



UCSB Audit and Advisory Services  
Internal Audit Report

**Construction Activities**

March 31, 2016

**Performed by:**  
Amin Berrah, Senior Auditor  
Laurie Liao, Staff Auditor

**Approved by:**  
Robert Tarsia, Director

Report No. 08-16-0008

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AUDIT AND ADVISORY SERVICES  
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March 31, 2016

To: Vice Chancellor Administrative Services Marc Fisher  
Jack Wolever, Director of Design and Construction Services  
Administrative Services

Re: **Construction Activities**  
**Audit Report No. 08-16-0008**

As part of the 2015-16 annual audit services plan and in conjunction with a systemwide effort, Audit and Advisory Services has completed an audit of Construction Activities. Enclosed is the audit report detailing the results of our review.

The primary purpose of the audit was to assess the effectiveness of University of California Santa Barbara (UCSB) construction management policies, procedures, internal controls, and processes related to selected construction activities in the areas of bidding, insurance, change orders, and funding requirements.

The scope of the review included construction projects currently in progress, or in progress during fiscal years 2012-13, 2013-14, and/or 2014-15.

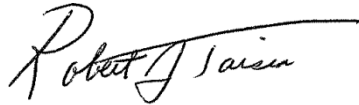
The scope of our review included:

- Bidding and Contracting - The bidding process, construction documents, contractor pre-qualification, and contract award.
- UC Insurance Program (UCIP) - General contractor and subcontractor enrollments.
- Change Orders - Data gathering for analysis, project management review and evaluation processes, change order volume, and change order pricing and compliance with base contracts.
- Construction Funding - Analysis of construction funding sources and restrictions, and monitoring responsibilities and practices.

The audit found no critical weaknesses in the areas included in the scope of our review. We did identify a need for better recordkeeping for bid and award processes, as well as opportunities for improvement in some campus practices for reviewing the costs of change orders, monitoring insurance compliance, and ensuring compliance with construction funding restrictions and requirements.

Detailed observations and management corrective actions are included in the following sections of the report. The management corrective actions provided indicate that each audit observation was given thoughtful consideration and that positive measures have been taken or planned to implement the management corrective actions. The cooperation and assistance provided during the review was greatly appreciated. If you have any questions, please feel free to contact me.

Respectfully submitted,

A handwritten signature in black ink that reads "Robert Tarsia". The signature is written in a cursive style with a long horizontal stroke extending from the end of the name.

Robert Tarsia  
Director  
Audit and Advisory Services

Enclosure

cc: Chancellor Henry Yang  
Greg Moore, Associate Director of Contracting Services, Campus Design and Facilities  
Karl Burrelsman, P.E., University Representative, Design and Construction Services  
Olga Mery, Financial Manager, Financial & Administrative Services, Campus Design and Facilities  
UCSB Audit Committee  
Senior Vice President and Chief Compliance and Audit Officer Sheryl Vacca

## **PURPOSE**

The primary purpose of the audit was to assess the effectiveness of University of California, Santa Barbara (UCSB) construction management processes, policies, procedures, and internal controls related to selected construction activities in the areas of bidding, insurance, change orders, and requirements and restrictions related to funding. This audit is part of UCSB's 2015-16 audit services plan and was performed in conjunction with a systemwide effort.

## **SCOPE, OBJECTIVES AND METHODOLOGY**

The scope of the review included construction projects currently in progress, or in progress during fiscal years 2012-13, 2013-14, and/or 2014-15.

The scope of our review included:

- Bidding and Contracting - The bidding process, construction documents, contractor pre-qualification, and contract award.
- UC Insurance Program (UCIP) - General contractor and first tier subcontractor enrollments.
- Change Orders - Project management review and evaluation processes, change order volume, change order pricing and compliance with base contracts, and data gathering for analysis.
- Construction Funding - Analysis of construction funding sources and restrictions, and monitoring responsibilities and practices.

The audit objectives, which are outlined in detail in Table 1, included:

- Gaining and documenting an understanding of campus processes in the areas included in the audit scope.
- Determining whether campus processes in those areas comply with sound business practices and University policies, including the University of California Facilities Manual.

