

City of

ALBUQUERQUE

Office of Internal Audit

**STRATEGIC REVIEW
17-302**

**ALBUQUERQUE
INTERNATIONAL SUNPORT
TERMINAL RESTROOM
REMODEL & CHANGE
ORDER No. 1**

OCTOBER 26, 2016

INTRODUCTION

On July 20, 2016, the Office of Internal Audit (OIA) received a request from a City Councilor to conduct an independent review to:

1. “Determine if the procurement process followed for the Albuquerque International Sunport Restroom Remodeling Project #7770.02, and the issuance of subsequent Change Order No. 1 complied with the City Public Purchases Ordinance, the Regulation Governing the Award and Debarment of Contractors for Public Works Projects of the City of Albuquerque, and other applicable state and federal regulations.”

Specifically, the Councilor requested that OIA perform an assessment of:

2. Whether material change orders may be negotiated between the time of a competitive bid opening and the time of award, and
3. Whether bidders (competitors) other than the low bidder have been, or should be, afforded the opportunity to provide competitive bids for additional work identified by the City prior to or shortly after the bid opening.

Additionally, the Councilor asked that OIA provide “recommendations for improvement to the capital project procurement process, especially in regard to the timing of competitive bids and material change orders.”

SUMMARY

Overall, the procurement process followed for the Albuquerque International Sunport (AIS) Restroom Remodeling Project and Change Order No. 1 complied with the City’s Public Purchases Ordinance and the “Regulation Governing the Award and Debarment of Contractors for Public Works Projects of the City of Albuquerque” (CIP Award Regulation).

Materiality of change orders is not defined and no regulations expressly addressing whether material change orders may be *negotiated* between the time of competitive bid opening and the time of award were identified.

Both the City’s Public Purchases Ordinance and the Federal Acquisition Regulation (FAR) imply that open market competition is preferred and should be used when possible. However, no City regulations expressly addressing whether other bidders/competitors should be afforded the opportunity to provide competitive bids for additional work that had been identified shortly after the bid opening of the original project were identified.

One miscellaneous area of concern pertaining to bond coverage was identified. The contractor furnished the necessary bonds for the original contract price of \$1.15 million. However, the contractor did not increase the bond amounts to reflect the increased contract value from the subsequent change orders. At a final project cost of \$2.33 million, the project exceeded the value of the bonds by \$1.18 million.

SCOPE

The work performed for this strategic review was limited to the items contained in the request from the Councilor and did not address any allegations of fraud, waste, or abuse. The City's Office of Inspector General is responsible for the investigation of possible fraud, waste, or abuse and may issue a separate report addressing any findings in these areas.

OBJECTIVE

The objective of the strategic review was to determine if the procurement process followed for the AIS Restroom Remodeling Project, and the subsequent issuance of Change Order No. 1, complied with:

- City Public Purchases Ordinance,
- CIP Award Regulation, and
- Other applicable City regulations.

Note: State and Federal procurement regulations are not applicable as no State or Federal funding was used for the project.

BACKGROUND

The AIS Restroom Remodeling Project was awarded to Enterprise Builders, Inc. as a lump sum contract totaling \$1.15 million. A lump sum contract involves one price that includes cost of work, fees, and general conditions. This type of contract is appealing for government entities as the majority of the risk lies with the contractor.

On September 18, 2013, a Request for Bid (RFB) was issued for the AIS Restroom Remodeling Project. Sealed bids for the project were due by 1:30 pm on October 22, 2013. On that date, the project's architect, SMPC Architects, opened the sealed bids and tabulated the results. Ten bidders submitted proposals for the project, which ranged in cost from \$1.15 million to \$1.48 million, and all were below the SMPC Architect's opinion of probable construction cost of \$1.67 million. Enterprise Builders, Inc. was awarded the project based on its lowest responsible bid of \$1.15 million including New Mexico Gross Receipts Tax. According to the Deputy Director of the Department of Municipal Development, the contract award was not protested by any of the other bidders.

On February 14, 2014, Change Order No. 1 was initiated in the amount of \$940 thousand. The change order involved a change in scope, added work to the project, and received final approval from the City's Chief Administrative Officer on March 12, 2014.

