SUBJECT: Audit Report 2008-13 - Long Term Contract Review – Canada Fibers Ltd. (CM09010) (City Wide)

RECOMMENDATION:

(a) That Report CM09010 respecting Audit Report 2008-13, Long Term Contract Review, Canada Fibers Ltd., be received; and

(b) That the management actions plans as detailed in Appendix “A” of Report CM09010 be approved and the Acting General Manager of Public Works direct the appropriate staff to have the plans implemented.

Ann Pekaruk
Director, Audit Services
City Manager's Office

EXECLUTIVE SUMMARY:
The 2008 Internal Audit work plan approved by Council included the review of the long term contract with Canada Fibers Ltd. (the “Contractor”) to operate the Material Recovery Facility (MRF), the drop off location for recyclable materials (fibres [paper and cardboard]) and containers (plastics, glass, aluminium cans). The City’s management and administration of the contract was assessed as well as the Contractor’s and City’s compliance with individual contract terms and clauses.
The results of the review are included in a formal audit report attached as Appendix “A” of Report CM09010. In general, the contract has been adequately managed with both parties adhering to the significant requirements and terms of the contract. Some administrative issues had been identified and corresponding recommendations were made. Such recommendations include: amendments to the contract to clearly define “parts” in the maintenance clause and to correct the cost sharing factor for contamination audits; review and updating of documented procedures; and the retention of documentation to support charges on the monthly invoices.

BACKGROUND:
The original contract between the City and Canada Fibers Ltd. (the “Contractor”) covered a term of March 31, 2003 to December 31, 2005 and was subsequently extended for several one year terms. It is now set to expire in 2013 to align with the expiration dates of other waste contracts. The Contractor is to operate the Material Recovery Facility (MRF) in conformance with the contract, including receiving and processing recyclable materials delivered to the MRF, handling, sorting and marketing of the processed materials and disposing of the residue generated. The Contractor is also responsible for the maintenance of equipment and the management of personnel on site.

The MRF processed 40,025 MT of mixed fibre and container recyclables in 2007 (33,692 MT year-to-date November 2008). The Contractor was paid $2.11 million in 2007 ($1.24 million for year-to-date November 2008) under the terms and formulas of the contract.

The fieldwork for this review was conducted in November and December, 2008. The work focused on compliance with the terms of the contract and the administration of the agreement by the Waste Management Division of the Public Works Department.

The Audit and Administration Committee receives and approves final audit and review reports as its responsibilities for the oversight of governance and control.

ANALYSIS/RATIONALE:
Within the contract, there are many clauses and schedules which define specific terms and conditions to be met by the Contractor and the City. This review focused on the following Articles and Schedule:

- Article 3 Scope of MRF Operation and Maintenance Services
- Article 4 Maintenance of Material Recovery Facility, Equipment and Rolling Stock
- Article 5 Term of Contract
- Article 6 Compensation
- Article 12 Delivery and Collection Days
- Article 19 Contract Coordinator and Administrator of the Contract Designate
- Article 23 Reporting, Spills and Emergency Response
- Article 24 Claims Procedure and Contingency Plan
- Article 25 Workplace Safety and Insurance Board
- Article 26 Insurance
- Article 31 Performance of Contract Security
- Schedule C Compensation
Details of the review of the Articles and Schedule are provided in Appendix “A” of Report CM09010.

Based on Internal Audit’s on-site observation, review of records and documentation and discussion with management of the City’s Waste Management section, the operational requirements of the contract have been met.

However, some administrative matters need to be addressed. The recommendations made in this regard were:

- Review and updating of existing procedures with evidence of an annual review documented.
- Clarity in the definition of “part” for routine maintenance costs.
- Correction of cost sharing factor in the contract for contamination audits.
- Retention of documentation to support charges on the monthly invoices for processed materials.

Staff agreed with these recommendations and provided management responses as noted in Appendix “A”.

As part of the contract, there is a Certificate of Approval (CofA) issued by the Ontario Ministry of the Environment regarding the MRF operation, the terms of which must be complied with by the City and the Contractor. Having supplied the City’s Legal Services with various documentation and evidence collected during Internal Audit’s review, the Legal Services’ review did not reveal any significant issues of non-compliance with respect to the CofA. Some issues were identified for staff consideration to provide stronger compliance with the documentary requirements of the CofA for the MRF. Waste Management staff have indicated appropriate measures have or will be taken.

**ALTERNATIVES FOR CONSIDERATION:**
Not applicable.

**FINANCIAL/STAFFING/LEGAL IMPLICATIONS:**
None.

**POLICIES AFFECTING PROPOSAL:**
None.

**RELEVANT CONSULTATION:**
- Management and staff of Waste Management Division of Public Works Department
- Contractor – staff of Canada Fibers Ltd.
- City’s Legal Services
CITY STRATEGIC COMMITMENT:

By evaluating the “Triple Bottom Line”, (community, environment, economic implications) we can make choices that create value across all three bottom lines, moving us closer to our vision for a sustainable community, and Provincial interests.

