



City of Phoenix

Mission Statement

To improve the quality of life in Phoenix through efficient delivery of outstanding public services.

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Project Number

1250053

This report can be made available in alternate format upon request.

Phoenix Convention Center Contract Audit – Shoring Wall

January 13, 2025

Report Highlights

Contractor Payments

The Street Transportation Department administered the agreement as a “lump sum” contract. As such, payments were based on percent of project complete.

Payment Reviews and Approvals

Some payments were processed without required approvals.

Record Retention Requirements

The contractor did not maintain records of the project as required in the contract.

***City Auditor Department
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Executive Summary

Purpose

The City Auditor Department contracted with REDW Advisors & CPAs (Consultant), an external audit firm, to (1) assess relevant internal controls within the contract management process, and (2) determine whether the contractor complied with the contract terms. Specifically, the Consultant evaluated compliance with contract terms, including payments and service delivery.

Background

The Phoenix Convention Center (PCC) previously had a temporary shoring wall that was meant to exist for only two years and had required an engineer inspection annually. In 2019, approximately 15 years after the temporary wall was built, an inspection that occurred during the expansion of the PCC found that the wall required replacement.

In 2019, the City of Phoenix (City) contracted with DNG Construction, LLC (DNG) for the Shoring Wall capital improvement project (CIP), valued at \$25M. DNG engaged in an agreement with Gannett Fleming as the Design Professional for planning, design services, and payment request review. The project was funded by PCC, which assigned a project manager to oversee the work that DNG performed. Additionally, the Street Transportation Department (Streets) was assigned to monitor project payments and budgeting.

Job order agreements can be of two forms:

- Lump Sum – in lump sum agreements, the contractor and City negotiate the cost of the project up front, based on the contract's estimate for its work and based on bids received by the contractor for materials or sub-contractor work. In administering the project, the City only receives an invoice based on percent of project complete, not based on any actual costs incurred by the contractor.
- Time and Materials – in time and materials contracts, rates are established in the agreement. In administering the project, the City receives the invoice and all supporting documentation to then pay the contractor based on actual costs incurred.

In 2023, the City received a complaint alleging that DNG used City funds for goods and services unrelated to the Shoring Wall project. The City Auditor Department conducted an internal investigation in response to the complaint. The City Auditor reviewed a sample of payment applications and found there was insufficient documentation to substantiate inappropriate use of payments made to DNG; therefore, the findings of the investigation were inconclusive. Due to the cost associated with the project, the City Auditor contracted with the Consultant to complete an audit of all payment applications.

See **Attachment A – REDW Report** for a copy of the Consultant's report.

Results in Brief

Streets administered the project as a lump sum agreement, as payments were based on percent of project complete.

Streets administered the project as a lump sum agreement. As such, negotiations prior to project initiation determined the project price, and payments are made based on percent of project complete. Therefore, the Consultant could substantiate only 7% of the project costs due to limited documentation maintained by the City or provided by the contractor. Additionally, DNG did not provide the required Small Business Enterprise (SBE) Utilization forms for each of the sub-contractors as required in Section 7.1.4 of the contract.

Some payments were processed without the required approval.

The Consultant determined that some pay requests were missing required certification signatures and were not processed within 14 calendar days. One pay request included \$31K in duplicate charges; however, the agreement was administered as a lump sum contract, and the total payments to DNG did not exceed the agreement value of \$25M.

DNG did not maintain records of the project as prescribed in the contract.

Section 9.2.6 of the contract required the contractor to maintain all records related to the project for a period of three years after the final settlement. Based on the completion date of the project, the three-year period expires on March 1, 2025. DNG only retained the final pay requests for the project and, therefore, was unable to provide the project documents that were requested by the Consultant.

Recommendations

1. Office of the City Engineer – Ensure agreement language clearly specifies whether the project is a "lump sum" or "time and materials" project and includes requirements that identify the type of documentation to be provided by the vendor for payment requests.
2. Office of the City Engineer – Define criteria, to be used by all City departments when creating job order agreements, for when lump sum agreements are permissible and when time and material agreements should be used.
3. Office of the City Engineer – Document and establish training that is available as needed for City staff that identifies the roles and responsibilities of staff who review and approve payment applications.
4. Office of the City Engineer – As projects are completed, remind contractors in writing of their contractual obligation to maintain records after final settlement for the period specified in their contract.
5. Phoenix Convention Center – Document and establish monitoring procedures to ensure payment applications are processed accurately and timely.

