

# All American Asphalt Annual Street Improvement Contract Audit

*The contractor was paid \$2.5 million for projects outside of set contract pricing in a nine- month period. Not all of these projects adhered to City purchasing guidelines.*



*Independence you can rely on*

December 2018

**Laura L. Doud**

*City Auditor*

**Hannah Morgan**

*Performance Audit Manager*



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## Executive Summary

The City has committed significant resources in recent years to street repairs and improvements. Since 2013, All American Asphalt (AAA) has been the contractor of the as-needed Annual Contract for Street Improvements. The current as-needed contract was awarded in May 2017. It is valued at \$40 million per year and in effect until April 2019, with a City option to renew for one additional year.

Annual street improvement programs, such as reconstruction and resurfacing of arterial roads and residential streets are completed by AAA, are overseen by the Department of Public Works (Department) and funded by a variety of sources, including state gas taxes, one-time resources, City Council discretionary funds, and local measures and propositions. This amount of funding for street improvements underscores the need for the City to have clearly defined procedures and controls in place to ensure that the public is getting the most value for its investment.

Our audit examined pricing, quality, and extra work performed under the AAA contract. We found only minor improvements needed in the administration of the annual street improvement work; however, the audit found issues surrounding the use of the AAA contract's extra work provisions, which were established for services outside of set contract pricing.

**The desire to expedite projects drove the use of the Annual Contract for Street improvement for Extra Work Projects, which did not all adhere to the normal purchasing process.**

The Department utilized the extra work provisions of the contract to execute projects more quickly. While the contract allowed extra work, the executed projects under the provisions were not fully planned prior to commencing and included incorrect markup costs that led to overcharges. In addition, by using the contract for these Extra Work Projects, the Department did not adhere to City purchasing guidelines relating to procurement activities. In a nine-month period in 2017, the City paid AAA a total of \$2.5 million for Extra Work Projects, defined as projects with total costs comprised of over 80% non-contract items.

The more minor contract management issues that were identified include:

- City Inspectors documenting support for contract work was not consistent.
- Contract prices and corresponding time periods are not clearly communicated.

We recommend that pricing, not just speed, be considered when completing Extra Work Projects. Procurement for these projects should follow purchasing guidelines by requiring quotes from multiple contractors or bidding out these projects separately. Overall, the Department needs to be able to guarantee that the City receives quality services at competitive prices on all projects.

We thank the Department staff for their assistance and cooperation during this audit.

# I. Findings & Recommendations

**Finding #1** *\$2.5 million of the \$12.6 million paid to AAA between April and December 2017 under AAA's Annual Contract for Street Improvements was for projects outside of set contract pricing. Not all of these projects adhered to standard City purchasing guidelines.*

AAA's as-needed Annual Contract for Street Improvements (as-needed contract) allows for extra work or materials to be provided. Extra work is any additional service, material, or equipment provided by the contractor that is not included in the set list of contract items. The as-needed contract does not set restrictions on the dollar amount or scope of the extra work allowed, but does require quantities and prices to be agreed upon in writing prior to the commencement of work.

Extra work is billed at time and material costs plus additional markups allowed by contract specifications. From April to December 2017, AAA was paid \$2.5 million for Extra Work Projects under the as-needed contract, defined as projects with total costs comprised of over 80% non-contract items.

