



OIOS

Office of Internal Oversight Services

INTERNAL AUDIT DIVISION

AUDIT REPORT

Capital Master Plan project budgeting and financial control processes

The Office of the Capital Master Plan is applying effective financial controls, but further improvements are needed in the area of budget preparation and monitoring, and this will need the support of other departments

14 April 2010

Assignment No. AC2009/514/06

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: 14 April 2010

Mr. Michael Adlerstein, Assistant Secretary-General and
Executive Director, Capital Master Plan

REFERENCE: IAD: 10- 00265

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

Fatoumata

SUBJECT: **Assignment No. AC2009/514/06 - Audit of Capital Master Plan project budgeting
and financial control processes**
OBJET:

1. I am pleased to present the report on the above-mentioned audit.
2. Based on your comments, all recommendations will remain open in the OIOS recommendations database as indicated in Annex 1. In order for us to close the 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 1 and 2), in its annual report to the General Assembly and semi-annual report to the Secretary-General.

cc: Mr. Jun Yamazaki, Assistant Secretary-General, Controller, Office of Programme Planning, Budget and Accounts
Mr. Swatantra Goolsarran, Executive Secretary, UN Board of Auditors
Ms. Susanne Frueh, Executive Secretary, Joint Inspection Unit
Mr. Moses Bamuwamye, 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 Capital Master Plan project budgeting and financial control processes

OIOS conducted an audit of Capital Master Plan (CMP) project budgeting and financial control processes. The overall objective of the audit was to assess the adequacy of budgetary control, management information, financial planning, and payments as they relate to the capital master plan. The audit was conducted in accordance with the International Standards for the Professional Practice of Internal Auditing.

In OIOS' opinion, the Office of CMP is applying effective financial controls. Furthermore, review and approval of invoices and payments includes appropriate checks and balances to ensure accountability and a formal process for approving payments. However, further improvements are needed in the area of budget preparation and monitoring, which will also require the support of other departments.

The major findings were as follows:

- (a) The provision for contingencies/escalation costs may not be sufficient to cover actual expenditures.
- (b) The budget submission for associated costs prepared by OPPBA covers the period 2008 to 2012 but does not include projected expenditures for 2013, when the completion of CMP is scheduled.
- (c) The timeliness of payments to the construction manager has improved but further efforts are needed in order to comply with the contractual obligations.

OIOS has made five recommendations that include reviewing the calculation of contingencies/escalation costs and improving the timeliness of payments to the construction manager. The Office of CMP accepted all the recommendations and has initiated action to implement them.

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I. INTRODUCTION

1. The Office of Internal Oversight Services (OIOS) conducted an audit of CMP project budgeting and financial control processes. The audit was conducted in accordance with the International Standards for the Professional Practice of Internal Auditing.
2. The current budget of \$1,876.7 million for CMP was approved by the General Assembly in its resolution 61/251 of 22 December 2006. As at September 2009, it was projected that the CMP would be subject to a cost overrun of \$91.371 million.
3. Several departments of the Secretariat requested temporary increases in staffing and operational costs to support the construction activities of CMP. These increases, as well as ongoing capital improvements and investment costs, have been identified as associated costs related to CMP.
4. The General Assembly, in its resolution 63/270, decided that the resources approved for associated costs for CMP will be financed from within the approved budget of CMP unless otherwise specified by the General Assembly. The associated costs for the biennium 2008-2009 amounted to \$30.272 million. The General Assembly in its resolution 64/228 approved associated costs in the amount of \$42.069 million for 2010 to be financed from within the overall budget of CMP.
5. This was the second audit of CMP project budgeting and financial control processes. The first audit report on this subject (Assignment No. AC2008/514/04) was issued on 9 January 2009.
6. Comments made by the Office of CMP are shown in *italics*.

II. AUDIT OBJECTIVES

7. The main objectives of the audit were to:
 - (a) Determine whether the budgetary provision for CMP is adequate, and whether remedial action has been taken to bring the budget back on track, as necessary;
 - (b) Assess the adequacy of financial planning as it applies to CMP and the system for monitoring costs against budget;
 - (c) Ascertain whether management information has been adequate and acted upon as necessary; and
 - (d) Determine whether payments were duly authorized, correct and timely.
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III. AUDIT SCOPE AND METHODOLOGY

8. OIOS reviewed budgets, cash flow projections and monthly status reports relating to CMP. OIOS reviewed invoices from the construction manager, payment confirmations and the timeframes within which the United Nations paid the construction manager. OIOS also interviewed personnel of the Office of CMP, the Office of Programme Planning, Budget and Accounts (OPPBA), the construction manager and the consultant project manager.

