

# ORANGE COUNTY TRANSPORTATION AUTHORITY INTERNAL AUDIT DEPARTMENT



## Right-of-Way and Appraisal Services and Activities

### Internal Audit Report No. 22-511

November 16, 2022



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On-Call Right-of-Way and Appraisal Services  
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## **Conclusion**

The Internal Audit Department (Internal Audit) of the Orange County Transportation Authority (OCTA) has completed an audit of right-of-way (ROW) and appraisal services and activities. Based on the audit, service procurements were handled in accordance with OCTA procurement policies, and oversight and invoice review controls are adequate. However, recommendations were made to ensure a documented cost or price analysis is conducted for contract amendments, and to expand policy and procedures to provide clarification on the application of settlement authority thresholds.

## **Background**

The Real Property Department (Real Property) provides general real estate and ROW services for the entire agency. ROW services include acquisition and negotiation, relocation assistance, utility coordination, title and escrow, and environmental site assessment. Real Property utilizes on-call consultants to support ROW activities.

### On-Call ROW Support and On-Call Appraisal Services Agreements

Effective July 29, 2020, OCTA entered into Agreement No. C-9-1613 with Epic Land Solutions, Inc. (Epic), for on-call ROW and property management services. The contract was set up as an on-call, time and expense agreement with an initial term of three years, with two, one-year option terms and a maximum obligation of \$3,500,000. On February 18, 2021, Amendment No. 1 was executed to add subcontractors to provide specialty appraisal services. On October 22, 2021, Amendment No. 2 was executed to update and add to the schedule of fees, and on May 11, 2022, Amendment No. 3 was executed to incorporate required Federal Transit Administration clauses.

Effective November 20, 2019, OCTA executed agreements with Hendrickson Appraisal Company, Inc., Hennessey & Hennessey, LLC, Integra Realty Resources – Los Angeles, and R.P. Laurain & Associates, Inc., to provide on-call real property appraisals and related services, in the aggregate amount of \$3,500,000, for a five-year term. As needed, contract task orders (CTO) are issued to the bench of firms and awarded based on evaluation of firm experience, workplan, project timeline and pricing.

### ROW and Appraisal Activities

The Real Property manager assigns work to Real Property agents (agents) and support consultants to conduct ROW activities. The agent oversees all work assigned to the on-call consultant to ensure compliance with policies and procedures. Depending on project size and the number of parcels that need to be appraised, the Real Property manager may utilize the on-call ROW consultant for appraisal services or may issue a CTO to consultants on the appraisal services bench. After obtaining an appraisal and review appraisal, the ROW consultant makes recommendations on the acquiring property

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for review and concurrence by the agent. The agent, Real Property manager, and OCTA's legal counsel review and approve offer packages before they are delivered to the property owner.

Real Property Policies and Procedures and Incentive Payment Program

The Real Property Policies and Procedures Manual outlines administrative and legal settlement authority thresholds as follows:

- The Executive Director, Capital Programs is authorized to execute real estate agreements, ROW contracts, utility agreements, deeds, certificates of acceptance, leases, licenses, permits or any Real Property agreement documents up to \$250,000, or 20 percent above the appraised value.
- The Chief Executive Officer (CEO) approval limit is up to \$250,000, or 50 percent above the appraised value.
- The CEO is also authorized to approve settlements when the difference between the approved appraisal and the settlement amount exceeds 50 percent but is not more than \$25,000 over the appraised value.

For the Interstate 405 (I-405), State Route 55, and the State Route 91 improvement projects (projects), the Board of Directors (Board) authorized an incentive payment program to expedite agreements with property owners to avoid construction delays. The payment program provides for an incentive payment to be provided to property owners that execute an agreement within 60 days of the first written offer. The incentive payment is calculated at 20 percent above the appraised value, with a minimum payment of \$1,000, and a maximum payment of \$100,000, for each acquisition. The Board also approved modifications to the CEO settlement authority thresholds for these projects, as follows:

- The CEO approval limit is up to \$500,000, or 50 percent above the appraised value.
- The CEO is also authorized to approve settlements when the difference between the approved appraisal and the settlement amount exceeds 50 percent but is not more than \$100,000, over the appraised value.

For these projects, the Board must approve any administrative or legal settlement above the CEO approval limits.

The Real Property Policies and Procedures Manual, along with the Board-approved modifications for these projects are collectively referred to as Policies hereafter.

