



**U.S. Department of
Transportation**

Office of the Secretary
of Transportation

The Inspector General

Office of Inspector General
Washington, D.C. 20590

May 21, 2003

The Honorable Don Young
Chairman
Committee on Transportation and Infrastructure
House of Representatives
Washington, DC 20515

Dear Chairman Young:

This is in response to your recent letter expressing the Committee's continued interest in the Central Artery/Tunnel Project (Project) in Boston. Congressman Michael E. Capuano of the Massachusetts' 8th District requested that this office review efforts to recover costs caused by design errors. You asked that we keep you informed about our review concerning these costs.

Recently, significant attention has been focused on opportunities to recover costs paid for change orders that might have been caused by design errors or omissions on the part of design and consulting contractors. In order to prevent delays and cost increases due to delays, the project approves change orders and pays the construction contractor for the work before determining whether the change was required due to a design error. The project has an opportunity to recover some of these costs from the design contractor if a subsequent review determines that the change order was required to correct a design error or omission.

To date, we have found that both the Federal Highway Administration (FHWA) and the Project have begun taking steps to strengthen their efforts to ensure that the cost recovery program successfully recovers costs paid for changes that were due to design errors. This is needed because past cost recovery efforts have been anemic and have not resulted in substantial recoveries—eight years of cost recovery efforts have yielded only \$30,000 in recoveries from a single consultant. Efforts have also not been timely—76 items have been under review from 2 to 7 years.

The Project recently revised its evaluation process by creating a Task Force, headed by a retired Probate Court Judge, to review all questionable change orders, including those identified in a recent series of Newspaper articles. FHWA's efforts are aimed at ensuring that the project properly resolves the backlog of existing cost recovery items, as well as new cost recovery items, in a timely manner. Specifically, the FHWA Division Office will (1) concur in the project's resolution of each cost recovery item, and (2) receive quarterly status reports from the project about the backlog of cost recovery items. FHWA has also established a task force to review the Cost Recovery Process.

In the last couple of months, the Governors Office, the State Auditor, and the Massachusetts Inspector General (State IG) have also indicated that they want to play a role in the process. Currently, however, the Governor has a limited role in determining how the cost recovery process will be organized and staffed because the process is established by an independent State Agency--the Massachusetts Turnpike Authority (Authority)--and approved by FHWA. The Governor has a limited institutional role because, although the Authority's Board of Directors is appointed by the Governor, once appointed, the Board operates independently.

The credibility of the current process is also open to question because many of the pending and closed questionable change orders involve Bechtel/Parsons-Brinkerhoff, the Project's design engineer and construction manager. Because the Project and Bechtel/Parsons-Brinkerhoff have operated as partners to design and build the Central Artery/Tunnel, a legitimate issue exists regarding whether the Project will be able to maintain organizational independence and objectivity when reviewing questionable change orders. Adequate controls to ensure an independent and credible Cost Recovery Program are important not only to ensure that costs are recovered when appropriate, but also to provide assurance to taxpayers that the process is credible. To provide this assurance, we believe it is essential that the various parties, including the Governor's office, work together to agree on:

- A proper governance framework to provide independent, credible executive direction;
- An appropriate review methodology to provide the engineering, forensic accounting/auditing, and legal analyses to document any design errors and the resulting costs; and
- The proper mix of skills, including engineering, accounting, and legal expertise related to construction change orders in order to apply the methodology and resolve questionable change orders appropriately.

Because FHWA, the Project, and several State entities are in the process of strengthening and revising the Cost Recovery Program, we will defer, for the time-being, a detailed review of the Cost Recovery Program. Instead, given the continuing efforts to clarify and finalize a credible, robust process to resolve these cost recovery items, we plan to monitor these efforts and to keep your office informed of the progress being made.

We are enclosing a copy of a memorandum we recently sent to FHWA Administrator Mary Peters which further describes some of the actions being taken and highlights three issues that deserve attention by the FHWA's Massachusetts Division Office—(1) the limited recoveries to date, (2) the lack of timely resolution of items, and (3) the potential to address additional items.

If I can answer any questions or be of further assistance, please feel free to contact me at (202) 366-1959, or my Deputy, Todd J. Zinser, at (202) 366-6767.

Sincerely,

A handwritten signature in black ink, appearing to read "Kenneth M. Mead". The signature is written in a cursive style with a large initial "K".

Kenneth M. Mead
Inspector General

Enclosure



Memorandum

**U.S. Department of
Transportation**

Office of the Secretary
of Transportation
Office of Inspector General

Subject: **ACTION:** Opportunities to Recover Costs Paid to
Contractors, but Caused by Design Errors on the
Central Artery/Tunnel Project

Date: April 18, 2003

From: Kenneth M. Mead
Inspector General

A handwritten signature in black ink, appearing to read "Kenneth M. Mead".

