



Office of Internal Oversight Services

INTERNAL AUDIT DIVISION

AUDIT REPORT

The Office of the Capital Master Plan's management of trade contracts

The system of internal controls instituted for the oversight and control of contract management is effective, but further efforts are required to improve turnaround time for payment of invoices

31 August 2009

Assignment No. AC2008/514/07

United Nations  Nations Unies

INTEROFFICE MEMORANDUM

MEMORANDUM INTERIEUR

OFFICE OF INTERNAL OVERSIGHT SERVICES · BUREAU DES SERVICES DE CONTRÔLE INTERNE
INTERNAL AUDIT DIVISION · DIVISION DE L'AUDIT INTERNE

TO: Ms. Angela Kane, Under-Secretary-General for
A: Management

DATE: 31 August 2009

FROM: Fatoumata Ndiaye, Acting Director
DE: Internal Audit Division, OIOS

REFERENCE: IAD: 09- 02788

SUBJECT: **Assignment No. AC2008/514/07 – Audit of the Office of the Capital Master Plan's management
of trade contracts**

1. I am pleased to present the report on the above-mentioned audit.
2. Based on your comments, we are pleased to inform you that we will close recommendations 2 and 4 in the OIOS recommendations database as indicated in Annex 1. In order for us to close the remaining recommendations, we request that you provide us with the additional information as discussed in the text of the report and also summarized in Annex 1.
3. Please note that OIOS will report on the progress made to implement its recommendations, particularly those designated as high risk (i.e., recommendations 3, 5, and 6), in its annual report to the General Assembly and semi-annual report to the Secretary-General.

cc: Mr. Michael Adlerstein, Assistant Secretary-General and Executive Director, CMP
Mr. Swatantra Goolsarran, Executive Secretary, UN Board of Auditors
Ms. Maria Gomez Troncoso, Officer-in-Charge, Joint Inspection Unit Secretariat
Mr. Moses Bamuwanye, Chief, Oversight Support Unit, Department of Management
Mr. Byung-Kun Min, Special Assistant to the USG/OIOS
Mr. William Petersen, Chief, New York Audit Service, OIOS

INTERNAL AUDIT DIVISION

FUNCTION

“The Office shall, in accordance with the relevant provisions of the Financial Regulations and Rules of the United Nations examine, review and appraise the use of financial resources of the United Nations in order to guarantee the implementation of programmes and legislative mandates, ascertain compliance of programme managers with the financial and administrative regulations and rules, as well as with the approved recommendations of external oversight bodies, undertake management audits, reviews and surveys to improve the structure of the Organization and its responsiveness to the requirements of programmes and legislative mandates, and monitor the effectiveness of the systems of internal control of the Organization” (General Assembly Resolution 48/218 B).

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EXECUTIVE SUMMARY

Audit of the Office of the Capital Master Plan's management of trade contracts

OIOS conducted an audit of the Office of the Capital Master Plan's (CMP) management of trade contracts. The overall objective of the audit was to ascertain that a process of systematically and efficiently managing trade contracts exists to attain best value and minimize risks. The audit was conducted in accordance with the International Standards for the Professional Practice of Internal Auditing.

Overall, OIOS assessed the system of internal controls instituted for the oversight and control of contract management to be effective.

The major findings of OIOS were as follows:

- (a) There were too few CMP project managers to provide full project management. However, at the time of the audit, resources were supplemented by the consultant programme manager. Recruitment of additional staff would be necessary if the deficiency in project management capacity becomes protracted.
- (b) The Office of the CMP has not always paid the construction manager's invoices within 30 days. Most delays have occurred because of the need to resolve queries with regard to the review of general conditions, including timesheets.
- (c) A comprehensive risk assessment of CMP was conducted by the consultant programme manager in October 2008 and an updated risk register has been produced.
- (d) The ex post facto committee for the review of change orders issued under the delegation of authority to the Assistant Secretary-General and Executive Director, CMP has not yet been established by the Office of Central Support Services.
- (e) The schedule disclosed in the Secretary-General's sixth annual progress report has slipped by several months. There may be opportunities to bring the programme back on schedule that should be reviewed by the Office of the CMP in conjunction with the Department of Safety and Security.