Standards

This audit was conducted by REDW Advisors & CPAs. REDW Advisors & CPAs was contractually obligated to conduct this performance audit in accordance with generally accepted government auditing standards. Those standards require that REDW Advisors & CPAs plan and perform the performance audit to obtain sufficient, appropriate evidence to provide a reasonable basis for its findings and conclusions based on the audit objectives.

Department Responses to Recommendations

<p>Rec. #: 1. Office of the City Engineer – Ensure agreement language clearly specifies whether the project is a "lump sum" or "time and materials" project and includes requirements that identify the type of documentation to be provided by the vendor for payment requests.</p>	
<p>Response: An indicator will be added to the JOA agreements that will clearly identify the type of JOA agreement (which will inform the documentation necessary)</p>	<p><u>Target Date:</u> April 1, 2025</p>
<p>Rec. #: 2. Office of the City Engineer – Define criteria, to be used by all City departments when creating job order agreements, for when lump sum agreements are permissible and when time and material agreements should be used.</p>	
<p>Response: Criteria will be determined, documented, and shared with CIP Task Force, included in the OCE PM Training course, and OCE Standards (2.4 Scope of Work Development & 2.4a Scope of Work Checklist)</p>	<p><u>Target Date:</u> April 1, 2025</p>
<p>Rec. #: 3. Office of the City Engineer - Document and establish training that is available as needed for City staff that identifies the roles and responsibilities of staff who review and approve payment applications.</p>	
<p>Response: Payment Application Review/Approval criteria will be documented and shared with CIP Task Force, included in the OCE PM Training course, and OCE Standards (3.3 Pay Application Review/Approval)</p>	<p><u>Target Date:</u> April 1, 2025</p>
<p>Rec. #:4. Office of the City Engineer – As projects are completed, remind contractors in writing of their contractual obligation to maintain records after final settlement for the period specified in their contract.</p>	
<p>Response: OCE Standards (6.13 Project Close Out & 6.13a Project Close Out Guidelines Checklist) will be updated to include contractor reminder of mandatory document retention requirements. Updated Standard to be shared with CIP Task Force and included in the OCE PM Training course.</p>	<p><u>Target Date:</u> April 1, 2025</p>
<p>Rec. #: 5. Phoenix Convention Center – Document and establish monitoring procedures to ensure payment applications are processed accurately and timely.</p>	
<p>Response: PCC will include in future service level agreements with Streets a clear understanding & responsibility by project manager for reviewing pay requests.</p>	<p><u>Target Date:</u> April 9, 2025</p>

Attachment A – REDW Report

City of Phoenix
Phoenix Convention Center
Shoring Wall

Phoenix Convention Center Shoring Wall Project
Internal Audit
July 2024

**City of Phoenix
Internal Audit
Phoenix Convention Center Shoring Wall Project**

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**City of Phoenix
Internal Audit
Phoenix Convention Center Shoring Wall Project
Report**

Introduction

We performed the internal audit services described below to assist the City of Phoenix in evaluating processes related to the construction and project administration of the Phoenix Convention Center Shoring Wall Project. Our services were conducted in accordance with the Consulting Standards issued by the American Institute of Certified Public Accountants, relevant portions of the Generally Accepted Government Auditing Standards and the terms of our contract for internal audit services.

Although we have included management's responses in our report, we do not take responsibility for the sufficiency of these responses or the effective implementation of any corrective action.

Purpose and Objectives

On August 21, 2023, the City of Phoenix City Auditor received a complaint that alleged a City contractor, DNG Construction, LLC (DNG), used City funds for goods and services that were not related to City projects. The complaint specifically named the project for the Phoenix Convention Center (PCC) Shoring Wall. The City Auditor Department began an investigation into the complaint by selecting a sample of payment applications and applicable supporting documentation to determine if payments had been made for goods and services not related to City projects. In addition, the City Auditor evaluated internal controls over billing reviews for this project to ensure proper controls were in place prior to payments being made.

