State of California
DEPARTMENT OF TRANSPORTATION

California State Transportation Agency

Memorandum

Serious drought.
Help Save Water!

To: FRANCESCA NEGRI , Chief
Division of Procurement and Contracts

CLARK PAULSEN, Chief
Division of Accounting

CHARLIE FIELDER, District Director
District 1

JOHN BULINSKY, District Director
District 2

BIJAN SARTIPI, District Director
District 4

Date: August 29, 2014

File: P3000-0416

From: WILLIAM E. LEWIS
Assistant Director
Audits and Investigations

Subject: **FINAL AUDIT REPORT OF THE EMERGENCY CONTRACT PROCESS**

Attached is Audits and Investigations' (A&I) final audit report of the Emergency Contract Process. The responses of the Division of Procurement and Contracts, District 2 and District 4 are included as part of the final report.

Please provide our office with status reports on the implementation of audit findings 60-, 180-, and 360-days subsequent to the report date. If all findings are not corrected within 360 days, please continue to provide status reports every 180 days until the audit findings are fully resolved. If you would like, the audit staff can be available to consult in the early stages of implementation to help ensure that changes address the findings and recommendations in our report. As a matter of public record, this report and the status reports will be posted on A&I's website.

If you have any questions or need additional information, please contact Laurine Bohamera, Chief, Internal Audits, at (916) 323-7107, or me at (916) 323-7122.

Attachments

c: Malcolm Dougherty, Director
Norma Ortega, Acting Chief Deputy Director
Mark Leja, Chief, Division of Construction
Tony Tavares, Chief, Division of Maintenance
Megan Rettke, Assistant Division Chief, Services & Commodities, Division of Procurement and Contracts
Jennifer Burnett, Office Chief, Policy, Protest and Communications, Division of Procurement and Contracts
Mark L. Suchanek, Deputy District Director, Maintenance and Operations, District 1
Don Anderson, Acting Deputy District Director, Maintenance and Operations, District 2
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Douglas Gibson, Audit Manager, Audits and Investigations
Roger Takao, Program Controller, Audits and Investigations

P3000-0416
Emergency Contract Process Audit
August 2014

William E. Lewis, Assistant Director
Audits and Investigations
California Department of Transportation

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Summary

The California Department of Transportation's (Caltrans), Audits and Investigations (A&I) completed an audit of the emergency contract process. We performed the audit to determine the adequacy of internal controls, and effectiveness of the emergency contract initiation, execution and payment processes. The audit was conducted as a result of concerns expressed by certain districts about the timeliness of emergency contract payments. We initiated the audit after implementation of the Emergency Force Account (EFA) Team's recommendations to improve the emergency contract process.

The scope of the audit was limited to the review and tests of records and procedures based on the State Administrative Manual, State Contracting Manual and Caltrans' emergency contract process policies and procedures. The audit found that the Division of Procurement and Contracts (DPAC) implementation of the EFA Team's recommendations have significantly reduced the length of time taken to process emergency contracts, enabling more timely payments to contractors.

The audit also determined that the Division of Accounting processed emergency contract invoices and approved claim schedules for payment promptly after receiving the invoices.

Our audit disclosed that adequate internal controls are generally present over the emergency contract process; however, we found the following:

- Further improvements needed to ensure timely execution and payment of emergency contracts.
- Internal control deficiencies noted in the emergency contract process.

Background

Caltrans uses emergency contracts when services or goods are needed to immediately respond to "a sudden, unexpected occurrence that poses a clear and imminent danger requiring immediate action to prevent or mitigate the loss or impairment of life, health, property, or essential public services" as provided by Public Contract Code Section 1102. There are several types of emergency contracts that are processed through DPAC. The most common types are:

Emergency Force Account (EFA) Contracts: These contracts are used to obtain labor, materials, and equipment at direct cost plus prescribed markup for emergencies requiring immediate action because of road closure or danger to public safety. An example of an EFA contract is the repair of a highway section washed away by a mudslide. EFA contracts do not require bids.

Emergency Highway Spills Contracts: These contracts are used to acquire clean up and disposal services of hazardous material such as diesel fuel spilled on highways. Emergency highway spills contracts are also exempt from bids.

Emergency Limited Bid (ELB) Contracts: ELB contracts are a modified type of force account that includes a competitive bidding element. These contracts are used for emergency work that is urgent, but stable. ELB contracts require bids of at least three contractors, and contractors to compete on markup rates of the prime contractor's labor, equipment rental and materials. An example of an ELB contract would be the repair of a state building's roof leak.

