provided to the audit staff during this audit. For questions or additional information concerning this audit report, please contact Amanda Jenami at 512-463-1438.

# Detailed Issues with Management Responses

## 1. Operational Effectiveness

### 1.1 Protecting State Funds

While the agency recently enhanced its construction contracts with the inclusion of specific language regarding rebates, refunds, discounts and any savings identified by cost review or audit, management has not developed a framework to monitor vendor compliance with these new provisions. Such a framework could include recovery audits. This is particularly important because the agency does not require contractors to provide detailed documentation (i.e. invoices, payroll summaries, etc.) in support of the individual line items within the schedule of values (SOV). The SOV provides the project manager, and architect with good high-level information on the description of work performed, percentage of completion, and the value of any materials on hand.

In approving the vendor payment applications based on the SOV alone, the agency does not currently ensure that the SOV does not include items that are not allowable. Verifying some SOV items (such as insurance, bonds, general conditions, etc.) against invoices would not only provide assurance that the expenditures included in the SOV were incurred on the specific TFC project but also that they are allowable. A desktop review of the SOV against supporting invoices and other documentation could significantly improve the current control environment. Requiring supporting invoices is a good control that reduces the risk of overpayment.

The auditors are aware that both these desktop reviews and recovery audits would require additional resources. However, a streamlined, risk-based approach that focuses on the high-risk areas (i.e. types of expenditure items such as insurance, bond payments, general conditions, etc.) and utilizes review checklists would significantly increase the level of assurance that state funds are protected. Recovery audits could be performed by a third party strictly on a commission basis (i.e. the audit fee would be based on the total amount recovered).

### Recommendations

Management should improve construction contract management processes by developing a framework to monitor vendor charges on projects and their compliance with the rebates, refunds, and discounts provision by:

- (i) Developing a risk model for use in determining the SOV items on which to perform desktop reviews.

- (ii) Developing desktop review procedures, including a checklist for use by staff.
- (iii) Providing staff with the necessary training.
- (iv) Exercising the agency's "right to audit" by using the above risk model and performing recovery audits on some of the projects.

## **Management Action Planned**

*FDC Management will collaborate with TFC's Fiscal division to develop a risk assessment model to yield an achievable level of desk reviews of Construction Manager-at-Risk costs that present the highest potential for recoverable savings. Additionally, desk review procedures and training will be developed and implemented. The performance and prospective frequency of these reviews shall reflect a justifiable business case for the additional staffing hours required either from current staff or potentially unidentified additional staff.*

*FDC will collaborate with executive management, Legal Division, Internal Audit and Procurement to develop a procurement method for Recovery Audit services either through A/E professional service contracts or Interagency Cooperation Contracts with SAO or the Comptroller while also ensuring compliance with the General Appropriations Act Article IX Sec. 6.20 Use of Appropriations to Contract for Audits.*

## **Responsible Parties**

*Responsible parties will include John Raff, FDC DED, Marti Walsh, Director of Project Management, Project Management staff, Rob Ries, Budget Director, Fiscal staff and Richard Ehlert, Procurement Director.*

## **Estimated Completion Date**

*April 1, 2017*

## **1.2 Communication Processes**

Management of the agency's construction and deferred maintenance projects, many of which are sizable and complex, requires close collaboration and communication between the contractor, architect, project manager, and FDC management. While the agency project management function has well established communication processes, including the use of a web-enabled project management system to facilitate document sharing and communication between the project team (i.e. project manager, architects, and contractors), periodic status update meetings,

contractor daily activity logs, and project manager site visits, the review found missed opportunities on some of the projects reviewed.

#### *Project Daily Activity Logs*

Contractors do not always complete the project daily activity logs timely. For 60 % (3 out of 5) of the projects reviewed, the contractor did not complete daily activity logs, in accordance with the contract. One contractor did not report information in the log at all. Another contractor created the daily entries for the period 11/3/2014 through 12/30/2014 on 8/9/2016. Daily logs assist project managers in keeping track of the project from the office and ensuring the contractor completes the project on time. This is especially important when one considers that each project manager oversees a portfolio of as many as ten projects at any one time.

#### *Project Manager Site Visits*

Forty percent (2 out of 5) of the projects reviewed lacked documentary evidence of the project manager site visits. Project manager visits to the construction site serve as physical verification of the work performed and assist in ensuring timely project delivery. Without site visits, projects may not be completed timely.