IV. AUDIT FINDINGS AND RECOMMENDATIONS

A. The capital Master Plan budget

9. The seventh annual progress report of the Secretary-General on the implementation of the capital master plan (A/64/346) dated 16 September 2009 presented the following projected costs (see Table 1). OIOS has determined the variances for the period from September 2008 to September 2009 in the right hand column.

Table 1: Capital master plan projected costs as at September 2009
(Millions of United States dollars)

	<i>As at September 2008</i>	<i>As at September 2009</i>	<i>Variance</i>
	<i>(1)</i>	<i>(2)</i>	<i>(2)-(1)</i>
Renovation			
Construction	1,032.900	1,057.402	24.502
Professional fees, management costs	280.340	302.365	22.025
Subtotal	1,313.240	1,359.767	46.527
Swing space estimate			
Office swing space	273.441	273.622	0.181
Library swing space	2.714	2.714	-
Conference swing space	149.540	150.545	1.005
Subtotal	425.695	426.881	1.186
Total cost for renovation and swing space	1,738.935	1,786.648	47.713
Contingency/escalation	235.236	181.423	(53.813)
Total project	1,974.171	1,968.071	(6.1)
Approved budget	1,876.700	1,876.700	-
Projected cost overrun	97.471	91.371	(6.1)

10. The overall projected cost over-run has reduced by \$6.1 million since the last report.

11. OIOS, in its report on the project budgeting and financial control dated 9 January 2009 (Assignment No. AC2008/514/04), recommended that the Office of CMP include a brief explanation of cost variances in the Secretary-General's annual progress reports to the General Assembly on the implementation of CMP. OIOS is of the opinion that the seventh annual progress report (A/64/346) does not include sufficient explanation of the variances, and therefore this recommendation will remain open in the OIOS database.

12. The reasons for the cost variances were discussed by OIOS with the consultant programme manager and the following breakdowns with regard to construction costs, professional fees and management costs and conference swing space were received.

Table 2: Analysis of cost variances for the period from September 2008 to September 2009
(Millions of United States dollars)

	Increase/(decrease)
Construction costs	
- transfer from contingency	6.939
- projected costs for basement and mechanical, electrical and plumbing infrastructure	18.905
- projected costs for exterior wall	(1.342)
Total increase for construction costs	24.502
Professional fees and management costs	
- existing condition and capacity review	2.740
- blast design	3.156
- renovation design	2.037
- swing space design	5.245
- CMP staff	7.500
- other costs	1.347
Total increase for professional fees and management costs	22.025
Conference swing space	
- construction cost	1.005

Note: Variance for office swing space of \$ 0.181 millions (shown in Table 1 above) is not considered material and therefore not included in the Table 2.

13. The \$53.813 million decrease in contingency/escalation costs (shown in Table 1 above) is due to the change in the basis for calculating contingency/escalation costs. In the previous progress report, the contingency/escalation costs were calculated as 5 per cent of committed costs and 20 per cent of estimated future costs. The current progress report calculated contingency/escalation costs as 10 per cent of the actual value of signed guaranteed maximum price (GMP) contracts, and 20 per cent of projected unsigned GMP contracts. OIOS analysis of ongoing projects showed that the change orders for the three swing space renovations (North Lawn Conference Building, 305 E 46 Street and 380 Madison Avenue) exceeded 10 per cent of the original contract amounts as indicated in the Table 3.

Table 3: Percentage of change orders to the value of GMP contracts
(Millions of United States dollars)

<i>Guaranteed maximum price</i>	<i>Approved GMP value</i>	<i>Approved change orders as at December 2009</i>	<i>Percentage of change orders to GMP</i>
North Lawn Conference Building	133.306	22.633	17
Swing space-305 E 46 Street	22.158	3.291	15
Swing space-380 Madison Ave	34.033	14.998	44
United Nations Federal Credit Union Building (UNFCU)	8.589	0.00091	0.012
Contract B-Package 1	12.645	0.579	5
Contract B-Package 2	166.893	0.295	0.18
Curtain wall	128.338	1.189	0.93
Hoist	20.934	0.073	0.35
Furniture for swing space	13.745	0.308	2.24

14. The figures in Table 3 show that the change orders for mature swing space projects like North Lawn Conference Building, 305 E 46 Street and 380 Madison Avenue vary between 15 and 44 percent which will increase further because of the number of unapproved change orders. However, the UNFCU fit out was conducted in a brand new building for a predetermined user resulting in a small percentage of change orders. Other projects are still in their infancy. The Office of CMP explained that the high percentage of change orders for swing spaces is a result of multiple redesigns due to the changes in user requirements. The reason for change orders and controls over change orders are the subject of another audit (AC2009/514/03) that is proceeding concurrently with this audit.