On January 31, 2024, the City Auditor released the results of their investigation. The report included a recommendation that a full internal audit be performed over the remaining payment applications and supporting documentation both for DNG and its subcontractors to determine if DNG utilized City funds for goods and services not related to City projects. REDW was selected to perform the internal audit.

Our internal audit focused on testing all payment applications received by DNG during the course of the PCC Shoring Wall project to ensure they were properly reviewed and approved prior to payment. In addition, we evaluated the supporting documentation in place to determine if amounts requested for payment were properly supported. Finally, we tested each pay application for mathematical accuracy to ensure amounts paid were calculated correctly.

Observations, Recommendations and Management Responses

As a result of our testing, REDW identified the following observations:

1. *Unsupported Costs*

Upon selection of DNG as the contractor for the PCC Shoring Wall project, Job Order Contract (JOC) No. 138905 was executed between the City and DNG to establish the terms of the project. The total not to exceed cost of the project was \$25,000,000, of which \$24,999,999.99 was paid to DNG. As part of those terms, the contractor was required to keep records of all JOC Contractor's direct personnel payroll, reimbursable expenses pertaining to each Job Order and records of accounts between the City and the JOC Contractor (Section 7.6.1).

Our testing of all 46 pay requests submitted by DNG determined there was limited information (such as invoices for materials used or stored, timesheets, subcontractor pay apps, etc.) included with the pay requests to support personnel payroll, reimbursable expenses pertaining to each Job Order, and other costs incurred. As a result, we were only able to identify \$40,500 in supported costs based off information submitted to and retained by the City by DNG. REDW then requested additional records from both DNG as well as the three largest subcontractors on the project to determine if additional costs could be substantiated. With this information, we were able to substantiate an additional \$1,728,966.40 in project costs. After all analysis was completed based on information received, we were able to substantiate \$1,769,466.40 of total project costs (which was approximately 7% of the total project).

Additional inquiry into why pay requests were processed without proper supporting documentation yielded limited results as there was turnover in the City Project Management team after construction had already begun. DNG had also expressed that this support was never requested/required from the City during the course of the project. Further discussions with the Office of the City Engineer and others who were on the City's project management team indicated that this contract was executed outside of the normal procurement process as a sole source procurement and was agreed upon as a lump-sum contract during the pre-construction conference; however, language contained within the contract and other supporting documents utilized wording consistent with a time and materials contract therefore necessitating the need for supporting documentation.

We also noted that the contract required (Section 7.1.4) the completion of Small Business Enterprise (SBE) Utilization forms listing each approved SBE subcontractor which was to be submitted with each pay request to ensure DNG was able to meet the SBE utilization contract requirements set at 14%. During the course of our pay application reviews, we determined these forms were not submitted therefore we were unable to verify if the SBE utilization percentage reported on each pay request form was correct and that subcontractors actually performed or delivered the percentage of costs reported.

Based on the limited documentation in place to support costs and time incurred, we were unable to determine if the City was charged for work that was either not performed, or if payments for the Shoring Wall project may have subsidized work performed on other non-City projects. However, for the costs that could be substantiated, all work appeared to be related to the Shoring Wall project.

Potential Risk – High: The absence of proper supporting documentation for construction costs incurred by the contractor and subcontractors increases the risk that the City paid for costs not related to the project. Since the majority of the costs were unsupported, we have assessed the risk at high.

Recommendation: The City of Phoenix should ensure the type of contract utilized for each project is clearly documented to ensure proper documentation is provided. In addition, for time and material contracts, minimum requirements for documentation to be submitted with pay requests should be established for all Capital Improvement Plan (CIP) related contracts. Pay requests should not be processed if costs are unsubstantiated with evidence of actual costs incurred. Items that should be included with pay requests are (but not limited to):