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I. INTRODUCTION

1. The Office of Internal Oversight Services (OIOS) conducted an audit of the Office of the Capital Master Plan's (CMP) management of trade contracts. The audit was conducted in accordance with the International Standards for the Professional Practice of Internal Auditing.
2. Effective contract management is essential if the CMP is to achieve all its objectives. Time, budget and quality are three critical elements that were the focus of this audit.
3. The United Nations has entered into a Preconstruction Services Agreement and more recently a Coordination Agreement with Skanska USA Building Inc. Skanska is now referred to as the construction manager. The United Nations and the construction manager will enter into approximately 25 construction management agreements with guaranteed maximum price (GMP contracts) for the different projects that together comprise the entire CMP project. For each GMP contract, the construction manager procures the services of a number of trade contractors for elements of the work. At the time of the audit the construction manager had entered into 114 separate contracts with trade contractors, who will undertake the construction work. The construction manager manages and pays the trade contractors.
4. Comments made by the Office of Capital Master Plan are shown in *italics*.

II. AUDIT OBJECTIVES

5. The main objectives of the audit were to:
 - (a) Determine whether suitable governance mechanisms are in place in terms of organization, policies and contractual requirements between:
 - (i) the United Nations and the construction manager; and
 - (ii) the construction manager and the trade contractors;
 - (b) Determine whether payments to trade contractors have been timely and accurate, and that the payment processes ensure deliverables have been achieved;
 - (c) Ascertain whether a culture of ensuring the attainment of best value is embedded in the contract management processes. Review whether value for money is being achieved;
 - (d) Ascertain whether non-compliance with trade contracts and non-deliveries are promptly identified and brought to the attention of the construction manager for appropriate action;
 - (e) Examine the processes for ensuring the attainment of appropriate quality and assess whether they are effective; and
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- (f) Examine effectiveness of managing contract interfaces between the CMP and contracts managed by the Facilities Management Service, (FMS).

III. AUDIT SCOPE AND METHODOLOGY

6. OIOS interviewed personnel of the Office of the CMP, the construction manager and the consultant programme manager. OIOS reviewed the organizational structure of the individual projects and the responsibilities of the Office of the CMP, the construction manager and the consultant programme manager for contract management. OIOS reviewed invoices and payment confirmations and the timeframes within which the United Nations paid the construction manager, and the construction manager paid the trade contractors. OIOS reviewed minutes of construction meetings, coordination meetings, budgets and schedules. OIOS attended the April 2009 pencil requisition meeting during which the percentage of completion for each trade contract was agreed by responsible staff from the Office of the CMP, the construction manager, the architects and the consultant programme manager.

IV. AUDIT FINDINGS AND RECOMMENDATIONS

A. Governance

Organizational structure and responsibilities

7. CMP is broken down into about 25 individual projects. Each individual project will have a separate construction management agreement with a GMP contract signed between the United Nations and the construction manager. Each GMP contract in turn will have numerous trade contracts signed between the construction manager and trade contractors. Examples of GMP contracts include the construction of the North Lawn Conference Building, the fit out of 305 East 46th Street, and the fit out of 380 Madison Avenue swing spaces.

8. The construction manager prepares each GMP proposal and these are then reviewed and independently re-estimated by the consultant programme manager. Then the CMP's Director of Construction, the construction manager and the consultant programme manager meet to compare the two estimates and negotiate the GMP proposal on a line by line basis.

9. The organization of all projects includes personnel from the Office of the CMP, consultant architects/engineers, the consultant programme manager and the construction manager. Each project is headed by a designated UN/CMP Administrator with all parties involved ultimately reporting to him/her.

10. According to the GMP contract document, the construction manager's responsibilities include the coordination and direction of work of the trade contractors and supervision of work at the site. The organizational structure of the construction manager's personnel includes project managers, superintendents, schedulers, accountants, quality assurance/quality control manager and safety coordinators.

11. The consultant programme manager's responsibilities include reviewing the construction manager's invoices, providing estimates, scheduling and technical expertise.

12. The Office of the CMP has overall oversight responsibility to ensure that projects are progressing on time and within budget. The Director of Construction coordinates this effort. During the audit, members of the Office of the CMP, the consultant programme manager and the construction manager expressed the opinion that the Director of Construction is over-burdened and requires greater support. The Director of Construction acknowledged a need for more CMP project managers. However, he indicated that more resources will be available when the design stage starts winding down. At the time of the audit, additional resources from the consultant programme manager were used to supplement the CMP project managers' capacity. However, additional staff should be recruited if the deficiency in project management capacity becomes protracted.

