

Office of Audit and Advisory Services  
401 Golden Shore, 4th Floor  
Long Beach, CA 90802-4210

562-951-4430  
562-951-4955 (Fax)  
lmandel@calstate.edu

January 10, 2017

Dr. Eduardo M. Ochoa, President  
California State University, Monterey Bay  
100 Campus Center, Administration Bldg.  
Seaside, CA 93955-8001

Dear Dr. Ochoa:

**Subject: Audit Report 16-12, Academic Building II, California State University, Monterey Bay**


We have completed an audit of the *Academic Building II* construction project as part of our 2016 Audit Plan, and the final report is attached for your reference. The audit was conducted in accordance with the Institute of Internal Auditors' *International Standards for the Professional Practice of Internal Auditing*.

I have reviewed the management response and have concluded that it appropriately addresses our recommendations. The management response has been incorporated into the final audit report, which has been posted to the Office of Audit and Advisory Services' website. We will follow-up on the implementation of corrective actions outlined in the response and determine whether additional action is required.

Any observations not included in this report were discussed with your staff at the informal exit conference and may be subject to follow-up.

I wish to express my appreciation for the cooperation extended by the campus personnel over the course of this review.

Sincerely,



Larry Mandel  
Vice Chancellor and Chief Audit Officer

c: Timothy P. White, Chancellor

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**The California State University**  
Office of Audit and Advisory Services

## **CONSTRUCTION**

**California State University,  
Monterey Bay**

**Academic Building II**

Audit Report 16-12  
December 5, 2016

## EXECUTIVE SUMMARY

### OBJECTIVE

The objectives of the audit were to ascertain the effectiveness of construction management policies and procedures related to the fiscal, operational, and administrative controls over construction activities, determine the adequacy of internal controls and processes, identify cost recovery opportunities, and ensure compliance with relevant governmental regulations, Trustee policy, Office of the Chancellor directives, and campus procedures.

### CONCLUSION

Based upon the results of the work performed within the scope of the audit, a few specific control weaknesses were noted; generally, however, controls were adequate, appropriate, and effective to provide reasonable assurance that risks were being managed and objectives were met. We identified opportunities to improve controls over Group II equipment, assuming beneficial occupancy, and project completion.

Specific observations, recommendations, and management responses are detailed in the remainder of this report.

## OBSERVATIONS, RECOMMENDATIONS, AND RESPONSES

### 1. GROUP II EQUIPMENT

#### OBSERVATION

Group II equipment purchased for the Academic Building II project could not always be located.

Specifically, we were unable to locate an eight-channel audio mixer worth \$1,140.

Insufficient control over equipment increases the risk of theft, loss, or unauthorized use of state property and misstated property records.

#### RECOMMENDATION

We recommend that the campus promptly locate the missing audio mixer, or adjust the property records accordingly.

#### MANAGEMENT RESPONSE

We concur. Following a thorough search, the audio mixer (Tag # U026346) was declared lost and the property records were adjusted to reflect the retirement, effective August 30, 2016.

### 2. BENEFICIAL OCCUPANCY

#### OBSERVATION

The campus did not execute a change order following the issuance of field instructions when the campus began occupying the Academic Building II project.

Specifically, we found that the campus issued a field instruction to the construction manager starting on June 24, 2015, that notified the contractor that the campus was taking beneficial occupancy of the Academic Building II project. However, the campus did not execute a corresponding change order following the issuance of the field instruction, as required by Integrated California State University Administrative Manual (ICSUAM) §9830.02, *Occupancy Prior to Acceptance*.

When change orders are not properly executed before beneficial occupancy occurs, there is an increased risk of misunderstandings and miscommunication regarding rights and responsibilities.

#### RECOMMENDATION

We recommend that the campus execute change orders following the issuance of field instructions when it begins occupying a project.

**MANAGEMENT RESPONSE**

We concur. The campus will issue a memo stating that change orders should be executed following the issuance of field instructions when the campus begins occupying a project.