#### *Project Debriefing*

Project managers did not formally document “lessons learned” and best practices identified during the project. Sharing these with the individual project team as well as with the agency’s project managers could ensure all future projects would benefit, achieving continuous improvement. This could be done as part of a debriefing session, and as part of FDC’s project closeout process.

#### *Criteria for Contract Amendments*

The agency’s formal contract administration procedures do not include criteria for when an amendment is required. For a competitive sealed proposal (CSP), any change in the dollar amount (either increase or decrease) would necessitate a contract amendment. For a construction manager at risk (CMR) contract, an amendment is required when there is a change in the contract price above the guaranteed maximum price (GMP) or if there is a “significant” change to the scope of work. However, management has not defined a “significant” change. Formalizing the current practice with specific criteria for amendments would assist in communicating management’s expectations more clearly.

### **Recommendations**

Improve communication processes by:

- (i) Monitoring vendor compliance with the daily activity log requirement, and holding them accountable when they do not comply.
- (ii) Requiring project managers to not only visit project sites but also maintain documentation of such visits in the project files.
- (iii) Requiring the project team, as part of the debriefing process, to formally document and discuss “lessons learned” and best practices.
- (iv) Sharing the “lessons learned” and best practices with the rest of FDC’s project management staff.
- (v) In collaboration with FDC, developing, documenting and communicating formal criteria indicating when amendments are necessary.

## **Management Action Planned**

*Management will update project manager desk procedures to include an updated invoice review checklist coordinated with the new construction contract templates. Regular contractor reporting obligations will specifically be added to this tool as a gate for invoice approval.*

*While project managers, as a matter of process, are expected to complete site observation reports following every site visit, the A/E’s meeting minutes serve as a backup to evidence of the project manager’s presence on site. Additionally, the minutes will likely include much of the data that will be included in the project manager’s observation report. Additional training was conducted on December 5, 2016 to stress the importance of timely project documentation, PM’s uploading of site observation reports and meeting minutes for each site visit to ensure thorough documentation of project managers’ construction administration activities.*

*Legislative reporting on construction contract completion within schedule and within construction budget as a key performance measure provides a logical milestone for FDC management to conduct a debriefing for lessons learned and best practices. FDC management will incorporate this activity into the project process as well as regular reports/training sessions with project management staff to disseminate these findings. On December 5, 2016, training was conducted on use of the “Lessons Learned” tab of the Project Execution Plan while conveying the requirement to utilize this tab through the course of every project.*

*The competitive sealed proposal contract template for lump sum construction has been revised to include criteria describing when amendments are required relative to changes in value of the contract. This is also the case for Construction Manager-at-Risk contracts.*

*What remains to be further defined is what comprises a “significant change in scope” described in the contract manual as requiring a formal amendment. It is important to point out that it is*

*most probable that a significant change in scope would be accompanied by a change in contract value documented in accordance with the aforementioned new contract provisions. However, it could happen that a deferred maintenance contract, for example, could have surplus value remaining to address additional scopes of repair. A significant change in scope would refer to an addition of scope from a different but related legislative funding strategy than what the contract was initially formulated for, i.e., a subsequent biennium's funding. Procurement scopes are broadly written to accommodate the evolving conditions and needs of our facilities. Subsequent biennium strategies or other related scopes of work that fit within the solicitation scope of work are sometimes amended into a construction contract. This achieves a best value for the state in that mobilization costs are avoided and general conditions costs are leveraged from on-going work to achieve best value from the contract.*

*Significant change in scope means additional scopes of work that are funded from related but different legislative funding strategies such as a subsequent biennium's funding. These additional scopes are reconciled with the scope description for the original construction procurement.*

## **Responsible Parties**

*FDC Management – John Raff, DED, Marti Walsh, Director of Project Management and Project Management staff.*

## **Estimated Completion Date**

*April 1, 2017*

## **2. Operational Efficiency**

### **2.1 Unintegrated Information Systems**

As reported in the Review of Contract Management (Phase One), the lack of integrated information systems continues to pose operational efficiency and data integrity challenges for contract management staff. For example, the agency does not maintain one central repository that provides project/contract management staff with a comprehensive overview of the status of projects. The different staff teams use different systems: FDC uses IMPACT, a hosted project management system for construction, Procurement uses the Automated Procurement System (APS), HUB uses the Progress Assessment Report (PAR) access database, Legal Services uses an in-house developed contracts database and a (manual) contract approval folder (i.e. the purple folder), and Fiscal Services uses GUI Fund Accounting System (GFAS). These systems are not integrated and operating them results in significant operational inefficiencies.

