

EXECUTIVE SUMMARY
AUDIT OF THE TRI-GOLD JOINT VENTURE
(HDR ENGINEERING, INC., JACOBS CIVIL, INC. AND KWAME BUILDING GROUP, INC.)
UNDER CONTRACT R00-11

INTRODUCTION

Internal Audit performed interim audits of HDR Engineering, Inc. (HDR), Jacobs Civil, Inc. (Jacobs) and Kwame Building Group, Inc., (Kwame), the three members of Tri-Gold, the joint venture that is providing project management and construction management services for the North Shore Connector project. The scope of this audit is February 26, 2001 through September 1, 2007. The amount authorized by Port Authority's Board of Directors for this contract as of November 2008 is \$33,200,000.00. For direct costs, indirect costs and fees during the period audited, these companies were paid approximately \$5.3 million, \$4.4 million and \$1.4 million respectively, a total of \$11.1 million.¹

STATEMENT OF AUDIT OPINION

Based on the results of these three audits, we concluded that, with the exception of Kwame's overhead costs, in general, the contractors' accounting systems are adequate to track and invoice costs under this agreement and Port Authority personnel are doing a good job in managing Tri-Gold's work and costs. This audit identified a net total of \$66,681.41 in cost recoveries. This amount represents 0.6% of the total amount audited of \$11.1 million and is an indication that project invoices are being monitored appropriately. However, several observations and recommendations were made to improve Tri-Gold's billing and invoicing practices (and Port Authority's management of same) as summarized below.

AREAS IDENTIFIED FOR PROCESS IMPROVEMENT WITH MANAGEMENT RESPONSES

- 1) Provisional overhead rates are typically used for billing purposes during the year because actual overhead rates cannot be calculated until the fiscal year is complete. This approach is a standard industry practice. For the overhead adjustments for HDR and Jacobs, we calculated the difference between overhead costs paid using provisional overhead rates and overhead costs adjusted using audited overhead rates.

For HDR, this difference is a credit due to HDR in the amount of \$119,698.22. If the contractual language in Section 8 of the contract which limits overhead costs to amounts paid based on provisional overhead rates is applied, Port Authority is due \$16,557.35.

For Jacobs, this difference is an amount due to Port Authority of \$181,836.31. If the contractual language in section 8 of the contract which limits overhead costs to amounts paid based on provisional overhead rates is applied, Port Authority is due \$198,416.73.

For Kwame, because an overhead audit had not been performed by an independent public accounting firm during the audit period, an overhead adjustment was not calculated. As a result, \$565,653.60 in overhead costs is considered to be unresolved. Kwame's independent certified public accountants are in the process of completing their audit of Kwame's overhead rates for fiscal years 2006 and 2007. Internal Audit considers Kwame's overhead charges to be unresolved because Kwame has not submitted audited overhead rates for years 2001 through 2007. In addition, Internal Audit has concerns regarding whether Kwame's records related to overhead costs for this time period are auditable.

- We recommend that the overhead adjustments should be resolved and Kwame should engage its certified public accountant to provide audited overhead rates for Kwame's

¹ Please note that all three Tri-Gold joint venture entities were audited for this period and separate audit reports were produced for each of these entities.

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fiscal years 2001 through 2005 as soon as possible. This information was provided to Port Authority's contracting officer and general counsel for resolution.