**3. PROJECT COMPLETION**

**OBSERVATION**

The campus filed the Notice of Completion for the Academic Building II project before finalizing the project closeout checklist and the certification of completion, as required by ICSUAM §9830.03, *Final Inspection of Construction*.

Filing the Notice of Completion before finalizing the project closeout checklist and the certification of completion increases the risk of misunderstandings and miscommunication regarding rights and responsibilities.

**RECOMMENDATION**

We recommend that the campus reiterate to staff that the project closeout checklist and the certificate of completion should be finalized before the Notice of Completion is filed.

**MANAGEMENT RESPONSE**

We concur. The campus will issue a memo to reiterate to staff that the project closeout checklist and the certificate of completion should be finalized before the Notice of Completion is filed.

## GENERAL INFORMATION

### BACKGROUND

In November 2011, the Board of Trustees (BOT) approved schematic plans for the California State University, Monterey Bay (CSUMB) Academic Building II project at a cost of \$44,313,000, with funding from lease revenue bonds approved in fiscal year 2011/12 and \$2,000,000 in non-state funds from the CSUMB University Corporation.

In April 2011, the campus executed an agreement with the architectural firm HMC Architects for services related and incidental to the design and construction of the Academic Building II project. It also executed an agreement with the construction manager (CM), Rudolph and Sletten, Inc., for preconstruction services that included design and bid phase services. In January 2014, the campus executed a guaranteed maximum price (GMP) agreement with the CM for construction phase services at a construction cost of \$33,215,132 and issued a Notice to Proceed on January 6, 2014, with a completion date of March 31, 2015. The campus filed a Notice of Completion on December 15, 2015.

The Academic Building II project is a 58,000-square-foot facility located west of the Tanimura and Antle Family Memorial Library. The facility serves as the new home to the College of Business and the School of Information Technology and Communications Design. The building has two and three levels tied together by an atrium and includes eight classrooms; 12 laboratories; offices for faculty members, departments, and the dean of the College of Business; conference rooms; student study areas; and a graduate student lounge. Spaces were organized to ensure learning environments and staff areas receive natural light; storm water runoff will be contained on site; water-conserving plumbing fixtures were used; and heat-producing direct sunlight is kept to a minimum with an exterior screen wall. The project achieved a Leadership in Energy and Environmental Design (LEED) gold rating. LEED is a third-party certification program begun in 1999 by the United States Green Building Council and is a nationally accepted benchmark for the sustainable “green” design, construction, and operation of buildings.

The CSUMB campus managed the Academic Building II project, and it chose the CM at Risk with GMP delivery method. In this method, a construction management firm chosen by a competitive bidding process provides all or significant portions of design and construction administrative services and takes part in establishing the GMP. The CM at Risk acts as the general contractor during construction, assumes the risk of subcontracting the work, and guarantees completion of the project. The liability for the success in completing the project on time and in budget lies with the construction manager, and not with the university. Further, there is a potential for cost savings should the project be completed below the GMP.

Campus presidents have been delegated the authority to directly manage state and non-state funded capital outlay projects. The chancellor’s office issues this delegated authority to the campus subject to its compliance with the capital outlay certification procedure. To comply, the campus submits a request for Delegation of Capital Outlay Management Authority to the Certification Review Board (CRB) for review. Then the executive vice chancellor and chief financial officer in the chancellor’s office must approve the request. The campus president is responsible for ensuring that he or she exercises delegated authority in compliance with applicable statutes, regulations, and BOT policies; the campus manages capital projects via a

process consistent with the provisions of the ICSUAM; and the campus has in place appropriate internal controls and processes to ensure that responsibilities are carried out in a manner consistent with the campus capital outlay management plan submitted with the request for delegated authority.