15. OIOS discussed with the Office of CMP and the consultant project manager whether the calculated contingency/escalation costs of 10 per cent of the actual value of signed GMP contracts is reasonable. The Office of CMP considers that 10 per cent of the contract value is a prudent estimate and should

be sufficient for other GMP contracts since their design is complete. However, OIOS notes that there has been no decision on the allocation of space for the Secretariat after renovation, and there is a risk that user requirements may further escalate costs for redesign and change orders. Furthermore, the 10 per cent contingency amount will only cover contingencies without consideration for potential escalation and inflation. OIOS is of the opinion that the Office of CMP needs to review the reasonableness of contingency/escalation costs at least annually to ensure that CMP projections are realistic.

Recommendation 1

(1) The Office of CMP should review the calculation of contingency/escalation costs at least annually and make adjustments as necessary to keep projections for cost over-runs realistic.

16. *The Office of CMP accepted recommendation 1 and stated that it has been implemented. The contingency/escalation costs are reviewed annually. Recommendation 1 remains open pending OIOS' review of the next annual progress report.*

17. The General Assembly resolutions 63/269, 63/270 and 64/228 requested the Secretary-General to absorb, within the approved budget of CMP, the requirements of secondary data centres and associated costs for the biennium 2008-2009 and 2010. Table 4 below also shows the projected requirements for associated costs for 2011-2012. This information was submitted in the report of the Secretary-General to the General Assembly A/64/346 Add. 2.

18. The associated costs are covered in more detail in Section C of this report.

Table 4: Overall financial requirements of the capital master plan
(Millions of United States dollars)

	<i>Projected requirements</i>
Capital master plan project	1,968.071
Secondary data centre for 2008-2009 (A/RES/63/269)	5.100
Associated costs for the biennium 2008-2009 (A/RES/63/270)	30.300
Associated costs for 2010 (A/RES/64/228)	42.070
Risk mitigation measures to protect data and the information and communications systems of the Secretariat during construction work under the capital master plan for the biennium 2010-2011 (A/RES/64/228)	11.644
Estimated associated costs for 2011-2012 (A/64/346 Add.2)	91.875
Total requirements to be financed from the approved capital master plan budget	2,149.060
Approved capital master plan budget	1,876.700
Variance against approved budget	272.360

19. OIOS is of the opinion that the magnitude of the projected costs to be absorbed by the CMP budget presents a major risk to completing the CMP within budget. OIOS will continue to monitor the issue of associated costs and the ability of the Office of CMP to complete the project within the budget.

B. Monitoring and controlling the capital master plan budget

20. OIOS reviewed the monthly report for November 2009 produced by the consultant programme manager. The monthly status report provides the latest update on the project, including the estimated budget forecast, projected costs to complete the project, status of appropriations, expenditures and disbursements, as well as an update to the project schedule.

21. However, the monthly reports do not provide a clear comparison between budgeted costs and actual costs over time to enable a quick assessment of overall project performance. OIOS, in its report on the project budgeting and financial control (AC2008/514/04) dated 9 January 2009, recommended that the Office of CMP supplement the existing management information by monitoring project progress against 'earned value'. The Office of CMP accepted the recommendation, but unfortunately it proved to be impractical due to the complex nature of the multiple GMP contracts composing the project.

22. OPPBA receives the monthly status reports for information purposes. OPPBA periodically extracts expenditure reports from the Integrated Management Information System (IMIS), to ensure that there are no over-expenditures within the different classes of expenditures. OPPBA sends a reminder to the Office of CMP to request reclassification between the classes of expenditures if needed. OIOS' review of the expenditure report for November 2009 confirmed that there were no over-expenditures within the classes of expenditures.

23. The Office of CMP maintains detailed project information on GMP contracts, change orders, purchase orders, invoices received, and disbursements in NOVA, the CMP plan project database. NOVA also contains information on invoices approvals and payment recommendations. Total project expenditures recorded in NOVA together with personnel, travel, office supplies and materials expenditures are recorded in IMIS. IMIS has no capabilities to monitor CMP's actual expenditures against the budget, since IMIS records allotments and expenditures on a biennium basis and CMP budget was approved for the duration of the project. Limitations in IMIS capabilities mean that OPPBA has to largely rely on the monthly status reports from the Office of CMP.

