

# COMPTROLLER ALERT

INVESTIGATIONS DIVISION · MARCH 2014

## **IS YOUR SCHOOL DISTRICT OVERPAYING FOR ARCHITECTURAL SERVICES?**

Nearly half a billion dollars in state grants are currently being directed toward construction projects in school districts across the state.

Given the large amount of public funding at stake, it is more important than ever for school districts to reduce the potential for waste and abuse when procuring architectural and design services for such projects.

An Office of the State Comptroller (“OSC”) review has found instances of school districts having spent more tax dollars than necessary on architectural and design services for construction projects because of poor contract negotiation and limited oversight from public officials.

OSC issues this alert to provide guidance to public officials so they can carry out their responsibility to oversee the procurement of construction projects in a manner that best protects the interests of taxpayers.

### **Retaining Architectural Services**

Except for a small subset of school districts whose school construction projects are overseen by the New Jersey Schools Development Authority, districts generally have wide discretion when entering into contracts with architectural and design firms. Such architectural and design services are exempt from public bidding requirements under state law. This discretion opens the door for school districts to enter into contracts that may be inflated with unnecessary costs.

### **OSC’s Review**

OSC’s review focused on the procurement of architectural and design services by a school

district in Ocean County (referred to herein as “the District”) primarily for the installation of solar panels on six schools. We found a number of issues that contributed to the District’s overpayment for these services.

The District’s contract with the architectural firm allowed the firm to set its compensation as a percentage of the estimated construction budget. Such an arrangement gave the firm a perverse incentive to inflate the estimated project costs. As it turned out, the firm estimated the project construction costs at \$16 million, but the actual costs were only \$9.9 million.

The firm overestimated the project costs by more than 38 percent, and as a result the

District paid the firm \$455,000 more than it would have had the firm estimated the project costs accurately. Although basing compensation on estimated construction costs is a standard practice, this arrangement can easily result in such overpayments in the absence of proper oversight.

The firm's inexperience with solar projects may have also contributed to its gross overestimation of project costs. Its only other solar projects were being constructed simultaneously with the District's solar project and paled in size compared to that project. Although the District was not required to publicly bid the contract for architectural and design services, it failed to engage in any competitive process designed to find the most qualified or experienced firm. Instead, the District simply negotiated a contract with an architectural firm with which it was familiar. It also failed to have its attorney review the contract.

The firm's significant overestimate of project costs also resulted in the District overbonding for the project by \$8,240,000. This in turn caused the unnecessary expenditure of an additional \$4,717,576 in state tax dollars, as the Department of Education ("DOE") subsidized the project by funding a percentage of the firm's projected budget. The District used the unexpended funds to pay down unrelated debt, but taxpayers will ultimately bear the responsibility for the additional costs and interest associated with the overbonding, including \$3.5 million in additional interest. While DOE had approved the project for state aid, it confirmed to OSC that its review did not include any detailed analysis of construction cost estimates or the reasonableness of the project costs.

Some of the factors that led to the overestimate could have easily been uncovered if the District or its representatives had provided more effective oversight. For example, the District did not have an accurate understanding of the costs included in the firm's estimate of project costs and may have duplicated some of those costs when calculating the total project expenses. In addition, the firm considerably overstated the number of watts required for the project, resulting in approximately one million dollars of additional projected costs.

OSC acknowledges that the market costs of constructing solar installations decreased after the architectural firm estimated the project. We found, however, that nearly 70 percent of the overestimation of project costs was likely attributable to the lack of District oversight described above, and not to the market decrease of construction costs.

### **Recommendations**

OSC specifically recommends the following:

- In hiring an architectural firm, school districts should make sure that the firm has experience in projects of similar scope and size. Although not required to publicly bid contracts for architectural services, school districts should nonetheless look at more than one firm and use a competitive vendor-selection process whenever practicable.
- School districts should carefully structure architectural service contracts and related documents to prevent overbonding and waste of taxpayer money, and to prevent architectural

firms from receiving windfall compensation. School districts should have their attorneys, their architect of record and/or other representative review the contracts and other documents.

OSC will continue to audit and review these projects to provide assistance in this regard.