Community Well-Being is enhanced. ☑ Yes ☐ No
The provision of efficient and effective waste disposal facilities is important to the residents of the community.

Environmental Well-Being is enhanced. ☑ Yes ☐ No
Ensuring the MRF operates in an efficient and environmentally responsive manner and in compliance with contract terms and regulations is necessary for the environmental well-being of the City.

Economic Well-Being is enhanced. ☑ Yes ☐ No
City Council's strategic commitment to "Best Practices - Best Value" under "A City That Spends Wisely and Invests Strategically" is addressed through audits and reviews and their subsequent follow up to ensure controls are in place to protect the assets of the City and promote efficient, effective and economic services and programs.

Does the option you are recommending create value across all three bottom lines? ☑ Yes ☐ No

Do the options you are recommending make Hamilton a City of choice for high performance public servants? ☐ Yes ☑ No

ap:dt
Attachment – Appendix “A”
Background
On March 31, 2003, a contract (the Contract) was entered into by the City of Hamilton (the City) and Canada Fibers Ltd. (the Operator) to carry out the operation at the Material Recovery Facility (MRF) in conformance with the Contract, including receiving and processing recyclable materials delivered to the MRF, handling, storing and marketing of the processed materials and disposing of all residue generated. The Operator is also required to maintain a safe working environment at the MRF and to administer all facets of the Facility such as maintenance of equipment and management of personnel on site.

As part of the 2008 Internal Audit work plan, Council approved the review of the long-term Contract between the City and the Operator. The Contract is comprised of 38 Articles and 5 appended Schedules. This review focused on the following Articles and Schedule:

Article 3 - Scope of MRF Operation and Maintenance Services
Article 4 - Maintenance of Material Recovery Facility, Equipment and Rolling Stock
Article 5 - Term of Contact
Article 6 - Compensation
Article 12 - Delivery and Collection Days
Article 19 - Contract Coordinator and Administrator of the Contract Designate
Article 23 - Reporting, Spills and Emergency Response
Article 24 - Claims Procedure and Contingency Plan
Article 25 - Workplace Safety & Insurance Board
Article 26 - Insurance
Article 31 - Performance of Contract Security
Schedule C - Compensation

Based on Internal Audit’s on site observation, review of records and documentation and corroboration obtained from the management of the City’s Materials Recycling Section, the operational requirements from the Contract have been met but some administrative issues need to be addressed for compliance with the Contract.

Details of the above focused Articles and Schedule are provided in the following text with further information and comments provided as needed. In addition, recommendations for strengthening the process and ensuring compliance with the stated terms of the Contract will be made at the end of this report along with the corresponding management responses noted.

Focused Articles and Schedules
Article 3 – Scope of MRF Operation and Maintenance Services
- Sections 4 to 9 stipulate requirements for processing of recyclable materials including Operator staffing levels. Based on audit work performed, the Operator is in compliance with this Article.
Article 4 – Maintenance of Material Recovery Facility, Equipment and Rolling Stock

Sections 10 to 15 dictate requirements for the preventative maintenance of equipment at the MRF and the responsibility for the associated costs. There is compliance with Article 4 except for the following:

- Section 12 c) stipulates that payment responsibility for routine maintenance costs for parts of the City-owned processing equipment be shared 50/50 for any part costing between $1,000 and $5,000 (a part costing under $1,000 is solely the Operator's responsibility and any part costing more than $5,000 is the City’s responsibility). “Part” is further defined in this clause as a single unit and not the accumulation of single units. Using Internal Audit's interpretation that unit costing applies to the part itself, a review of maintenance invoices revealed some instances in which the City appears to have overpaid as individual parts’ unit costs were under the $1,000 threshold but the gross invoice accumulated costs of several of the same part amounted to between $1,000 and $5,000. The total overpayment for this interpretation on the review of seven monthly maintenance charges amounted to approximately $5,000. Both City and Operator management disagree with Internal Audit's interpretation and have stated that this clause was meant to refer the per unit pricing to a single unit of equipment, not a single part. Due to the disagreement and the definitions in the current Contract, Internal Audit is indicating non-compliance.

Article 5 – Term of the Contract

- Sections 16 to 18 stipulate the Contract period and the options for extending the Contract period. Based on audit work performed, Council approval was sought and granted for extensions to the Contract period. The City and Operator are in compliance with this Article.

Article 6 – Compensation

Section 19 outlines the compensation that the City agrees to pay the Operator for operation of the MRF. There is compliance with Article 6 except for the following:

- Section 19 a) notes that records provided with each invoice are to be maintained by the Operator and/or the City. Based on Internal Audit’s sampling of invoices from 2003 to 2008, there were instances where supporting information (i.e. invoices for maintenance items) to the Operator’s monthly invoice was not on file with the City and/or Operator. These omissions were mainly for the years prior to 2005 with much fewer instances in the more recent past. Nonetheless, there was non-compliance with this provision.