C. Associated costs

24. The General Assembly, in its resolution 63/270, decided that the associated costs for CMP will be financed from the approved budget of CMP unless otherwise specified by the General Assembly. The report of the

Secretary-General on proposals for financing the associated costs for 2010 from the approved CMP budget includes the following requirements:

Table 5: Summary of resource requirements for associated costs by budget section
(Millions of United States dollars)

	<i>Approved 2008-2009</i>	<i>Estimated 2010</i>	<i>Estimated 2011-2012</i>
Department for General Assembly and Conference Management	0.995	0.645	1.319
Department of Public Information	3.823	30.035	—
Office of Central Support Services	11.720	6.141	66.727
Construction, alteration, improvement and major maintenance at Headquarters	4.521	2.289	1.500
Department of Safety and Security	7.576	10.358	21.033
Office of Information and Communications Technology	1.636	0.644	1.295
Total	30.272	50.114	91.875

25. OPPBA informed OIOS that associated costs for 2013 have not been projected and included in the estimated costs shown above. This is contrary to the report of the Secretary-General on proposals for financing the associated costs for 2010 which indicates estimated resource requirements from 2011 to 2013. OPPBA explained that if the renovation of the Secretariat building is completed in 2012 as planned, the associated costs needed to cover CMP related activities in 2013 should be marginal. These costs will mostly include staffing costs for the Department of Safety and Security. As some costs are dependant on the duration of the project, there is a risk that associated costs will increase if the CMP project schedule slips. OPPBA further indicated that the associated costs budget is submitted for consideration annually. The 2013 estimates will be calculated after the consideration of the effect of updated schedule information on the associated costs projections.

26. The Office of CMP has weekly coordination meetings with the Office of Central Support Services, the Department of Safety and Security, the Department of Public Information and the Office of Information and Communications Technology. These meetings are used to discuss move schedules, procurement and installation of broadcast equipment, and secondary data centre issues, etc. However, there are no coordination meetings on associated costs. The report of the Advisory Committee on Administrative and Budgetary Questions A/64/7/Add.5 noted “a lack of adequate planning and coordination of the associated costs for the various departments and offices involved with the capital

master plan” and “encourages the Secretary-General to make every effort to ensure close coordination of activities across departments involved in the capital master plan to ensure that the project is completed on time and within the approved budget, and stresses the importance of designating a focal point in this regard.” The Office of CMP informed OIOS that a coordination committee will be set up for this purpose by the Office of the Under-Secretary-General for Management.

Recommendation 2

(2) The Office of CMP, in cooperation with the Office of Programme Planning, Budget and Accounts, should use the coordination committee to consult with other departments to ensure that estimates for associated costs are kept up to date and cover the entire programme of the capital master plan.

27. *The Office of CMP accepted recommendation 2 and stated that the coordination committee is yet to be established by the Office of the Under-Secretary-General for Management. The recommendation will be implemented upon the establishment of the committee.* Recommendation 2 remains open pending its full implementation.

D. Payments

28. OIOS reviewed 6 invoices amounting to \$51.634 million, which represented 58 per cent of the invoices issued by the construction manager for the North Lawn Conference Building between May and November 2009. Each invoice is supported by copious documents and consists of three parts. 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 only included allowable expenses, and supporting documents such as receipts and invoices were filed. OIOS performed a test through Interactive Data Extraction and Analysis software to identify double billing for reimbursable expenses since the start of the project, but found no duplications. The Office of CMP does not have an inventory for the office equipment purchased for the construction manager’s staff. The consultant programme manager informed OIOS that it was aware of the issue and had initiated a review of all previously issued invoices to identify equipment such as laptops and printers purchased for the project to enable the creation of an inventory log.

(b) **Trade costs and allowances.** OIOS checked: (i) the construction manager’s invoices; (ii) applications and certificates for payment that are 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 CMP, the consultant programme manager, the architects/engineers and the construction manager. No errors or exceptions were noted.

