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# **Construction Contracts—Final Payment and Closing Project Process Review**

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**To:** Kevin Carpenter, Finance & Property Services (Finance)  
Jeremy Hanson-Willis, Community Planning & Economic Development (CPED)  
Jeff Johnson, Minneapolis Convention Center (MCC)  
Velma J. Korbek, Civil Rights (CR)  
Steve Kotke, Public Works (PW)

**Re:** Construction Contracts—Final Payment and Closing Project Process Review

The Internal Audit Department (IA) conducted a review of Final Payment and Closing Project Process for Construction Contracts within the Finance, CPED, MCC, and PW Departments within the City of Minneapolis (The City). This review was included in the 2013 Internal Audit Plan and was completed in June 2013.

### **Background**

The City performs a number of construction projects per year through the departments of PW, CPED, Finance, and MCC. Some of these construction projects are performed by the City and others are contracted by outside construction firms. In 2012, 39 construction project final payments were made to outside construction companies. The total cost of these construction contracts combined was approximately \$29 million.

### **Objectives**

To ensure required documents, in accordance with the contracts, were delivered by the contractor before the final payment was processed.

### **Scope**

This review included identifying key internal controls, including current policies and procedures (P&P), through observation, inquiry, analytical procedures and limited testing within the final payment process. IA performed, on a sample basis, testing of current processes and transactions within the period of January 1, 2012 through the end of field work for construction projects completed by outside contractors.

### **Summary of Findings and Management Responses:**

#### **1. Policies and Procedures**

The requirements for construction contract close-out and final payment are not identified or formally documented in related P&P.

#### ***Management Response***

*Management will review and update current written construction contract management P&P for the final payment and project close-out processes to include: (a) identifying departmental roles and responsibilities (b) developing a checklist before issuing the final payment, and (c) approving and signing off on the checklist prior to sending to Accounts Payable (AP) for processing final payment.*

## 2. Civil Rights Requirements

There appears to be a lack of communication between CR and the other departments regarding the Small and Underutilized Business Program (SUBP) and Affirmative Action plan requirements. There is a difficulty determining if the requirements have been met before final payment has been processed.

### **Management Response**

*Management will develop and implement a communication plan to keep construction contract and project management staff informed about: (a) P&P that need to be followed related to CR monitoring and final payment processing; and (b) review and update of the construction contract management final payment P&P, and the final changes in requirements that will be made.*

## 3. Training

Currently, training for project managers regarding the processing of final payments on construction contracts is not provided. Some project managers do not have the knowledge of required documentation for construction final payments.

### **Management Response**

*Training materials on construction contract final payment P&P for PW project managers and/or construction project managers will be developed and provided on a regular basis to all construction project managers.*

## Conclusion

Based on our review, we believe there are opportunities for improvements to address risk areas identified in this report. Finance, CPED, MCC, PW, and CR worked collaboratively with IA to develop action plans.

IA would like to extend our appreciation to CPED, CR, Finance, MCC, PW, and personnel who assisted and cooperated with us during this review.

**Cc:** Paul Aasen, City Coordinator's Office  
Chris Backes, Finance  
Sandra Christensen, Finance  
Sara Dietrich, Communications  
Pam Fernandez, Finance  
Karen Francois, CR  
Connie Griffith, Finance  
Heidi Hamilton, PW  
Brette Hjelle, PW  
Chris Larson, MCC  
Rich Perrizo, Finance  
Elfric Porte, CPED  
Leslie Woyee, CR

# Construction Contracts—Final Payment and Closing Project Process Review Audit Findings and Management Responses

## 1. Policies and Procedures

The final payment for the construction contracts in the City may have different requirements, some of which could be mandated by a state or federal law, based on the source of funding. Although there are general guidelines and procedures for contract close-out and final payment on the procurement website (<http://citytalk/finance/procurement/cm/WCMS1P-082520>), the requirements specific to the close-out and final payment of construction contracts are not formally documented by procedures or guidelines. Each of the project managers has developed his/her own method of reviewing documents required for requesting the payment. We acknowledge that there is a contract closing checklist on the procurement website (<http://citytalk/finance/procurement/cm/WCMS1P-082501>) for the project managers; however, it does not include the documents required to be completed before issuing final payments. Also, the final payment requirements are not consistently documented in the contract, which could lead to an unintentional omission of required documents.

### Recommendation

To ensure compliance with laws and regulations, we recommend:  
Reviewing and updating the current written procurement and construction contract management policies, procedures, and requirements for the final payment and project close-out process.

### Management Response

*A management work team that includes representatives of all the parties involved including Finance (Controller, Procurement/Contracting, AP, and Property Services), CR, PW, CPED, and MCC will review and update the current written procurement and contract management P&P to include specific processes and procedures for the construction contract final payment and project close-out. Once the P&P are updated, there will be a communication of and training about all of the updated P&P related to construction contract management and in particular, updates in the agreed upon procedures and requirements related to the final payment process. These activities are included in the action plan outlined at the end of this report.*