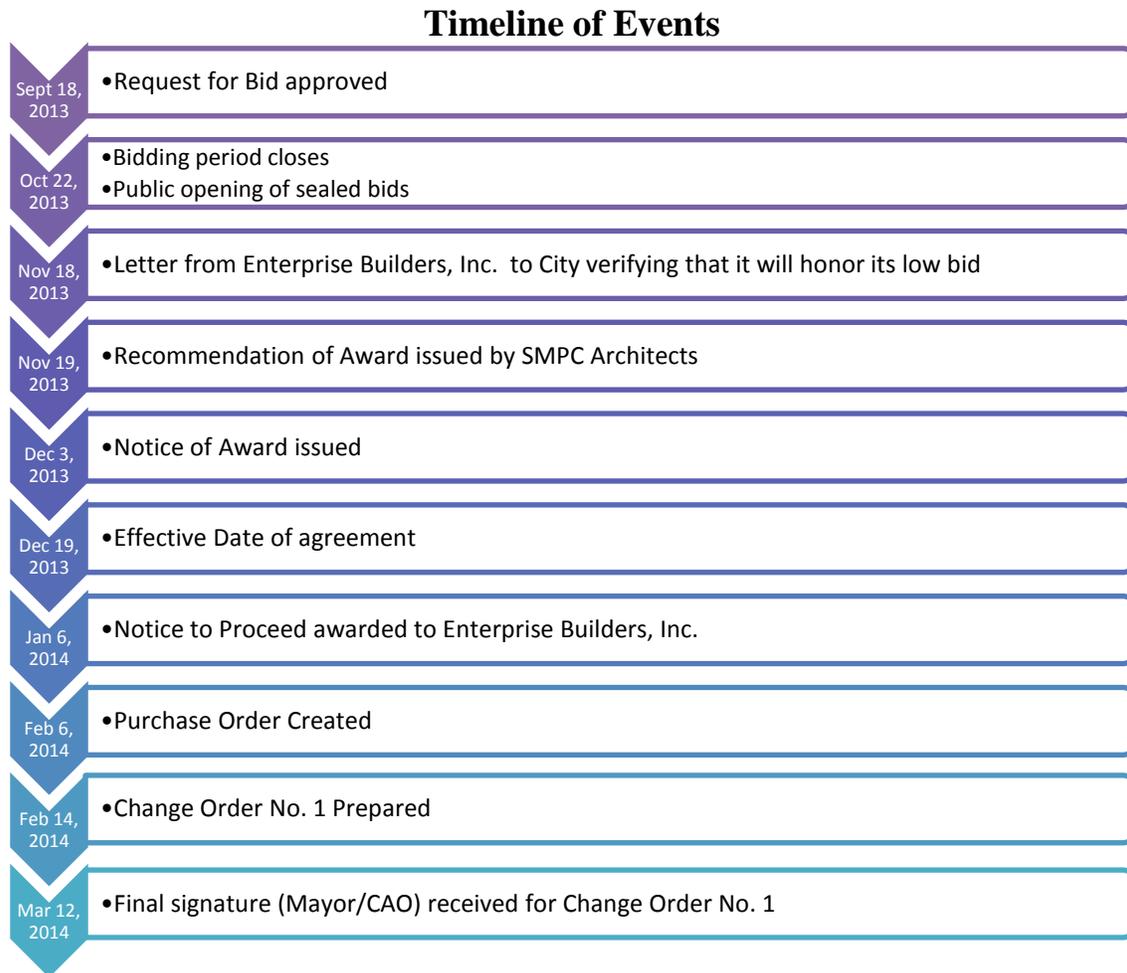
The parties involved throughout the remodeling project were:

- Project Manager & Oversight – City of Albuquerque, Aviation Department
- Project Oversight – City of Albuquerque, Department of Municipal Development
- Contractor – Enterprise Builders
 - Various subcontractors
- Architect/Consultant to the City – SMPC Architects

The CIP Award Regulation establishes the “procedures for solicitation and consideration of bids or requests for proposals, the award or rejection of bids or proposals, determining the

responsibility of bidders or offerors, and to protect substantial interest of the City of Albuquerque and the integrity of the City’s Public Works construction contracting process.”

The timeline of project events is depicted below.



RESULTS

The results presented are based on information obtained through interviews with City personnel and related parties, and a review of contracts and supporting documentation pertaining to the AIS Restroom Remodeling Project. The results below address the City Councilor’s concerns as listed in the Introduction section of this report.

1. Procurement

Original Project

Overall, the procurement process followed for the AIS Restroom Remodeling Project complied with the City’s Public Purchases Ordinance and the CIP Award Regulation. The only exception noted involved a 13-day delay of the contract award.

The procurement process and the AIS Restroom Remodeling Project’s compliance with the process are listed in the chart below. A more detailed chart referencing the applicable authoritative documents is attached as **Appendix A**.