- Schedule of Values/Continuation Sheet – For both contractors and subcontractors, detailed cost reports showing actual expenditures against budgeted amount should be provided to allow for easy reconciliation of costs and budget tracking.
- Invoices and Receipts – Original or certified copies of invoices from subcontractors and suppliers showing materials purchased and/or services provided.
- Timesheets and Wage Reports – Detailed labor records showing hours worked, rates, and charges for each labor category. For projects involving public funds, certified payrolls may be required to verify compliance with wage rates and labor laws.
- Expense Reports – Documentation of reimbursable expenses incurred such as equipment rentals.
- Change orders – Approved change orders that outline any alterations to the original scope of work and associated costs.
- Material Receipts – Receipts or proof of delivery for purchased materials, ensuring that all material costs are justified and traceable.
- Subcontractor Pay Applications - Pay applications from subcontractors showing the work completed and billed to the contractor.
- Project Reports - Progress reports detailing the work completed, issues encountered, and how they were addressed. Photos and other supporting documentation may be included.

Pay requests should not be processed for payment if supporting documentation is not included with the pay request. It may be beneficial to implement additional procedures with Accounting Specialists/Accounts Payable to spot check the supporting documentation and verify there are Project Manager comments, markups, or tie-out notes, indicating that due diligence over amounts reported has occurred.

2. Payment Approvals and Reviews

Job Order Contract No. 138905 with DNG includes the following term regarding the requirements over procedures for payment:

- Section 7.3.1 - The City shall make payment in accordance with Arizona Revised Statutes Section 34-607. Payment will be made no later than fourteen (14) calendar days after the JOC Pay request is certified and approved.

In order to process payment requests for this project, the Contractor, the Consultant, if required, the City Project Manager, and the City Engineer must all certify the pay request prior to submitting for payment, per best practices. This certification serves as the first-hand verification of the work's progress and the accuracy of the pay application. Once submitted and approved by the project management team and the City's representative (i.e. City Engineer), the pay request packet is routed to an Accountant 1, who is responsible for the initial review and checks that supporting documentation is attached and validates numbers on the pay request form. They then approve the payment and push to an Accountant 2 for a second review. The Accounting Specialists then processes the payment in accordance with contract timelines. The approved payment is finally submitted to the City's vendor information management system where the Finance Department performs an additional review before issuing payment. During our testing of the 46 pay requests certifications, we determined:

- 8 pay requests were approved for payment by the PCC prior to evidence of the City's project management team having completed their review of the pay request, with variances ranging from 1 day to 6 days.

- 6 pay requests were approved 17 to 55 days after the final certification was signed. This exceeded the contract's payment terms of 14 calendar days by 10 to 41 days;
- 4 pay requests were certified by the City Project Manager or City Engineer 2 to 6 days prior to the Contractor's self-certification and therefore were out of order with the approval sequence;
- 2 pay requests did not contain sufficient information to determine certification and payment timelines, as the payment approval sheet was missing indicating potential document retention issues on behalf of the City; and,
- 19 pay requests were missing the City Engineer certification indicating the final step of the certification sequence did not occur.

Further testing over the mathematical accuracy of all 46 pay requests determined an amount of \$31,000 appeared to have been double counted on an application as it was included in two different line items regarding current work. As a result, it appears \$31,000 was overpaid to DNG.

Lastly, we noted several mathematical inaccuracies between pay request forms and detail sheets, transposition errors, and issues with line items rolling forward from one period to the next. We also noted minor inconsistencies in the performance period dates. While it does not appear that these issues resulted in overpayments to DNG, the absence of reviews appears to have contributed to these inaccuracies not being caught and corrected prior to payment approvals.

Potential Risk Level – High: Inconsistent reviews regarding certifications and payment approvals increases the risk of paying for work that hasn't been completed or non-compliance with contract payment terms, potentially resulting in financial losses, liens, or legal issues. Given that 23 of 46 pay requests analyzed had issues with reviews and approvals and it does appear an overpayment occurred, we have assessed this risk at high.

