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San Mateo Union High School District Construction Contracting Procedures

Contract Award Procedures Require Immediate Improvement

Issue

What immediate steps should be taken to address concerns about the San Mateo Union High School District Measure M construction contracting procedures?

Background

The 2006-2007 San Mateo County Civil Grand Jury (Grand Jury) was motivated to investigate the San Mateo Union High School District (SMUHSD or District) by media reports of the District's financial difficulties. The Grand Jury has chronicled these difficulties in a report entitled "Problems in Fiscal Management at San Mateo Union High School District."¹ The focus of the Grand Jury investigation then shifted to the questionable selection and contract award process for the construction management contract for the Measure M bond projects. This second report is a result of the Grand Jury's investigation of this process.

History of School Bonds

In 2000 (and amended in 2002), District voters approved a \$137.5 million bond issue (Measure D) for renovation, demolition and construction on SMUHSD campuses. In November 2006, District voters approved a \$298 million bond issue (Measure M) to renovate and rehabilitate seven SMUHSD campuses and fund the completion of additional needed projects. The District has employed (for Measure D) and proposes to employ (for Measure M) a construction management firm to manage and coordinate the various parties involved in these significant bond-funded projects.

History of Construction Management Contracting

Kitchell/CEM, Inc. (Kitchell) was the construction management company for the District's Measure D projects. For various reasons, the Measure D projects experienced significant cost-overruns. One of the Measure D project directors employed by Kitchell worked on District projects beginning in 2001 and left the employ of Kitchell in January 2006 to work for Skanska USA Building, Inc. (Skanska), a subsidiary of Skanska AB, a large Swedish construction firm. In February 2006, the former Kitchell employee now working for Skanska became an unpaid advisor to the SMUHSD to assist the District in pre-bond planning for Measure M.

In July 2006 Skanska submitted a proposal to the District for further pre-bond planning services. The proposal included developing a plan for the implementation of a six-year modernization program for "six comprehensive high schools, the Crestmoor site, and the San Mateo Performing Arts Center."² The proposal also included assisting the District in hiring "architectural and engineering firms to begin the design phase of the new modernization program."³

Because it was not required, no competitive selection process was used and on July 13, 2006, the Board of Trustees awarded Skanska a \$97,765 contract for the pre-bond work. The Grand Jury was told that this contract was awarded to Skanska, in part, because of the previous free assistance provided by Skanska to the SMUHSD.

2006-2007 Construction Management Contract Award Process

On November 13, 2006, a Request for Qualification was sent out by the District to select a construction management company for the District's Measure M projects. This process is used to identify qualified firms. Twenty construction management companies indicated interest, and four were interviewed in December by a five-member committee consisting of District administrators, consultants and Trustees, none of whom had the appropriate financial, contractual or construction expertise. During this process, there is no evidence that the District requested fee information from the four candidate firms. The committee recommended that Skanska be awarded the contract as the sole construction management company for all District Measure M projects despite the fact there was disagreement among District staff over awarding such a large construction management contract to a single company. Skanska has not managed or otherwise participated in any other school construction projects in California.

Unsubstantiated Contract Increases

Documents prepared in the course of pre-bond planning estimated construction management fees for Measure M projects to be approximately \$11 million. The SMUHSD Revised Facilities Master Plan⁴ of February 9, 2006, which Skanska reviewed, includes construction management fees of \$11,346,548. The Skanska Bond Projects List of July 13, 2006⁵, similarly projected construction management fees of \$10,940,990. The contract selection and award process described above resulted in Skanska being awarded the sole construction management contract with the District. Prior to Skanska's submission of its draft contract to the District, the Superintendent allegedly requested

Skanska to: (1) increase its scope of work to include architect design management; (2) reassign the cost escalation expenses (a line item in the pre-bond planning estimate); and (3) reflect these changes in the management construction contract. Skanska submitted its broadened contract to the Superintendent six days prior the Board meeting at which it was scheduled for approval. Skanska's proposed contract included construction and design management fees totaling \$23,966,660.

While some explanation was given during the Grand Jury investigation, witnesses were unable to justify the entire increase from \$10,940,990 to \$23,966,660. Witnesses explained that very little or no negotiation occurred over Skanska's fees or contract terms. Similarly, witnesses were unable to provide any evidence that the numerous architect contracts or fee agreements were ever negotiated or reviewed by District's legal counsel.