The EFA Task Force, comprised of 20 Caltrans' division representatives, was formed to identify areas of delay, and find solutions to streamline the EFA/ELB process to expedite contractor payments. The task force, which issued its findings in August 2011, found that at least 20 EFA or ELB contracts experienced delayed payments from mid-2010 to mid-2011. These delays averaged approximately two to three months.

The task force made recommendations to DPAC that would reduce the time taken to process emergency contracts, and thus improve the timeliness of emergency contract payments. Based on the recommendations, DPAC re-established a contract submittal box for districts to submit all documents to one location, providing a more efficient way to track and assign contracts; and added an additional analyst to process emergency contracts.

Our audit found that since DPAC implemented these changes, the average days to process emergency contracts decreased from 41.9 days between July 1, 2011 and December 31, 2011 to 33 days between January 1, 2012 and December 31, 2012. In addition, the number of emergency contracts that took 100 days or more to process fell from 10 to 7 during the same time period.

Objectives, Scope, and Methodology

We conducted an audit of the emergency contract process to determine the adequacy of internal controls over their initiation, execution, and timeliness of payments.

The audit was performed in accordance with the International Standards for the Professional Practice of Internal Auditing. The objectives of the audit were to:

- Determine if adequate policies, procedures and controls are present to assure proper initiation, execution and timely payment of emergency contracts.
- Determine if established policies and procedures for emergency contracts are followed.

Objectives, Scope and Methodology (Continued)

- Determine if adequate justification exists for emergency contracts.
- Identify factors affecting timeliness of payment for emergency contracts.
- Determine if recommendations of the Enterprise Financial Infrastructure System (E-FIS) Task Force and the EFA Task Force were implemented to improve timeliness of payments.
- Determine the effectiveness of the EFA Task Force's implemented recommendations.

The audit covered the period January 1, 2012, through June 30, 2013, and focused on internal controls and procedural compliance as they related to emergency contract processes. Changes after these dates were not tested, and accordingly, our conclusion does not pertain to changes arising after June 30, 2013.

The audit included interviews and tests as we considered necessary to achieve the above audit objectives. The entities included in the audit were the Divisions of Maintenance, Accounting, Procurements and Contracts, and Districts 1, 2 and 4.

Conclusion

The audit disclosed that adequate policies, procedures and internal controls are generally present over the initiation, execution and payment processes for emergency contracts. Policies and procedures for emergency contracts are followed, and adequate justification exists for emergency contracts.

The audit also found that DPAC implemented the EFA Task Force's recommendations and that the timeliness of emergency contract processing has improved; however, we found the following:

- Further improvements needed to ensure timely execution and payment of emergency contracts.
- Internal control deficiencies noted in the emergency contract process.

Views of Responsible Officials

We requested responses from the Chief of DPAC, and management in Districts 2 and 4. These officials have, in general, concurred with the findings and recommendations. However, with respect to Finding 1, District 4 believes that there could be an encumbrance issue pertaining to unneeded funds and that there should be a revision of the 10-day limit for contract request submittals. Summaries of the responses are included in the body of the report. For the complete responses, please see Attachments 1 to 3.

William E. Lewis,
Assistant Director
Audits and Investigations
August 26, 2014

FINDINGS AND RECOMMENDATIONS

Finding 1 - Further Improvements Needed to Ensure Timely Execution and Payment of Emergency Contracts

We reviewed contract files for thirty emergency contracts and found 10 instances (33 percent) in Districts 2 and 4 where the timeliness of contract request submissions to the Division of Procurement and Contracts (DPAC) could be improved. Eight of these were for contracts to clean hazardous spills; one was for cleaning a homeless encampment, and the other was for grinding overlay at the San Francisco Oakland Bay Bridge Plaza. The contract managers took between 14 and 48 working days after the work was completed to submit the contract requests to DPAC.

Staff in Districts 2 and 4 stated that the cost of hazardous material spills was hard to determine, and an incorrect estimate could result in a contract request that was substantially different than the actual cost of work. To avoid this, staff only submitted service contract requests to DPAC once they received the invoices from the contractor.

The State Contracting Manual (SCM), Section 4.09.B, "Necessity of Time Management", requires contracting departments to execute and submit contracts timely. In addition, the Division of Maintenance's Maintenance Policy Directive, Number 601, on emergency spills, requires that requests for contracts should be sent to DPAC within 10 working days after spill clean-up is completed.

Recommendations

We recommend that the districts submit emergency contract requests to DPAC as soon as possible with estimates large enough to cover unexpected additional costs. For hazardous material spill contracts, where experience indicates a certain range of costs, the districts should consider using set threshold estimates above average contract costs, to expedite contract request submittal.