The campus capital outlay management plan defines the campus organizational and operational structure and expenditure authority and serves as the campus policies and procedures for the administration of construction activities. Updated plans are to be submitted when campus operational structure changes are made that impact the plan. Certification is continuous unless a Capital Planning, Design and Construction (CPDC) post-project performance review determines that problems were caused by campus negligence, in which case the CRB may recommend that the campus be placed on probation. The CRB may ultimately recommend that certification be withdrawn if identified operational/management deficiencies are not remedied.

For those campuses that are not certified, the chancellor's office may execute a Memorandum of Delegation for a capital outlay project, which delegates administration, including construction management, to the campus. Alternatively, the CPDC construction management unit may perform construction administration and management.

Each campus president (or designee) also has been delegated authority to make all professional appointments relative to capital outlay projects and campus physical development in accordance with applicable statutes, regulations, BOT policies, and ICSUAM provisions; and must ensure the use of systemwide standardized architectural, engineering, and other professional appointment contract forms. Further, each construction administrator, project manager, inspector of record, campus representative, and design professional is required to use the California State University (CSU) *Construction Management Project Administration Reference Manual*, which contains the CSU construction management policies and procedures that apply to a project.

## SCOPE

We visited the CSUMB campus and the offices of the CM and selected subcontractors from July 18, 2016, through August 19, 2016. Our audit and evaluation included the audit tests we considered necessary in determining whether fiscal, operational, and administrative controls for the Academic Building II project were in place and operative.

Specifically, we reviewed and tested:

- Delegation of construction management authority.
- Review and approval of project design, budget, and funding.
- Professional services agreements and any extra services changes.
- Administration of the bid and award process.
- Contract execution and required contract bonds and insurance.
- Subcontractors and subcontractor substitutions.
- Contract and service agreement payment processing.

- Procurement of major equipment and materials.
- Performance of required inspections and tests.
- Review, approval, pricing, and tracking of change orders.
- Administration of subcontractor labor rates and associated burden.
- Construction management and overall project cost accounting and reporting.
- Construction allowances and contingency balances.

As a result of changing conditions and the degree of compliance with procedures, the effectiveness of controls changes over time. Specific limitations that may hinder the effectiveness of an otherwise adequate system of controls include, but are not limited to, resource constraints, faulty judgments, unintentional errors, circumvention by collusion, and management overrides. Establishing controls that would prevent all these limitations would not be cost-effective; moreover, an audit may not always detect these limitations.

Our testing and methodology was designed to provide a review of key operational and administrative controls, which included detailed testing on a limited number of CM and selected subcontractor transactions. Our review did not examine all aspects of financial controls or encompass all financial transactions for every contractor and subcontractor.

## CRITERIA

Our audit was based upon standards as set forth in CSU Board of Trustee policies; Office of the Chancellor policies, letters, and directives; campus procedures; and other sound administrative practices. This audit was conducted in conformance with the Institute of Internal Auditors' *International Standards for the Professional Practice of Internal Auditing*.

This review emphasized, but was not limited to, compliance with:

- Executive Order (EO) 672, *Delegation of Capital Outlay Management Authority and Responsibility*
- EO 666, *Delegation of Professional Appointments Related to Capital Outlay Projects and Campus Physical Development*
- ICSUAM §9000 through §9005, *Capital Outlay and Public Works Contracts*
- ICSUAM §9200 through §9212, *Professional Services for Campus Development*
- ICSUAM §9230 through §9237, *Project Plan Development for Major Capital Construction Projects*
- ICSUAM §9700 through §9843, *Construction Management for Public Works Contracts*
- CSU *Construction Management Project Administration Reference Manual*
- CSU *Administration of University Property - Equipment Procedures*
- *Contract General Conditions for CM at Risk with GMP Projects*
- Public Contract Code Chapter 2.5, *CSU Contract Law*
- Public Contract Code §4100 *et seq.*, *Subletting and Subcontracting Fair Practices Act*
- Government Code §13402 and §13403



## AUDIT TEAM

Assistant Vice Chancellor/Deputy Chief Audit Officer: Janice Mirza  
Senior Auditor: Jamarr Johnson