## A. Defining Extra Work

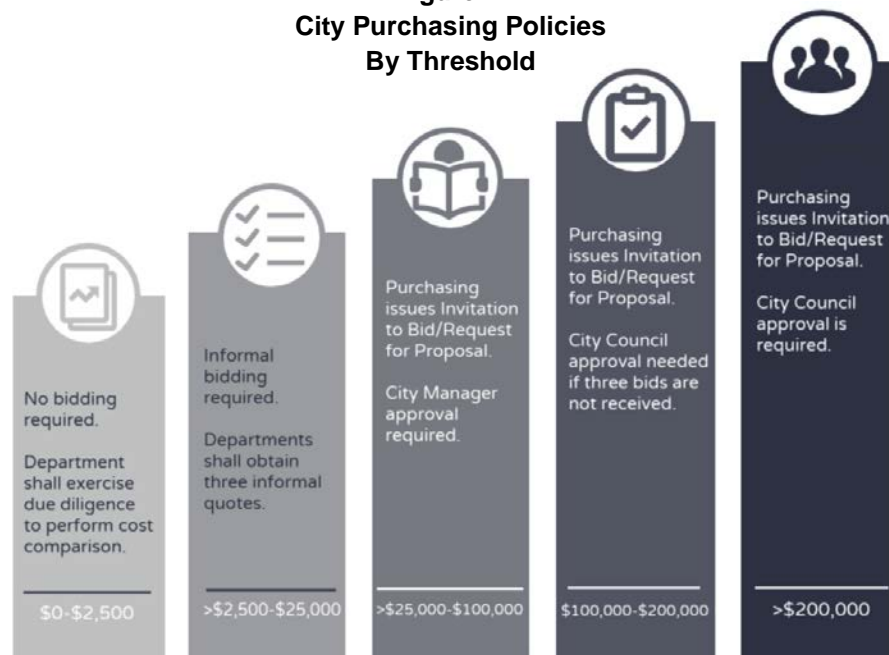
Since the as-needed contract does not explicitly define or restrict extra work projects, we interviewed Public Works Department staff to establish how it determined which extra work projects were to be completed by AAA. Department staff indicated that the extra work projects performed by AAA should be for small (staff defined small as under \$500,000 in costs) and emergency (defined as urgent and unexpected) projects. The Department needs to formalize its criteria for extra work projects and ensure they are followed and documented.

## B. Purchasing Policies

Using the as-needed contract allows for the Department to move projects along more quickly than would be the case with standard City purchasing policies. These purchasing policies stipulate various procurement approvals and requirements, including formal or informal bidding, depending on the total project cost. These requirements can delay the start of projects.

These purchasing policies are outlined in Figure 1 on the next page.

**Figure 1.  
City Purchasing Policies  
By Threshold**



**Some Extra Work Projects should have required a formal bidding process under City purchasing guidelines.**

The dollar value of each Extra Work Project reviewed in this audit was above \$2,500 and, therefore, should have required some form of competitive bidding, whether formal or informal. At least seven projects were above the \$25,000 threshold, requiring an Invitation to Bid or Request for Proposal to be sent to potential vendors. While exceptions to purchasing guidelines can be requested, an explanation for why the project cannot be procured using a competitive bid process must be provided. In addition, exceptions must be approved by City purchasing personnel or the City Manager, depending on the cost.

### **C. Establishing Project Pricing and Scope**

Another consequence of pushing projects through quickly is that some projects are started without full plans in place. Department staff stated that although required by the contract, pricing was not always clearly documented and the scope was not always agreed upon for Extra Work Projects prior to the commencement of work. Staff expressed that with some of these projects, the full scope may not be known until the project has started; therefore, there are unknown circumstances that may arise. When this occurs, there is the possibility that the cost and/or scope of the project may increase more or decrease less than originally expected.

### **D. Cost of Work**

In addition, there are cost considerations when using the AAA as-needed contract instead of receiving multiple bids on a project. Because these special projects were not procured through a competitive process, it is not possible for the City to know if they received the best price. Project Managers were not able

to say that the lowest price or best value was received on these projects.

Since extra work is billed on a lump sum or time-and-material basis with allowable markups, AAA and its subcontractors understood that they would be paid for as many hours as it takes for the work to be completed. Furthermore, AAA frequently relied on subcontractors to execute the extra work projects because either AAA was occupied performing annual street improvement work or the extra work projects were outside of AAA's expertise.

- AAA used a total of 66 subcontractors to complete the seven extra work projects we reviewed. The number of subcontractors used on each project ranged from one to thirty.
- Allowed markups can be up to 31% on top of the cost of the work.

It is important that the City ensures that the best value is received and the lowest price is paid for the projects completed. Department staff was unable to attest that utilizing the AAA contract in this manner did or did not result in the best value and lowest price, because the primary emphasis was on the speed of project completion and secondarily on cost and value.