Lack of Opportunity for Contract Review

The agenda for the March 8, 2007 Board of Trustees meeting included the Superintendent's recommendations to select both the architects and the construction management firm. Prior to the meeting, Skanska distributed a document addressing the *Agreement for Architectural Services* that stated, "The attached Agreement has been thoroughly reviewed, and amended, as agreed upon between the architects and the District's legal counsel." The District's legal counsel's review of the architects' agreement was limited to matters of form: there were no substantive contractual terms or fees reviewed. Prudent business practice requires the Board of Trustees to seek assurances from its own advisor(s) about the thoroughness of the review of the proposed agreement; reliance on statements such as the one by Skanska mentioned above, was misplaced. Furthermore, in regard to Skanska's contract, the District's legal counsel apparently played no role in the drafting or negotiation.

The Board of Trustees voted to accept the architects' agreement, but the recommendation to approve the Skanska contract was withdrawn because it had been received too late for the Trustees to consider.

Subsequent to the March 8, 2007 Board meeting, the District's counsel informed some Trustees that he had not reviewed the reasonableness of either the proposed architects or construction management fees. This information was communicated to the Grand Jury by several sources. Furthermore, the Grand Jury learned that the District's counsel believes that some of the architectural fees set forth in the approved agreements could be as much as 100% above customary fees. Additionally, it is the District's counsel's opinion that the architectural design fees set forth in Skanska's proposed contract could be as much as \$8 million above customary fees.

On April 5, 2007, a District trustee called for a temporary halt to the Measure M project work. As reported in the *Daily Journal*, "The Oakland-based business slated to oversee the six-year construction plan, Skanska, submitted its contract at a cost more than \$10 million over the estimate without explanation or notice to trustees before last month's

scheduled vote. The item was pulled from the March 8 agenda and has not been revisited publicly. This was just one of many concerns Hanley expressed before suggesting a few remedies at the special board meeting Tuesday. To get the Measure M work back on track, Hanley proposed starting clean by cutting ties with Skanska, suspending all work pending review of management and creating new board protocols for contracts.”⁶

During the April 19, 2007 regularly-scheduled board meeting, Skanska was invited to explain its approach to Measure M projects as well as its fees for such services. As a result of Skanska’s presentation and comments by the public and District trustees, the Board reportedly decided to “begin a new search for construction experts to oversee Measure M projects, after the original company slated to do the work raised its fees by \$4.5 million without informing the school board.”⁷

“Questions of inflated costs, miscommunication, lack of state requirements and experience, and an authorless contract plagued the board’s discussion before it decided to go forward on the projects scheduled for this summer but start from scratch on all other projects. The board discontinued its relationship with Skanska — which it previously agreed to work with for the duration of the project. A subcommittee of trustees Linda Lees Dwyer and Peter Hanley was formed to find an interim construction manager to oversee this summer’s work and inform the architects to stop work on other projects. In the near future the district will begin to reevaluate the architect fee structure, create new protocols for reviewing contracts, create the description of a district construction manager and start the search for new project management. Skanska is free to resubmit.”⁸

The District’s problems are serious and ingrained. As stated in the *San Mateo Daily News*, the District’s legal counsel, “called Skanska’s \$24 million construction bid ‘shocking.’ But more than the firm, the district’s own ‘power vacuum’ was to blame for the pricey bid, Haesloop said. ‘What Skanska has done ... is make an omnibus proposal to fill that power vacuum,’ he added. ‘The real question is, who’s managing the managers?’”⁹

Findings

- A senior Skanska employee was provided at no charge to the District for pre-bond work. This employee was a former employee of Kitchell, the construction management company that oversaw Measure D.
- Skanska was selected as a paid pre-bond consultant. There was no competitive process in awarding this contract for \$97,000.
- Skanska, as the pre-bond construction management company for the initial project planning, assisted in the selection of architects, some of whom are charging fees allegedly exceeding current market value.
- Some or all Trustees relied upon a document stating that architect agreements and fees were thoroughly reviewed by counsel.

