

City Auditor Finds Long Beach Jobs Order Contracts Process Was Prone to Fraud, Lacked Oversight

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A report released by the Long Beach City Auditor's office Wednesday detailed the systemic pressures and lack of control that led to city job contracts for the Department of Public Works were being overinflated, inappropriately priced and were vulnerable to fraud. The nearly two-year review of the city's Job Order Contracting program (JOC) showed that the city has paid over \$1.9 million more than it was contractually obligated.

The JOC program was initiated in 2003 as an alternative way to contract out work for routine maintenance, repair and minor construction throughout the city using general contractors to fulfill a large number of jobs under the umbrella of a single awarded contract. When a bid is received for these types of contracts the bidder doesn't typically submit a price for the contract but a "task catalog percentage" with that number being applied to the entire contract to arrive at a final price. The bidder that submits the lowest percentage is awarded the JOC contract.

Examples of work carried out under JOC contracts are the roof replacement at Bixby Park, the Somerset Playground replacement, the resurfacing of Silverado Parks' sports courts and the re-carpeting of multiple community rooms at various branch libraries.

City Auditor Laura Doud's 33-page report shows that the JOC program within the Department of Public Works had created an environment "highly vulnerable to fraud," partially because it placed an emphasis on getting jobs done quickly instead of ensuring that they were competitively priced and properly defined.

The "Triangle of Fraud" as defined in Doud's report, was created by contractor's pressure to inflate costs because the city was accepting bids that were unrealistically low. The three points of the triangle

were listed as the pressure to inflate costs, opportunity without detection and justification for quick completion.

The report showed that the average current bid percentage is between 50-71 percent, with the percentages bid by contractors declining by over 30 percent since the program's initiation. This, the report said, caused bid winners to adjust the proposals by adding non-catalog items, which are priced at 110 percent of costs, rather than the submitted winning catalog percentage in an effort to turn a profit on an otherwise unrealistic offer.

These adjustments were able to fly under the radar because of a lack of structure and oversight in the JOC program, the report said. This ranged from the initial scope of work (SOW) that made it difficult to assess whether the submitted price was appropriate. The lack of clarity led to order changes and cost overruns to occur in 91 percent of the projects surveyed in the report that spanned 17 months.

Adding non-catalog charges requires three independent quotes that are reviewed by the city prior to approval. The audit found that 67 percent of the non-catalog items documented had no independent quotes, but also had no documentation of justification explaining why the quotes were forgone.

Furthermore, Long Beach's program, unlike other JOC's, does not have a cap on how many "non-catalog" items can be added once a bid is awarded. This resulted in over 40 percent of contractor jobs having these items added, resulting in an overall expenditure increase of almost \$2 million.

"If a 10% cap on these non-catalog items had been in place, the City could have potentially saved \$1.9 million, or 15% of overall costs," the report said. "Based on the average JOC project price, that savings equates to 19 additional projects that could have been completed."

Doud's report noted that despite a former city project manager issuing a letter to a JOC contractor addressing the overinflation of a proposal, one that was circulated to JOC management staff, the city continued to grant over \$3.8 million of work to that contractor who had allegedly "padded proposals" to inflate pricing.

The report added that during the audit, a recurring theme with project managers was that JOC contractors "regularly inflate proposals due to the inability to make a profit from the low bid percentages."

Part of the problem may lie in how many people have access to the system where catalogs and the scopes of work can be manipulated. The audit found that 33 individuals, eight of whom no longer work for the city, have access to those files and could potentially edit them. During the audit, one project could not be located in the system although the documents showed that it had at one time existed on the server.

The last component of the fraud triangle is the city's emphasis on completing projects quickly. JOC projects are not to exceed \$500,000—the current average is \$100,000—but projects like the Belmont Pool demolition (\$2.6 million) and the remodel of the Harbor Department's administrative offices (\$14 million) were processed through the JOC because of "a need for quick implementation."

Focusing on speed rather than quality led to many issues, none more alarming than the lack of evaluation of the subcontractors' work. The audit found that the city does not currently do post-project evaluation of the work performed to make sure it meets the city's expectations. In one case, the audit stated that a project manager had expressed concern over the performance of a sub-contractor. They were removed from that particular project but went on to receive \$1.2 million in work from the city.

The report acknowledge the obvious advantages of using the JOC program—speed—but showed that in terms of getting projects up and going Long Beach, ironically, lags behind the industry standard. During the audit period seven projects amounting to \$3.3 million took more than 90 days to initiate. The industry standard is 25 days with an existing design and 55 days without.

Many of the contractors that hold JOC bids have held them since 2003 when the program was initiated. In January 2015, the city awarded a bid to a company that had held the contract since 2003—only the most recent proposal was for 50 percent, an all-time low figure, according to the audit.

This came one month after a letter to the JOC program manager from the Gordian Group, the city's consultant, warned the city to reject all bids that offered a catalog percentage that was below 80 percent because "it's not possible to be successful" with those price points. It added that below 80 percent, the contract morphs into negotiated contract instead of a fixed one.

"Contractors bid these extremely low percentage factors to win the contract; however, as it is impossible to make money using these low percentage factors, it creates a pressure, or need, to find

other ways to increase project costs,” the report stated. “Their long-term relationship with the City and experience with the JOC program likely influenced the decline in bid percentage factors.”

The report found that the lack of policies, procedures or program standards led to inconsistencies in how projects were managed and the level of documentation that was maintained. In total, the report made 40 recommendations detailed recommendations to address the shortcomings. During last night’s city council meeting, a vote to incorporate future controls was passed unanimously. The requirements include the ability to reject any bids if it’s found to be in the best interest of the city to rebid them, add the 10 percent cap for non-catalogue charges, the pre-qualification of JOC contractors, independent review of project proposals and the oversight of contract work. The current program has also been suspended while the audit’s concerns are addressed.

“I want to thank the Department’s staff for their assistance, patience and cooperation during this lengthy audit,” Doud said in a statement. “I am pleased the City has acknowledged the severity of the issues surrounding the program and has taken immediate steps to address the recommendations. The JOC program has the potential to make timely and much needed capital improvements for our City.”