

FOLLOW-UP REPORT

National Western Center

Hensel Phelps Construction Contract

SEPTEMBER 2021



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DENVER AUDITOR

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Cover photo courtesy of the National Western Center.

City and County of Denver



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AUDITOR'S LETTER

September 2, 2021

In keeping with generally accepted government auditing standards and Auditor's Office policy, as authorized by city ordinance, the Audit Services Division has a responsibility to monitor and follow up on audit recommendations to ensure city agencies address audit findings through appropriate corrective action and to aid us in planning future audits.

In our follow-up effort for the "Hensel Phelps Construction Contract" assessment report completed by BKD LLP and issued in September 2020, we determined the National Western Center fully implemented two recommendations from the original report and partially implemented another. Although the National Western Center made progress, auditors determined one risk associated with the audit team's initial findings was not fully mitigated. As a result, the Audit Services Division may revisit this risk area in future audits to ensure the city takes appropriate corrective action.

The Highlights page in this report provides background and summary information about the original assessment and the completed follow-up effort. Following the Highlights page is a detailed implementation status update for each recommendation.

I would like to express our sincere appreciation to the personnel at the National Western Center who assisted us throughout the audit and the follow-up process. For any questions, please feel free to contact me at 720-913-5000.

Denver Auditor's Office

A handwritten signature in black ink, appearing to read "Timothy M. O'Brien".

Timothy M. O'Brien, CPA
Auditor



Hensel Phelps Construction Contract

SEPTEMBER 2021

Objective

To evaluate how well the National Western Center reviewed Hensel Phelps' compliance with contract terms, including payment applications, change orders, the use of subcontractors, and project reporting requirements.

Background

BKD LLP conducted this assessment on behalf of the Auditor's Office.

In June 2018, the National Western Center awarded Hensel Phelps a \$275 million contract to perform construction updates to the National Western Complex. The updates include a riverfront open space and improvements to the complex's infrastructure. National Western Center staff monitor the progress of construction by performing site visits and reviewing payment documentation to support the work completed.

ORIGINAL REPORT HIGHLIGHTS

Observation 1

Although the contractor reviewed the subcontractor's payment support, the National Western Center did not perform additional review before approving payments to the subcontractor.

Observation 2

City rules require contractors to pay subcontractors within seven days to avoid interest payments. BKD found one instance in which the contractor paid the subcontractor six days late.

Observation 3

The city's contract with Hensel Phelps does not reference the contractor or other vendors in its conflict-of-interest clause.

WHY THIS MATTERS

A closer review of subcontractor payments helps ensure the city appropriately spends taxpayer money. Additionally, by including the contractor and other vendors in a contract's conflict-of-interest clause, the city ensures contractors select vendors fairly and competitively.



2

FULLY IMPLEMENTED



1

PARTIALLY IMPLEMENTED



0

NOT IMPLEMENTED

Sept. 2, 2021

Action Since Audit Report

Hensel Phelps Construction Contract

3 recommendations proposed in September 2020



FULLY
IMPLEMENTED

2



PARTIALLY
IMPLEMENTED

1



NOT
IMPLEMENTED

0

The National Western Center fully implemented two recommendations from the original report and partially implemented a third.

National Western Center staff updated and implemented procedures to review and track payments to subcontractors and to ensure the contractor pays its subcontractors on time. Staff also met with an employee from the City Attorney's Office to update the conflict-of-interest clause in future contracts. However, the National Western Center has not executed any new construction contracts yet so we could not test whether the conflict-of-interest clause was incorporated, presenting a lingering risk to the city.

Recommendation 1

BKD recommends that NWC implements a review process that would incorporate subcontractor support from a financial perspective. This could include, obtaining a sample of invoices supporting charges made within the contractor’s monthly payment applications that would allow for a more thorough review of subcontractor payment applications and decrease the risk of unallowed costs being paid for by the city.



**FULLY
IMPLEMENTED**

AGENCY ACTION

Original target date for completion: Dec. 17, 2020

In December 2020, the National Western Center updated its invoice review procedures. The procedures now include new steps to ensure subcontractor costs are supported only when an invoice contains costs not already in the contract. Depending on the type of contract, prices are set during the procurement process. Therefore, these types of costs identified by the National Western Center arise when unforeseen circumstances occur, such as damages to materials. Therefore, the contract would not specify the pricing for the additional labor and materials needed.

The National Western Center held a training with its employees to review the new invoice review steps. Staff provided a copy of the training and a list of signatures for employees who attended.