- Port Authority management reports that an agreement has been finalized with Tri-Gold to address all overhead rate issues for the audited period for all three Tri-Gold entities, which resulted in a net credit of \$62,138.09 in favor of Port Authority and that Kwame's certified public accountant, Reuben Brown, has now produced audited overhead rates for Kwame for 2006 through 2008. Reuben Brown was unable to certify audited overhead rates for 2001-2005, but as part of the agreement with Tri-Gold to resolve all overhead issues, Kwame and Port Authority management have agreed that Kwame will only be entitled to the provisional overhead rates it was paid for the period audited. Management found this resolution to be reasonable due to the fact that Kwame's overhead rate appeared to be very low for a portion of the period under review, and if an audit could have been conducted, it would have likely resulted in a credit due to Kwame or, at best, an insignificant recovery for Authority. Further, Kwame will ensure it keeps auditable overhead records going forward, and Internal Audit will monitor same for compliance.
- 2) In two instances, work continued under Agreement R00-11 even though the authorized cost limitations as stated in the agreement had been reached. Invoices associated with this work totaled \$618,053.50 and \$1,353,000.00. Although the agreement's cost limits were exceeded, we stress that these amounts were within the overall spending limits authorized by Port Authority's Board of Directors, invoices were held for payment until the amendments were executed and the vast majority of these costs were not actually paid until the amendments were executed.
- We recommend that amendments, where reasonably possible, should be initiated well in advance of reaching the contract cost limitations to allow adequate time for developing the amendments and obtaining management review and approval.
 - Port Authority's management asserts that it maintains a schedule of expenditures to assist in determining when amendments should be initiated so that contractual not-to-exceed amounts are not surpassed. In this instance, Tri-Gold's delay in submitting information necessary for the completion of the amendments was a significant factor in the invoices being held for payment, and Port Authority management is working with Tri-Gold to ensure this does not occur in the future.
- 3) Contrary to the terms of the agreement but with minimal impact on project costs, HDR, Jacobs and Kwame billed wage rate increases that were not limited to 4% annually within each incremental work program and paid hourly wage rates greater than \$40.00 per hour without Port Authority authorization. Specifically,
- HDR billed wage rate increases that were not limited to 4% annually within each incremental work program for 32 employees and paid hourly rates greater than \$40.00 per hour to 22 employees without proper Port Authority authorization.
 - Jacobs billed wage rate increases that were not limited to 4% annually within each incremental work program for 20 employees and paid hourly rates greater than \$40.00 per hour to 19 employees without proper Port Authority authorization.

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- Kwame billed wage rate increases that were not limited to 4% annually within each incremental work program for 3 employees and paid hourly rates greater than \$40.00 per hour to 1 employee without proper Port Authority authorization.

- We recommend that Port Authority's contract administrator work with the director of the North Shore Connector project to pursue recoveries of \$18,201.48 from HDR, \$11,211.84 from Jacobs and 3,617.66 from Kwame.
 - Tri-Gold asserts that the wage rate increases, although not approved, were appropriate and that the limitations on wage rates should only be applied to Tri-Gold employees who are assigned to the project on a full time basis due to the complexity of administering this requirement for Tri-Gold employees who are assigned to work on the project as they are needed. Port Authority's rail operations / engineering officer and the director of the North Shore Connector project agree that the administrative requirement for non-core employees on the part of Tri-Gold would be burdensome and agree to limit the cap to full time core employees going forward. Port Authority management will review the wage rate increases in question and pursue a recovery in those instances where the increases were not warranted.
- 4) Tri-Gold billed Port Authority the full 10% of burdened labor for the fee under Incremental Work Program #1 on three separate invoices during the period February 23, 2002 through May 24, 2002 and did not wait for the contractually required Fee Determination Review to be performed.
- We recommend that Tri-Gold should only bill 6% of burdened labor as the fee on each invoice. Tri-Gold should not bill the performance-based portion of the fee until the Fee Determination Review is performed.
 - Management of Port Authority and Tri-Gold concur.
- 5) We noted several instances where subcontractors were not approved by Port Authority and they had not submitted the required disclosure forms for Certification of Debarment and Lobbying prior to beginning work under this agreement.
- We recommend that Port Authority approvals and properly executed Certification of Proposed Subcontractor Forms should be obtained and filed for all proposed subcontractors.
 - Management of Port Authority and Tri-Gold concur.
- 6) Several other minor observations were made for which we recommended a cost recovery including:
- Duplicate travel/subsistence costs totaling \$1,306.25,
 - Duplicate labor costs totaling \$1,927.13,
 - A duplicate expense report for \$1,077.24,
 - Several miscellaneous amounts totaling \$322.70 and a credit to Tri-Gold of \$90.00,
 - Some of Kwame's supporting documentation that we requested was unavailable, however we were able to use alternate sources of documentation to verify project costs.