To accomplish our objectives, we reviewed:

- University and campus policies, procedures, and practices, including relevant sections of the University of California Facilities Manual. The Facilities Manual incorporates key policies, procedures, and guidelines for facilities management and operation; the sections that address funding of capital projects, bidding, and contract modifications were particularly relevant to the areas in the audit scope.
- External guidance and legal and regulatory requirements, including the State of California Public Contract Code and Labor Code.
- Campus reports based on general ledger data that include details of UCSB's construction program, its funding sources, and the status and costs of individual projects.

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We also:

- Interviewed personnel from campus departments involved in various facets of capital improvement and construction, including Design and Construction Services, the Financial & Administrative Services unit of Facilities, and Finance and Resource Management.
- Performed analysis of trends or patterns in the award of projects to contractors and subcontractors in the past 3 years to determine whether they appeared appropriate and reasonable.
- Gathered and analyzed data on all projects with construction costs of \$5 million or more that were fully substantially completed within the last three fiscal years, to determine whether there were possible correlations between contract type/bid selection process and total dollar amount of change orders or construction delays.
- Analyzed and summarized campus construction funding sources and associated requirements and restrictions, and assessed processes in place to monitor and ensure compliance.
- For a sample project, the Davidson Library Addition and Renewal, our work included, but was not limited to:
  - Review and evaluation of documentation of the bidding and award process and contract/construction documents.
  - Consultation with the UC Insurance Program Administrator to determine whether the general contractor and all first tier subcontractors have appropriate insurance coverage.
  - Review of processed change orders over \$100 thousand to determine whether they were competitively bid or had documentation of factors and conditions justifying not conducting competitive bidding.
  - Review of lump sum change orders to ensure that amounts were supported by detailed cost breakdowns, as required.
  - Detailed testing of change orders for proper approvals and costing in accordance with contract terms and conditions; appropriate labor and labor burden rates; reasonableness of material pricing; and determination of whether change order scope of work represented legitimate changes in scope. We also performed recalculations of change orders to check for mathematical errors, and visual inspections of change order work at the project site.
  - Determining whether there were any scope changes between the time of Regental approval of the contract scope and the signing of the contract, and whether any change orders in excess of 25% of total project costs were properly approved.

This audit was conducted in conformance with the *International Standards for the Professional Practice of Internal Auditing*.