DPAC's Response

DPAC stated that it would revise the Contract Manager training section on emergency contracts to emphasize the importance of submitting contract requests as soon as the need is identified. For details of DPAC's response, please see Attachment 1

District 2's Response

The District concurred with the finding and has taken steps to address the finding and recommendations. For details of the District's response, please see Attachment 2

District's 4 Response

The District stated that using estimates could result in the encumbering and subsequent disencumbering of unwarranted funds. The District also believes that the Division of Maintenance should revise its 10 day policy for contract request submittal to DPAC. For details of the District's response, please see Attachment 3.

A&I's Analysis of District 4's Response

While the amount encumbered may exceed the final amount due the contractor, we believe the District should consider the necessity for timely contractor payments and disencumber excess funds at that time. Waiting to submit a contract request until the work is complete will further delay payments to contractors.

Finding 2 - Internal Control Deficiencies Noted in the Emergency Contract Process

Our review of the emergency contract process identified the following process and internal control deficiencies in eight of thirty (27 percent) contracts reviewed:

- **Late approval of the Confirmation of Verbal Agreement (CVA):** For one contract in District 2, the CVA was signed 51 days after work began, and 16 days after the contract request was submitted. The delay of 51 days occurred because the contract manager was replaced and it took the new contract manager additional time to complete the CVA.

  Allowing work to start before a CVA is signed means that the contractor is permitted to proceed without a documented, approved understanding of the nature and scope of the work to be done. Signing the CVA after the contract request is submitted further poses a risk of misunderstanding between the contractor and Caltrans on the required work. Ultimately, this could result in the contract request amount being insufficient to cover the cost of the work required.

  DPAC's Emergency Contract Guidelines require that a CVA is signed before the contractor starts work and submitted with the contract request to DPAC.

- **Lack of district approval signatures**. A request for contract in District 2 did not have the approval signatures of the district budget representative and the District Director or the Division Chief. Additionally, the contract request was submitted 47 days after the work had ended.

  Approval signatures provide evidence of proper authorization for emergency work contracts. In addition, untimely submittal of the contract request after emergency work begins can delay payment for work performed.

  DPAC's Emergency Guidelines require the approval of the District Director or functional District Division Chief. The approval should accompany the service contract request and the signatures of the required approving authority must be on the service contract request.

Finding 2 - (continued)

- **Incorrect posting to the Contract Administration Tracking System (CATS).** Four non-emergency contracts were logged incorrectly in CATS as emergency contracts. Since DPAC uses CATS to track service contracts, inaccurate data in may compromise the integrity of their contract management information.

- **Incomplete contract officer documentation.** Two contracts did not have completed contract officer's checklists. The checklists were left blank in one contract file and missing in the other.

  The contract officer's checklist ensures compliance with the Caltrans' policies and procedures, as well as progress and completeness of the emergency contract work. It provides assurance that all the contract requirements are met and that the contractor provided all required documents. Without it, contract officers may overlook the inclusion of important documents or miss steps necessary to complete the contract process.

Recommendation

We recommend:

1. Districts ensure proper authorization of service contract requests by the District Directors or Division Chiefs.
2. DPAC correct the inaccurate data in CATS and implement procedures to ensure verification of data accuracy.
3. DPAC ensure contract officer checklists are completed and included in all contract files.

DPAC's Response

DPAC concurred and has already taken steps to address the findings and recommendations. For details of DPAC's response, please see Attachment 1.

District 2's Response

The District concurred with the finding and will take steps to address the finding and recommendations. For details of the District's response, please see Attachment 2.

Audit Team

Laurine Bohamera, Chief, Internal Audits
Douglas Gibson, Audit Manager
Mohammad Eslamian, Auditor
Mandy Ip, Auditor

ATTACHMENT 1

DIVISION OF PROCUREMENT AND CONTRACTS' RESPONSE

State of California
DEPARTMENT OF TRANSPORTATION

California State Transportation Agency

Memorandum

Serious drought.
Help Save Water!

To: WILLIAM E. LEWIS
ASSISTANT DIRECTOR
AUDITS AND INVESTIGATIONS

Date: July 25, 2014

File: P3000-0416

Kelly Takizawa/for

From: FRANCESCA NEGRI
Division Chief
Division of Procurement and Contracts

Subject: **RESPONSE TO DRAFT EMERGENCY CONTRACT PROCESS AUDIT**

Attached is the Division of Procurement and Contracts' (DPAC) response to the Draft Emergency Contract Process Audit. We have successfully implemented changes that address three of the four recommendations to ensure timely execution of emergency contracts, payment of emergency services and internally controlled deficiencies as noted. The disposition of the final recommendation will be satisfied by August 1, 2014 with an update to the Contract Manager training.

