Testimony of

The Hon. Kathy Patterson

D.C. Auditor

Before the

Council of the District of Columbia
Committee on Transportation and the Environment
and
Committee on Education

Joint Oversight Roundtable on
The Department of General Services Contracting and Procurement Practices
For Constructing and Modernizing District of Columbia Public Schools

July 8, 2015

The John A. Wilson Building
1350 Pennsylvania Avenue N.W.
Washington D.C. 20004
Good morning, Chairman Cheh and Chairman Grosso, and other members of the Council. I am Kathy Patterson and currently serve as D.C. Auditor. I greatly appreciate the opportunity to testify today on the recent reports issued by my office, entitled *The District’s School Modernization Program Has Failed to Comply with D.C. Code and Lacks Accountability, Transparency and Basic Financial Management*, and a companion report, *Audits of Public School Construction Programs: A Literature Review*. With me today are the principal authors of the audit, Julie Lebowitz and Lilai Gebreselassie, as well as Gregory Creighton who wrote the literature review.

I will provide an overview of the findings and recommendations of the audit, which covers fiscal years 2010 through 2013 and the expenditure of $1.2 billion, and outline next steps in the annual audits of the school modernization program required of my office.

Our findings fall into three broad categories: failure to adhere to provisions of the D.C. Code regarding school modernization, failure to monitor and secure cost savings, and failure to provide basic financial management which has created the risk that we have not obtained maximum value for the taxpayer dollars expended in the four-year period.

**Failure to comply with D.C. Code**

As you know and as our audit outlines, in 2006 the Council enacted the School Modernization Financing Act of 2006 setting up a financing structure that would augment capital funds over a ten-year period, adding what was then estimated to be $1.3 billion to be spent on school facilities. The D.C. Code describes two major documents designed to guide school modernization: the Master Facilities Plan and the Capital Improvement Plan, each requiring analysis and sharing of information on all aspects of modernization of schools. Our audit found that:

- The District has not met the process and schedule objectives of the Master Facilities Plan and does not have a process in place for actually selecting schools for modernization. We recommend that the Mayor and Council develop a clear and consistent selection process that is available and transparent for the public, including stakeholders such as parents and taxpayers.

- The Capital Improvement Plan submitted by the Mayor to the Council in each of the four fiscal years covered by the audit did not comply with Code provisions requiring information such as a description of the scope of work, a schedule of milestones, a fully funded cost estimate, and justification of the work as outlined in the MFP. We recommend that all statutorily-required elements be provided to the Council in each submission of the Capital Improvement Plan. The law requires that all expenditures be school-specific – but the FY16 CIP continues to include projects such as “boiler repairs” and “major repairs/maintenance” not allocated to schools.
The 2006 legislation created a Modernization Advisory Committee to provide expertise and oversight in executing the MFP and CIP, based on what the Council determined to be national best practices in school construction. The advisory committee was duly appointed, but disbanded in 2008 after failing to receive staff support which was to have been provided by the Office of the Chief Financial Officer. My report recommends that the Mayor and Council reappoint the Advisory Committee or seek an alternative means that will provide accountability, transparency and oversight.

The legislation mandated the creation of a separate fund for school modernization to include the allocation each year of $100 million in sales tax revenues – funding that occurred in fiscal years 2007, 2008 and 2009, but was not provided in fiscal years 2010 and 2011. In 2012 the Council amended the law to remove this funding source so that Mayor and Council would no longer allocate a portion of annual revenues to the priority work of rebuilding schools. A chart on page 20 of the report shows the funding source for school modernization from 2007 through 2016. We recommend that the Mayor and Council reconsider the decision to rely solely on the issuance of debt for modernizing schools, based on the large impact that borrowing has had on the annual cost of debt service.

**Lack of monitoring and securing cost savings**

We found that the Department of General Services and its predecessor, the Office of Public Education Facilities Modernization, did not secure all of the required documentation on school modernization contracts and may have spent more on construction costs than was necessary or contractually required. We looked in particular at the five high school modernizations that were completed in our audit scope (Eastern, Woodson, Cardozo, Anacostia and Wilson) and requested monthly reports and records of contingency expenditures and “buy-out” logs. Briefly, each contract specified a guaranteed maximum price (referred to as “GMP”) to the contractor and a contingency sum and savings from either are required to be split between the District and the contractor. DGS was not able to provide us with any evidence of any savings within the contingency expenditures or the contractor’s buy-out logs.