Recommendation: The City should ensure no payments are approved and/or issued without going through the required certification and approval channels. It may be beneficial to implement additional procedures for Accounting Specialists/Accounts Payable to quickly verify that the pay request packet is complete by verifying the existence of all certifications (signatures), which should be in a particular sequence (e.g. Contractor, Consultant, Project Manager, then City Engineer in this case). The City should also consider the use of a detailed checklist that can be utilized to guide Project Managers and/or Engineers through the pay request review process, such as the one the Water and Wastewater Engineering group has implemented and utilizes during each pay request review, to ensure all certifications are present prior to approving payment. The checklist should accompany each completed pay request with all certifications in proper sequence prior to routing for payment approval and processing. This will also aid in improving the overall reliability of the reimbursement process for construction projects.

Lastly, City Standards or desktop procedures should be developed outlining proper procedures for CIP related projects when it comes to payment reviews and timelines to ensure compliance with contract payment terms. Such a document should define and communicate the responsibilities for each stage of the approval and payment process to all relevant staff. Ongoing training should be provided to Project Managers city-wide, to the extent possible, to emphasize the importance of compliance with proper approval processes and the risks associated with bypassing them.

3. Record Retention Requirements

Job Order Contract No. 138905 with DNG includes terms regarding the requirements over records and documentation including:

- Section 2.1.5.1 – The JOC Contractor will be required to maintain all project records in electronic format.

- Section 7.1.4 - With every JOC Payment Request for the Work, the JOC Contractor will attach a completed SBE utilization form listing each approved SBE Subcontractor to be utilized during construction of the Project and the amount of work performed by each through the end date of the applicable Job Order Pay Request. A SBE utilization form must be included with the JOC Payment Request even if no SBE utilization occurred for the respective month.
- Section 7.6.1 - Records of the JOC Contractor's direct personnel payroll, reimbursable expenses pertaining to each Job Order and records of accounts between the City and the JOC Contractor shall be kept on a generally recognized accounting basis and shall be available for three years after completion of the Work.
- Section 9.2.6 - The JOC Contractor shall maintain all records and documents for three years after final settlement. These records shall be maintained and subject to auditing as prescribed in Section 7.6.

Our testing determined that while DNG had some records from the project in electronic format as of July 2024, DNG only maintained the final pay requests for subcontractors and no other documentation (such as cancelled checks to validate amounts received/paid, backup documents to support amounts reported on subcontractor pay requests, SBE utilization reports, etc.) As a result, DNG appears to have violated the three-year record retention requirements, per the contract, as the project was completed on March 1, 2022; therefore, requiring records to be maintained until March 1, 2025.

Potential Risk Level – High: An absence of compliance with record retention requirements increases the risk of contract breaches, loss of trust, and an inability to effectively resolve claims or disputes. Since records do not appear to have been maintained for the required period, we have assessed the risk at high.

Recommendation: The City of Phoenix City Engineer, in collaboration with the departments overseeing projects, should implement a process to ensure all relevant records are obtained from the contractor at the end of the project to mitigate the risk that records may not be held for applicable periods of time. In addition, the City should periodically remind contractors of the record retention requirements and evaluate what processes contractors have in place to effectively retain records. In the event a contractor is unable to ensure proper record retention, the City should evaluate whether work should continue with that contractor for future projects.

Process Improvement Opportunity

1. *Post Project Lessons*

Lessons learned after the completion of a construction project allow project management teams to opportunity to document and share the insights, successes, challenges, mistakes, and recommendations gained during the project to improve any future projects, as well as inter-departmental collaboration and communication, and improve overall project performance. Our testing determined the City does not have a process in place to capture lessons learned from CIP related projects. The City should ensure that as part of project close-out, any lessons learned during the lifecycle of a construction project are communicated, documented, and shared with other City staff, such as other Project Managers, the Finance Department, City leadership, and others involved in CIP processes. This document should also include any vendor-specific issues encountered during projects so the City can make better data-driven decisions when contracting with general contractors and third-party vendors. Lessons learned should be documented in a centralized file or portal that is available to relevant staff for reference.