We requested all invoices from January 2021 through May 2021 that contained costs that would prompt the National Western Center’s new review steps. However, staff said subcontractors had not submitted any costs during this time that would require the extra layer of review. After several attempts by us to verify no costs were submitted, staff ultimately provided documentation late in the follow-up process — which confirmed subcontractors had not submitted any costs requiring the extra layer of review.

Because the National Western Center added new steps to its procedures to ensure staff review subcontractors’ support for costs not included in a contract, we consider this recommendation fully implemented.

Recommendation 2



**FULLY
IMPLEMENTED**

To comply with the prompt pay ordinance at the city, NWC and the contractor should calculate and pay interest for the late payment that was identified during this assessment. Additionally, NWC should implement a process to assess that all payments to subcontractors were paid in accordance with the prompt payment ordinance. NWC should document any instances of late payments and the resolutions.

AGENCY ACTION

Original target date for completion: Dec. 17, 2020

This recommendation required the National Western Center to perform three steps for full implementation:

1. The National Western Center needed to calculate and pay interest for the late payment identified in BKD's original assessment.
2. Staff needed to implement a process to ensure all subcontractor payments complied with the city's prompt payment ordinance.
3. Staff should have documented any instances of late subcontractor payments and their resolutions.

Regarding the first step, we found National Western Center staff incorrectly calculated the interest payment to the subcontractor. National Western Center staff based their interest calculation on the total invoice amount rather than the amount owed to the subcontractor – which led to a higher interest calculation.

Despite the incorrect calculation, the subcontractor said in an email to the National Western Center's project manager that it cost more to adjust its accounting entries than accept the interest and therefore, the subcontractor declined the higher interest payment of \$2,181.

For the second step, we found the National Western Center updated its contractor payment procedures by including steps to track the payment dates between contractor Hensel Phelps and the subcontractors. The procedures also include steps to ensure staff apply a prompt payment if the contractor does not pay its subcontractors within seven days, as required by city ordinance. In addition, the National Western Center conducted a training with its staff responsible for processing contractor payments. We reviewed both the training documents and the sign-in sheet, which was dated and signed by each attendee.

Regarding the last step of the recommendation, the National Western Center provided its payment tracker, which contains all the contractor and subcontractor payment dates from January 2021 through June 2021. We reviewed the tracker and found the payment date indicated the contractor paid three invoices one day beyond the seven-day deadline.

Staff explained the contractor payment dates to subcontractors could

be impacted by a lag in the payment processing time. We requested documentation to support this claim during the follow-up process. However, staff did not provide documentation until during the draft report stage.

Because the National Western Center does not have access to Hensel Phelps' banking records, staff investigated the three potential late payments with Hensel Phelps and determined the payments were made within the seven days, as required. National Western Center staff said, in the future, they will use their internal payment tracker as a guide to identify any potential delays in payments to subcontractors and then discuss them with Hensel Phelps.

By following up with the subcontractor regarding the late payment identified in the original assessment — including adding procedures to track the payment dates between Hensel Phelps and the subcontractors — and by resolving the late payments included on its tracker, the National Western Center has taken action to ensure subcontractors are paid in a timely manner. As a result, we consider this recommendation fully implemented.

Recommendation 3

The NWC and the City Attorney's Office should enhance the existing clause to include the contractor and other vendors. Over the course of construction projects, conflicts of interest may arise for all parties involved. The contractor may work closely or have a partial ownership agreement with a subcontractor that bids on a scope of work. The architect may have a relative that works for a general contractor that is bidding on the work. These related party and similar types of relationships should be disclosed when they arise. It is important to note that just because a conflict of interest may arise that should not automatically exclude an individual or firm from participating. Appropriate competition and quality of work may be impaired if a firm or individual are excluded, however it is important to be disclosed. It is important for the clause to be in line with any potential conflict of interest or related party policy or law.



**PARTIALLY
IMPLEMENTED**

AGENCY ACTION

Original target date for completion: Nov. 17, 2020

National Western Center managers said they met with an employee with the City Attorney's Office to discuss BKD's original recommendation. Management explained city staff agreed with the recommendation to enhance the conflict-of-interest clause in future construction contracts by including the contractor and other vendors.

At the time of our follow-up, we confirmed the National Western Center had not executed any new construction contracts. Therefore, we could not test

whether city staff had updated the conflict-of-interest clause to include the contractor and other vendors.

Although staff met with the City Attorney's Office to update the conflict-of-interest clause in future contracts, until new construction contracts are executed with the updated language, a lingering risk to the city remains. Therefore, we consider this recommendation only partially implemented.

Office of the Auditor

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