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Table 1		Audit Objectives
Review Area	Objectives	
<p><b>Bidding and Contracting</b></p> <ul style="list-style-type: none"> <li>• Bidding Process</li> <li>• Construction Documents</li> <li>• Contractor Pre-Qualification</li> <li>• Contract Award</li> </ul>	<ul style="list-style-type: none"> <li>• Gain and document an understanding of the bidding process for the various types of construction projects and contracts.</li> <li>• Identify trends or patterns in the award of projects to contractors and subs in the past 3 years; determine whether trends or patterns are appropriate and reasonable.</li> <li>• Determine whether bidding processes comply with the University Facilities Manual.</li> <li>• Through review of construction documents for a sample project, determine whether designs, scope, building requirements, etc. are appropriately documented, reviewed, and approved as required by the Facilities Manual.</li> <li>• Determine whether there is an appropriate contractor prequalification process, including proper advertisement, issuance of bidding documents only to prequalified bidders, appropriate prequalification evaluation of potential bidders, and acceptance of bids only from prequalified bidders.</li> <li>• Through review of a sample project, determine whether the contract award process includes proper advertisement of an invitation for bids; bids collected are received on or before the bid deadline and are opened publicly; required items are submitted; contractor selection is appropriate and based on evaluation method prescribed; and whether selected contractors meet the minimum responsibility requirements of licensing, bonding, and insurance.</li> <li>• Because our selected project for detailed review involved a CM-At-Risk contract, determine whether subcontract awards agree to the bid package certification.</li> </ul>	
<p><b>UC Insurance Program</b></p>	<ul style="list-style-type: none"> <li>• For the project selected for review, review the status of all contractor and subcontractor enrollment in UCIP and validate appropriate insurance coverage.</li> </ul>	
<p><b>Change Orders</b></p> <ul style="list-style-type: none"> <li>• Project Management Review and Evaluation</li> <li>• Change Order Volume</li> <li>• Pricing</li> <li>• Compliance With Base Contract</li> <li>• Data Collection and Analysis</li> </ul>	<ul style="list-style-type: none"> <li>• Gain and document an understanding of change order procedures, including thresholds for change orders being treated as a new contract, routing and review processes, and required supporting documentation.</li> <li>• Through review of a sample project, determine whether any change orders exceeding \$100,000 are competitively bid, or that the justification for not competitively bidding is properly documented; and whether change orders based on agreed-upon lump sum amounts are supported by a detailed cost breakdown.</li> <li>• Determine whether change orders have been properly approved, and whether change order costs are in accordance with contract terms and conditions, including labor and labor burden rates, material pricing, etc.</li> <li>• Determine whether change order scope of work represents legitimate changes in scope, and (if possible) whether the work was properly executed.</li> <li>• Collect information on all projects with construction costs of \$5 million or more that were substantially completed within the last three fiscal years, for the purpose of identifying possible correlations between contract type/bid selection process and total dollar amount of change orders or construction delays.</li> </ul>	
<p><b>Construction Funding</b></p> <ul style="list-style-type: none"> <li>• Analysis of Construction Funding Sources and Restrictions</li> <li>• Monitoring Responsibilities and Practices</li> </ul>	<ul style="list-style-type: none"> <li>• Gain and document an understanding of the sources of funding for construction projects over the past three years, and the benefits and/or challenges of particular funding sources; identify the top 3-5 funding sources.</li> <li>• Categorize funding restrictions and requirements by source, determine the most common types of restrictions, gain an understanding of more frequently applied types.</li> <li>• Determine whether funding restrictions and requirements are being interpreted and applied correctly, and identify those that appear to have the most significant risk or negative implications if compliance is not maintained.</li> <li>• Evaluate the adequacy of departmental and staff accountability for ensuring compliance with funding requirements, and the adequacy of departmental practices, procedures, and control structure to monitor compliance with funding restrictions and requirements.</li> </ul>	

Source: Auditor Analysis

## **BACKGROUND**

Design and Construction Services (DCS), a unit of Campus Design and Facilities in the Administrative Services Division, is responsible for the delivery of UCSB's major and minor capital improvement program. Based on data provided by DCS, there have been approximately 157 major and minor projects for the period of 2010 through 2015, with total budgets of \$628 million. Project funding comes from various sources, including state, federal, gift, grant, and University funds.

DCS staffing includes 19 project managers, 10 inspectors, and other support staff. The work of DCS is directly supported by two other Campus Design and Facilities units: Contracting Services, which provides contract administration and other administrative oversight for capital improvement projects; and Financial & Administrative Services, which provides financial, information systems, and personnel and payroll services.

UCSB's Capital Development Office, which is part of the Finance and Resource Management Division, assists the campus in maximizing the utilization of its existing physical facilities and acquiring the physical resources necessary to meet its instruction, research, and public service goals. Through the Campus Planning Committee, the Capital Development Office advises the Chancellor on all matters relating to long range planning, major capital developments on campus, and physical environment, including proposals and progress of capital projects.

### *Davidson Library Addition and Renewal*

The Davidson Library Addition and Renewal project (Library project) expands and updates the existing campus library located at the heart of the UCSB campus. The project adds approximately 60 thousand gross square feet of space and involves renovation of roughly 92 thousand square feet, with a total of 20% more study space. In fall of 2012, the University of California Regents approved the full cost of the building with interim financing for the Library project. The budgeted cost of the Library project was \$79,018,000. Work was started in mid-June 2013 and was completed by December 2015, with the grand opening in January 2016. The four distinct components of the project included:

- A three-story building addition on the north side of the Library to include faculty and student collaboration spaces and Special Research Collections.
- A complete renovation and seismic retrofit of the original two-story building to house the Arts collection, plus additional study and gathering spaces.
- A newly built Paseo, or grand walkway, which connects all parts of the Library as well as the campus.
- A seismic retrofit of the eight-story tower and life-safety upgrades throughout.