- The Board of Trustees did not use its legal counsel to perform a full review of the proposed architect agreements in a timely manner.
- The Board of Trustees approved the architects' agreement subject to approval of contract language by the District's legal counsel, with fees that allegedly exceed customary industry rates. There appeared to have been little or no negotiation of the fees or terms of the agreement.
- Skanska was selected as the sole construction management company even though there had been significant disagreement among District staff about awarding the oversight of the \$298 million Measure M construction projects to a single company.
- Skanska's proposed contract for \$23,966,660 was placed on the Board of Trustees' agenda for approval despite the fact that: (1) there was no competitive process used for the \$5 million design management portion of the proposed contract - only the construction management portion was competitive¹⁰; (2) there was little or no negotiation of the terms and fees set forth in the proposed contract; (3) witnesses were unable to justify the entire increase in Skanska's proposed management fees from \$10,940,990 to \$23,966,660.
- Witnesses informed the Grand Jury that Skanska management fees set forth in its proposed contract submitted to the Board of Trustees for approval on March 8, 2007, exceed current industry norms.
- On April 19, 2007, the Board of Trustees discontinued its relationship with Skanska.
- California Education Code Section 15278 requires a citizen's oversight committee be established to review bond expenditures.

Conclusions

The Grand Jury asserts that the process by which the proposed construction management contract was developed was flawed and that the District must improve the process for selecting and retaining construction managers.

The SMUHSD Measure M construction management selection committee lacked sufficient financial, contractual and construction experience (or failed to engage persons with such experience) to assist them in their selection process for the award of the Measure M construction management projects.

The considerable influence exerted by Skanska's project executive throughout both the contracting process and the alleged negotiations raises questions about whether the

District should have allowed a party who had a significant financial stake in this project to have so much responsibility.

The Skanska proposed contract for \$23,966,660 was the result of a deficient contracting process. There appears to have been little or no negotiation or review of the management fees.

A majority of District Trustees neglected their oversight responsibilities in accounting, financial and contractual matters regarding the District's Measures D and M construction projects.

The Superintendent failed to provide adequate management oversight to ill-equipped District staff in accounting, financial and contractual matters, especially those surrounding Measures D and M construction projects.

Recommendations

The Grand Jury recommends that the San Mateo Union High School District Board of Trustees direct the Superintendent, by formal resolution, to:

1. Improve the process for selecting construction management firms. The Request for Qualifications and Request for Proposal processes must be impartial, transparent and competitive.
2. Use the improved selection process to award the Measure M construction management contract and strongly consider awarding the contract to a pool of companies rather than a single company.
3. Assemble a proposal review team that includes individuals with financial, construction and contractual expertise to select the construction management contractor(s).
4. Actively negotiate the construction management contract(s) with the chosen candidate(s).
5. Provide the statutorily-required citizen's oversight committee with independent advisors with financial, construction and legal expertise to, among other things, monitor the progress of construction, the expenditure of funds and adherence to contractual requirements through the completion of the Measure M construction projects.
6. Immediately engage the services of a qualified outside consultant, whose primary allegiance is to the District, to review and advise the Board and staff on management control procedures, especially those surrounding the accounting and budgeting for Measure M construction projects.

¹ <http://www.sanmateocourt.org/grandjury>

² San Mateo Union High School District - Proposal for Pre-Bond Management Services, July 13, 2006, by Skanska

³ Ibid

⁴ Revised Facilities Master Plan – 2007-2012, February 9, 2006, by the San Mateo Union High School District

⁵ Bond Projects List 2007-2013 Master Budget for the San Mateo Union High School District, July 13, 2006, by Skanska

⁶ Spending at schools under fire,” The Daily Journal, April 5, 2007 page 1.

⁷ Board dumps project managers,” San Mateo County Times, April 20, 2007 page Local 1.

⁸ “Pink slip for company in school mess” San Mateo Daily Journal, April 20, 2007 page 1.

⁹ “School board kills Skanska deal,” San Mateo Daily News, April 20, 2007

<http://www.sanmateodailynews.com/article/2007-4-20-04-20-07-smuhsd-skanska>

¹⁰ The Grand Jury was informed that the \$10.9 million fee for construction management was increased by \$5 million to cover the separate services of design management.

San Mateo Union High School District

David Miller, Ph.D., Interim Superintendent

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July 23, 2007

The Honorable John L. Grandsaert
Judge of the Superior Court
Hall of Justice
400 County Center; 2nd Floor
Redwood City, CA 94063-1655

RE: SAN MATEO UNION HIGH SCHOOL DISTRICT CONSTRUCTION CONTRACTING
PROCEDURES Report

Dear Judge Grandsaert:

On May 3, 2007, the Grand Jury of San Mateo County published its "San Mateo Union High School District Construction Contracting Procedures" report. We take the Grand Jury's findings and recommendations very seriously. We fully intend to take all action necessary to restore confidence in our ability to manage our construction program. In support of our commitment to address these construction issues, we have contracted with Mark Haesloop, an experienced San Mateo county construction attorney, and added the District Associate Superintendent of Business Services, who has significant construction experience, to the Measure M team. The District is addressing the issues identified in the Measure M program and investing the required time and resources to ensure a detailed plan is in place prior to beginning any construction work.