Article 12 - Delivery and Collection Days

- Sections 29 to 30 outline the requirement that acceptable recyclable materials be discharged and processed in a timely manner. Based on audit work performed, there is compliance with this Article.

Article 19 - Contract Coordinator and Administrator of the Contract Designate

- Section 40 stipulates that the City and Operator designate representatives as Administrator (City) and Contract Co-ordinator (Operator). These designates are to meet on a regular basis. Both the City and the Operator have made such assignments. Monthly meetings are held. The City and the Operator are in compliance with this Article.
Article 23 – Reporting, Spills and Emergency Response
Sections 47 to 49 outline environmental responsibility for any spills that occur at the MRF. There is **compliance** with Article 23 except for the following:

- Section 49 requires the Operator to develop a written protocol for the mitigation of and appropriate remedial actions for any spill. The Operator is also required to review this protocol annually.

  Based on Internal Audit’s review, such protocol is in place so the Operator is **in compliance** as far as developing the protocol. The original protocol (dated March 2006) remains in effect and thus requires no amendment. However, at the time of the audit, there was no evidence of the Operator’s annual review of this protocol as required under this section. In this regard, there is **non-compliance**.

Article 24 - Claims Procedure and Contingency Plan
- Section 50 stipulates the Operator’s responsibility for dealing with claims made by third parties and the requirement for written procedures and a contingency plan to deal with work stoppages. Based on the work performed, the Operator is **in compliance** with this Article.

Article 25 - Workplace Safety & Insurance Board
- Section 51 notes that the Operator shall submit a Clearance Certificate from the Workplace Safety & Insurance Board (WSIB) and keep this certificate in good standing. Based on audit work performed, the Operator is **in compliance** with this Article.

Article 26 – Insurance
- Section 52 sets out the requirement for insurance certificates to be obtained and maintained by the Operator. There is **compliance** with Article 26.

Article 31 - Performance of Contract Security
- Section 57 sets out detailed requirements for a letter of credit and performance bond from the Operator serving as security in the performance of the Contract. There is **compliance** with Article 31.

Schedule C – Compensation
- Schedule C lists the payment rate per tonne for processed recyclable materials at the MRF under the Contract. Based on audit work performed, there is **compliance** with Schedule C.
Recommendations and Management Responses

Definition of “part” for Maintenance Costs

It is recommended:
• That the Contract revision (dated January 1, 2008) currently under review be adjusted to incorporate precise wording more definitive of the meaning of “part” wording in regard to the City and Operator responsibility for routine maintenance costs for parts as per 12 c) of the current Contract.

Management Response:
Agreed. Section 12 of the revised Contract has been adjusted to clarify the original intent of this Section. The original clause in the RFP was meant to refer the per unit pricing to a single unit of equipment, not a single part and this was confirmed with the consultant hired to assist City staff in the preparation of the request for proposal specifications. The revised wording reflects how the parties have been operating and clarifies the intent so as to avoid any misinterpretations.

Supporting Documentation

It is recommended:
• That all supporting documentation to the monthly invoices for processed materials be retained at all times by the City and/or Contractor to ensure compliance with section 19 a) of the Contract.

Management Response:
Agreed. Files containing copies of invoices and supporting documentation to those invoices are retained in the Division’s Finance and Administration (F&A) area. Original invoices and supporting documentation are retained corporately. As noted in the auditor’s comments, retention of the supporting documentation has improved in recent years. Copies of invoices and supporting documentation will continue to be maintained within the F&A area of the Division with added attention paid to those vendor files requiring additional documentation to satisfy contractual obligations. In addition, the Contractor retains all supporting documentation not on site but at their head office location.
Annual Procedures Review

It is recommended:
• That existing procedures such as the written protocols for spills and the Operator Operations Plan be reviewed annually and updated, as appropriate, with evidence of review documented for future reference.

Management Response:
Agreed. The written protocol which is contained in the Contractor’s Operations Plan has been reviewed. A sign-off section will be included on the protocol and operations plan that references the date of the annual review and signature by both City and contractor staff who conducted the review. In addition, staff will incorporate this item in the monthly contract administration meetings under “Important Dates” so that both parties are aware of this annual requirement and the impending date for review.

Other

As per Article 1 (Schedules and Definitions), section 2 v) states that the cost of contamination audits are to be shared by the Operator (2/3) and the City (1/3). Review of several monthly invoices shows the cost sharing at 50/50. From 2006 to September 2008, the overpayment amounts to approximately $5,900. Divisional management has stated that this was an error in the executed Contract but has never been corrected with an amendment to read 50%. This will be corrected in the revised Contract noted above.

Management Response:
Agreed. The revised Contract has been adjusted to correct the error and reflect the 50/50 cost sharing.