Within FDC, the inconsistent documentation practices between different project managers increases these efficiency challenges. While individual project managers are aware of the

dynamics and details of their respective projects, the auditors found it difficult to locate certain key information and documentation. This was partly because project managers do not use IMPACT in a consistent manner and do not maintain documentation in a standardized order. For example, project schedules and final punch lists were not always available in IMPACT. In one instance, a document that should have been maintained in IMPACT was not available at TFC and had to be obtained from the contractor. Consistency is important as projects are often transferred from one project manager to another during the life of the project. IMPACT is not easily searchable, which makes locating information time consuming and cumbersome.

The review also found that data recorded in IMPACT is not always in agreement with supporting documentation.

## **Recommendations**

Agency management should continue to pursue practicable short-term solutions to integrate data between existing systems utilized by the agency. In addition, management should continue to seek funding for data integration projects within the General Appropriations Act and funding for a comprehensive Integrated Workplace Management System and other Enterprise Resource Planning technology systems (that contain robust contract performance measure and project management capabilities to achieve full integration of agency systems, as part of the agency's Legislative Appropriations Request (LAR)).

FDC leadership should revisit its expectations for the contract administration files to ensure they are appropriate. After making warranted revisions (if any), the expectations should be formally documented and communicated to FDC employees. The file structure should be organized in a logical manner, standardized and should be followed consistently by all relevant agency employees and contractors.

FDC leadership should perform periodic reviews of the project manager's use of the desired structure to ensure documentation is available, accessible, and maintained according to the prescribed file structure.

Management should include project data accuracy as part of individual project manager performance plans.

## **Management Action Planned**

*An improved file structure for Impact has been developed and rolled out with training for the project managers. FDC management will develop a desk procedure and document/transaction checklist that will be implemented at key milestones in each project, i.e., first A/E payment approval, first contractor payment approval, payment of contract balance and final payment/release of retainage. Proper documentation in proper locations will be required for approval of invoices at specific milestones. The milestone checkups for project documentation*

*will allow management to measure project manager performance in this area and facilitate inclusion in their performance reviews.*

*The agency has requested an IWMS in its FY 2018-19 LAR, and the LAR request to initiate implementation of the statewide CAPPS ERP system was delayed until FY 2020-21 at the request of the CPA.*

## **Responsible Parties**

*FDC management, John Raff, DED, Marti Walsh, Director of Project Management and Project Management staff.*

## **Estimated Completion Date**

*April 1, 2017*

## **2.2 Timely Completion and Closeout**

Projects were not always completed or closed out timely. The five projects reviewed were completed an average of 44 days after the planned completion date (i.e. the actual substantial completion was an average of 44 days after the planned substantial completion date). See below for some project specific details.

- One of the five projects tested was 339 calendar (244 working) days late. The project accomplished actual substantial completion on 3/20/2015 instead of 4/15/2014, as planned. Management assessed liquidated damages on the vendor.
- While two of the projects were completed on time (3/1/2015), they had not yet been closed out by the end of the warranty period (3/1/2016). The final closeout occurred on 9/28/2016. Final payment checklist procedures ensure that the vendor submits all the required documentation (including warranty documents, surety release, mark-up documents, etc.) and that any deficiencies have been resolved.

The executed contract for each of the five projects tested clearly emphasized that time is of the essence and that timely substantial completion as well as final completion is expected. Timely completion is one of TFC's key performance measures reported to the Legislative Budget Board.

## **Recommendation**

FDC leadership should hold the contractors accountable by including timely project delivery as one of the key considerations in the vendor performance evaluation.