Recommendation 1

(1) The Office of the Capital Master Plan's Director of Construction should keep the need for project management resources under close review and, if necessary, initiate the recruitment of additional project management staff through the Assistant Secretary-General and Executive Director, Capital Master Plan.

13. *The Office of the CMP accepted recommendation 1 and stated that the requirement for project managers will be reviewed on the completion of swing projects.* Recommendation 1 remains open pending the review of requirements.

Weekly Meetings

14. There are various meetings conducted on a weekly basis to coordinate work between the Office of the CMP, the construction manager and the consultant programme manager. There are also different stakeholders that are important to the success of CMP, such as the Department of Safety and Security, the Office of Information and Communications Technology, the Office of Legal Affairs, the Procurement Division, the Facilities Management Service and others. OIOS reviewed the weekly schedule of meetings and concluded that all decision makers and stakeholders meet regularly to discuss and coordinate issues. Minutes of the meetings are prepared and distributed to participants, and were available for OIOS' review.

Coordination Agreement with the construction manager

15. The Preconstruction Services Agreement with Skanska expired on 27 January 2009. The contract was extended for a further three months under the delegation of authority to the Procurement Division. Section 12.27 of the Agreement has a requirement for the United Nations and the construction manager to develop and enter into a Coordination Agreement upon conclusion of the Preconstruction Services Agreement to address the coordination and management of all GMP projects, including the master project schedule and individual project schedules, development of drawings and specifications for various projects, and budgeting to comply with the CMP financial constraints. At the time of the audit, the Coordination Agreement with the construction manager was being negotiated. The presentation to the Headquarters Committee on Contracts estimates the cost of the Coordination Agreement not to exceed \$41,500,000 based on the estimates of the consultant programme manager. Cost control for this contract will be undertaken by the consultant programme manager on behalf of the Office of the CMP.

Integrity monitoring

16. In April 2009, the United Nations entered into a contract with a consultant for the provision of integrity monitoring services. The contract is for an amount not to exceed \$1,192,000. The purpose of integrity monitoring is to: (i) help prevent fraud, waste, abuse and corruption; (ii) alert CMP management to potentially risky or weak areas through periodic reports and interim updates; and (iii) report actual transgressions if found. The consultant will work with CMP management to design and implement corruption prevention programs and provide ongoing investigative services as necessary.

17. OIOS examined the Scope of Professional Services for the integrity monitors and observed that there is no requirement for cases of fraud or misconduct to be reported to the Under-Secretary-General, OIOS and the Controller.

Recommendation 2

(2) The Office of the Capital Master Plan should establish procedures whereby cases of fraud and misconduct are reported to the Under-Secretary-General, OIOS and the Controller.

18. *The Office of the CMP accepted recommendation 2 and stated that the integrity monitoring consultant has been requested to send a copy of his reports directly to OIOS, and the OUSG, Department of Management is kept informed of any issues by the Office of the CMP.* Based on the action taken by the Office of the Capital Master Plan, recommendation 2 has been closed.

Risk management

19. The consultant programme manager drafted a fourth comprehensive CMP risk assessment in October 2008, and a risk register that gives probabilities, values and impact assessments. The Chief, Administration and Communications facilitates regular reviews of the risks and individual risks have been assigned to risk owners. Risks are reviewed periodically and if necessary recategorised as low, medium or high risks. Furthermore, a summary of risks and mitigation actions is provided by the consultant programme manager as part of the monthly status reports.

Outside agencies

20. According to the Office of the CMP, the CMP will be in compliance with the City of New York Building Code on a voluntary basis. All drawings are submitted to the New York City Building Department for review. The Building Department has conducted a walk through of the North Lawn Conference Building. The Office of CMP also coordinates with the United States Environmental Protection Agency, the New York City Department of Transportation, Fire Department and Police Department.

21. Overall, OIOS assessed the governance framework instituted for the oversight and control of contract management to be effective. Recommendations are made below with regard to the timeliness of payments and the need for 'ex post facto' review of change orders.