If you have any questions or concerns, please contact Sabrina McGlothin at (916) 227-6071.

Attachments
(1) Response to Draft Report
[redacted]

Audits and Investigations (A&I) - Response to Draft Report

Audit Name: Emergency Contract Process **Audit No.** P3000-0416

Auditee: Division of Procurement and Contracts

Audit Report Finding # 1

List Finding Here: Further Improvements Needed to Ensure Timely Execution and Payment of Emergency Contracts

A&I Audit Recommendation	Auditee Response to Draft Report	Estimated Completion Date	Staff Responsible	A&I Analysis
Audits recommends that the districts submit emergency contract requests to DPAC as soon as possible with estimates large enough to cover unexpected additional costs. For hazardous material spill contracts, where experience indicates a certain range of costs, the districts should consider using set threshold estimates above average contract costs, to expedite contract request submittal.	DPAC will revise the Contract Manager training section on emergency contracts to emphasize the importance of submitting contract request as soon as the need is identified	August 1, 2014	Lisa Martin	A&I will follow up on the revised training prcedures.

Audit Report Finding # 2

List Finding Here: Internal Control Deficiencies Noted in the Emergency Contract Process

Audits recommends that districts ensure proper authorization of service contract requests by the district directors or division chiefs.	DPAC will not process any contract request that does not include proper authorization of the district directors or division chiefs. Contracts received without proper authorization will be returned to the requestor for compliance and resubmission.	On-going	Lindy Wilson	A&I will follow up to determine whether these steps are being carried out.
Audits recommends that DPAC correct the inaccurate data in CATS and implement procedures to ensure verification of data accuracy.	DPAC corrected the inaccurate data in CATS for two (2) of the four (4) contracts identified through the audit. DPAC verified that contract numbers 02A1109 and 12A1395 were coded properly in CATS as emergency contracted services. Contract Officers were reminded via email on July 1, 2014 of their responsibility to conduct a thorough review of each contract file and ensure coding is properly entered in CATS prior to signing any contract.	July 1, 2014	Lindy Wilson Sabrina McGlothin	A&I reviewed the supporting documentation of the steps implemented by DPAC. No further follow-up action is necessary.
Audits recommends that DPAC ensure contract officer checklists are completed and included in all contract files.	DPAC reminded Contract Officers via email on July 1, 2014 of their responsibility to ensure all checklist items are complete and included in all contract files. DPAC also revised the Contract Officer checklist on July 25, 2014 to include a signature block for the Contract Officer to certify that they have reviewed each item listed on the checklist.	July 25, 2014	Sabrina McGlothin	A&I reviewed the supporting documentation of the steps implemented by DPAC. No further follow-up action is necessary.

ATTACHMENT 2

DISTRICT 2'S RESPONSE

State of California
DEPARTMENT OF TRANSPORTATION

California State Transportation Agency

Memorandum

Serious drought.
Help save water!

To: WILLIAM E. LEWIS
Assistant Director
Audits and Investigations

Date: August 5, 2014

File: P3000-0416

From: SUSAN LAMB
Deputy District Director, Administration
District 2

Subject: **DRAFT AUDIT REPORT OF THE EMERGENCY CONTRACT PROCESS**

Attached is District 2's written response to the draft report of the Emergency Contract Process. Our response includes five action items; four of the action items will be implemented immediately and continue as part of our practice, the remaining action item will require additional time to be adequately implemented, possibly up to 12 months.

Upon receipt of the final report, we will begin providing progress reports as requested.

If you have any questions or need additional information, please feel free to contact me at (530) 225-3430.

Attachment:
Written response to Draft Audit Report.

c: Douglas Gibson, Audit Manager, Audits and Investigations
Laurine Bohamera, Chief, Internal Audits, Audits and Investigations
Don Anderson, Acting Deputy District Director, Maintenance & Operations, District 2
Bill Stein, Maintenance Manager I, District 2

Audits and Investigations (A&I) - Response to Draft Report

Audit Name: Emergency Contract Process **Audit No.** P3000-0416

Auditee: District 2

Audit Report Finding #1

Further Improvement Needed to Ensure Timely Execution and Payment of Emergency Contracts