Davidson Library, UC Santa Barbara

The Library project was selected as the sample project for detailed testing in the areas of Bidding and Contracting and Change Orders, because it met the criteria established for this systemwide audit. The project:

- Was an active construction project with an estimated completion by January 2016.
- Received Proposition 1D funding.<sup>1</sup>
- Has a budget of \$79 million, which satisfied the \$60 million threshold that was one of the criteria.

The Davidson Library was also chosen over other campus projects because it is considered a critical project approved by the Regents.

#### *University Controlled Insurance Program (UCIP)*

The University of California (UC) has implemented a University Controlled Insurance Program (UCIP) that provides workers compensation, employer's liability, general liability, and excess liability coverage for the enrolled construction manager/general contractor, design-builder, prime contractors, and subcontractors on project sites. The UCIP is a single insurance program that also insures UC, the campus, and other designated parties. UC pays premiums associated with the UCIP, subject to verification that the contract amount is exclusive of all cost of UCIP coverage, and unless otherwise stated in the contract documents.

#### **SUMMARY OPINION**

The audit found no critical weaknesses in the areas included in the scope of our review. We did identify a need for better recordkeeping for bid and award processes, as well as opportunities for improvement in some campus practices for reviewing the costs of change orders, monitoring insurance compliance, and ensuring compliance with construction funding restrictions and requirements.

Audit observations and management corrective actions are detailed in the remainder of the audit report.

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<sup>1</sup> Bond funds designated for the construction and renovation of University of California facilities to address enrollment growth, seismic and life safety needs, and renewal of outdated infrastructure.

**DETAILED OBSERVATIONS AND MANAGEMENT CORRECTIVE ACTIONS**

**A. Bidding and Contracting**

1. Distribution of Construction Contract Awards

Our work in this area included an analysis to identify trends or patterns in the award of construction contracts, and to determine whether any identified trends or patterns appear appropriate and reasonable. To complete this analysis, we analyzed contractor awards over \$100 thousand, and contract awards under \$100 thousand, for the period July 2012 through June 2015, including:

- Number of contracts, and percentage of the count of all contracts, awarded to individual firms.
- Value of contracts, and percentage of the \$ value of all contracts, awarded to individual firms.

The results of this analysis indicate that UCSB awards its construction contracts to a fairly diverse pool of contractors:<sup>2</sup>

- We noted one contractor whose percentage of total awards over \$100 thousand was 27.08%. However, this high percentage resulted from only one award, the North Campus Faculty Housing project (Phase III), a major construction project. Therefore, this percentage does not represent or imply a history of repeated contract awards.
- Also for awards over \$100 thousand, we noted that one contractor was awarded contracts three times over the past three fiscal years, with awards representing approximately 11.36% of total awards over \$100 thousand. A separate contractor was awarded contracts six times over the same period, with awards representing approximately 7.6% of total awards over \$100 thousand. These percentages appear reasonable; in addition, we noted that the average contract value for both of these contractors appears reasonable.
- For awards under \$100 thousand, the contractor with the highest percentage of awards was awarded 39 contracts representing only 5.65% of total awards under \$100 thousand. The average contract value was well within the range of other contractors reviewed.
- We identified five active CM-at-Risk projects during this period. For these projects, we found that each contractor received only one award, and that these selections were based on the "best value" score for each project, as required.

2. Bidding and Contracting

As stated in the Background section of this report, we selected the Library project as our sample project for our assessment of UCSB compliance with Facilities Manual requirements pertaining to the bidding and contract award process, and for our review of contract/construction documents. The Facilities Manual and California Public Contract Code require that all projects with a total budget above \$640 thousand be subjected to a formal, competitive bid process. The Library project had a budget of \$79,018,000, and therefore met that threshold.

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<sup>2</sup> Percentages in this section are based on \$ value of awards, not number of contracts.