#### **Recommendations:**

- 1.1. **Explore other options of getting extra work projects completed within time constraints, including the use of other City as-needed contractors or contractors in the Job Order Contract program. At a minimum, quotes should be obtained to be able to compare across bidders to ensure lowest pricing is considered.**
- 1.2. **Finalize scope of work before a project begins.**
- 1.3. **Develop and enforce written guidelines that spell out the circumstances in which extra work projects can be assigned to AAA or similar as-needed contractor. Guidelines should consider standard purchasing policies and the consequences of not following them.**

#### **Finding #2**

***Insufficient review of billing accuracy was done for extra work, resulting in errors and slight overcharging due to incorrect markups.***

**It is unclear who has the responsibility to review extra work invoice backup for correct markups.**

Invoices and supporting documentation must be reviewed to ensure that the City is paying the correct amount for the services and materials provided and that applicable contract specifications are being followed.

For extra work, the Inspector, Project Manager, and Administrative Analyst positions are all involved in the payment process. However, we did not see evidence that these parties were reviewing backup documentation to ensure that it adhered to contract specifications surrounding allowable markups. There is no clarity regarding whose responsibility it is to check for billing accuracy.

Extra work is billed at time-and-materials or lump sum with the following markups allowed for both AAA and subcontractors:

For AAA-performed extra work, the City can be charged:

- A 20% markup for labor and 15% markup for materials and equipment by AAA
- A 1% surcharge for AAA's bond premium

For subcontractor-performed extra work, the City can be charged:

- A 20% markup for labor and 15% markup for materials and equipment by the subcontractor
- A 1% surcharge for the subcontractor's bond premium
- A 10% markup on the first \$5,000 and 5% markup on the remaining costs by AAA

The audit found that the incorrect application of these allowed markups resulted in overcharges to the City for extra work. In the sample of invoices reviewed, while we identified only \$14,000 in overcharges, almost 50% of the invoices we reviewed had some combination of incorrect fees charged. Some invoices had incorrect bond fees, incorrect markups, or both.

### **Recommendations:**

- 2.1 Develop written guidelines that assign and clarify responsibility for invoice review and communicate those guidelines to the Project Managers and Administrative Analysts.**
- 2.2 Those responsible for review should ensure backup documentation supports the amounts charged and follows all contract specifications.**
- 2.3 Work with AAA to recoup overcharged amounts on previous invoices.**

### **Finding #3**

*Not all price changes that occurred during AAA's tenure as the as-needed contractor (2013 to present) were officially adopted. Pricing overlapped time periods and contract allocations.*

#### **A. Price Changes**

Changes to any City contract should be made official through an amendment. This ensures that changes in price or other contract terms are agreed upon by both parties in writing.

In November 2015, the Department asked the City Council to authorize a fourth amendment to the 2013 as-needed Annual Contract for Street Improvements. The memo included with the City Council item stated that an additional \$13 million as well as a term extension were needed for the contract. The item also discussed that AAA had asked the City to agree to price changes (included increases and decreases in price) for seven concrete items and twelve asphalt items.

When the amendment for the contract was executed, the price changes for the 19 items noted above were not included. The Department and AAA continued to operate as if they were officially changed. In addition to the 19 items discussed, there were eight additional line items that were also changed due to confusion surrounding handwritten prices on the original contract. Some prices were written illegibly, and as a result, AAA thought the prices needed to change when they were the same as what was previously agreed upon.

## **B. Contract Overlap**

AAA had two as-needed Annual Contracts for Street Improvements in effect for four months during 2017. The first (2013) contract was in effect from March 2013 to August 2017, while the second (2017) contract was in effect from May 2017 to April 2018, with two one-year extension options. There was a four-month overlap from May to August 2017.

This overlap caused confusion about which contract prices should be used. Some invoices that were paid through the 2017 contract purchase order were paid at 2013 contract prices. It was difficult to determine which prices should be applied to each invoice. Department staff explained that prices charged were based on when the project was agreed upon to occur, not when the work was actually completed. However, this “agreed to” date was not specifically documented and the invoices reflected the work completed date. Therefore, it was difficult to determine which price should be in effect.

