Contract Management

February 2015

Prepared by the Audit Division

Report Number 14-03

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EXECUTIVE SUMMARY

The California High-Speed Rail Authority's (Authority), Audit Division has completed an audit of the Authority's contract management activities. According to the State Contracting Manual, a contract manager is the authorized representative of the State of California responsible for administering a contract and monitoring the contractor's performance.

To administer its contracts, the Authority uses contract managers. The Authority's contract manager provides oversight of contract activities and deliverables, reviews and approves invoices, and responds to any concerns regarding contract performance.

The objective of the audit was to determine if the Authority is managing contracts effectively and in accordance with the State Contracting Manual and the Authority's 2009 Contract Administration Manual. To accomplish this objective, we selected a sample of contracts executed on or before August 31, 2014, with an amount equal to or greater than $250,000. In addition, we took into account the auditor's perception of the complexity of contract management for sample selection.

Our audit identified the following issues:

- The Authority has not sufficiently implemented a structured contract management process
- Responsibility for contract management is not always coordinated when divided among multiple Authority staff and/or other contractors
- Performance of contract management activities is not always documented
- Contract managers do not have a clear understanding of what constitutes rework
- Not all contract provisions are being monitored

The report contains the following recommendations:

- Implement contract management policy and procedures already in place. Develop effective, comprehensive contract management processes unique to the types of contracts the Authority manages.
- Disseminate policies and procedures to staff that are tasked to perform contract management
- Provide additional training specific to contract management activities and emphasize the need for adequate documentation and monitoring of contract provisions
- Implement a formalized system of review and oversight of staff tasked to perform contract management

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BACKGROUND

The California High-Speed Rail Authority (Authority) is tasked with developing the nation's first high-speed rail system to connect the mega-regions of the state, spur economic development, protect the environment, and create jobs while preserving agricultural and protected lands. To achieve these goals, the Authority contracts with numerous consultants and governmental agencies to provide products and services.

According to the Authority's Contract and Expenditure Report for August 2014, the Authority has active contracts totaling approximately $2.2 billion of which approximately $300 million has been expended. The contracts include, but are not limited to: a Program Management Team, Regional Consultants (responsible for developing engineering, planning, and environmental documents), Project Construction Managers, Right-of-Way Consultants, and Legal Services. Many of the contracts have a scope of work that require complex engineering and environmental deliverables.

The State Contracting Manual, Volume 1, Chapter 9, specifically outlines requirements and recommendations for the conduct of contract administration and management. The State Contract Manual states that a contract manager is the authorized representative of the State of California responsible for administering a contract and monitoring the contractor's performance.

To administer these contracts, the Authority uses contract managers. The Authority's 2009 Contract Administration Manual details guidelines for contract managers to follow when managing and administering contracts. A Contract Manager's Handbook was issued in July 2014. Contract management training is conducted by the Authority's Fiscal Services Division and offered to employees engaged in contract administration and management activities.

The Authority's contract manager provides oversight of contract activities and deliverables, reviews and approves invoices, and responds to any concerns regarding contract performance. The contract manager is required to follow applicable State guidelines and Authority policies and procedures.

The Authority's business risks related to the effective management of contracts include, but are not limited to: non-compliance with contract provisions; contractors paid for work not performed; and, cost claimed that are not in accordance with the contract.

SCOPE AND METHODOLOGY

The scope of the audit was to examine contract management activities after contracts are approved and executed. To accomplish this, we selected a sample of contracts executed as of August 31, 2014, with an amount equal to or greater than $250,000. The objective of the audit was to determine if the Authority is managing contracts effectively and in accordance with the State Contracting Manual and the Authority's 2009 Contract Administration Manual.

In selecting individual contracts for testing, we took into consideration the number of contracts, contract amounts, and the auditor's perception of the complexity of contract management. Our testing included 23 of the 31 (74%) Authority contract managers and $1.3 of the $1.8 Billion (72%) of contract dollars, excluding the design-build contract. The design-build contract was excluded because a performance audit of this contract is planned for 2015.