B. Payments to the construction manager and trade contractors

Payments to the construction manager

22. OIOS reviewed 60 per cent and 85 per cent of invoices issued by the construction manager for the North Lawn Conference Building and 305 East 46th Street projects, respectively. Each invoice consists of three parts and OIOS made detailed checks as follows:

(a) **General conditions**, including the construction manager's personnel and reimbursable expenses. OIOS checked that all personnel with billable rates were authorized for these projects, rates had been applied correctly and timesheets did not exceed 40 hours a week. OIOS also checked that the reimbursable expenses did not include disallowable expenses, and supporting documents such as receipts and invoices, were filed.

(b) **Trade costs and allowances**. OIOS checked: (i) the construction manager's invoices; (ii) applications and certificates for payment, certifications by the construction manager and architect that the work had progressed as indicated, the quality of work was in accordance with the contract documents and the contractor was entitled to payment of the amount certified; and (iii) the pencil requisition, an agreement on

the percentages of completion for each trade contract negotiated between responsible staff from the Office of the CMP, the consultant programme manager, architects/engineers and the construction manager.

(c) **Construction manager's fee and insurances.** OIOS recalculated the construction manager's fee and insurances in accordance with Article 10.1 of the construction management agreement for accuracy. The consultant programme manager performs similar reviews for each invoice and recommends payment to the Office of the CMP.

23. OIOS found that the overall process for invoice review by the consultant programme manager and the Office of the CMP is very thorough with adequate separation of duties and different levels of review. There are no materiality levels set and all discrepancies are investigated. The process ensures that the United Nations only pays the correct amount for work completed.

24. According to the Preconstruction Services Agreement, applications for payment filed by the construction manager should be processed within 30 days (subject to provisions in the event of disputes or discrepancies). However, OIOS found that it takes the Office of the CMP, the consultant programme manager and the Accounts Division between 30 and 60 days to review and process the payments, with most payments exceeding 30 days. The Office of the CMP and the consultant programme manager explained that most of the delays occur due to the review of general conditions, including timesheets. Clearance of trade costs is usually straight forward since the trade costs have been certified by the architects and pencil requisition process. Delays are important as the construction manager indicated that if an invoice is not paid by the United Nations for 60 days, the trade contractors are not paid for almost three months.

Recommendation 3

(3) The Office of the Capital Master Plan should ensure that invoices are paid within 30 days in accordance with contractual requirements. Invoice amounts pertaining to work satisfactorily completed should be settled and any balance amount held back (for example, in the event of disagreement or dispute) should be settled on resolution.

25. *The Office of the CMP accepted recommendation 3 and stated that it had been implemented.* Recommendation 3 remains open pending further review by OIOS which will be included in a forthcoming audit of project budgeting and financial control.

Payments to trade contractors

26. The construction manager is required to pay trade contractors within 15 days after the United Nations pays the corresponding amount under Article 5.1. of the trade contract. OIOS found that the construction manager was in compliance and paid trade contractors within four to ten days after receiving payment from the United Nations for all invoices reviewed.

Budget

27. In September 2008, it was projected that the CMP budget would be exceeded by \$97 million (A/63/477). In March 2009 this over-expenditure had been reduced to \$91 million. The consultant programme manager estimates that the projected over-expenditure could be further reduced due to the current economic outlook as savings may be realized for swing space fit out, campus renovation and a reduced utilization of contingency sums.

C. Attainment of appropriate quality

Quality control by the construction manager

28. To ensure quality, the construction manager has contracted an inspection company that performs inspections determined by architects/engineers. OIOS reviewed two reports on the company's inspection of concrete and steel for the North Lawn Conference Building and noted no deviations from standards. Copies of all reports are submitted to the Office of the CMP.

29. The construction manager also employs quality control/assurance staff on site who perform reviews in accordance with the construction manager's Quality Manual. OIOS reviewed minutes of the weekly coordination meetings and noted no issues pertaining to poor quality.

Quality control by the consultant architects/engineers

30. The Office of the CMP commissioned additional professional services from the architect/engineer for the North Lawn Conference Building on a time card basis. This provides for their representation on site to facilitate reviews of the requests for information and coordination of trades during construction of the North Lawn Conference Building. These services are contracted not to exceed \$364,500. There is one full time and one part time architect on the North Lawn Conference Building site. They monitor the work and submit to the Office of CMP weekly field observation reports. These reports inform the Office of the CMP whether the work was being performed in accordance with reviewed submittals and design documents. OIOS reviewed field observation reports from 24 August 2008 to 3 April 2009 and noted no issues.