### **Recommendations:**

- 3.1 Make all price changes official by amending the contract to reflect them.**
- 3.2 Clearly delineate which prices should be charged and for what time period during communication between AAA and Project Managers.**
- 3.3 Review invoices to ensure agreement between contract and purchase order pricing.**



#### **Finding #4**

*Based on the documentation retained in some project files, it was not possible to determine if all work paid for was performed and up to quality standards.*

For both regular contract activities and extra work, Inspectors are assigned to verify the work of AAA and the company's subcontractors. The Inspectors visit the job site on a periodic basis to document AAA's labor, materials, and equipment used. The Inspectors document their observations in writing within their Inspector Journals. The purpose of these inspections is:

- For contract work: to verify that all contract work is received, the quality of the work performed is up to the City's standard, and that the quality of materials used are those that are charged to the City.
- For extra work: to verify that all contract work is received and the time-and-materials costs are accurate by determining the number of workers and labor hours, as well as the types of materials and equipment that are on site.

At the end of the work day, the Inspector signs the Daily Report to certify the work that was completed. This signature is later used by Project Managers as verification that the invoice could be paid.

**Project files varied between projects and inspectors. Files did not support all the charges paid.**

Project files did not contain the backup needed to certify that all work was performed. Inspector Journals varied by file and Inspector; there was no standard form or checklist requiring certain information to be retained. For example, inspector files did not always match bills and invoices provided by AAA.

- Inspector Journals for contract work were generic and did not list all items found on the invoice.
- Inspector Journals for extra work had different totals for labor hours worked and did not document the use of equipment that was on the invoice.
- Not all Inspector Journals were signed, which serves as the official certification that the work could be paid.

#### **Recommendations:**

- 4.1 Determine which labor, materials, and equipment Inspectors must document and use to approve payment.**
- 4.2 Develop written procedures and tools to help Inspectors reconcile their observations with AAA's records. For example, the journals used by all City inspectors should be uniform to ensure everyone is collecting the same information and that the information collected is in the same format.**

- 4.3    Develop written guidelines for Project Managers and Inspectors regarding what a complete project file should include.**
- 4.4    Develop written guidelines to evaluate work and ensure that poorly performing subcontractors are not used on future projects.**

## II. Background

### A. Department of Public Works

**The Department is responsible to improve and maintain our City streets and sidewalks.**

The Department of Public Works (Department) is responsible for working to keep the City's physical infrastructure and transportation systems in usable and safe condition for our residents, businesses, and visitors. The Department provides a variety of services that include the repair, rehabilitation, and general upkeep of City streets and sidewalks. Some of these services are completed through the City's various Capital Improvement and Infrastructure Plans.

There are various Project Managers and Inspectors within the Department's Engineering, Transportation Mobility, and Public Service Bureaus that help to oversee the projects completed by AAA under the as-needed contract. Some of them are City employees and others work as consultants on these projects.

### B. Annual Contract for Street Improvements

**AAA provides as-needed street improvement work. The current contract is for \$40 million per year.**

All American Asphalt (AAA) has been a City contractor since 1998, working on various contracts and projects. Since 2013, AAA has held the City's as-needed Annual Contract for Street Improvements. AAA was awarded the as-needed contract in March 2013 and again in May 2017. The as-needed contract includes specific pricing on 361 line items that are designed to cover all kinds of street improvement work, including various quantities of asphalt concrete pavement, slurry seal, stamped concrete, curb and gutter, traffic striping, and pothole repair.

The major City infrastructure programs that are completed under the as-needed contract are Major/Secondary Highways, Citywide Residential Streets, and Citywide Slurry Seal. The 2017 as-needed contract was awarded for a not-to-exceed annual amount of \$40 million. The original contract term was from May 2017 to April 2018 and has been extended until April 2019, with an additional one-year option available.

In addition to the annual street improvement work completed under the contract, AAA also completes special projects that include work not covered under the contract line items (extra work). These projects follow separate contract specifications related to extra work.

There are various funding sources for the work covered under the as-needed contract. Funding is sourced from various taxes, one-time resources, City Council discretionary funds, as well as local and state measures and propositions.