Reply to
Attn. of: JA-30

To: Mary E. Peters
Federal Highway Administrator

We have received requests from Congressman Michael E. Capuano of Massachusetts' 8th District and Congressman Don Young, Chairman, House Committee on Transportation and Infrastructure, that we review the reasons behind some of the cost increases on the Central Artery/Tunnel Project (Project). Recently, significant attention has been paid to opportunities to recover costs paid to contractors for change orders that might have been caused by engineering design errors or omissions on the part of Bechtel/Parsons-Brinkerhoff Joint Venture (Bechtel), the Project's preliminary design engineer and construction manager.

FHWA has recently taken several actions to strengthen the Cost Recovery Program, including requesting the Project to prepare an action plan with key milestones to resolve the cost recovery items. In addition, several State organizations are looking into this issue including the Governor's office, the State's Office of Inspector General, and the State Auditor's Office. This reemphasis is needed because, although the Project and FHWA have had a cost recovery program in place since 1994, it has yielded little in actual recoveries. Eight years of cost recovery efforts have led to only \$30,000 in recoveries from a single consultant. The process has also not resulted in the timely resolution of change orders referred to the Cost Recovery Program--76 items are between 2 and 7 years old.

As a result of the current reviews and oversight efforts by your office and State entities, we will defer for the time being our detailed review of the Cost Recovery Program. We plan on monitoring FHWA's efforts and progress.

Opportunity to Recover Costs Due to Design Errors or Omissions

Cost recovery offers an important opportunity to reduce costs on a project that has been cited as an egregious example of runaway costs. Because the recoveries are returned to the Project and, if FHWA participated in the change order, to the State's Federal aid account, it is important to aggressively pursue cost recovery efforts, which would benefit both the State and Federal Government.

We recognize the strong emphasis you have placed on improving oversight practices of FHWA Division Offices since being appointed FHWA Administrator. In that regard, your March 14, 2003 letter to the Chairman of the Massachusetts Turnpike Authority (MTA) cited several steps that FHWA is taking to strengthen the Project's Cost Recovery Program in order to protect Federal interests. The Cost Recovery Program, which FHWA approved in 1994, allows the Project to approve the change order, pay the consultant contractor for the work, and seek reimbursement from FHWA, before determining whether the change was due to a design error.

Your letter noted that the Cost Recovery Program was designed to make sure questionable change orders were evaluated and resolved before FHWA allowed the contract to be formally closed. The letter also cited recent changes to the Cost Recovery Program that call for the Division Office to (1) concur in the Project's resolution of each cost recovery item and (2) receive quarterly status reports from the Project about the backlog of cost recovery items. Finally, your letter noted that FHWA is taking additional oversight actions to ensure that the Project's Cost Recovery Program will be successful. To assist in that effort, you asked the Project to prepare an action plan that includes key milestones to resolve the cost recovery items.

In addition to your efforts, several different entities in the State are reviewing the change orders to determine whether improper payments were made. As a result, we believe it would be counter-productive for this office to do a detailed review of the Cost Recovery Program at this time. Therefore, we will defer, for the time being, to FHWA's efforts to ensure that the Project's Cost Recovery Program operates effectively. We plan to monitor FHWA efforts in this area to ensure that the Project implements an effective Cost Recovery Program.

Your attention to this issue also provides an opportunity to make further progress in efforts to improve Division Office oversight. In that regard, we believe three

issues deserve attention by the Massachusetts Division Office. According to Project documents:

- Eight years of cost recovery efforts have led to only \$30,000 in recoveries from a single consultant, even though 76 change orders, involving \$53.7 million have been resolved to date. The \$30,000 represents less than one-tenth of 1 percent (.056 percent) of the amount in question. This is a very low recovery rate on a Project of this size and complexity.
- The process has not resulted in the timely resolution of many change orders that have been referred to the Cost Recovery Program. Currently, the Project has approximately 295 unresolved change orders, valued at \$188 million. Of these, the Project identified 76 items that are between 2 and 7 years old. Timely resolution of change orders is important, because the longer the issues remain unresolved, the more difficult it becomes for the Project to determine whether the change orders were caused by design errors.
- The Cost Recovery Program may not be evaluating some change orders that might be due to design errors. To date, the Project's Cost Recovery Program has been assigned about 371 change orders suspected of being caused by design errors. In total, these change orders are valued at about \$241 million. However, the Massachusetts Office of the Inspector General recently issued a report noting that its audits had identified \$730 million in change orders that potentially could have involved design errors.

We would appreciate quarterly updates from your staff to keep us advised of progress in ensuring that the Project resolves cost recovery items in a timely and cost-effective manner. We plan to report periodically to Congressman Capuano and Chairman Young about the progress being made.

If you have any questions or are in need of further assistance, please do not hesitate to contact me at (202) 366-1959, or Todd J. Zinser, Deputy Inspector General, at (202) 366-6767.

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cc: Secretary
Deputy Secretary
DOT Chief of Staff