A&I Audit Recommendation	Auditee Response to Draft Report	Estimated Completion Date	Staff Responsible	A&I Analysis
Improve timeliness of contract request submission	District agrees to take steps for cross training, etc. to ensure turn over in staff does not affect process time	Ongoing	DDD Maintenance and Operations	A&I will conduct follow up steps to determine what training is implemented and its effectiveness in reducing delays caused by staff turnover.
Improve timeliness of contract submittals and make large enough to cover unexpected additional costs	District agrees to the recommendation to submit the request estimating costs at a level sufficient to cover unexpected costs.	Immediately	Maintenance Manager I	No follow up is necessary.
Improve timeliness of contract submittals and develop cost thresholds for Hazardous Waste contracts.	In an effort to resolve these and other issues, the District will pursue developing and requesting a District wide hazardous materials contract.	Jun-15	Maintenance Manager I	A& I will follow up in June 2015 to determine whether the District implements this step.

Audit Report Finding #2

Internal Control Deficiencies Noted in the Emergency Contract Process

Ensure replacement of staff do not affect proper and timely processing of emergency contracts	District agrees to take steps for cross training, etc. to ensure turn over in staff does not affect process time	Ongoing	DDD Maintenance and Operations	A&I will conduct follow up steps to determine what training is implemented and its effectiveness in reducing delays caused by staff turnover.
Ensure Proper authorization of service contract requests by DD	District agrees to ensure proper authorization from the DD is obtained	Immediately	Maintenance Manager I	No follow up is necessary.

Audit Report Finding #
List Finding Here

ATTACHMENT 3

DISTRICT 4'S RESPONSE

State of California
DEPARTMENT OF TRANSPORTATION

California State Transportation Agency

Memorandum

Serious drought.
Help Save Water!

To: WILLIAM E. LEWIS
Assistant Director
Audits and Investigations

Date: August 26, 2014

File: P3000-0416

From: PREMJIT RAI
Deputy District Director of Administration
District 4

Subject: **D4 Response to Draft Audit Report # P3000-0416 Regarding Emergency Contracts**

As a result of reviewing the draft audit report and participating in the exit conference, attached is District 4 plan to address the findings of the audit.

If you have any questions or need additional information, please contact me at (510) 286-5894.

Attachment
Auditee (D4) response to draft audit report June 2014

c: Nader Eshghipour, Deputy District Director, District 4, Maintenance
Laura Horan, Maintenance Manager II, District 4, Maintenance
Laurine Bohamera, Chief, Internal Audits, Audits & Investigations
Douglas Gibson, Audit Manager, Internal Audits, Audits & Investigations

Audits and Investigations (A&I) - Response to Draft Report

Audit Name: Emergency Contract Process Audit **Audit No.** P3000-0416

Auditee: Laura Horan

Audit Report Finding # 2

List Finding Here

A&I Audit Recommendation	Auditee Response to Draft Report	Estimated Completion Date	Staff Responsible	A&I Analysis
Districts submit emergency contract requests to DPAC as soon as possible with estimates large enough to cover unexpected additional costs. For hazardous material spill contracts, where experience indicates a certain range of costs, districts should consider using set threshold estimates above average contract costs, to expedite contract request submittal.	The hazardous spills are unique and vary from location, chemicals, terrain, weather conditions, and other factors. It is difficult to arrive at an estimate based on the spill until the contractor has disposed of the hazardous material. The material may have to be disposed in landfills or incinerated in other states causing more delays and expenses. The invoice received from the contractor, is the accurate cost of the work performed and not based on an estimate. The contractor is paid in arrears and this is written into the contract. Of the 6 contracts that were audited, after receiving the invoice, the contract submittal to DPAC was between 10 and 17 days. The fully executed contracts received from DPAC took between 50 to 125 days. It would be more cost effective and beneficial to the contractors to have the invoices paid in full and not based on an estimate. This would avoid encumbering unwarranted funds and then having to either disencumber or amending the contract for additional costs. Amending the contract for additional funds would further delay payment for services to the contractor. District 4's recommendation is to HQ Maintenance to revise "The SCM Section 4.09B, Division of Maintenance, Maintenance Policy Directive, Number 601". It should be amended to: *"The request for contracts should be sent to DPAC within 15 days after receiving the final invoice".*	N/A	HQ Maintenance	While the amount encumbered may exceed the final amount due the contractor, we believe the District should consider the necessity for timely contractor payments and disencumber excess funds at that time. Waiting to submit a contract request until the work is complete will further delay payments to contractors. In its quarterly meeting with the Division of Maintenance, on July 8, 2014, A&I requested the Division to determine whether the 10 day limit could be revised. The Division stated that it would look in to the matter.
Audit Report Finding #				
Audit Report Finding # **List Finding Here**				