Scope and Procedures Performed

In order to gain an understanding of the controls and processes, we interviewed the following personnel:

- Gary Nelson, Office of the City Engineer VPM Project Manager assigned to the Street Transportation Department

- Eric Froberg, Street Transportation Department City Engineer
- Rick Castro, Convention Center Project Manager
- Lee Councilor, Convention Center Maintenance and CIP Superintendent
- Bob Fingerma, Convention Center Assistant Director
- Christopher Nipar, Street Transportation Department Accounting Supervisor
- Joseph Brown, Street Transportation Department Director

In order to gain an understanding of the processes and controls in place we read relevant portions of:

- Job Order Contract No. 138905 (“Master Agreement”) with DNG Construction, LLC (approved July 2, 2014) and related adjustments and change orders.
- On-Call Master Agreement 153159 with Gannett Fleming (effective January 1, 2021)
- City of Phoenix Standard # 6.13 – Contract Close-Out/Final Acceptance (December 26, 2017)
- City of Phoenix Standard # 2.1 – Negotiation – Construction Cost Proposals (August 30, 2017)
- City of Phoenix Standard # 2.3 – Negotiation – Study, Design and Construction Administration Fee Proposals (August 15, 2017)
- City of Phoenix Standard # 2.4 – Scope of Work Development (September 2017)
- City of Phoenix Standard # 2.5 – Department Amendment and Change Order (September 17, 2019)
- City of Phoenix Standard # 3.1– Treatment of Capital Construction Project Allowances and Contingencies (September 16, 2016)
- City of Phoenix Standard # 3.2 – Cost Estimating (July 26, 2018)
- City of Phoenix Standard # 6.13 – Contract Close-Out/Final Acceptance (December 26, 2017)
- City of Phoenix Project Closeout Guideline Checklist
- Phoenix Convention Center PCC JOC Integrity Line Case #1484 Investigation Report (January 31, 2024)

We performed the following testwork:

Pay Request Analysis: We obtained all pay requests submitted to the City by DNG Construction (46 total) for the Shoring Wall Project. We analyzed the pay requests to determine if they were consistently filled out, contained all required fields, information properly rolled forward from one period to another, were mathematically accurate, and reconciled to any detail or documents included in the packet. In addition, we analyzed line-item budgets to ensure line-items did not exceed budgeted amounts.

Pay Request Supporting Documentation: For all 46 pay requests submitted to the City by DNG Construction, we obtained all documentation maintained by the City to support costs reported on pay requests and subsequently reimbursed. In addition, we obtained any documentation maintained by DNG to support amounts requested for reimbursement. We analyzed supporting documentation to ensure the costs incurred were allowable, reasonable, and were supported with invoices, receipts, labor reports, etc. per contract terms.

Certification and Payment Approval Timelines: We obtained 46 pay requests for the Shoring Wall project and tested to determine if:

- The Contractor certified the pay request;
- The Consultant certified the pay request;

- The City's VPM Project Manager certified the pay request;
- The Owner's Representative (City Engineer) certified the pay request;
- Certifications occurred in the proper sequence (Contractor, Consultant, Project Manager, then City Engineer) and were obtained prior to the approval of payment for processing by an Accounting Specialist; and,
- Payment was processed timely in accordance with contract payment terms (14 days).

Subcontractor Pay Requests: We obtained all subcontractor pay requests maintained by the Contractor. Of 30 subcontractors utilized, we received documentation for 28. We scanned each pay request packet provided for supporting documentation to substantiate costs reported. In addition, we selected the 3 largest subcontractors and contacted them to provide copies of cancelled checks and all pay requests submitted to DNG with all support for costs. If documents were provided, we tested to ensure the pay requests were mathematically accurate, and amounts reported for reimbursement were supported, allowable, and reasonable.

Reporting and Communication: We gained an understanding of the various reporting and communication channels and mechanisms utilized during the lifecycle of the Shoring Wall project to understand how project progress and quality were monitored. We obtained and quantified site visit documentation produced by the Consultant, daily reports produced by DNG, and owner meeting minutes and tested to ensure reporting and communication were occurring at a frequency appropriate for the size, complexity, and duration of the project.

* * * * *

This report is intended for the information and use of the City of Phoenix and others within the organization.

We discussed and resolved other minor observations with management and received excellent cooperation and assistance from personnel of the City of Phoenix previously mentioned in this report during the course of our interviews and testing. We sincerely appreciate the courtesy extended to our personnel.

REDW LLC

Phoenix, Arizona
October 29, 2024