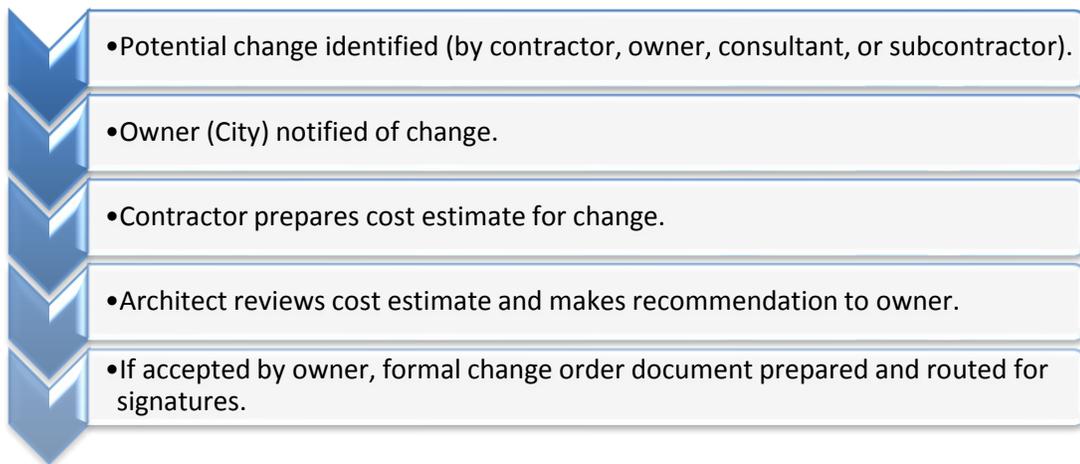
**Procurement Process
Original AIS Restroom Remodeling Project**

Description of Regulatory Event	Deadline	Actual Completion Date	Compliant
Bidding Closes	October 22, 2013	October 22, 2013	Yes
Notice of Award	November 21, 2013	December 3, 2013	No – 13 days late
Award of Contract	November 21, 2013	December 3, 2013	No – 13 days late (Request to Extend not issued)
Delivery of formal contract documents (including Performance Bond, Labor & Material Payment Bond, and required Certificates of Insurance)	December 13, 2013	December 12, 2013	Yes
Execution of Agreement	December 27, 2013	December 19, 2013	Yes
Contract Date	January 6, 2014	January 6, 2014	Yes
Notice to Proceed	January 18, 2014	January 7, 2014	Yes

Source: City documents

Change Order

The general process for issuing a Change Order is detailed below:



Change order No. 1 followed the above process and was finalized on March 12, 2014 by the City’s Chief Administrative Officer.

2. Negotiation of Material Change Orders

No City regulations expressly addressing whether material change orders may be negotiated between the time of competitive bid opening and the time of award were identified. At a cost of \$940 thousand, Change Order No. 1 totaled 82 percent of the original project cost.

Although there is no formal definition of materiality or percentage threshold in the City's regulations, based on the following definitions, OIA concludes that Change Order No. 1 for the AIS Restroom Remodeling Project is material.

- According to the on-line legal dictionary (www.law.com), materiality is an adjective meaning "relevant and significant".
- The Merriam-Webster Dictionary defines relevant as "relating to a subject in an appropriate way" and significant as "large enough to be noticed or have an effect; very important".

Although City regulations do not address materiality levels, State regulations do. The NM State Department of Transportation's Standard Specifications for Highway and Bridge Construction, Section 104.2 states:

"Significant change" applies only to modifications or alterations that:

1. Materially change, in kind or nature, the character of the Work including the Critical Path; or,
2. ***Increase or decrease a Major Contract item by twenty-five percent (25%)*** [Emphasis added].

Federal regulations contain language that provides guidance regarding the avoidance of conflicts of interest. Subpart 3.1 of the Federal Acquisition Regulation (FAR) Safeguards, 3.101 Standards of Conduct, 3.101-1 General states:

Government business shall be conducted in a manner above reproach and, except as authorized by statute or regulation, with complete impartiality and with preferential treatment for none. Transactions relating to the expenditure of public funds require the highest degree of public trust and an impeccable standard of conduct. ***The general rule is to avoid strictly any conflict of interest or even the appearance of a conflict of interest in Government-contractor relationships.*** [Emphasis added]

By treating additional work that nearly doubled the total project cost as a change order, rather than a separate project, the City has caused the overall integrity of the procurement process to be questioned by the appearance of a conflict of interest.