Please find our specific responses in the paragraphs below.

DISTRICT'S RESPONSE TO GRAND JURY'S FINDINGS

The Grand Jury's Findings appear on page 4 of its report.

Findings in First Paragraph: A senior Skanska employee was provided at no charge to the District for pre-bond work. This employee was a former employee of Kitchell, the construction management company that oversaw Measure D.

Response to Findings in First Paragraph: This finding is not accurate and is actually discussed on page 2 of the Grand Jury report. The facts, as stated in the report, are that the employee was paid through the contract that the District had with Skanska. It is correct that the employee was a former employee of Kitchell, the construction management company that oversaw Measure D. John Maloblocki resigned from Kitchell at the end of January 2006. Sometime between his resignation with Kitchell and July 2006 he went to work for Skanska. He maintained a relationship with the District during the interim. The Skanska contract was approved by the Board in July for work to be performed from July to November 2006.

Findings in Second Paragraph: Skanska was selected as a paid pre-bond consultant. There was no competitive process in awarding this contract for \$97,000.

Response to Findings in Second Paragraph: This finding is correct. For the record, the actual contract amount was \$97,765. No competitive bidding process is required under any regulation or legislation for these services.

Findings in Third Paragraph: Skanska, as the pre-bond construction management company for the initial project planning, assisted in the selection of architects, some of whom are charging fees allegedly exceeding current market value.

Response to Findings in Third Paragraph: Skanska did assist in the selection of the architects. Although the fees proposed by the architects would have exceeded current market value, the fee agreements were not finalized and the District is in the process of negotiating agreements that will be well within accepted industry norms. The District is re-negotiating all of the architect's contracts and aligning fees with those recommended by the Office of Public School Construction. Furthermore the selected construction management firms will be required to fix their fees in accordance with OPSC guidelines and will not be allowed reimbursable and open-ended expenses.

Findings in Fourth Paragraph: Some or all Trustees relied upon a document stating that architect agreements and fees were thoroughly reviewed by counsel.

Response to Findings in Fourth Paragraph: This finding is correct. The Trustees were told that the architect agreements and fees had been thoroughly reviewed by counsel. Based on the problems the Skanska contract presented, the Board of Trustees has reiterated that it expects long-existing protocol to be followed in the future and directed staff to have all contracts thoroughly reviewed by legal counsel.

Findings in Fifth Paragraph: The Board of Trustees did not use its legal counsel to perform a full review of the proposed architect agreements in a timely manner.

Response to Findings in Fifth Paragraph: The Board of Trustees was told that the proposed architect agreements had been fully reviewed by legal counsel prior to the agreements being brought to the Trustees for approval. The Trustees had no information at that time to contradict what they had been told. Adequate time for counsel to conduct a thorough review had been available.

Findings in Sixth Paragraph: The Board of Trustees approved the architects' agreements subject to approval of contract language by the District's legal counsel, with fees that allegedly exceed customary industry rates. There appeared to have been little or no negotiation of the fees or terms of the agreement.

Response to Findings in Sixth Paragraph: This finding is correct as to the approval. There was no information in the documents provided to the Board of Trustees to show whether or not fee negotiations had taken place. As noted above, the Board was informed that counsel had thoroughly reviewed the contracts, which customarily included the proposed fees.

Findings in Seventh Paragraph: Skanska was selected as the sole construction management company even though there had been significant disagreement among District staff about awarding the oversight of the \$298 million Measure M construction projects to a single company.

Response to Findings in Seventh Paragraph: The Board of Trustees was not provided with any information to agree with or refute this finding. The Board of Trustees was not, at any time prior to or since the Grand Jury's report, provided with any information or evidence of "a significant disagreement among District staff."

Findings in Eighth Paragraph: Skanska's proposed contract for \$23,966,600 was placed on the Board of Trustees' agenda for approval despite the fact that: (1) there was no competitive process used for the \$5 million design management portion of the proposed contract – only the construction management portion was competitive; (2) there was little or no negotiation of the terms and fees set forth in the proposed contract; (3) witnesses were unable to justify the entire increase in Skanska's proposed management fees from \$10,940,990 to \$23,966,600.