## **Management Action Planned**

*FDC will collaborate with the procurement division to devise an internal reporting mechanism for vendor performance on complex and uniquely scoped services supporting capital improvements that, for the short term, will translate to the existing CPA system and for the long term, help formulate a better statewide system. Timely completion of construction will be a key measure of performance.*

## **Responsible Parties**

*FDC management, John Raff, DED, Marti Walsh, Director of Project Management and Procurement management Richard Ehlert, Director and John Goodrich, Purchaser.*

## **Estimated Completion Date**

*April 1, 2017*

## **3. Regulatory Compliance**

### **3.1 Vendor Performance Reporting**

The agency's construction contract management processes do not ensure compliance with SB 20's vendor performance reporting requirements. Currently, the project managers do not evaluate and document vendor performance for reporting to the Comptroller of Public Accounts' (CPA) vendor performance tracking system as required by the Texas Government Code §2155.089. The Procurement Director acknowledged that although the agency has a process for reporting vendor performance, it has not been effective in ensuring compliance for FDC contracts. Noncompliance with this requirement means that other state agencies do not have the benefit of the information when considering doing business with a vendor that has worked with TFC before.

## **Recommendations**

The Procurement Division, in collaboration with FDC management, should improve the current process for collecting vendor performance information at the end of each construction project as required. This could include revising the TFC form (currently used to capture performance information on the other agency contracts) so that it is better suited for construction projects.

Once the process improvements are in place, FDC management should provide project managers with training on meeting the requirements.

The Procurement Division, or a delegated program designee, should report vendor performance to the CPA, as required.

## **Management Action Planned**

*FDC will collaborate with the procurement division to devise an internal reporting mechanism for vendor performance on complex and uniquely scoped services supporting capital improvements that, for the short term, will translate to the existing CPA system and for the long term, help formulate a better statewide system. Timely completion of construction will be a key measure of performance. FDC management will implement training on the performance reporting system and ensure final payment approval is a milestone for this documentation.*

## **Responsible Parties**

*FDC management, John Raff, DED, Marti Walsh, Director of Project Management, Project Management staff and Procurement management Richard Ehlert, Director and John Goodrich, Purchaser.*

## **Estimated Completion Date**

*April 1, 2017*

# Objectives and Conclusions

The overall objective of this audit was to determine the extent to which TFC contract administration and oversight activities ensure agency goals are accomplished effectively and efficiently, and in compliance with relevant regulations, policies and procedures. The audit focused primarily on contract management activities from September 2014 through January 2016. The detailed audit objectives and conclusions are described next.

## Objective 1 – Operational Effectiveness - General

### 1.1 Determine the extent to which contract management procedures ensure that the agency receives the services it contracted for and that the contractor corrects any identified deficiencies.

The agency's contract management processes include robust project management procedures that ensure the agency receives the services it contracted for and that the contractor addresses any identified deficiency before final payment. TFC contracts grant the agency the right to withhold payment in the event that the contractor does not fully fulfill their responsibilities.

In addition, FDC has experienced professional project managers monitor contractor performance throughout the project by:

- Visiting the project site;
- Approving contractor submittals, payment requests, and proposed change orders;
- Reviewing comprehensive observation reports prepared by the AE and by TFC's inspector;
- Maintaining frequent communications with the stakeholders via emails, phone calls, daily project activity logs, and face-to-face meetings; and,
- Identifying deficiencies or deviations and ensuring they are resolved before final payment.

### 1.2 Determine the extent to which contract management procedures ensure that services do not cost more than they should.

Agency contracts define the contract sum. The agency utilizes both competitive sealed proposal (CSP) and contract manager at risk (CMR) contracts. A CSP is a fixed price contract while the pricing on a CMR is based on a guaranteed maximum price (GMP) stated in the contract. The GMP is the maximum price that TFC will pay for completion of the project (subject to any approved change orders).

**1.3 Determine the extent to which contract management procedures ensure that contractor charges only include allowable costs.**

Agency procedures do not adequately ensure that contractor charges only include allowable costs. The agency does not require contractors to provide detailed documentation (i.e. invoices, payroll summaries, etc.) in support of the individual line items within the schedule of values (SOV). In approving the vendor payment applications based on the SOV alone, the agency does not currently ensure that the SOV does not include items that are not allowable. Agency management should consider requiring contractors to provide documentation in support of the SOV, for a desktop review. In addition, management should consider exercising its “right to audit” by performing recovery audits on the key contract expenditure items.