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Our review of the bidding and contract award process (including review of all related documents) for the Library project found that the bidding and contract award process followed by Design and Construction Services and Contracting Services overall complied with the Facilities Manual, with some documentation issues. We found that the following required processes were followed:

- Project designs and scope were reviewed by the UC Office of the President, and funding for the Library project was appropriately approved by the UC Regents. We also found documentation of approval by local authorities for water reclamation and recycling aspects of the project.
- The advertisement for prequalification included the date, time, and place from which bidders could obtain pre-qualification documents, and a notice that bidders who submit a proposal for this project must be prequalified.
- Prequalification documents were reviewed using Facilities Manual evaluation parameters.
- Supplementary instructions provided to bidders stated that bidding and bidding documents were limited to prequalified bidders, listed prequalified bidders, specified where bids must be delivered, that submissions were to be accepted on or before the bid deadline, and that bids were to be opened publicly.
- The project was advertised twice in one general circulation publication and twice in a trade paper; and we were able to obtain and review proof of publication. The advertisement for bids stated that the University would follow a best value selection methodology to determine the apparent lowest responsible bidder.
- Firms on the final bid summary sheet had been prequalified, and the awarded contractor was the lowest responsible bidder based on the best value methodology. The selected contractor's bid package included the items listed on the bid form checklist, and other documentation that the minimum responsibility requirements of licensing, bonding and insurance were met.
- The final awards under the contract were consistent with the data contained in the bid certification packages.

We did identify opportunities to improve documentation that proper practices were followed:

- Although we obtained documentation of instructions that bids would not be accepted after the bid deadline and that bids would be publicly opened, we could not obtain documentation of time-stamped bid envelopes or sign-in sheets for the public bid opening. Although we were able to utilize additional audit techniques to ensure that bidding processes were appropriate, Design and Construction Services should ensure that all appropriate documentation, including time-stamped bid envelopes and sign-in sheets for the public bid opening, are maintained as required by the UC policy for records retention and disposition.<sup>3</sup>

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<sup>3</sup> BFB-RMP-2, *Records Retention and Disposition*

**Management Corrective Actions**

Design and Construction Services will remind all personnel to maintain all appropriate bid-related documentation in project records, including time-stamped bid envelopes and sign-in sheets for public bid openings, and copies of all advertisements.

*Audit and Advisory Services will follow up on the status of this issue by May 31, 2016.*

**B. UC Insurance Program (UCIP)**

Our selection of the Library project also included work to verify that contractor and first tier subcontractors were enrolled and covered under UCIP, or had other appropriate insurance coverage, as required. The results of our work indicate that of 38 of the 43 total contractor and subcontractors for the project were appropriately enrolled, and 5 were properly excluded from enrollment due to the specific type of work, which justified exclusion based on UCIP Insurance Manual guidance.

We selected a sample of five contractor and subcontractors to validate appropriate insurance coverage in greater detail, and found that:

- One subcontractor had been appropriately excluded based on UCIP Insurance Manual guidance at the time, but the UCIP Administrator noted that there had been a shift in guidelines that required that the contractor be enrolled in UCIP. To avoid a recurrence, it may be advisable to implement a periodic review process to ensure that any changes in UCIP guidance are reflected in enrollments.
- Two subcontractor suppliers were appropriately excluded from UCIP coverage based on UCIP Insurance Manual guidance. Both subcontractors properly maintained non-UCIP coverage, which was documented by certificates of insurance. We did note, however, that the UCIP Administrator needed to obtain documentation of insurance in response to our requests. The administrator indicated that it is the responsibility of the general contractor to inform the administrator of non-UCIP covered subcontractors, after which the administrator will perform the necessary tracking to ensure that documentation of current coverage is maintained. Due to the duration of the project and a change in administrators, the administrator may not have been adequately ensuring the proper tracking of non-UCIP coverage, especially for subcontractors whose work had already been completed.

To ensure that the University is adequately protected, it may be appropriate for Design and Construction Services to request that contractors ask the UCIP Administrator to perform, and report on, a periodic review to ensure that coverage reflects any changes in UCIP guidance, and that the status of all enrollments and other coverage is appropriate.

**Management Corrective Actions**

Design and Construction Services will request the UCIP Administrator to provide periodic reporting that will enable DCS and contractors to ensure that coverage reflects any changes in UCIP guidance, and that the status of all enrollments and other coverage is appropriate.