To determine if the Authority was effectively managing contracts in accordance with requirements of the State Contracting Manual and the Authority's 2009 Contract Administration Manual we reviewed and analyzed the Authority's contract records and other supporting documents. In addition, the following procedures were performed:

- Reviewed State Contracting Manual, Volume 1, Chapter 9, related to contract administration and management
- Reviewed the Authority's 2009 Contract Administration Manual for policies and procedures to be followed by the Authority. The revised Contract Administration Manual was not utilized because it was released two months prior to the initiation of our audit.
- Interviewed Authority employees involved with contract management activities to determine the processes followed related to contract administration and management
- Reviewed provisions and deliverables for Authority contracts
- Reviewed contract file documentation and correspondence
- Obtained evidence related to methods the Authority uses to manage contracts

Except as noted, we conducted our audit in accordance with the standards for the professional practice of internal auditing. However, we are unable to cite compliance with the standards because the Authority's Audit Division has not undergone a peer review as required by the standards due to the recent formation of the Audit Division and the lack of a body of work to be reviewed.

The review took place at the Sacramento, San Jose, Los Angeles, and Fresno offices.

The results of the audit were discussed with management on December 19, 2014. The Authority has provided a response to the findings and recommendations identified in this report, which is attached. We have reviewed the response and it satisfactorily addresses the findings and recommendations.

This report is intended for management's use. However, this report is a public document and its distribution is not limited.

RESULTS AND RECOMMENDATIONS

The results of our audit are discussed below along with recommendations for improvement.

1. The Authority has not sufficiently implemented a structured contract management process.

   A structured contract management process ensures the lines of responsibility are clear for administering a contract, and monitoring and evaluating the contractor's performance. Authority contract managers did not always receive proper guidance, and/or the contract manager lacked the technical expertise required to provide overall management of a contract. Furthermore, contract managers were not completely aware of their responsibilities such as ensuring invoices comply with agreement provisions.

   Our audit identified that Authority staff are not always being utilized as subject-matter experts. For example, an Authority contract manager provided a matrix used to track and log review comments made by the Federal Railroad Administration for a deliverable submitted by an Authority regional consultant. The matrix identified the consultant staff that responded to the Federal Railroad Administration review comments. However, it did not identify the use of Authority staff members who are subject-matter experts and whose work is possibly impacted as a result of the deliverable produced by the regional consultant.

   There were numerous instances where the Authority utilized personnel and/or outside consultants to manage contract duties, but roles were not defined regarding responsibilities for ensuring cost incurred complied with agreement provisions. For example, six out of twenty contract managers interviewed did not provide us with sufficient evidence in their contract files that ensured agreement provisions were complied with. In addition, the contract manager often was not provided information from the previous contract manager; therefore, they had no evidence of how the contract was managed prior to inheriting contract management duties.

   <u>Recommendations:</u>

   - Implement contract management policies and procedures in place. Develop effective, comprehensive contract management processes unique to the types of contracts the Authority manages, specifically addressing responsibilities of contract managers, procedures for use of responsible subject-matter experts, and contract management responsibilities when performed by other entities (e.g. Program Management Team, and San Joaquin Regional Rail Commission)
   - Establish performance standards for contract management
   - Implement a formalized system of review and oversight of the staff that perform contract management
   - Provide additional training specific to contract management activities including the need for adequate documentation
   - Disseminate policies and procedures to staff tasked to perform contract management

2. Responsibility for contract management is not always coordinated when divided among multiple Authority staff and/or other contractors. While segmented contract management evolved out of necessity due to low staffing levels and complexity of the Authority's various agreements, roles and responsibilities have not been clearly defined. The Authority contracts with a Project Management Team that has expertise in developing High-Speed Rail programs. The Project Management Team is often used for designated assignments such as assisting the Authority in monitoring contract performance of other contractors because of their expertise and the complexity of the agreements. However, roles and responsibilities were not always clearly defined and communicated between the Division, contract managers and the Project Management Team before contract management duties were segmented. For instance, the Project Management Team develops the workload per task order, and management subsequently oversees the workload, but the contract manager reviews the deliverables and approves invoices. As a result of the lack of communication of roles and responsibilities, contract managers were not fully aware whether invoices being approved were for services in compliance with agreement provisions and/or that deliverables in relation to costs incurred were reasonable.