### III. Objective, Scope, and Methodology

The objectives of this audit were to analyze the processes surrounding the methodology used to select the vendor, assignment of work, and the pricing and quality of the work received under Annual Contract for Street Improvements with All American Asphalt (AAA). The audit scope covered payments made from April to December 2017 under the Department of Public Works. To achieve this objective, we:

- Interviewed Public Works staff, including Project Managers, Inspectors, and Administrative Analysts involved with the AAA contract;
- Reviewed the 2013 and 2017 as-needed Annual Contracts for Street Improvement between the City and AAA, as well as corresponding contract specifications, pricing schedules, and amendments;
- Evaluated payments against contract specifications for a sample of contract and extra work projects;
- Examined project files for a sample of contract and extra work projects; and
- Reviewed the City's Procurement Policy;

We conducted this performance audit in accordance with Generally Accepted Government Auditing Standards (GAGAS). Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

## IV. Appendices

## **Appendix A. Management Comments**

Following this page are management's comments to the audit findings and recommendations.



**City of Long Beach**  
*Working Together to Serve*

**Memorandum**

**Date:** December 17, 2018  
**To:** Patrick H. West, City Manager *T.H.W.*  
**From:** *CB* Craig A. Beck, Director of Public Works  
**For:** Laura L. Doud, City Auditor  
**Subject:** All American Asphalt Street Improvement Contract Audit

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The on-call All American Asphalt Annual Street Improvement Contract is a vital resource to deliver infrastructure improvements citywide. The Department of Public Works appreciates the City Auditor's interest and efforts in improving the administration and use of the contract. The Auditor's staff conducted a thorough review in a professional manner which facilitated the exchange of information.

Public Works looks forward to implementing recommendations resulting from this audit and revisiting current practices. Public Works recognizes the need for standardization in project management and is developing a Project Management Manual. The department is also soliciting proposals to provide additional on-call contacts for future infrastructure projects.

In developing the contract for on-call street improvement services, every effort is made to anticipate services necessary to deliver carefully designed and planned projects. This includes considering provisions for unforeseen conditions, as well as balancing cost, timing and quality. The All American Asphalt Street Improvement Contract allows Public Works to complete defined projects with effectiveness and efficiency.

Public Works will monitor the implementation of the recommendations and continue working with the City Auditor's Office to improve our services to the community.

If you have any questions, please contact Malcolm Oscarson, Business Operations Bureau Manager, at (562) 570-6325.

CB:MO:ccb

**CC:** TOM MODICA, ASSISTANT CITY MANAGER  
KEVIN JACKSON, DEPUTY CITY MANAGER  
JOHN GROSS, DIRECTOR OF FINANCIAL MANAGEMENT  
REBECCA GARNER, ASSISTANT TO THE CITY MANAGER  
MALCOLM OSCARSON, BUSINESS OPERATIONS BUREAU MANAGER



**MANAGEMENT RESPONSE AND ACTION PLAN**  
**All American Asphalt Annual Street Improvement Contract Audit**  
**Public Works Department**

No.	Recommendation	Priority	Page #	Agree or Disagree	Responsible Party	Action Plan / Explanation for Disagreement	Target Date for Implementation
1.1	Explore other options of getting extra work projects completed within time constraints, including the use of other City as-needed contractors or contractors in the Job Order Contract program. At a minimum, quotes should be obtained to be able to compare across bidders to ensure lowest pricing is considered.	H	4	Agree	Engineering/ Project Mgmt	Public Works recognizes the need for specialized on-call contracts and is currently in the process of drafting specifications for ADA Curb Ramps, Community Development Block Grant work, Concrete Work, Bridge Repairs, Pump Stations, Major Arterials, Residential Street Repairs, and Traffic Improvements. Soliciting quotes from other contractors for work in progress may be problematic in having multiple contractors working on the same project, resulting in increased costs, mobilization and responsibility.	April 2019
1.2	Finalize scope of work before a project begins.	H	4	Agree	Engineering/ Project Mgmt	The Bureaus will reinforce the importance of determining Scope of Work (SOW) prior to initiating construction. Due to timing concerns, there may be situations where it is more practical or cost effective to initiate construction while finalizing SOW.	January 2019
1.3	Develop and enforce written guidelines that spell out the circumstances in which extra work projects can be assigned to AAA or similar as-needed contractor. Guidelines should consider standard purchasing policies and the consequences of not following them.	M	4	Agree	Engineering/ Project Mgmt	The Department has been compiling a project management manual which contains guidelines for (a) extra work, (b) reviewing and certifying invoices for payment, (c) backup documentation to include with invoices, (d) documenting and reconciling field work and invoices, and (e) project files. Although the manual will be completed in March 2019, staff will be reminded effective immediately during division meetings.	March 2019
2.1	Develop guidelines that assign and clarify responsibility for invoice review and communicate those guidelines to the Project Managers and Administrative Analysts.	L	5	Agree	Business Operations/ Engineering/ Project Mgmt	Please reference 1.3 response.	March 2019
2.2	Those responsible for review should ensure backup documentation supports the amounts charged and follows all contract specifications.	H	5	Agree	Business Operations/ Engineering/ Project Mgmt	Please reference 1.3 response.	March 2019
2.3	Work with AAA to recoup overcharged amounts on previous invoices.	H	5	Agree	Business Operations	The Business Operations Bureau with work with the City Auditor to identify overcharge amounts and then work with AAA.	January 2019
3.1	Make all price changes official by amending the contract to reflect them.	L	6	Agree	Engineering/ Project Mgmt	In effect with the current Annual Street Improvements Contract and amendments will be processed as needed.	January 2019