*Audit and Advisory Services will follow up on the status of this issue by May 31, 2016.*

## C. Change Orders

### 1. Project Change Order Data Collection and Analysis

As requested by the Office of the President, our work included collecting information on all projects with construction costs of \$5 million or more that were substantially completed within the last three fiscal years, for the purpose of identifying possible correlations between contract type/bid selection process and total dollar amount of change orders or construction delays. We were able to identify one project that fulfilled the selection criteria.

### 2. Change Order Review

As discussed in our background section, the Library project, a major project with 29 processed change order amendments at the time of the audit, was also selected as our sample project for detailed review and testing of change orders.

One of our audit objectives was to determine whether any change orders exceeding \$100 thousand were competitively bid, or that the justification for not competitively bidding was properly documented, as required by the Facilities Manual. We found that eight change orders for the Library project met the \$100 thousand threshold:

- Two change orders were for the purpose of incorporating appropriate subcontractor bid packages, which occurs during Phase 2 in CM-at-Risk projects.
- Six change orders were not competitively bid, but their justifications were all generally appropriate.

We found the following:

- One change order was comprised of multiple changes involving concrete work based on the subcontractor's cost estimates, for a total of \$101,437. However, justification for not putting the work out for bid had not been documented. Since our observation, management has completed sufficient documentation of the justification.
- One change order, associated with a field order for the completion of an in-house cafe, cost approximately \$188,306. The project was the result of plans to upgrade space to accommodate the installation of coffee service equipment. This work was not bid out, based on the judgment that doing so would have caused a critical delay to the entire project. At the time of our review, justification for not putting the work out for bid had not been documented. However, since our observation, management has completed sufficient documentation of the justification.

We also identified one change order that resulted in an increase of the Phase I fee of \$180,000; the documentation for this change did not include support to show that this additional fee was discussed with the Office of the President or Office of the General Counsel, which is recommended in the Facilities Manual for a substantial change in the fee.

To ensure that change orders over \$100 thousand are in compliance with the Facilities Manual, Design and Construction Services should ensure that justifications for not competitively bidding change order work are timely documented, and should retain this documentation in the project records.

### 3. Change Order Pricing

We selected and reviewed eight Library project change orders based on high value for detailed testing of pricing. We found that:

- All change orders were properly approved in accordance with contract terms and conditions.
- There were only minor math or calculation errors that were not material to the change orders or the project as a whole.
- Material quantities appeared reasonable, based on our understanding of the project and our discussions with the project manager.
- Material pricing also appeared reasonable, based on our understanding of the project and in comparison to prices found through internet research.

We also reviewed a sample of five change orders to determine whether change order scope of work represented legitimate changes in scope, and whether the work was properly executed. Our work in this area, which included discussions with the project manager and visual inspection of the change order work, did not disclose any concerns.

Our review of change order pricing also found that:

- One lump sum change order for \$300,000 lacked a detailed cost breakdown, as required by the Facilities Manual. Without this documentation, it would not be possible to review whether charges were being priced appropriately, in accordance with the Facilities Manual or the construction contract documents. The main purpose of this change was to move up the completion date, which did not directly fall under the listed allowable costs of extra work in the contract's general conditions. Although the business decision that resulted in this change order appeared appropriate, in the absence of rain impacts or other contractual reasons, better documentation of the breakdown of related costs should have been prepared and maintained.
- One change order for re-roofing costs of \$252,480 included a quotation for the scope of work. Although the quotation included a brief scope of work, it did not have a detailed cost breakdown. Without this documentation, it would not be possible to review whether charges were being priced appropriately, in accordance with the Facilities Manual or the construction contract documents.
- Supporting documentation for the change order for the in-house cafe work included detailed cost breakdowns, but the change order amount had been negotiated downward, with only the totals adjusted. A revised cost breakdown was not obtained, which precluded us from reviewing whether charges were being priced appropriately, in accordance with the Facilities Manual or the construction contract documents. DCS believes they fulfilled the requirements of the Facilities Manual by obtaining and retaining the original cost breakdown, even though the total cost was subsequently negotiated downward.
- Design and Construction Services did not consistently receive and review a detailed enough cost breakdown to support the labor cost component of change orders. There was no consistent detailed breakdown of labor classifications, hours, and labor and burden rates; this level of detail is needed to adequately review cost estimates before agreeing to the price of a change order.