**Responsible Party** See Management Action Plan on page 6

**Expected Completion Date** See Management Action Plan on page 6

**Projected Cost of Implementation** See Management Action Plan on page 6

## 2. Civil Rights Requirements

In accordance with the Minneapolis Code of Ordinances, Title 16, Chapter 423 (Small and Underutilized Business Enterprise Program – SUBP) and Title 7, 139.50 (Affirmative Action and other stated requirements), SUBP requires that specific goals be set for both women and minority businesses to participate based on the scope of work, as follows: (a) for any construction contract or development project, or any part of or combination thereof, in excess of one hundred thousand dollars (\$100,000); (b) for any professional, technical and service contract, or any part or combination thereof, in excess of one hundred thousand dollars (\$100,000) and (c) for any contract for non-construction-related equipment, food, material, or any part or combination thereof, in excess of fifty thousand dollars (\$50,000). Also, the City requires the submittal and approval of an Affirmative Action Plan from contractors, subcontractors, and suppliers with contracts exceeding \$50,000. CR monitors and verifies committed and approved

participation goals throughout the project; however, there appears to be a need for enhancing communication. Based on the work performed, some project managers were unaware of the CR monitoring process and developed their own process to monitor achieving the SUBP requirements, which is a duplication of efforts. Other project managers were unaware of whether or not goals were met. The lack of consistency in validating whether necessary actions were taken if goals are not met may result in a perception of contractor favoritism, affect program credibility, or prevents achieving the purpose of the SUBP. In addition, it is not clear whose responsibility it is to implement any actions recommended by CR, if any, before issuing final payment.

### **Recommendation**

We recommend that CR, in collaboration with impacted City departments, develop and agree upon a communication protocol between CR and the project managers. This protocol should include roles and responsibilities related to action to be taken to address the results of monitoring goals before final payment issuance.

#### **Management Responses:**

*Included in the management review and update of P&P related to the construction contract final payment in the first recommendation will be a review and update of the current procedures already in place related to the CR processes around construction contract management. While the P&P review and update are occurring, the management work team will develop and continue to provide information and clarification to construction contract managers on current procedures and requirements including the CR processes. These activities will be incorporated in the action plan at the end of this report.*

**Responsible Party** See Management Action Plan on page 6

**Expected Completion Date** See Management Action Plan on page 6

**Projected Cost of Implementation** See Management Action Plan on page 6

### **3. Training**

For some project managers there is not sufficient knowledge related to the documents required for final payments. We acknowledge that there is a project management annual training for PW; however, there is no training on requirements for final payment. It is beneficial for project managers to enhance their understanding of the documents required for final payment to ensure completeness of these documents before the final payment is made.

### **Recommendation**

IA recommends developing and providing training on final payment processes and procedures and incorporating the training in sessions provided annually at the PW project manager training and/or in a separate training to be provided on a regular basis to all construction project managers.

#### **Management Responses:**

*Included in the action plan at the end of this report is the development of training activities related to construction contract final payment processes and procedures and the providing of that training to all construction project managers in PW, CPED, MCC and Property Services.*

**Responsible Party** See Management Action Plan on page 6

**Expected Completion Date** See Management Action Plan on page 6

**Projected Cost of Implementation** See Management Action Plan on page 6

### **Management Action Plan**

*The action plan to address each of these issues will consist of the following three activities:*

1. *The review and update of current written construction contract management P&P for the final payment and project close-out processes to include:*
  - a. *Identification of roles and responsibilities of department contract managers and other staff, CR management and staff, and Finance procurement and contracting, AP, accounting, and internal control monitoring staff;*
  - b. *Development of appropriate checklists and related procedures to ensure all documents and processes to be completed and requirements that need to be met are incorporated in the construction contract language and completed/met before issuing the final payment; and*
  - c. *Identification of the final payment and incorporation of the properly signed off and approved checklist with the payment paperwork sent to AP for processing of the final payment.*
2. *The development and implementation of a communication plan to keep construction contract and project management and staff informed about:*
  - a. *Current construction contract management requirements and related P&P already in place that need to be followed related to CR monitoring and final payment processing; and*
  - b. *The review and update of the construction contract management final payment P&P, and the final changes in requirements that will be made.*
3. *The development of training materials on construction contract final payment processes and procedures, to be incorporated into the training materials in the PW project manager training and/or separate training sessions developed and provided on a regular basis to all construction project managers.*

### **Responsible Parties**

*The following work team will be responsible for completing this action plan:*

Connie Griffith, Controller (Management Action Plan Work Team Coordinator)  
Chris Backes, Finance  
Sara Dietrich, Communications  
Pam Fernandez, Finance  
Brette Hjelle, PW  
Chris Larson, MCC  
Rich Perrizo, Finance  
Elfric Porte, CPED  
Leslie Woyee, CR

### **Expected Completion Date**

*All activities are expected to be initiated over the next year and completed by October 31, 2014.*

### **Projected Cost of Implementation**

*The cost is approximate and is based on the hours involved to do each activity by the above key people and other staff at an average salary/benefit cost of \$48.6/hour. This is not a request for additional budget but an indication of the time and cost it takes to do this work in lieu of other activities.*

<b>Projected Cost of Implementation</b>		
<b>Audit Finding</b>		<b>Total Estimated Cost</b>
<b>1</b>	<b>Policies and Procedures</b>	45,500
<b>2</b>	<b>Civil Rights Requirements</b>	4,800
<b>3</b>	<b>Training</b>	10,000
<b>Totals</b>		<b>*\$60,300</b>

*\* This is not a request for additional budget but an indication of the time and cost it takes to do this work in lieu of other activities. Internal Audit believes that the benefit of implementing these action plans outweighs the cost of implementation.*

<b>Abbreviations Used Throughout the Report</b>	
<b>AP</b>	Accounts Payable
<b>City</b>	The City of Minneapolis
<b>CPED</b>	Community Planning & Economic Development
<b>CR</b>	Civil Rights Department
<b>Finance</b>	Finance and Property Services
<b>IA</b>	Internal Audit Department
<b>MCC</b>	Minneapolis Convention Center
<b>P&amp;P</b>	Policies and Procedures
<b>PW</b>	Public Works
<b>SUBP</b>	Small and Underutilized Business Program