(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 to check for accuracy. The consultant programme manager performs similar reviews for each invoice and recommends payment to the Office of CMP. OIOS' calculation showed that the construction manager over billed the insurance portion for the North Lawn Conference Building by \$555,863. The construction manager and the consultant programme manager explained that the entire amount of insurance costs for the subproject is billed by the construction manager in the first invoice and is based on the subproject GMP in accordance with Article 10.10.1. The difference of \$555,863 is due to the deduction of \$4.053 million in allowances not fully expended that resulted in the decrease of total GMP costs as per Amendment No. 4 to the GMP contract dated 2 April 2009. Furthermore, the Amendment No. 4 also incorporated minimum trade contract buyout savings in the amount of \$2 million that decreased the GMP contract amount. However, the calculation of insurance did not reflect the above mentioned decreases in the GMP contract. The consultant programme manager indicated that Article 10.15 of the construction management agreement with GMP stipulates that upon completion of the project, a true-up of insurance costs will be performed and any over-payments credited to the UN. Also the cost of indicated buyout savings remains subject to verification by the parties. OIOS is of the opinion that since the above decreases in the GMP costs have significantly impacted on the insurance costs, they should have been adjusted at the time when Amendment No. 4 to the GMP contract was signed. OIOS checked the insurance costs for two other GMP contracts and there were smaller variances that should be easily adjusted during the true-up process.

29. OIOS found that the overall process for invoice review by the consultant programme manager and the Office of CMP includes adequate separation of duties and different levels of review. There are no materiality levels set and all discrepancies are investigated. After the consultant programme manager performs detailed checks, each invoice is reviewed and approved in NOVA by the Director of Construction, the Finance Officer and the Chief, Administration and Communications. OIOS determined that payments were withheld in instances when deliverables had not been achieved or supporting documentation missing.

30. The GMP contracts allow up to 30 days for the UN to make payments to the construction manager. However, OIOS found that it took between 35 and 49 days for the Office of CMP to pay the invoices reviewed.

Recommendations 3 to 5

The Office of CMP should:

- (3) Ensure that it has an inventory of equipment purchased by the construction manager for the subprojects and request the construction manager staff to sign for the assets received. Upon closure of swing space field offices, these assets should be transferred to other subprojects;**
- (4) Immediately seek reimbursement from the construction manager for the insurance costs overpaid for the North Lawn Conference Building; and**
- (5) Improve the timeliness of payments to the construction manager in accordance with contractual requirements.**

31. *The Office of CMP accepted recommendation 3 and stated that the construction manager has been requested to provide an updated inventory of all assets acquired by the Office of CMP. The assets from swing space field offices are currently being transferred to other subprojects. OIOS reiterates that the inventory records of assets purchased for the construction manager by the Office of CMP should be compiled and maintained by the Office of CMP. Recommendation 3 remains open pending creation of the inventory log by the Office of CMP.*

32. *The Office of CMP accepted recommendation 4. The Office of CMP commented that since the Amendment 4 did not stipulate any adjustments to the insurance amounts, the difference referred to by OIOS should not be considered overpayment. Nevertheless, the Office of CMP stated that it has mutually agreed with the construction manager to do an interim true up. Recommendation 4 remains open pending review of the results of the interim true-up.*

33. *The Office of CMP accepted recommendation 5 and stated that payments to the construction manager are processed only when invoices recorded as final are submitted to the Office of CMP by the construction manager. The Office of CMP stated that it will seek clarification from the construction manager on the delays in issuing final invoices. Recommendation 5 remains open pending receipt of written clarification on the timeliness of payments issued by the construction manager.*

V. ACKNOWLEDGEMENT

34. We wish to express our appreciation to the Management and staff of the Office of CMP, OPPBA, 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 CMP should review the calculation of contingency/escalation costs at least annually and make adjustments as necessary to keep projections for cost overruns realistic.	Financial	High	O	Issuance of the next annual progress report.	4 Qtr. 2010
2	The Office of CMP, in cooperation with the Office of Programme Planning, Budget and Accounts, should use the coordination committee to consult with other departments to ensure that estimates for associated costs are kept up to date and cover the entire programme of the capital master plan.	Financial	High	O	Establishment of the coordination committee and full implementation of the recommendation.	June 2010
3	The Office of CMP should ensure that it has an inventory of equipment purchased by the construction manager for the subprojects and request the construction manager staff to sign for the assets received. Upon closure of swing space field offices, these assets should be transferred to other subprojects.	Financial	Medium	O	Compilation of the inventory log by the Office of CMP.	June 2010
4	The Office of CMP should immediately seek reimbursement from the construction manager for the insurance costs overpaid for the North Lawn Conference Building.	Financial	Medium	O	Performance of a true-up between the Office of CMP and the construction manager.	July 2010
5	Improve the timeliness of payments to the construction manager in accordance with contractual requirements.	Financial	Medium	O	Receipt of written clarifications from the construction manager on the timeliness of payments.	May 2010

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