We recommend that DGS perform an assessment of each of the five high school contracts to determine if any savings should have accrued to the District. This should include an item by item reconstruction of how the GMP contingency was used, including supporting documentation to verify that the District approved each expenditure from the contingency fund. It should include a report on the “buy-outs” to assess whether there were individual subcontractor savings, and if there were, to secure the appropriate payment to the District. We were pleased to see in the DGS preliminary response to the audit – which is included in our report -- an acknowledgement that the monthly reports and use of contingency funds is, in fact an industry practice, notwithstanding the fact that we did not receive these documents that we had sought over a period of several months. The agency states that “prior to issuance of final payment to a contractor, a reconciliation of the project costs occurs between the Contractor and assigned Project Manager to determine and reconcile the actual cost of the work” including a “determination of savings.”
I would reiterate, today, the recommendation that DGS be required to reconstruct those final payment reconciliations and, further, that your committees request that those reconstructions be provided to you for review. We also recommended that the Council require that DGS submit the job cost analysis to the Council for approval before a final payment is made on each modernization project. DGS objects to such a step being required and I am sympathetic to the notion that such a step might bring the legislature into what should be an executive function. But the fact is this: today no one from the District government sees these job cost reports. The Project Manager who approves the final reconciliation works not for the District but for DC PEP, short for D.C. Partners for the Revitalization of Education Projects, LLC, the private sector project management partnership. At a minimum, our procedures should involve some responsible District party who signs off on such a critical and potentially expensive element of our school modernization program.

We also found:

- The five high school modernizations exceeded the cost per square foot standard included in the 2010 version of the Master Facilities Plan. The published standard was $210 to $255 per square foot and the five schools ranged from $259 to $348. As we note in the report, two additional high schools are currently at an even higher cost: Roosevelt High School at roughly $400 per square foot, and Duke Ellington School of the Arts, more than $1000 per square foot. The 2013 version of the MFP omitted a standard for construction costs, and we recommend that a per-square-foot standard be reestablished as one potential tool for controlling costs.

- A majority of the projects we reviewed exceeded the District’s LEED standards, potentially driving costs higher. We recommend that policymakers revisit the costs and benefits of LEED certification.

Lack of basic financial management and oversight

We found a series of deficiencies in record-keeping and basic documentation of processes and payments across the school modernization projects we reviewed. This lack of internal controls raises concerns about whether the District is obtaining maximum value for tax dollars and about the potential misuse of funds.

- As noted in the audit report, the project management firm, DC PEP, failed to secure appropriate documentation for payments made to subcontractors, and when we requested additional documentation on samples, provided altered documents that still did not add up to the final payments made and registered in the District’s financial system.

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1 The Ellington number in the report is from the 2016 CIP submitted by the Mayor. According to DGS, with the additional square footage planned, the estimate as of 7/10/2016 is $638.64 per square foot.
• Documentation was not available on a range of other payments made by DC PEP. For example, 32 of 71 payments were missing certified payroll records totaling $38 million, indicating an inability to prove compliance with federal prevailing wage law.

• We were not able to verify the approvals given on 166 out of 458 budget transfer requests totaling $169 million.

• Our efforts to verify DGS payment application and invoices found a lack of any documentation on 32 of 779 items selected in one instance, totaling $6 million, and some but not all documentation for 76 of 752 payments in another, totaling $32 million.

These next numbers are not in our audit but are calculations my team did for this hearing. Of all of the financial records we sampled and tested at DGS, we found 37% lacked some form of documentation. With regard to the financial records we tested at DC PEP – the project management firm – we found issues with 84% of the documentation. If we applied that failure rate from the sample of invoices tested to the total dollar value of all invoices, it would mean that $455 million in payments by DGS were not properly supported, and that more than $1 billion in DC PEP payments were not properly supported. [See attached chart for more details.]

We have recommended that the Mayor direct DGS to improve its internal controls environment, and we are pleased that DGS has acknowledged the importance of improving their procedures. We similarly recommend that the Executive make sure that DC PEP – or any successor project management firm hired by the District – develop and document a process for properly reviewing and approving all invoices before they are paid. We also recommend occasional random audits of the project management firm to ensure that District contractors are submitting all documentation required by their contracts.

Another element of the 2006 School Modernization Financing Act that we reference in the audit was the discretion provided first to the Board of Education then the Mayor to determine whether to operate the program internally -- as was the case in earlier years -- or to privatize the program. The Fenty Administration, then the Gray Administration, chose to contract out project management to a partnership of two large project management firms, McKissack & McKissack and Brailsford & Dunlavey, operating as DC PEP.

In extending a successor contract to DC PEP in 2014, then-Mayor Gray wrote to the Council, “DGS lacks sufficient staff to effectively manage such a large, diverse and complex portfolio, and for the last seven years, the District has relied on staff augmentation from the private sector to manage these projects.” During the four year period of our audit, the District paid DC PEP $37 million. The current contract, signed last summer, calls for payment of $9.4 million in the current year to “fund 30 full-time staff positions at fixed-monthly rates, additional support staff as needed, and limited reimbursable costs.”
We are recommending that the Mayor perform an analysis of the contract in accordance with the current law governing privatization which requires, among other elements, “the ability to demonstrate savings of at least 5% over the duration of the contract” and “a description of the expected impact of the privatization contract on the quality of goods and services.”

