



CITY OF HAMILTON
CITY MANAGER'S OFFICE
Audit Services Division

TO:	Chair and Members Audit, Finance and Administration Committee
COMMITTEE DATE:	March 6, 2017
SUBJECT/REPORT NO:	Audit Report 2015-11 Public Works – Capital Projects Contract Review and Follow Up to Audit Report 2013-11 Construction Contracts Review (AUD17005) (City Wide)
WARD(S) AFFECTED:	City Wide
PREPARED BY:	Charles Brown CPA, CA, CPA (Illinois) 905-546-2424 x4469
SUBMITTED BY:	Charles Brown CPA, CA, CPA (Illinois) Director, Audit Services City Manager's Office
SIGNATURE:	

RECOMMENDATIONS

- (a) That the Management Action Plans as detailed in Appendix “A” of Report AUD17005 be approved;
- (b) That the General Manager of Public Works be directed to instruct the appropriate staff to have the Management Action Plans (attached as Appendix “A” to Report AUD17005) implemented; and
- (c) That Appendix “B” of Report AUD17005, respecting the follow up of Audit Report 2013-11, Construction Contracts Review, be received.

EXECUTIVE SUMMARY

The 2015 Internal Audit work plan approved by Council included a review of capital works projects. The audit included a review of the adequacy of controls and management of two selected Roads construction contracts. Payments were tested and contractors' compliance with contract terms and conditions were evaluated. The results of the audit are presented in a formal Audit Report (2015-11) containing observations, recommendations and management responses. Audit Report 2015-11 is attached as Appendix “A” to Report AUD17005.

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In addition to Audit Report 2015-11, Audit Services has included the results respecting the follow up of Audit Report 2013-11 as both projects pertained to Roads construction contracts. Audit Report 2013-11 was originally issued in February 2014 and management action plans with implementation timelines were included in the Report. In March 2016, Audit Services conducted a follow up exercise to determine if appropriate and timely actions had been taken. Of the four recommendations made in the original Report, two recommendations have been completed, one recommendation is initiated and one recommendation is not completed. Details of implementation specific to each recommendation are included in Appendix “B” to Report AUD17005.

Alternatives for Consideration – Not Applicable

FINANCIAL – STAFFING – LEGAL IMPLICATIONS (for recommendation(s) only)

Financial: More consistent treatment and application of liquidated damages may result in additional recoveries from contractors who fail to complete contracts on time. The annual capital budget process would benefit from more consistent allocation of operating costs to the type of work being performed. Progress payment quantities that align with quantities in Inspectors’ diaries provide assurance that the contractor is only paid for completed work.

Staffing: None.

Legal: None.

HISTORICAL BACKGROUND (Chronology of events)

The audit leading to Audit Report 2015-11 was scheduled as part of the 2015 Internal Audit work plan approved by Council. The results of this audit are attached as Appendix “A” of Report AUD17005.

The Audit, Finance and Administration Committee receives and approves final audit and review reports as part of its responsibilities for the oversight of governance and control.

Audit Report 2013-11, Construction Contracts Review, was originally issued in January 2014. The report provided four recommendations to improve compliance, identify opportunities to strengthen internal procedures and improve governance processes. The results of this follow up audit are attached as Appendix “B” of Report AUD17005.

It is normal practice for Audit Services to conduct follow up reviews within 12-18 months following the issuance of the original report in order to determine whether action plans committed to by department management have been implemented.

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The follow up audit and submission of Audit Report 2015-11 were delayed as a result of staffing vacancies and Council-directed projects assigned to Audit Services during the 2016 calendar year.

POLICY IMPLICATIONS AND LEGISLATED REQUIREMENTS

Cost Recovery Process and Methodology

Various manuals and procedures maintained by Construction and Design Services

RELEVANT CONSULTATION

Appendix “A” to Report AUD17005 includes action plans which reflect the responses of management responsible for the contracts that were reviewed as well as the General Manager of Public Works. Appendix “B” to Report AUD17005 contains the results of the follow up that were provided to management responsible for the administration of construction contracts. In both cases, this management team resides in the City’s Engineering Services Division of the Public Works Department.

ANALYSIS AND RATIONALE FOR RECOMMENDATION

(Include Performance Measurement/Benchmarking Data if applicable)

Continuing with Audit Service’s annual review of capital projects for contract management and administration, two specific capital projects, completed or substantially completed by the end of September 2015, and their related major construction contracts were selected for detailed examination. Each contract had a value of over \$1,000,000.

The review of files, contracts, accounting records and other documentation, as well as discussions with relevant staff, provided information on project management and controls over payments to the contractors. The two projects were also assessed as to any change orders, their nature and approvals.

A formal Audit Report (2015-11) containing observations, recommendations and resulting management action plans was issued. Thirteen recommendations were included in Audit report 2013-11 (attached as Appendix “A” of Report AUD17005). Some of the recommendations made are as follows:

- Develop procedures to guide the application of Liquidated Damages against contractors who fail to complete contracts on time. Decisions to waive large amounts should be documented and authorized by management.
- Return Change Orders to management for proper authorization before processing the payment.

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- Update and periodically review the Cost Recovery and Process Methodology to ensure operating costs are appropriately allocated to capital projects.
- Develop a Project Deficiency Log to record deficiencies during final inspections and follow up with contractors when delays in correcting deficiencies exceed 90 days.
- Periodically review Contract Inspectors' project diaries and quantity books to ensure they are up to date. Performance manage and discipline staff that are not compliant.
- Refrain from approving Progress Payments without verifying that work invoiced has been completed as documented in project diaries, quantity books and material sheets. Performance manage and discipline staff that do not follow this process.

Management has agreed with all of the recommendations. Specific action plans can be found in the audit report attached as Appendix "A" to Report AUD17005.

In addition to Audit Report 2015-11, Audit Services has included the results respecting the follow up of Audit Report 2013-11 as both projects pertained to Roads construction contracts.

The report attached as Appendix "B" to Report AUD17005 contains the original report, Audit Report 2013-11, along with comments indicating Audit Services' findings as a result of the follow up work that was performed. There were four recommendations. Two recommendations were "Completed", one was "Initiated" and one was "Not Complete". Appendix "B" to Report AUD17005 contains the details of implementation by recommendation.

Audit Services conducted the above review and follow up audit in conformity with the *International Standards for the Professional Practice of Internal Auditing*. These standards require that Audit Services plan and perform the review and follow up audit to obtain sufficient, appropriate evidence to support the findings and conclusions based on the review and follow up objectives. Audit Services believes that the work performed provides a reasonable basis for the review and follow up comments and conclusions.

**ALTERNATIVES FOR CONSIDERATION
(Include Financial, Staffing, Legal and Policy Implications and Pros and Cons for each alternative)**

Not applicable.

ALIGNMENT TO THE 2016 – 2025 STRATEGIC PLAN

Our People and Performance

Hamiltonians have a high level of trust and confidence in their City government.

APPENDICES AND SCHEDULES ATTACHED

Appendix “A” to Report AUD17005

Appendix “B” to Report AUD17005

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