- One change order increased the construction manager's fee for Phase I of the project, including costs that were not allowable according to the contract's general conditions. We were informed that Design and Construction Services had consulted with the Office of the General Counsel prior to approving this change order, but did not retain any formal documentation.

The results of our work indicate that change order administration would be improved by:

- Ensuring that there is a detailed cost breakdown in all cases.
- Requiring and reviewing detailed cost breakdowns that specify labor classifications, hours, and pay and labor burden rates.
- Maintaining documentation in the project records of consultations with the Office of the General Counsel, especially in instances in which the change is related to the construction manager's fee.

#### **Management Corrective Actions**

We understand that good business practices dictate that DCS should consistently obtain and review detailed breakdowns of labor classifications, hours, and labor and burden rates before agreeing to the price of lump sum change orders. DCS should also ensure that labor rates are consistent with the contract rates for time and materials change orders, and that project records include documentation of consultations with the Office of the General Counsel. DCS will conduct training for project managers to ensure that they understand these issues, and that they conduct reviews of contractor change order pricing in a consistent fashion. The plan is to incorporate, into an upcoming training agenda, a review of the findings of the audit, with a specific focus on change order pricing. Training will be conducted in April 2016.

*Audit and Advisory Services will follow up on the status of this issue by May 31, 2016.*

**D. Construction Funding**

<b>Table 2</b>		<b>UCSB Construction Program Top 6 Funding Sources FY 2012-13 Through FY 2014-15</b>		
<b>Funding Source</b>	<b>Appropriations FY 2012-013 Through FY 2014-15</b>	<b>Active Projects <sup>1</sup></b>		
		<b>FY 2012-13</b>	<b>FY 2013-14</b>	<b>FY 2014-15</b>
Commercial Paper <sup>2</sup>	\$255,983,010	9	13	12
University Funds	114,049,123	91	104	103
State Appropriations	71,544,560	6	4	3
Bonds	8,287,059	5	3	2
Gifts and Private Grants	7,713,784	22	17	29
Federal Grants	1,212,937	6	9	7
<b>Total</b>	<b>\$458,790,473</b>			

Source: Auditor Analysis of General Ledger Data

<sup>1</sup> Active Projects: Capital projects showing appropriation and/or expenditure activity during the audit period.

<sup>2</sup> Serves as a temporary funding source; included two substantial housing projects, with a combined commercial paper appropriation of \$237 million. This temporary funding source will be replaced by long-term bonds, with primary funding for debt service being student housing income.

**1. Funding Sources**

UCSB's construction program is funded by various sources, including state appropriations, University funds, gifts and private grants, bonds issued by the UC Office of the President, and federal grants. State appropriations have been one of the largest funding sources for construction in the past, and are considered to have a greater net impact because they represent new money to the campus, above and beyond operating funds. University funds include campus-based fees, auxiliary fund reserves, and Garamendi funds.<sup>4</sup> Although campus-based fees are also new funds to the campus, they result in higher costs of attendance for students. All funding sources contribute to the University's mission through the development of instructional, research, housing, parking and other general facilities to accommodate present and future growth. Table 2 summarizes the top six sources of funding for UCSB's construction program during the previous three fiscal years.

<sup>4</sup> Garamendi funds are federal indirect cost recovery funds used for the acquisition, construction, renovation, equipping, financing, and maintenance of certain research facilities.



## 2. Funding Restrictions and Requirements

Restrictions and requirements are usually placed on specific sources of funding provided to the campus for construction projects. State funds authorized under Assembly Bill 94 are mainly used for the construction and maintenance of instructional facilities; state funds provided as *general operating funds* can account for a maximum of \$100,000 of the cost of smaller projects with a total cost of \$750,000 or less. Campus-based fees may only be used for the project specified in the ballot language for the related student election that approved the fees, and are reaffirmed on a recurring basis, although any remaining funds (after construction costs) may be used for capital debt repayment, operation and maintenance, and programming within the building. Gift restrictions are usually specific to the gift and may be rigid, although they can be easily identified via the donor letters. Table 3 highlights common requirements and restrictions that come with UCSB's top funding sources for construction.