This completes a summary of the top-lines of our audit. One final oversight mechanism built into the 2006 modernization bill was an annual audit requirement. The four-year audit we released last week was only the second such audit that the Office of the D.C. Auditor has produced. The purpose of the audit requirement was to aid in keeping the program on track and my office will meet that responsibility, going forward.

Next steps

We will continue to look at issues in the school modernization program, and have just begun a review of the cost drivers at the Duke Ellington School for the Arts modernization. We will also be looking at the DGS policies and procedures and whether modernization projects are complying with those written procedures and whether the procedures themselves reflect best practices in school construction. I hope the Council, and the Mayor, will not simply put this report on the shelf, but will review, discuss, and act, as appropriate.

Our findings are broad and complex, but can be summarized as follows: the school modernization program has no effective cost controls, and no one is in charge. There is no clear accountability for the decisions made and the money spent. And the two – no effective cost controls and no clear accountability – go together. There are steps that can be taken; there are things that can be done. That said, the record to date suggests that neither a majority of the Council nor the last two administrations have seen the level of spending for school modernization as a problem that needed addressing.

If you are concerned today with the level of spending and the variability in spending—and I hope you are — my staff and I would like to work with you and with the Executive on alternatives that could be pursued to improve the lines of authority, the spending discipline, and the overall accountability for what was in 2006 and remains today one of the highest priorities for the District – securing facilities that support high quality public education for District children.

Thank you and I would be happy to respond to questions.
## School Modernization Testing Summary

<table>
<thead>
<tr>
<th></th>
<th># of transactions</th>
<th>Total of transactions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total invoice population</td>
<td>11,838</td>
<td>$1,229,122,889</td>
</tr>
<tr>
<td>Total DGS samples selected for testing</td>
<td>779</td>
<td>$215,331,045</td>
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<tr>
<td>Total DC PEP samples selected for testing</td>
<td>174</td>
<td>$99,798,374</td>
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### Issues Noted from DGS Sample

<table>
<thead>
<tr>
<th>Issue</th>
<th>#</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>DGS could not produce documentation</td>
<td>32</td>
<td>$5,866,309</td>
</tr>
<tr>
<td>Charged to wrong school project</td>
<td>75</td>
<td>$13,820,233</td>
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<tr>
<td>Charged to wrong project code</td>
<td>90</td>
<td>$5,914,723</td>
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<tr>
<td>Payments not supported by vendor invoices</td>
<td>76</td>
<td>$32,067,287</td>
</tr>
<tr>
<td>Incorrect purchase order number</td>
<td>4</td>
<td>$1,432,000</td>
</tr>
<tr>
<td>Signature approvals for payment were missing</td>
<td>8</td>
<td>$1,757,372</td>
</tr>
<tr>
<td>Total number of DGS payments that had errors</td>
<td>285</td>
<td>$60,857,924</td>
</tr>
</tbody>
</table>

**Percentage of documents that DGS could not support**: 37%  
37% of the total transactions: $454,775,469

### Issues Noted from DC PEP Samples

<table>
<thead>
<tr>
<th>Issue</th>
<th>#</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>DCPEP could not produce documenttion</td>
<td>7</td>
<td>$5,120,694</td>
</tr>
<tr>
<td>Payment not supported by documentation</td>
<td>59</td>
<td>$84,127,423</td>
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<tr>
<td>Did not contain supporting documentation identified by DC PEP on their invoice approval checklist</td>
<td>21</td>
<td>$8,462,110</td>
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<tr>
<td>Missing invoice checklist</td>
<td>87</td>
<td>$29,334,125</td>
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<tr>
<td>Missing certified payroll</td>
<td>32</td>
<td>$37,804,620</td>
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<tr>
<td>missing CBE forms</td>
<td>32</td>
<td>$29,903,195</td>
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<tr>
<td>missing lien releases</td>
<td>36</td>
<td>$41,153,837</td>
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<tr>
<td>Total number of DCPEP payments that has issues**</td>
<td>147</td>
<td>$235,906,004</td>
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</table>

**Percentage of documents that DC PEP could not support**: 84%  
84% of the total transactions: $1,032,463,227

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*DGES could not properly support 37 percent of documents tested. If the failure rate from the sample of invoices tested is applied to the total dollar value of all invoices, it would mean $454,775,469 in payments were not properly supported.

**Total number of unique DC PEP invoices that had issues. Many invoices had multiple documentation issues.

***DCPEP could not properly support 84 percent of documents tested. If the failure rate from the sample of invoices tested is applied to the total dollar value of all invoices, it would mean $1,032,463,227 in payments were not properly supported.