**1.4 Determine the extent to which contract management procedures ensure that the contractor protects the assets purchased with state funds.**

Construction contracts include a provision requiring the contractor to protect equipment, materials and property purchased with state funds. By signing the contract, the contractor agrees to protect these assets.

**1.5 Determine the extent to which contract management procedures ensure that the contractor accurately reports their progress.**

Project managers visit the project site to evaluate the accuracy of the progress reported to the agency. Additionally, a specially designated TFC inspector performs comprehensive observations periodically throughout the project using a standardized template.

## **Objective 2 – Operational Effectiveness - Monitoring Performance**

### **2.1 Determine the extent to which agency contract monitoring procedures include project site visits, and comprehensive and objective site monitoring checklists.**

Agency processes include several site visits by the AE, project manager and inspector. The inspector maintains his observation reports within the project file in IMPACT. Project management staff utilizes punch lists to identify, document and keep track of deficiencies requiring attention and resolution. While site visits are integral to TFC's project management, 40% (2 out of 5) of the projects tested did not have evidence of project manager site visits on file.

### **2.2 Determine the extent to which project managers perform desk reviews in managing agency contracts/projects.**

FDC has documented procedures available on the TFC Intranet that offer comprehensive guidance for desk reviews. Project managers review submittals, proposed change orders, payment requests, and the contractor's daily log. Testing of five projects confirmed that project managers review submittals and change orders. However, as discussed above, the contractors did not always complete the contractor's daily activity log, as required by the contract provisions.

### **2.3 Determine the extent to which the agency has established policies and procedures in instances where the obligation of monitoring the progress of a contract is assigned to another contractor.**

Currently, FDC does not have projects where it has assigned the obligation of monitoring the progress of the contract to another contractor. FDC has not used this practice for several years.

## **2.4 Determine the extent to which contract management procedures include periodic and well-developed reporting.**

### *Reports to the Commission*

FDC management has enhanced its reporting to the Commission regarding the agency's ongoing construction and deferred maintenance projects and relevant contracts. Recent enhancements include the Project Status Reports (PSR) showing financial and operational performance (i.e. schedule and time) aspects of the agency's projects. The Project Status Reports are color-coded, highlighting projects that are encountering difficulties. In addition, FDC management reports on executed Guaranteed Maximum Price (GMP) transactions, and change orders to the Commission. The agency also reports to the Legislative Joint Oversight Committee on Government Facilities.

### *Contractor to Contract Manager Reporting*

Contract provisions require contractors to report their progress to FDC in IMPACT using the contractor's daily log. However, contractors did not always complete the contractor's daily log as required. Our review found that 60% (3 out of 5) of the projects tested did not include daily entries in the contractor's daily log.

### *Agency's Report to the Comptroller's Statewide Procurement Division*

The agency reports to the Comptroller's Statewide Procurement Division as required. A review of the Texas Comptroller of Public Accounts website confirmed the agency's compliance with this requirement.

## **2.5 Determine the extent to which contract management procedures ensure that contractors complete the projects in a timely manner, per the contract.**

Contract management procedures provide reasonable assurance that contractors complete projects in a timely manner. A written Project Execution Plan (PEP) that specifies the project schedule (including the expected substantial completion date) and monitoring plan is key in ensuring timely project delivery. Contracts include provisions that allow for liquidated damages in the event that the contractor does not complete the project timely. Further, TFC withholds retainage until the contractor completes the project and submits the required documentation. Furthermore, project management staff's final payment checklist ensures that the contractor submits all the required documentation before final payment. However, 20% (1 out of 5) of the projects tested were not timely. Thus, improvement is needed in this area.

## **2.6 Determine the extent to which contract management procedures consistently measure contract compliance and performance.**

Project managers assess performance and compliance throughout the project by visiting the site, reviewing observation reports, attending team meetings, communicating with the contractor, reviewing submittals, and reviewing pay applications.

### **Objective 3 – Operational Effectiveness – Change Management**

#### **3.1 Determine the extent to which contract management procedures ensure that change orders comply with the contract documents.**

The agency has procedures for processing change orders. Change orders require supporting documentation, review, and approval. Significant changes require contract amendments. However, the agency has not defined what constitutes a “significant” change.