3. Opportunity for Competitive Bid

No City regulations expressly addressing whether other bidders/competitors should be afforded the opportunity to provide competitive bids for additional work that had been identified shortly after the bid opening of the original project were identified. However, both the City's Public Purchases Ordinance and the FAR imply that open market competition is preferred and should be used when possible.

The Public Purchases Ordinance, Section 5-5-11 Capital Projects (D) ROA 1994 states: “It is the policy of the city to require local participation in capital projects where possible.”

Additionally, Title 41, Section 3301, part (a) of the United States Code states:

In general...an executive agency in conducting a procurement for property or services shall:

- (1) Obtain full and open competition through the use of competitive procedures in accordance with the requirements of this division and the Federal Acquisition Regulation; and
- (2) Use the competitive procedure or combination of competitive procedures that is best suited under the circumstances of the procurement.

To help ensure the integrity of government procurement, Subpart 3.5 of the FAR addresses “Other Improper Business Practices” and what contract managers should be aware of. According to Section 3.5 of the FAR, “buying-in” is defined as “submitting an offer below anticipated costs, expecting to –

- (1) Increase the contract amount after award (e.g., through unnecessary or excessively priced change orders); or
- (2) Receive follow-on contracts at artificially high prices to recover losses incurred on the buy-in contract.”

Further, FAR 3.501-2 states:

(a) Buying-in may decrease competition or result in poor contract performance. The contracting officer must take appropriate action to ensure buying-in losses are not recovered by the contractor through the pricing of—

- (1) Change orders; or
- (2) Follow-on contracts subject to cost analysis.

It is customary for additional work to be added to an existing contract. However, without clearly defined requirements, additional guidance, or limitations to potential changes of scope, the inclusion of material change orders may persist. Although previous construction contracts at the Aviation Department also contained Change Orders that involved a change of scope, none of the other scope changes were as significant as Change Order No. 1 of the AIS Restroom Remodeling Project as shown in the table below.

AIS Construction Projects with Change of Scope Change Orders

Project #	Project Name	Original Amount	Change Orders		Total Project Cost	Change Order % to Original Amount
			Change of Scope	Other Reason		
777002	AIS Terminal Restroom Remodeling Project	\$1,147,757	\$1,183,205*	\$0	\$2,330,962	103%
* Amount includes Change Order No. 1 of \$939,676						
770002	AIS Taxiway A Reconstruction (Phase A & B)	\$10,208,753	\$48,930	\$0	\$10,257,683	.48%
770004	Sunport Electrical Ground Service	\$448,715	\$43,486	(\$2,503)	\$489,698	9.13%
770005	AIS Taxiway A Reconstruction (Phase C)	\$7,966,329	\$188,148	\$158,493	\$8,312,969	4.35%
725703	AIS Central Utility Reconstruction	\$699,780	\$18,413	(\$1,212)	\$716,980	2.46%
722291	AIS Terminal Parking Structure Lighting Remodel	\$1,566,209	\$127,559	\$1,217	\$1,694,985	8.22%
722104	AIS Snow Barn Complex	\$4,423,464	\$202,580	\$89,353	\$4,715,397	6.60%
722293	AIS Terminal 2 nd Level Police Suite	\$1,421,590	\$39,869	\$2,448	\$1,463,907	2.98%
722292	AIS Terminal Fitness Center	\$211,118	\$13,831	\$365	\$225,314	6.72%
722294	AIS Terminal Mechanical Penthouses Reconstruction	\$3,857,348	\$48,698	\$0	\$3,906,046	1.26%
770007	AIS Terminal Apron Reconstruction (Phase III)	\$3,744,832	\$56,971	\$0	\$3,801,803	1.52%
Average Project Amount**		\$3,454,813			Average Change **	4.37%

** Does not include AIS Restroom Remodeling Project

Source: Project Change Orders

The documentation for Change Order No. 1 indicates that the reason for the change was “changed scope” and that the cost adjustment was “negotiated”. All parties involved (architect, contractor, Director of DMD, Aviation Finance Officer, CIP, and CAO) agreed to the change and approved the Change Order.

According to Public Purchases Ordinance, Section 5-5-11 ROA 1994, Capital Projects:

(C) The Mayor may promulgate additional or revised rules and regulations regarding the solicitation of offers for capital projects and the award or rejection of offers therefor, including but not limited to establishing procedures for the solicitation and consideration of offers, award or rejection of offers, determining the responsibility of offerors, and such other matters as the Mayor deems desirable for the efficient administration of capital projects.

