



September 13, 2017

To: Finance and Administration Committee

From: Darrell Johnson, Chief Executive Officer

Janet Sutter, Executive Director
Internal Audit Department

Subject: Contracted Fixed-Route Operations, Internal Audit Report No. 17-508

Overview

The Internal Audit Department has completed an audit of contracted fixed-route operations provided by First Transit, Inc. The audit found that, in April 2016, Transit Division management changed the threshold used to measure on time performance for both contracted and directly-operated fixed-route bus service. This change, which resulted in more favorable performance results, was not disclosed to the Board of Directors. In addition, penalties for failure to meet preventative maintenance standards and missed trips have been waived without adequate justification and documentation. Calculation errors in contract amendments and weaknesses in monitoring and enforcement of other contract requirements were also observed.

Recommendation

Direct staff to implement six recommendations provided in Contracted Fixed-Route Operations, Internal Audit Report No. 17-508.

Background

The Orange County Transportation Authority (OCTA) and First Transit, Inc. (First Transit) entered into Agreement No. C-4-1737 (Agreement) in June 2015, in an amount not to exceed \$143,487,171. Under the Agreement, First Transit provides management and operation of fixed-route, StationLink, and Express Bus services. Amendments No. 2 and 3 added operation of iShuttle and expanded Project V services, with an increase to the maximum obligation of \$3,476,956, and \$1,838,402, respectively.

The Agreement establishes performance standards including standards for on-time performance (OTP), valid complaints, accidents, preventive maintenance, miles between road calls, and missed trips. Penalties and/or incentives are applied based on First Transit's achievement of performance standards. Additional requirements and standards not tied to penalties and/or incentives are also included in the Agreement.

Discussion

The contractual OTP standard requires buses to depart between zero minutes early and five minutes late, 85 percent of the time. Performance results for all transit services, including the OTP, are transmitted to the Transit Committee (Committee) and the Board of Directors (Board) on a quarterly basis. In January 2016, citing concerns with First Transit's performance, the Committee directed staff to provide monthly updates of performance results. Effective February 2016, Transit management directed a change to the OTP threshold from five minutes to five minutes and thirty seconds, resulting in a two percent improvement to OTP results. An update was presented to the Committee the day following the change; however, staff did not disclose this during the presentation, nor in ensuing monthly updates or quarterly performance reports provided to the Committee and the Board. During the period March through December 2016, the Internal Audit Department (Internal Audit) estimates that \$13,000 in OTP penalties were avoided as a result of the change. Internal Audit recommended that performance standards be measured consistent with the Agreement or be processed as amendments to the Agreement, and Board notification and/or approval be obtained prior to the change. Management agreed and responded that the OTP measurement has been retroactively adjusted to reflect a zero to five minute window. Management also responded that any changes in methods used to collect data will be reported in the quarterly performance reports provided to the Board.

Additionally, penalties for failure to meet preventative maintenance (PMI) standards have been regularly waived without adequate justification and documentation. To date, Transit staff has not exercised the option to withhold payment of service hours operated with vehicles that have exceeded required PMI intervals. To monitor PMI performance, Transit staff selects and reviews records of about 20 vehicles per month. Although numerous vehicles were identified as exceeding the PMI intervals, staff assessed penalties only one month during the period from inception through December 2016. The Agreement states that the contractor may be given an opportunity to demonstrate that the failure could not have reasonably been prevented, and to provide documentation to support such claims; however, there was no documentation on file that First Transit requested the penalty waivers or the reasons that penalties were not

assessed. Internal Audit recommended that management consistently apply penalties and consider non-payment of revenue hours for vehicles that exceed PMI intervals. Penalties should only be waived at First Transit's request and with adequate evidence demonstrating that the failures could not have reasonably been prevented. Management agreed to implement more consistent application of penalties and to document and justify the decisions. Management also indicated that the Agreement will be amended to allow for appropriate discretion with regard to penalty waivers.

Similarly, missed trip penalties of \$16,000 related to Orange County (OC) Fair trips were waived without adequate justification. First Transit management had requested 12 of 14 missed OC Fair trips be waived, claiming that when they contacted OCTA Central Communications (CC) to report a lack of drivers, they were told "not to worry," and OCTA drivers completed the trips. First Transit acknowledged that the first two trips would have been missed by the time of the call, but implied that efforts to identify coverage for the remaining trips would have continued had OCTA not offered to cover the service. Review of OCTA CC recordings did not substantiate this assertion. On August 5, 2016, First Transit missed another two OC Fair trips. Penalties for these missed trips were also not assessed, and there was no waiver request or justification. Again, Internal Audit recommended that management consistently apply penalties and requests for penalty waivers include documentation to justify how the failures could not have reasonably been prevented. Management agreed to require written requests from the contractor as well as supporting documentation for penalties waived. Management also indicated that the contract will be amended to allow for appropriate discretion with regard to penalty waivers.

Internal Audit observed that staff erroneously incorporated fleet projections from the original request for proposal (RFP) into the final contract, rather than using updated fleet projections that had been issued through an RFP addendum. Also, contract Price Summary Exhibits, which reflect agreed-upon rates and costs, were not properly prepared to reflect updates resulting from contract amendments. Lastly, Internal Audit identified errors in the calculation of contract maximum obligation amounts for two amendments. The errors resulted in an overstatement of the contract maximum obligation of \$285,581. Recommendations were made to ensure proper update to contract exhibits and review of final contract packages for inclusion of the latest attachments and/or exhibits. Management agreed to update contract exhibits as needed, and indicated that Contracts Administration and Materials Management (CAMP) staff reviews contracts and circulates them to requesting departments for review and concurrence prior to final execution.

First Transit's performance bond amount was not increased with amendments as required, and the insurance certificate on file did not reflect all required coverage. Upon notice, First Transit obtained the required increases in the performance bond and provided evidence of adequate insurance coverage. Internal Audit recommended that CAMM develop monitoring procedures to ensure contract bond and insurance requirements are met. Management agreed and has taken steps to review and track bond and insurance documents for compliance with contract terms. Management also responded that a recently procured insurance brokerage services contract includes responsibilities for tracking of insurance certificates.

With regard to performance requirements that are not tied to penalties and/or incentives, Internal Audit also made recommendations for improvement. First, the Agreement requires an accident report be submitted within 24 hours of the time of an accident or incident, and that monthly summary reports be prepared and submitted. Review found that First Transit regularly fails to send all accident reports and identified two incidents that were omitted from a monthly report. Another requirement is that repair or replacement of major mechanical components be initiated only upon OCTA's written approval; however, multiple instances of repairs being initiated prior to written approval were observed. Finally, First Transit did not meet the unclassified revenue percentage standard for eight of 19 months reviewed. To improve monitoring and compliance, Internal Audit recommended that accident reports be reconciled to monthly summary reports and that procedures be developed for progressive enforcement actions. Management agreed to conduct monthly reconciliations of accident reports. With regard to pre-approval of major mechanical repairs, management indicated that contract language will be amended to eliminate the pre-approval requirement. Finally, management indicated that documentation will be maintained to evidence ongoing monitoring and actions taken to address performance results related to the unclassified revenue percentage.

Summary

Internal Audit has completed an audit of contracted fixed-route operations provided by First Transit and has offered several recommendations for improvement.

Attachment

A. Contracted Fixed Route Operations, Internal Audit Report No. 17-508

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