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Invoice Processing

A senior real estate agent monitors on-call contract burn rates and forwards invoices to the agent responsible for the transaction to confirm services before forwarding invoices to Project Controls. Project Controls staff compares invoiced rates to contracted rates and verifies accounting charge codes, using an invoice review checklist to document the review. Invoices are then forwarded to the Real Property manager for review and approval. The Real Property manager forwards the invoice package to Accounts Payable for processing.

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## **Objectives, Scope, and Methodology**

The objectives were to assess and test procurement, contract amendment, contract compliance, invoice review, and ROW transaction controls for compliance with Policies.

According to Generally Accepted Government Auditing Standards (GAGAS), internal control is the system of processes that an entity's oversight body, management, and other personnel implement to provide reasonable assurance that the organization will achieve its operational, reporting, and compliance objectives. The five components are control environment, risk assessment, control activities, information and communication, and monitoring.<sup>1</sup> The components and principles that were evaluated as part of this audit are:

- Control Environment
  - OCTA demonstrates a commitment to integrity and ethical values.
  - The Board demonstrates independence from management and exercises oversight of the development and performance of internal control.
  - Management establishes, with Board oversight, structures, reporting lines, and appropriate authorities and responsibilities in the pursuit of objectives.
  - OCTA demonstrates a commitment to attract, develop, and retain competent individuals in alignment with objectives.
  - OCTA holds individuals accountable for their internal control responsibilities in the pursuit of objectives.
- Risk Assessment
  - OCTA specifies objectives with sufficient clarity to enable the identification and assessment of risks relating to objectives.
  - OCTA identifies risks to the achievement of its objectives across the entity and analyzes risks as a basis for determining how the risks should be managed.
  - OCTA considers the potential for fraud in assessing risks to the achievement of objectives.
  - OCTA identifies and assesses changes that could significantly impact the system of internal control.
- Control Activities
  - OCTA selects and develops control activities that contribute to the mitigation of risks to the achievement of objectives to acceptable levels.
  - OCTA selects and develops general control activities over technology to support the achievement of objectives.
  - OCTA deploys control activities through policies that establish what is expected and procedures that put policies into action.

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<sup>1</sup> See U.S. Government Accountability Office publication, "Standards for Internal Control in the Federal Government," available at <http://www.gao.gov/products/GAO-14-704G>, for more information.

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- Information and Communication
  - OCTA obtains or generates and uses relevant, quality information to support the functioning of internal control.
  - OCTA internally communicates information, including objectives and responsibilities for internal control, necessary to support the functioning of internal control.
  - OCTA communicates with external parties regarding matters affecting the functioning of internal control.
- Monitoring
  - OCTA selects, develops, and performs ongoing and/or separate evaluations to ascertain whether the components of internal control are present and functioning.
  - OCTA evaluates and communicates internal control deficiencies in a timely manner to those parties responsible for taking corrective action, including senior management and the Board, as appropriate.

The methodology consisted of testing compliance with selected procurement policies and procedures, testing compliance with bond and insurance contract requirements, testing a sample of ROW invoices and all appraisal invoices for compliance with invoice policy and contract provisions, and testing a sample of ROW transactions for compliance with Policies regarding offer letters, approvals, and executed contracts.

The scope was limited to Agreement No. C-9-1613 with Epic, and Amendment No. 1 and No. 2 to the agreement, Agreement No. C-9-0995 with Hendrickson Appraisal Company, Inc., Agreement No. C-9-1473 with Hennessey and Hennessey, LLC., Agreement No. C-9-1474 with Integra Realty Resources - Los Angeles, and Agreement No. C-9-1475 with R.P. Laurain & Associates, Inc., and all CTOs and CTO amendments. The scope included a judgmental sample of ROW contractor invoices from November 2021 through May 2022, with a bias towards obtaining sample coverage throughout the years and all paid appraisal invoices from July 2020 through May 2022. The scope also included a judgmental sample of ROW payments to property owners during the period July 2021 through May 2022, with a bias towards obtaining coverage throughout the period and the related ROW offers, approvals, and executed contracts. Since the samples were non-statistical, any conclusions are limited to the sample items tested.

We conducted this performance audit in accordance with GAGAS. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

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**Audit Comments, Recommendations, and Management Responses**

**Cost or Price Analysis for Contract Amendments**

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Two amendments that included pricing adjustments to the ROW services contract were executed without evidence of a cost or price analysis, as required. Procurement policies and procedures require a cost or price analysis be performed in connection with every procurement action, including contract amendments. This analysis is used to determine if proposed prices are fair and reasonable.