31. The architects also visit swing space buildings regularly to monitor the progress of fit out.

Quality control by the Office of the CMP

32. In November 2008, the Office of the CMP contracted a commissioning agent to perform independent testing of heating, ventilation and air conditioning systems, building automation systems, plumbing and fire protection systems, electrical systems, vertical transportations and other systems in the United Nations campus. The contract will cover the duration of the projects and was approved for an amount not to exceed \$2,371,675. At the time of the audit, the

commissioning agent was reviewing shop drawings submitted by the construction manager and was developing a commissioning plan.

33. The project managers from the Office of the CMP and the consultant programme manager also visit the site regularly to observe progress and quality of work.

34. OIOS assessed that rigorous arrangements have been established for achieving the required level of quality.

D. Change orders

Delegation of authority

35. On 15 January 2009, the ASG and Executive Director of CMP was delegated an authority by the ASG, Office of Central Support Services (OCSS) to approve a cumulative amount of change orders not to exceed the lower of either \$5 million or a ten per cent contract contingency amount for each GMP contract. The contingency amount is approved by the Headquarters Committee on Contracts at the same time that the GMP contract is approved. The ASG and Executive Director of CMP authorized over \$7.6 million of change orders under his delegation of authority as of 31 March 2009.

36. The ASG and Executive Director of CMP in his memorandum to the ASG, OCSS dated 24 March 2009 requested clarification as to whether the provision should refer to “any single change order should not exceed \$5 million” rather than to the cumulative value of change orders for a contract as long as the cumulative value does not exceed ten per cent contingency. No response was received from OCSS at the time of the audit, but OIOS’ interpretation of the written delegation has been that the cumulative amount of change orders approved by the ASG and Executive Director of CMP for a single GMP contract should not exceed \$5 million unless Procurement Division’s involvement is sought.

Recommendation 4

(4) The Office of Capital Master Plan should follow up with the Office of Central Support Services to obtain clarification on procedural and control requirements pertaining to the delegation of authority to approve change orders.

37. *The Office of the CMP accepted recommendation 4 and stated that they had written officially to OCSS to clarify the issue.* OCSS has now responded and given the required clarification. Based on the action taken by the Office of the CMP and the response received from OCSS, recommendation 4 has been closed.

38. Furthermore, the change orders approved by the ASG and Executive Director of CMP should be subject to review by a committee set up for ex post facto review of contractual amendments exceeding \$200,000. At the time of the

audit, however, this committee had not been set up and this does not comply with the terms of the authority that was granted.

Recommendation 5

(5) The Office of Central Support Services should establish an ex post facto committee that will review change orders approved by the Assistant Secretary-General and Executive Director of the Capital Master Plan.

39. *The Office of the CMP accepted recommendation 5 and stated that it would follow this up with OCSS.* Recommendation 5 remains open pending the establishment of an ex post facto committee for the review of change orders approved by the Assistant Secretary-General and Executive Director of CMP.

40. OIOS has included an audit of CMP change orders and associated processes in its 2009 audit work plan, and this area of project management will be tested in detail at a later stage.

E. Scheduling and slippages

41. The construction manager prepares detailed project schedules that are then consolidated into the master schedule. The consultant programme manager then reviews the construction manager's schedule and revises its own master schedule that consolidates all the tasks of CMP including construction and relocations. The Office of the CMP, the construction manager and the consultant programme manager monitor the scheduling status through weekly Directors' meetings where scheduling is a standard agenda item. The construction manager tracks progress of each contract with the scheduled goals.

42. OIOS reviewed the construction manager's master schedule dated 27 February 2009 against a projected schedule disclosed in the Secretary-General's sixth annual progress report on the implementation of the CMP (A/63/477). OIOS identified a number of slippages of several months. The Office of the CMP and the consultant programme manager informed OIOS that the original schedules were conservative and provided assurances that there will be opportunities to make up for slippages in the future. This is important because delays to a project invariably lead to increased costs.