Miscellaneous Item of Concern

Bonds

The contractor furnished the necessary bonds for the original contract price of \$1.15 million. However, the contractor did not increase the bond amounts to reflect the increased contract value from the subsequent change orders. At a final project cost of \$2.33 million, the project exceeded the value of the bonds by \$1.18 million.

According to the “Instructions to Bidders,” Section 17, Bonds and Insurance Certificates, “...the Contractor shall furnish separate surety bonds in the form provided in the Contract Documents each in the amount of one hundred percent (100%) of the total Contract Price, as follows:

- A Performance Bond as security for the faithful performance of the Contract and
- A Labor and Material Payment Bond for the payment of all labor and materials.”

Contract Price is defined in the General Specifications as “the total monies payable to Contractor under the Contract Documents.” Contract Documents is defined as “the Agreement, Addenda, Advertisement for Bids, Instructions to Bidders...and all Modifications, also referred to as the contract.”

Without the necessary bond coverage, the City would not have a guaranteed remedy should the contractor default.

RECOMMENDATIONS

The City Council should work with the City’s Administration to:

- Review and update the CIP Award Regulation to include:
 - The definition of material change orders,
 - Clarify language to address:
 - Whether material change orders require a separate bidding process,
 - Whether the other qualified, losing bidders should be afforded the opportunity to provide competitive bids for additional work identified by the City shortly after the original bid opening.
- Ensure bonding clauses address the increase in contract price caused by material change orders, as no City regulation currently addresses this issue.

CONCLUSION

Change orders to construction contracts are not uncommon. Since 2013, change orders for the Aviation Department's construction projects, increased the average total project cost by 4.4 percent. Change order No. 1 of the AIS Terminal Restroom Remodeling Project exceeded the average and was an 82 percent increase of the original project value. Without clearly defined requirements, additional guidance, or limitations to potential changes of scope, the inclusion of material change orders may persist.

Opportunities for improvement exist within the construction contracting process as the items contained in the City Council's request are not clearly addressed in City regulations. Aside from the 13-day delay of the contract award, the procurement of the AIS Terminal Restroom Remodeling Project complied with the City's Public Purchases Ordinance and CIP Award Regulation.

The purpose of the CIP Award Regulation is to "protect the substantial interest of the City and the integrity of the City's Public Works construction contracting process." By reviewing and updating City regulations, the City Council and Administration have the ability to clarify procurement regulations and address the issues raised by the Councilor. Updating these regulations will strengthen related processes, while protecting and ensuring the integrity of the City's construction contracting process.

APPENDIX A

**Procurement Process
Including Authoritative Documents**

Description of Event	Authoritative Document	Section Reference	Required Timing	Required/Specified Date	Actual Date	Results
Bidding Closes	Advertisement for Bid	N/A	N/A	October 22, 2013	October 22, 2013	On time
Notice of Award	Bid Proposal	Item #5	Within 30 days after scheduled closing time for receipt of bids.	No later than November 21, 2013	December 3, 2013	13 days late
Award of Contract	Instructions to Bidders	Item #15.D Time to Award	Within the period specified in the Bid Proposal unless the Bidder and the Owner agree <i>in writing</i> to extend the period specified.	Within 30 days after scheduled closing time for receipt of bids. No later than November 21, 2013	December 3, 2013	13 days late Request to Extend not issued.
Delivery of formal contract documents (including Performance Bond, Labor & Material Payment Bond, and required Certificates of Insurance)	General Specifications & Bid Proposal	2.1.1 & Item #6	Within 10 days of Bidder's receipt of Notice of Award.	No later than December 13, 2013	December 12, 2013	On time
Execution of Agreement	General Specifications	2.1.1	Within 15 days of receipt of agreement and all required contract documents	No later than December 27, 2013	December 19, 2013	On time

Description of Event	Authoritative Document	Section Reference	Required Timing	Required/Specified Date	Actual Date	Results
Effective Date	General Specifications	Definitions	The date on which the Agreement is signed and delivered by the last of the two parties to sign and deliver	N/A	December 19, 2013	N/A
Contract Time	General Specifications	2.5.1	Commence to run on the 30 th day after the Effective Date of the Agreement, or if a Notice to Proceed is given, on the day indicated.	January 6, 2014	January 6, 2014	N/A
Notice to Proceed	General Specifications	2.5.1	Within 30 days after the effective date of the Agreement	No later than January 18, 2014	January 7, 2014	On time

Source: CABQ documents

SUBMITTED:

Contract Auditor

REVIEWED & APPROVED:

Lawrence L. Davis, Acting Director
Office of Internal Audit

APPROVED FOR PUBLICATION:

Chairperson, Accountability in
Government Oversight Committee