

AUDIT AT A GLANCE

Audit of Corporate Real Estate Management: Strengthening Accountability and Oversight of Change Orders in Capital Projects

WHY THIS AUDIT MATTERS

The Corporate Real Estate Management (CREM) Division is responsible for delivering some of the City's largest capital construction projects.

Our audit focused on CREM's processes for reviewing capital project change orders and related documentation as changes on capital projects can result in project delays and significant cost increases.

BACKGROUND

This audit assessed whether CREM sufficiently monitors and oversees capital project change orders, ensuring that change orders are properly justified, appropriately reviewed and approved.

BY THE NUMBERS

In a sample of 105 change orders across eight capital projects, we identified:

- **\$58K** in overbilling by general contractors for subcontractor work. Another **\$500K+** in charges are currently under investigation
- **35%** of change orders had extra charges for supervision, project management, insurance and/or bonding totalling **\$403K**, in addition to contracted markups of 15-25% of the change order value
 - On one project, a further **\$219K** in extra charges for insurance and bonding on other change orders not in our sample
- **48%** of change orders where markups were not applied according to contract terms, resulting in approximately **\$50K** in overcharges

WHAT WE FOUND

A. Strengthening Processes to Ensure Appropriate Change Order Oversight

- Recently updated change order policies and procedures can be further enhanced to ensure consistent and effective change order oversight. In the sample of change orders we reviewed, we found:
 - Discrepancies between the amounts the general contractor billed and subcontractor invoices, indicating a need for additional review and scrutiny.
 - Incorrect markups as well as extra charges for supervision, project management, insurance, and bonding were applied, in addition to contracted markups. More rigorous review is needed to ensure contract compliance for markups and additional charges.
- CREM should reinforce staff accountability and responsibilities for reviewing, approving, and overseeing all change orders and related supporting documentation.

B. Reinforcing Roles and Accountabilities for Change Order Review and Approval

- There is limited evidence that CREM project managers independently review change orders and supporting documentation. They rely significantly on external consultants' review and recommendations when approving change orders.
- CREM is ultimately responsible and must ensure change orders are justified, properly documented, and in the best interest of the City. Review and approval processes can be improved. We found:
 - Change orders and directives did not always have timely approvals and were, at times, missing required approvals.
 - Limited evidence of the nature and extent of the CREM project manager and external consultant reviews. Supporting documentation, sufficient cost detail and accurate change order logs were also not always maintained.
- External consultants are often responsible for both project design and reviewing and recommending change orders for City approval. This could create a potential conflict of interest when the same consultant prepares the designs and then determines whether a change order is required, including identifying the reasons for the change (e.g., a design error or omission). CREM does not consistently track change orders resulting from design errors and omissions or have formal policies to address potential cost recoveries for these types of change orders.

C. Improving Performance Through Ongoing Monitoring, Evaluation, and a Stronger Project Management System

- Although some CREM project managers experienced ongoing performance issues with general contractors, the required contractor and consultant performance evaluations were often not completed. When required performance evaluations are not completed, past performance cannot be considered for future contract awards.
- CREM's existing quality assurance reviews of capital projects can be improved to include an expanded scope and more frequent reviews to verify that changes are properly reviewed, approved, documented, justified, and comply with contract terms.
- CREM does not have a centralized construction project management system. Standard tools and templates are not used to track change orders and monitor project activity. This limits the Division's ability to analyze trends and identify opportunities to improve change order processes.

HOW RECOMMENDATIONS WILL BENEFIT THE CITY

Implementing the 11 recommendations in the report will strengthen CREM oversight and accountability of capital projects, reduce the risk of errors, overpayments, and contract non-compliance, and support better management of changes within the project budget and schedule.