   Recommendation:

   Develop individual Contract Work Plans that include, but are not limited to, how segmented responsibilities will be managed. Specifically, a communication plan between parties involved in contract management that will:

   - Identify the roles of the parties involved and what their responsibilities are.
   - Match responsible parties with their expertise and/or provide training/expertise in their areas of responsibility.

3. Performance of contract management activities is not always documented. We found instances of insufficient evidence to ensure Scope of Work provisions, technical requirements, completion date, etc. were monitored. One instance occurred because the contract manager lacked experience and/or technical expertise to document and ensure that the Scope of Work was completed; therefore, an uncompleted requirement went unnoticed until it was brought to the contract manager's attention by another source. The Authority also has not sufficiently implemented contract management policies and procedures; therefore, a lack of review and oversight exists to assure contract management documentation was evident as required by the State Contracting Manual and Authority's 2009 Contract Administration Manual guidelines.

   Recommendations:

   - Implement contract management policies and procedures in place. Develop effective, comprehensive contract management processes unique to the types of contracts the Authority manages, specifically documentation requirements in compliance with scope of work, State Contract Manual, and Contract Administration Manual requirements.

- Implement a formalized system of review and oversight of staff who perform contract management.
- Provide additional training specific on contract management activities, including the need for adequate documentation.

4. Contract mangers do not have a clear understanding of what constitutes rework, which creates the risk of paying for unacceptable deliverables, due in part to the fact that the Authority does not have a clear policy in place for contract management and the definition of rework. Rework that is invoiced and ultimately paid for may not have been identified and/or defined as a result of lack of policies and definition of rework. The lack of clear understanding of rework contributed to the belief that the contract manager does not have adequate recourse to prevent reimbursing consultants for rework.

   Recommendations:

   - Develop contract management policies and procedures to define what constitutes rework for the types of contracts the Authority manages.
   - Develop training specific to contract management activities and the need for contract managers to apply standards that assure deliverables are satisfied within reasonable timeframes and costs.

5. Not all contract provisions are being monitored. The Authority has not sufficiently implemented a clear policy that requires Contract Managers review invoice requirements and ensure agreement provisions were satisfied. Furthermore, our review identified that some Contract Managers were not sufficiently experienced to provide adequate contract management. For instance, Contract Managers whose contracts had insurance provision requirements stated they did not monitor applicable insurance requirements because they were unaware of the specific contract provision.

   Furthermore, invoices sometimes do not comply with other agreement provisions. For example, invoices would only provide names and totals, but do not provide descriptions of the work, or do not identify the agreement numbers.

   Recommendations:
   - Implement contract management policy and procedures, specifically, documentation requirements in compliance with State Contract Manual and agreement provisions
   - Implement a formalized system of review and oversight of staff who perform contract management
   - Provide additional training specific to contract management activities and the need for adequate documentation

CALIFORNIA High-Speed Rail Authority

Memorandum

DATE: 02/19/2014

TO: Ms. Paula Rivera, Senior Management Auditor

FROM: Frank Vacca, Chief Program Manager
Russell Fong, Chief Financial Officer

CC: Jeff Morales, Chief Executive Officer
Dennis Trujillo, Chief Deputy Director
Thomas Fellenz, Chief Counsel

SUBJECT: Contract Management Audit Response

The Authority had an opportunity to review the draft Contract Management Audit, Report Number 14-03. Attached please find a written disposition of the findings and proposed actions for inclusion in the final report.

We concur with the findings in the draft report. In general, the Authority has established contract management policies, procedures, roles and responsibilities. However all contract managers have not implemented them consistently. In order to manage contracts effectively, the Authority will continue to focus on contract manager training, performance assessment, and improving communication and information dissemination.

If you have any questions or for further discussion, please contact Russell Fong, Chief Financial Officer, at (916) 431-2929 or Russell.Fong@hsr.ca.gov.

Attachments:

(1) Attachment A: Response to Audit Division Report Number 14-03

Attachment A

High-Speed Rail Authority
Response to Audit Division Report Number 14-03

Finding 1
The Authority has not sufficiently implemented a structured contract management process.