#### **3.2 Determine the extent to which contract management procedures ensure that change orders are approved in writing and in advance by the appropriate parties.**

The agency has processes in place to ensure that the appropriate parties provide advanced approvals, in writing. All the five change orders tested included advanced written approvals by the appropriate parties.

#### **3.3 Determine the extent to which contract management procedures ensure that change orders contain the required supporting documentation including cost analyses.**

Agency processes ensure that change orders contain the required supporting documentation. All of the five change orders tested included the required supporting documentation, including cost analyses.

## **Objective 4 – Operational Effectiveness – Payment Approval**

### **4.1 Determine the extent to which contract management procedures ensure that the contractor’s billing coincides with the contract’s progress.**

Agency procedures provide reasonable assurance that contractor billing is in line with the contract’s progress. The payment application includes not only the project’s schedule of values, but also the contractor’s signed and notarized certification that he has completed the work in accordance with the contract. In approving the payment application, agency project managers review the schedule of values to ensure it aligns with project completion status. The SOV documents the project progress in the current period as well as cumulative.

### **4.2 Determine the extent to which contract management procedures ensure that the agency’s contract managers approve all invoices, budget changes or fiscal amendments.**

The agency does not require that contractors submit invoices when requesting payment. Agency staff bases its payment application approvals on the SOV. Change orders, including zero-dollar change orders, are documented and reviewed prior to approval.

### **4.3 Determine the extent to which contract management procedures ensure that the agency’s contract managers keep a running payment log of all payments and the deliverables covered by each.**

The contractor includes project deliverables (progress) in the schedule of values submitted with the payment application. Staff reviews (and approves) electronic copies of the payment applications and maintains a running log of approved payments in the project management system, IMPACT.

### **4.4 Determine the extent to which contract management procedures ensure that the agency’s contract managers routinely interact with Fiscal Services regarding all fiscal contract matters, disputes, non-payment, etc.**

The project managers work with the agency’s Contract Accountant (in Fiscal) regarding fiscal contract matters, including the payment application approval process.

**4.5 Determine the extent to which contract management procedures include a detailed review of the contractor's invoices to ensure the agency only pays for allowable costs.**

Agency procedures do not include a detailed review of the contractor's invoices, and thus, do not ensure the agency only pays for allowable costs. Both the project manager and the contract accountant approve contractor payment applications based on the SOV.

**Objective 5 – Operational Effectiveness – Contract Termination**

**5.1 Determine the extent to which contract management procedures ensure that all contract parties are relieved from further unperformed obligations upon contract termination.**

The TFC Contract Manual (Revised 8/25/2016) provides guidance on the action to take in the event the agency is contemplating contract termination.

**Objective 6 – Operational Effectiveness – Contract Closeout**

**6.1 Determine the extent to which contract management procedures ensure that the parties to the contract have fulfilled their contractual obligations.**

FDC procedures, posted on the TFC Intranet, guide staff in performing project closeouts, warranties, final payments, and archiving. The procedures include the Final Payment Checklist to ensure that the contractor satisfies his responsibilities and submits all required documentation before he is paid.

**6.2 Determine the extent to which contract management procedures ensure project management staff collects and leverages “lessons learned” and best practices for continuous improvement.**

Currently, project management teams do not formally document and discuss “lessons learned” and best practices identified during the project as required by the agency's project closeout checklist. FDC management should share the lessons from each project with the rest of the project management teams, to ensure all future projects benefit.

## **Objective 7 – Operational Effectiveness – Vendor Relations**

### **7.1 Determine the extent to which contract management procedures ensure that there is frequent communication between the agency’s contract managers and vendors pertaining to all aspects of the contract, including issues, technical assistance, and overall progress of the contract.**

Contract management procedures include frequent communication between the project managers and vendors. Communication procedures include meetings with stakeholders, on-site visits, observations by the TFC inspector, emails, phone calls, document reviews and approvals. However, the review found that 60% (3 out of 5) of the projects tested did not include daily entries in the contractor’s daily log while 40% (2 out of 5) of the projects tested did not have evidence that the project manager had visited the construction site.

### **7.2 Determine the extent to which dispute resolution policies and procedures are clear.**

The TFC Contract Manual includes a clear dispute resolution policy. Audit testing confirmed that the dispute resolution provision was included in all of the five contracts tested.