43. If the renovation of the Secretariat Building overruns, additional lease expenses will be incurred. Staff moves from the Secretariat Building are scheduled between June and October 2009. Potentially, there is an opportunity to start first strip demolition (preparatory tasks, such as removal of carpets) when a number of floors are vacated by staff between August and October 2009. However, the Office of the CMP is assuming that no work will start until the Secretary-General and his office move to the North Lawn Conference Building. The Office of the CMP is also planning that no staff will move back into the Secretariat Building until all of the floors are completed. However, there might be opportunities to move staff back to the top floors of the Secretariat Building while the work continues on the lower floors. There are various ways to

minimize disruption to remaining staff that may be considered. For example, noisy work could be conducted outside United Nations normal working hours.

Recommendation 6

(6) The Office of the Capital Master Plan in coordination with the Department of Safety and Security should consider the possibility of first strip demolition in the Secretariat Building before the Secretary-General's move to the swing space in order to make up for past slippages and avoid additional lease expenses.

44. *The Office of the CMP accepted recommendation 6 and stated that it would be implemented by 30 October 2009. Recommendation 6 remains open pending receipt of documentation showing that it has been implemented.*

F. Managing interfaces between the CMP and other pre-existing contracts

45. OIOS reviewed a list of all active maintenance contracts identified by the FMS. FMS also identified systems that will have to remain operational during the CMP's execution. The new contracts to keep these systems operational are currently being negotiated by the Procurement Division.

46. FMS has started the take over of the 380 Madison Avenue swing space. However, the handover procedures are not yet finalized. The Office of the CMP, the Office of Information and Communication Technology and the Department of Safety and Security are working to finalize handover procedures. (This was the case at the time of the audit. Staff now occupy parts of the swing space at 380 Madison Avenue).

V. ACKNOWLEDGEMENT

47. We wish to express our appreciation to the Management and staff of the Office of the CMP, the consultant programme manager and the construction manager for the assistance and cooperation extended to the auditors during this assignment.

STATUS OF AUDIT RECOMMENDATIONS

Recom. no.	Recommendation	Risk category	Risk rating	C/O ¹	Actions needed to close recommendation	Implementation date ²
1	The Office of the Capital Master Plan's Director of Construction should keep the need for project management resources under close review and, if necessary, initiate the recruitment of additional project management staff through the Assistant Secretary-General and Executive Director, Capital Master Plan.	Human Resources	Medium	O	The Office of the Capital Master Plan's review of project management requirements that is planned on completion of swing projects.	31 March 2010.
2	The Office of the Capital Master Plan should establish procedures whereby cases of fraud and misconduct are reported to the Under-Secretary-General, OIOS and the Controller.	Operational	High	C	No further action required. The Office of the Capital Master Plan has arranged that the integrity monitoring consultant will send a copy of his reports directly to OIOS. Also, the OUSG, Department of Management is kept informed of any issues by the Office of the Capital Master Plan.	Implemented.
3	The Office of the Capital Master Plan should ensure that invoices are paid within 30 days in accordance with contractual requirements. Invoice amounts pertaining to work satisfactorily completed should be settled and any balance amount held back (for example, in the event of disagreement or dispute) should be settled on resolution.	Financial	High	O	The Office of the Capital Master Plan has stated that the necessary action has been implemented. Control of payments will be the subject of recurring CMP audits, and further review will be included in a forthcoming audit of project budgeting and financial control.	

Recom. no.	Recommendation	Risk category	Risk rating	C/O	Actions needed to close recommendation	Implementation date ²
4	The Office of the Capital Master Plan should follow up with the Office of Central Support Services to obtain clarification on procedural and control requirements pertaining to the delegation of authority to approve change orders.	Operational	Medium	C	No further action required. OCSS has now responded and given the required clarification.	Implemented.
5	The Office of Central Support Services should establish an ex post facto committee that will review change orders approved by the Assistant Secretary-General and Executive Director of CMP.	Governance	High	O	The establishment of an ex post facto committee for the review of change orders approved by the Assistant Secretary-General and Executive Director of CMP.	Not provided. (Dependent on action by OCSS).
6	The Office of the Capital Master Plan in coordination with the Department of Safety and Security should consider the possibility of first strip demolition in the Secretariat Building before the Secretary-General's move to the swing space in order to make up for past slippages and avoid additional lease expenses.	Operational	High	O	Documentation showing that the recommendation has been implemented.	30 October 2009.

1. C = closed, O = open
2. Date provided by Office of the Capital Master Plan in response to recommendations.