Recommendation
- Implement contract management policies and procedures in place. Develop effective, comprehensive contract management processes unique to the types of contracts the Authority manages, specifically addressing responsibilities of contract managers, procedures for use of responsible subject-matter experts, and contract management responsibilities when performed by other entities (e.g. Program Management Team, and San Joaquin Regional Rail Commission)
- Establish performance standards for contract management
- Implement a formalized system of review and oversight of the staff that perform contract management
- Provide additional training specific to contract management activities including the need for adequate documentation
- Disseminate policies and procedures to staff tasked to perform contract management

Response
We concur with this finding. The Authority is following the guidance provided by the State Contract Manual and has established the contract policies and procedures. The contract performance standards have been developed and focus on parameters surrounding scope, cost and schedule. The performance standards provide a platform for management oversight during biweekly contract process meetings which focus on contract monitoring and oversight. The quality management team continues to perform quality assessment to measure compliance to procedures and to ensure roles and responsibilities in contracts and procurements are evident. Training materials previously used for contract management were revised to include more information on contract monitoring and materials are posted on the Authority's intranet website for reference and refresher. Phase I of contract manager training, which provided a broad overview of the contract process, has been provided from July to December 2014 with seventy (70) managers and staff attending. Phase II of the training will focus more in depth on contract management and is scheduled for March and April 2015.

Finding 2
Responsibility for contract management is not always coordinated when divided among multiple Authority staff and/or other contractors.

Recommendation

- Develop individual Contract Work Plans that include, but are not limited to, how segmented responsibilities will be managed. Specifically, a communication plan between parties involved in contract management that will:
    - Identify the roles of the parties involved and what their responsibilities are
    - Match responsible parties with their expertise and/or provide training/expertise in their areas of responsibility.

Response
We concur with this finding. As the program is evolving, the Authority is continuing to evaluate the approach to contract management and assigning qualified contract managers and task managers. For contracts that span multiple disciplinary areas, such as the Program Management Team, the roles and responsibilities for approving deliverables and expenditures for the task managers, who are the subject matter experts, contract managers, and administration staff are clearly defined. This approach to documenting roles, responsibilities, and communication paths will be covered in the Phase II contract management training in March and April 2015.

Finding 3
Performance of contract management activities is not always documented.

Recommendation

- Implement contract management policies and procedures in place. Develop effective, comprehensive contract management processes unique to the types of contracts the Authority manages, specifically documentation requirements in compliance with scope of work, State Contract Manual, and Contract Administration Manual requirements
- Implement a formalized system of review and oversight of staff who perform contract management
- Provide additional training specific to contract management activities, including the need for adequate documentation

Response
We concur with this finding. Procedures and training materials were updated to include the requirements needed for appropriate contract documentation. Architectural and Engineering contract managers have been using a uniform filing system with standardized record keeping and contract file management practices. We have incorporated the uniform filing system into the Phase II contract management training which will be conducted in March and April 2015. The Authority quality management team will perform quality assessment of file documentation and evaluate compliance with the procedures.

Finding 4
Contract mangers do not have a clear understanding of what constitutes rework.

Recommendations:

- Develop contract management policies and procedures to define what constitutes rework for the types of contracts the Authority manages
- Develop training specific to contract management activities and the need for contract managers to apply standards that assure deliverables are satisfied within reasonable timeframes and costs

Response
We concur with this finding. The Phase II contract management training includes exercises involving rework scenarios to support best practices in a variety of situations and to support the delivery of the contract scope of work. These exercises include how to implement change orders and how to effectively review and approve, and if necessary, dispute, contract expenditures. Phase II contract management training is scheduled for March and April 2015.

Finding 5
Not all contract provisions are being monitored.

Recommendations:

- Implement contract management policy and procedures, specifically, documentation requirements in compliance with State Contract Manual and agreement provisions
- Implement a formalized system of review and oversight of staff who perform contract management
- Provide additional training specific to contract management activities and the need for adequate documentation

Response
We concur with this finding. Phase II contract manager training in March and April emphasizes monitoring and enforcing contract provisions and proper documentation. The quality management team has been assisting in the development of contract management performance standards to measure compliance to procedures and to ensure roles and responsibilities in contracts and procurements are evident. The Authority Quality Management team will continue to perform a quality assessment to ensure compliance among all Authority working groups. Some contract managers have been using the developed uniform record keeping system, but not all. The Phase II contract management training scheduled for March and April 2015 will emphasize usage of the uniform filing system.