The audit documented and evaluated the adequacy of departmental and staff accountability for ensuring compliance with funding requirements, and the adequacy of departmental practices, procedures, and controls for monitoring compliance. Several campus departments and units play a role in this area:

- The Office of Research is responsible for submission of faculty research proposals, specifically for preparing, interpreting, negotiating, and accepting agreements on behalf of the Regents for projects funded by federal and state agencies, foundations, and other public and private sources.
- Finance and Resource Management generally monitors restrictions and requirements on funding sources it distributes to Design and Construction Services.
- Extramural Funds Accounting performs financial reporting, gift processing, billing, and other support to departments in managing extramural funds.

Based on the work performed in the scope of this audit, we found that the Financial and Administrative Services unit of Campus Design and Facilities bears the overall responsibility for ensuring compliance with most restrictions and requirements of construction funding. However, Extramural Funds Accounting is responsible for filing the financial reports required by agencies that fund construction.

## 3. Ensuring Compliance with Funding Restrictions and Requirements

Our discussions with campus personnel and other audit work suggest that grant funds used for construction may pose the highest risk for non-compliance with funding restrictions and requirements. Because grant funds are not the most common source of campus construction funding, campus personnel may be less familiar with common restrictions and requirements, such as special reporting requirements, related to construction. In addition, sponsoring agencies have strict deadlines for financial, performance and/or progress reports; not reporting within the mandated timeframes may cause the agency to withhold payment and, in the most severe cases, disallow all or part of the cost.

To ensure compliance with all construction-related funding restrictions and requirements, Design and Construction Services should ensure that responsibility for monitoring compliance with grant funding restrictions is clearly assigned and communicated for each project with grant funding.

**Management Corrective Actions**

Design and Construction Services will issue a memorandum or other guidance to units with responsibilities for compliance with construction-related funding restrictions and requirements, including Finance and Resource Management, Office of Research, Business and Financial Services, and the Financial & Administrative Services unit of Facilities Management. This guidance will include a reminder that appropriate monitoring processes need to be in place.

*Audit and Advisory Services will follow up on the status of this issue by May 31, 2016.*

Table 3	Funding Requirements & Restrictions Highlights
<b>State Appropriations</b>	<ul style="list-style-type: none"> <li>■ Mainly used for the construction and maintenance of instructional facilities.</li> <li>■ State funds provided as general operating funds can account for a maximum of \$100,000 of the cost of smaller projects with a total cost of \$750,000 or less.</li> </ul>
<b>University Funds: Campus Based Fees</b>	<ul style="list-style-type: none"> <li>■ Funding approved by students and can only be used for the proposed project.</li> <li>■ Further restrictions are included in the ballot language.</li> <li>■ Funds remaining after completion of construction may be used for capital debt repayment, operation and maintenance, and programming within the building.</li> <li>■ Ongoing operating expenses associated with a capital project must be reaffirmed by student vote on a recurring basis.</li> </ul>
<b>Gifts</b>	<ul style="list-style-type: none"> <li>■ Restrictions are specific to the gift.</li> </ul>
<b>Bonds</b>	<ul style="list-style-type: none"> <li>■ Bond covenants, as written in the bond indenture.</li> </ul>
<b>Grants</b>	<ul style="list-style-type: none"> <li>■ Generally do not support project manager salaries.</li> <li>■ Will only fund up to eighty (80%) percent of the total construction costs.</li> <li>■ Reports must be received during the mandated timeframe.</li> </ul>
<b>Garamendi Funds*</b>	<ul style="list-style-type: none"> <li>■ Support a specific project scope.</li> <li>■ If change orders are necessary, new funding source(s) have to be identified.</li> </ul>

Source: Auditor Analysis

\* Garamendi funds are federal indirect cost recovery funds used for the acquisition, construction, renovation, equipping, financing, and maintenance of certain research facilities.



**UCSB Building Program 2013-23**

Source: UCSB Finance and Resource Management website