**MANAGEMENT RESPONSE AND ACTION PLAN**  
**All American Asphalt Annual Street Improvement Contract Audit**  
**Public Works Department**

No.	Recommendation	Priority	Page #	Agree or Disagree	Responsible Party	Action Plan / Explanation for Disagreement	Target Date for Implementation
3.2	Clearly delineate which prices should be charged and for what time period during communication between AAA and Project Managers.	M	6	Agree	Business Operations	When issuing a Notice To Proceed (NTP), the specific contract/PO will be listed, requiring all invoices submitted by the contractor to include the contract#/PO# and/or the contract amendment #.	January 2019
3.3	Review invoices to ensure agreement between contract and purchase order pricing.	M	6	Agree	Business Operations	Please reference 1.3 response.	January 2019
4.1	Determine which labor, materials, and equipment Inspectors must document and use to approve payment.	H	7	Agree	Engineering/ Project Mgmt	The labor, materials, and equipment are stipulated in the schedule of work and prices of the contract and the Extra Work provisions in the specification of the contract. This will be reinforced with the Inspectors.	January 2019
4.2	Develop procedures and tools to help Inspectors reconcile their observations with AAA's records. For example, the journals used by all City inspectors should be uniform to ensure everyone is collecting the same information and that the information collected is in the same format.	M	7	Agree	Engineering/ Project Mgmt	Please reference 1.3 response.	March 2019
4.3	Develop guidelines for Project Managers and Inspectors regarding what a complete project file should include.	L	7	Agree	Engineering/ Project Mgmt	Please reference 1.3 response.	March 2019
4.4	Develop guidelines to evaluate work and ensure that poorly performing subcontractors are not used on future projects.	L	7	Agree	Public Works/ FM-Labor Compliance	Guidelines will be developed to evaluate performance and recommend that poorly performing subcontractors are not used on future contracts. The City Council would need to approve the recommendations and Labor Compliance would need to maintain and publicize the list of the barred subcontractors.	Target date to be worked out with Labor Compliance

**Priority**

H – High Priority - The recommendation pertains to a serious or materially significant audit finding or control weakness. Due to the seriousness or significance of the matter, immediate  
M – Medium Priority - The recommendation pertains to a moderately significant or potentially serious audit finding or control weakness. Reasonably prompt corrective action should be taken by  
L – Low Priority - The recommendation pertains to an audit finding or control weakness of relatively minor significance or concern. The timing of any corrective action is left to management's

**Yellow areas - to be completed by the department**



**Long Beach City Auditor's Office**

333 W. Ocean Blvd., 8<sup>th</sup> Floor, Long Beach, CA 90802

Telephone: 562-570-6751

Website: [CityAuditorLauraDoud.com](http://CityAuditorLauraDoud.com)

Like us at [facebook.com/LongBeachCityAuditor](https://facebook.com/LongBeachCityAuditor)

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