Amendment No. 1 to Agreement No. C-9-1613 (Agreement) with Epic changed contract pricing by adding three subcontractors for specialty appraisal services, along with labor rates for firm personnel. The amendment file indicates that the Contracts Administration and Materials Management (Camm) administrator reviewed the labor rates proposed and found the rates consistent with prior agreement rates; however, no documentation of this review was on file. In addition, Internal Audit noted that most of the proposed rates exceeded those from the prior agreements for these services.

Amendment No. 2 to the Agreement also changed contract pricing by adding personnel and increasing labor rates for two staff and four labor categories that were already listed in the Agreement and subject to annual escalation of three percent. No cost or price analysis was performed for this amendment.

**Recommendation 1:**

Internal Audit recommends that a cost or price analysis be performed and documented as required. In addition, increases to rates already agreed-upon should be denied.

**Management Response (Camm):**

Management agrees with the recommendation and will ensure that a cost or price analysis is performed and documented to the file when personnel are being added to the agreement. Management will also ensure that there are no changes to rates already agreed-upon and any increases be subject to contractual escalation.

Camm staff will also be provided a refresher training on how to conduct rate validation, documentation of rate reasonableness, and quality review of documents when personnel are being added to the agreement.

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**Application of Settlement Authority Thresholds**

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Application of Board-approved authority thresholds for administrative and legal settlements should be clarified.

Interviews with management, and review of transactions with two property owners noted that for purposes of determining the required authorization level for settlement amendments, the appraised value, plus the incentive payment, from the original settlement agreement, is added to the value determined for the additional acquisition action.

For example, in 2017, in relation to the I-405 project, OCTA acquired, through a fee acquisition, approximately 713 square feet of land and a temporary construction easement (TCE) of approximately 407 square feet for a period of 60 months through March 30, 2022. The property owner participated in the incentive payment program and received payment for the appraised value of \$170,000 plus the 20 percent incentive payment of \$34,000. In 2022, the construction contractor requested an extension of the TCE for six months, through September 2022. A written evaluation of the TCE extension was performed and was valued at \$1,800. After negotiations, management agreed to settle with the owner for \$9,180. The ROW Department Manager sought, and obtained, authorization from the Executive Director of Capital Programs based on the following calculation:

Original Appraised Value (2017)	\$170,000
20 Percent Incentive Payment	<u>\$34,000</u>
Total	\$204,000
Written Valuation for TCE extension (2022)	\$1,800
Combined Values	<u>\$205,800</u>

Combined Settlements:  $\$204,000 + 9,180 = \$213,180$  (< 20% above combined values)

Internal Audit considered whether the second settlement transaction should be evaluated separately, as follows:

Written Valuation	\$1,800
Proposed Settlement	\$9,180 (>50% above waiver evaluation value)

Under management's calculation, the settlement may be authorized by the Executive Director of Capital Programs. If the secondary transaction was evaluated separately, it would require CEO approval.

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Discussion with legal counsel advised that the evaluation for settlement authority should include the original appraised value but should not include the incentive payment amount. Discussion with California Department of Transportation (Caltrans) ROW staff indicated that Caltrans' process would consider the subsequent transaction as separate from the original, and Caltrans Audits and Investigations staff indicated that OCTA should, at a minimum, clarify these interpretations in Board-approved policies.

**Recommendation 2:**

Internal Audit recommends management update Policies to clarify procedures for determining settlement authorities.

**Management Response (Capital Programs):**

Management agrees with the recommendation and will work with General Counsel to incorporate language into the Policies to address the recommendation. The language will provide guidelines how the Delegated Settlement Authority thresholds should be calculated and shall include the following:

“When calculating the threshold limits for CEO’s or Executive Director’s settlement authority, staff shall include the original and/or revised appraised values but will not include the incentive payment amount agreed upon by a property owner in the calculations.”

Management believes Caltrans ROW staff did not have adequate background or information regarding this specific transaction or knowledge of OCTA’s internal Delegated Settlement Authority Policy. The policy is not impacted by the Caltrans ROW Manual procedures or Caltrans funding requirements. When calculating the thresholds limits for the CEO settlement authority, staff will no longer include the incentive payment agreed upon by a property owner in the calculations. With respect to the specific transaction reviewed, had management not included the incentive payment, this transaction would have settled correctly by seeking authorization from the Executive Director and not the CEO as shown below: Administrative Settlement  $\$170,000 + 9,180 = \$179,180$  or 5.4 percent (< 20 percent above combined values), which is within the Executive Director’s approval authority.

To address any concerns, the Policies will be amended for clarity.