## **Objective 8 – Operational Effectiveness – Contract Administration**

### **8.1 Determine the extent to which contract management procedures ensure that the agency maintains one master contract administration file.**

The agency does not maintain one master contract administration file or a central repository where a project manager or FDC management can obtain a comprehensive overview of the status of the FDC projects. The agency uses multiple systems for contract administration activities, including:

- Legal Contract Database (tracking log) and Shared Contracts Folder
- Web-enabled project management information system, IMPACT
- Automated Procurement System (APS)
- GUI Fund Accounting System (GFAS)

As reported in the Review of Contract Management (Phase One), the lack of integrated information systems continues to pose operational efficiency and data integrity challenges for contract management staff. The project managers are aware of the dynamics and details of their respective contracts but key information and documentation can be difficult to locate.

## **Objective 9 – Operational Effectiveness – Bonds and Insurance**

### **9.1 Determine the extent to which contract management procedures ensure that the contractor carries the required payment and performance bonds and liability insurance coverages.**

Contract management procedures ensure that the contractor carries the required payment and performance bonds and liability insurance coverages. The contract requires the contractor to have insurance and bonds coverage. Management has developed written procedures to guide staff in the verification of payment and performance bonds and liability insurance coverages. The review tested five projects for evidence that TFC had verified the bond and insurance coverage in those projects. There were no exceptions.

### **9.2 Determine the extent to which procedures ensure that the agency receives credit for rebates, discounts, or refunds collected by the contractor from the suppliers of materials, subcontractors, or insurers.**

While the contract language has been strengthened to include more specific language regarding rebates, discounts and refunds collected by the contractor, neither FDC nor Fiscal Services has procedures in place to enforce the new provisions.

### **9.3 Determine the extent to which contract management procedures ensure that the payment and performance bond premiums the surety company charged to the contractor reconcile to the premiums the contractor charged TFC.**

Contract management procedures do not ensure that the payment and performance bond premiums the surety company charged to the contractor reconcile to the premiums the contractor recorded on the payment applications. The agency does not require contractors to provide documentation (i.e. invoices) to support the performance bond charges included on the SOV. This elevates the risk that the agency could be overpaying for performance bonds and similar items.

**9.4 Determine the extent to which contract management procedures ensure that the liability insurance premiums the insurance company charged to the contractor reconcile to the premiums the contractor recorded on the payment applications and charged to TFC.**

Contract management procedures do not ensure that the liability insurance premiums the insurance company charged to the contractor reconcile to the premiums the contractor recorded on the payment applications and charged to TFC. The agency does not require contractors to provide documentation (i.e. invoices) to support the liability insurance premiums included on the SOV. This elevates the risk that the agency could be overpaying for liability insurance.

**Objective 10 – Operational Effectiveness – Subcontractor Oversight**

**10.1 Determine the extent to which contract management procedures ensure that subcontractors submit itemized invoices to the contractor to support the amount requested in the payment applications.**

Current practice does not require the contractors to provide documentation in support of the SOV. Thus, agency processes do not ensure that subcontractors submit itemized invoices to the contractor in support of the amounts requested in the payment application. This elevates the risk that the agency could be paying for unallowable items.

**10.2 Determine the extent to which contract management procedures ensure that the agency validates the details of the subcontractor’s billings before paying the amount requested in the payment applications.**

The agency does not require contractors to provide documentation (i.e. invoices) to support amounts requested in the payment application. Thus, the agency’s payment approval process does not include validating the details of the subcontractor’s billings before paying the amount requested. This elevates the risk that the agency could be overpaying.

## **Objective 11 – Operational Efficiency**

### **11.1 Determine the extent to which contract managers within each division possess technical and/or programmatic expertise and knowledge or have the expertise and knowledge readily available to them.**

FDC's project management team consists of architects, engineers, interior designers and professional project managers with extensive project management experience from both public and private sectors.

### **11.2 Determine the extent to which the agency's contract management system(s) is searchable and allows for the approval, uploading, monitoring, and automated reporting of contracts.**

The agency's web-enabled project management system, IMPACT, facilitates document sharing and communication between project team members (i.e. project manager, AE, contractors and FDC management) by allowing document uploading, review, and canned reporting. However, it is not easily searchable, and FDC management has to manipulate the reports to a more user-friendly format for its stakeholders. Management is aware of both these issues.