Response to Findings in Eighth Paragraph: This finding is correct. The Board of Trustees did not have any information concerning (1), (2), or (3) at the time that the proposed contract was placed on the agenda for approval. The contract was recommended to the Board by the District's Superintendent. It was not reviewed by the District Associate Superintendent of Business Services nor by District legal counsel, both of whom have been part of long standing protocols for review of all contracts placed on the board agenda for action. An analysis of the contract was not provided to the Board to provide a foundation for evaluation.

Findings in Ninth Paragraph: Witnesses informed the Grand Jury that Skanska management fees set forth in its proposed contract submitted to the Board of Trustees for approval on March 8, 2007, exceed current industry norms.

Response to Findings in Ninth Paragraph: Then Superintendent Johnson did not provide a contract analysis or a comparison to industry standards. The Board subsequently investigated and determined that the contract exceeded the Office of Public School Construction fee structure.

Findings in Tenth Paragraph: On April 19, 2007, the Board of Trustees discontinued its relationship with Skanska.

Response to Findings in Tenth Paragraph: This finding is correct.

Findings in Eleventh Paragraph: California Education Code Section 15278 requires a Citizen's Oversight Committee be established to review bond expenditures.

Response to Findings in Eleventh Paragraph: This finding is correct. The District formed a Citizen Oversight Committee in a timely manner on January 18, 2007 to monitor the Measure M bond expenditures.

DISTRICT'S RESPONSE TO GRAND JURY'S RECOMMENDATIONS

Grand Jury Recommendation

1. Improve the process for selecting construction management firms. The Request for Qualifications and Request for Proposal processes must be impartial, transparent and competitive.

District Response

Although the District has not finalized the procedures for selecting construction management firms, it is likely that, at the very least, the District will conduct a standard RFP process like that performed for the Burlingame High School soil remediation project. This process includes the solicitation of as many firms as possible. From there, the District will narrow down the firms to interview by review of their fixed fee cost, experience, track record, and compatibility for district needs.

Grand Jury Recommendation

2. Use the improved selection process to award the Measure M construction management contract and strongly consider awarding the contract of a pool of companies rather than a single company.

District Response

The District will use the improved selection process to award all contracts necessary to implement Measure M construction. Consideration will be given to the use of multiple companies to manage the construction projects.

Grand Jury Recommendation

3. Assemble a proposal review team that includes individuals with financial, construction and contractual expertise to select the construction management contractor(s).

District Response

The District believes that it has a core team in place now that includes the Associate Superintendent of Business Services, Construction Counsel and the Bond Accounting Manager. We will add individuals who have the critical expertise needed to this team for the purpose of selecting the necessary construction management entities. It is likely that a District Construction Manager will be added to this team.

Grand Jury Recommendation

4. Actively negotiate the construction management contract(s) with the chosen candidate(s).

District Response

The Associate Superintendent of Business Services will rely on the assistance of the Bond Accounting Manager, the District's Construction Counsel and a District Construction Manager to complete this task.

Grand Jury Recommendation

5. Provide the statutorily-required citizen's oversight committee with independent advisors with financial, construction and legal expertise to, among other things, monitor the progress of construction, the expenditure of funds and adherence to contractual requirements through the completion of the Measure M construction projects.

District Response

The Citizen Oversight Committee was officially formed on January 18, 2007, and has an established charter and meeting schedule. Additional members are being added to the COC. These members will be selected for their financial, construction and legal expertise within the requirements for membership as set forth in Education Code Section 15282(a).

Grand Jury Recommendation

6. Immediately engage the services of a qualified outside consultant, whose primary allegiance is to the District, to review and advise the Board and staff on management control procedures, especially those surrounding the accounting and budgeting for Measure M construction projects.

District Response

The District's new Associate Superintendent of Business Services has a successful track record in construction. She was not included in the initial Measure M implementation process. The District, as previously noted, has also engaged the services of a construction attorney who will report to the Board of Trustees and work under the day-to-day guidance of the Associate Superintendent Business Services. The construction attorney has significant litigation and construction contract experience. The addition of a Construction Manager as a District employee should round out this new internal team.

In closing, the District, on behalf of its communities and students, would like to thank the members of the Grand Jury for the work that they do to safeguard the welfare of the citizens of San Mateo County. The District is committed to implementing a viable organizational structure using best practices to ensure Measure M construction is successful, accountable, and transparent. The District intends to provide frequent communications to ensure the community is aware of Measure M's progress as its implementation proceeds.

Sincerely,

Robert H. Griffin, President
Board of Trustees