### **11.3 Determine the extent to which the agency has independent and formal mechanisms in place to track compliance.**

A multiplicity of controls are in place to assist in ensuring that the contractor is providing the services and deliverables that the agency has contracted for, including site visits, desk reviews, and observation reports. The FDC staff now also uses the Project Execution Plan (PEP) to monitor performance and compliance.

## **Objective 12 – Regulatory Compliance**

### **12.1 Determine the extent to which contract management procedures ensure that TFC reviews vendor performance under a contract at termination and reports performance to the Comptroller's Office as required by Texas Government Code.**

The agency has not effectively implemented its current procedure to ensure compliance with SB 20, Section 13, §2155.089 of the Texas Government Code, for construction contracts. More specifically, TFC does not consistently ensure that FDC project managers review and report vendor performance.

**12.2 Determine the extent to which contract management procedures ensure that the agency pays the contractors as required by the prompt payment guidelines of the Texas Government Code, §2251.**

The agency has processes in place to ensure that contractors are paid within 30 days, as required by the prompt payment guidelines.

**12.3 Determine the extent to which contract management procedures ensure that certain contract claims against the state are resolved in accordance with the Texas Government Code, §2260.**

The agency's contract manual provides good guidance to staff on dispute resolution. In addition, the contracts include a dispute resolution provision. All five contracts reviewed included a dispute resolution provision which stated that disputes will be resolved according to Texas Government Code §2260.

**12.4 Determine the extent to which contract management procedures ensure that the state agency monitors the HUB Subcontracting plan monthly to determine if the value of the subcontracts to HUBs meets or exceeds the HUB subcontracting provisions specified in the contract as required by the Texas Administrative Code, §20.14.**

The agency has processes in place to ensure that subcontracting provisions specified in the contract are met as required by the Texas Administrative Code, §20.14. The HUB Coordinator reviews contractors' payment applications for compliance with the contractor's HUB subcontracting plan, as part of the agency's payment approval process.

# Scope and Methodology

The overall objective of the Contract Management Audit was to determine the extent to which TFC's contract management processes ensure that agency goals are accomplished efficiently, effectively, and in compliance with relevant regulations, policies and procedures. Further, determine the extent to which contract management activities are performed in line with the *State of Texas Contract Management Guide*. Phase One (Report issued February 2016) focused on contract planning, contract procurement, and contract formation. Phase Two focused primarily on contract administration and oversight activities from September 1, 2014 through December 2015.

Fieldwork was conducted from March 2016 through November 2016.

The audit was based upon standards as set forth in Texas Government Codes, Senate Bill 20, 84<sup>th</sup> Legislative Session, Texas Contract Management Guide, Texas Procurement Manual, TFC Contract Manual, agency policies, and other sound administrative practices.

We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. Our evidence-gathering methods included the following:

- We reviewed applicable laws, rules and established procedures, including Comptroller's Office requirements and Commission policies and procedures.
- We reviewed contract documents, contract exhibits, Uniform General Conditions, Supplemental General Conditions, Special Conditions, project schedules, observation reports, bond worksheets, insurance checklists, Project Execution Plans (PEP), closeout documentation, substantial completion certificates, payment requests and supporting documentation including the schedule of values, and others.
- We reviewed information and documentation maintained in the project management information system, IMPACT, including daily log entries, meeting minutes, submittals, change orders, approvals, and documented discussions.
- We obtained invoices and other documentation supporting payment requests directly from the contractor.
- We tested judgmentally selected samples of transactions and evaluated processes using relevant criteria.
- We interviewed staff.
- We reviewed reporting to the Commission and to external agencies.
- We observed staff as well as Commission procedures regarding contract management.
- We followed up on issues identified in Contract Management Phase One, issued February 2016.

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### **TFC Mission Statement**

The Texas Facilities Commission (TFC) mission is to support state government through strategic planning, asset management, design, construction, maintenance, and leasing of state facilities and the reallocation and/or disposal of state and federal surplus.

### **Office of Internal Audit's Mission Statement**

Our mission is to assist the agency in achieving its operational goals by using innovative and disciplined methods to objectively evaluate the effectiveness, efficiency, and integrity of agency operations and governance processes and making recommendations to improve operational performance and governance processes.

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