

GENERAL SERVICES ADMINISTRATION OFFICE OF INSPECTOR GENERAL

**Recovery Act Report –
Peace Arch U.S. Port of Entry Redevelopment: Construction Contract
Review of PBS’s Major Construction and Modernization
Projects Funded by the American Recovery and
Reinvestment Act of 2009
Audit Number A090172/P/R/R11007**

March 4, 2011





Date: March 4, 2011

Reply to: R. Nicholas Goco
Attn of: Deputy Assistant Inspector General
For Real Property Audits (JA-R)

Subject: Recovery Act Report – Peace Arch U.S. Port of Entry
Redevelopment: Construction Contract
Review of PBS’s Major Construction and Modernization Projects Funded by the
American Recovery and Reinvestment Act of 2009
Audit Number A090172/P/R/R11007

To: Robert A. Peck
Commissioner, Public Buildings Service (P)

As part of our oversight of the General Services Administration’s American Recovery and Reinvestment Act (Recovery Act) projects, we noted contracting violations related to the Peace Arch U.S. Port of Entry (Peace Arch) redevelopment project which we believe warrant your attention. Specifically:

- The construction phase services were awarded as an unpriced option and the exercise of the construction option violated competition requirements; and
- Contract modifications for construction activities were exercised in a manner that resembles cost reimbursable contracting.

Construction Contract Award Does Not Meet Competition Requirements

The project’s construction phase services were awarded in a manner that violated the competition requirements of both the Federal Acquisition Regulation (FAR) and the Competition in Contracting Act (CICA).

The construction contract for the Peace Arch project was to be awarded as a Construction Manager as Constructor (CMc) contract with a Guaranteed Maximum Price (GMP). This type of contract is initially awarded for design phase services¹ at a firm-fixed price with an option for construction phase services at a GMP that is established at contract award. The GMP acts as a ceiling price for the actual construction phase services. The proposed GMP should be evaluated along with the pricing for the design services for the award to be made in accordance with FAR 52.217-5.

¹ Design phase services include activities such as ensuring the design complies with applicable regulations, codes, and standards as well as ensuring the constructability of the design.

When PBS awarded the contract on March 14, 2007, the design phase services were awarded at a firm-fixed price of \$309,176, but a GMP for the construction option was not established. The CMc contractor had submitted a GMP of \$59,977,248 for the construction option along with its offer for the design phase services, but PBS did not include it in the award. Instead, the contract award document noted the award was made with the “intent to negotiate Construction Phase Services thereafter.”

PBS began construction prior to establishing the project’s GMP and exercising the construction option. Between August 2007 and December 2008, PBS issued 14 contract modifications, totaling \$66,320,559, to incrementally authorize construction activities. It was not until April 27, 2009, via Modification 15, that PBS established the \$91,440,824 GMP and exercised the option to construct the project.

Since PBS did not establish a GMP for the Peace Arch project at contract award, construction phase services represent an unpriced option, essentially an agreement to conduct negotiations with the CMc contractor on a sole-source basis. The exercise of this option without an approved justification for other than full and open competition² violated CICA and FAR competition requirements. Further, each of the 14 modifications that GSA used to commence construction activities violated competition requirements since each was issued under the authority of the initial contract’s unpriced option for construction phase services.

PBS needs to ensure that the CMc with a GMP approach is executed correctly and in compliance with all laws, regulations, and policies.

Contract for Construction Work Resembles a Reimbursable Contract

The basis for establishing the price of construction phase services was dependent on the selected CMc contractor’s subcontract bidding process, rather than on competition at the CMc level to establish a GMP. As a result, the approach deviates from being a firm-fixed price contract and resembles a cost contract.

The Peace Arch project was intended to be awarded as a firm-fixed price contract for design phase services, with a GMP for construction phase services. Prior to exercising the construction option, the parties were to agree to an Estimated Cost of Work under the GMP. However, PBS did not formally exercise the construction option and agree to a total project price until 20 months after construction commenced. As previously mentioned, 14 contract modifications, totaling \$66,320,559, were issued for early start construction services before the project price and \$91,440,824 GMP were finalized via Modification 15 on April 27, 2009.

To determine price reasonableness for the early start construction modifications and to finalize the GMP, the contracting officer primarily relied on the CMc contractor’s subcontract bidding process. The price negotiation memorandum finalizing the project price noted that from August

² The General Services Acquisition Manual 536.270 specifies that before an unpriced option can be exercised, the agency must cite the statutory authority permitting the use of other than full and open competition.

2007 to March 2008, the CMc contractor submitted subcontract buyout packages to PBS. PBS created a “Competition Analysis” worksheet which listed these subcontract bids, and the contracting officer conducted “variance analysis” to monitor adherence to the project budget.

For example, on December 21, 2007, Modification PS04 totaling \$21,827,227 was issued for early start construction to shift selected subcontract work to the design phase. Bid packages for electrical, sheet pilings, earthwork, landscape and mechanical services were included in this modification. Pricing for these services was based on the result of the subcontract bidding. This modification awarded the amount of the low bid on three of the bid packages; a value judgment was made to use other than the low bidder on two bid packages. Additional percentages were added to Modification PS04 for bonds, insurance, and profit based on the total cost of the work on the modification.

Similarly, for the determination of the final contract price, the contracting officer relied on the subcontractor bidding process. The price negotiation memorandum noted the range of high and low bids for all the subcontractor specialties in the project; this became the basis for negotiation of the Estimated Cost of Work of \$73,868,953. This Estimated Cost of Work, plus general conditions, bonds, other direct costs, contingency, and profit became the final project price.

This approach deviates from the tenets of a CMc contract that uses the GMP to set a fixed price ceiling and shifts the financial risk to the CMc contractor. As a result, as the costs climbed from the proposed GMP of \$59,977,248 to \$91,440,824, GSA retained the full financial liability.³ Further, the decision to enter into this work prior to setting the actual GMP reduced the Government’s negotiating leverage for the final GMP as it assumes the exercise of the construction option and risked having an incomplete project if Recovery Act funding had not been provided.

Further, PBS’s decision to fund a majority of the project construction through a series of modifications with pricing based on subcontract costs represents a cardinal change⁴ to the contract. The solicitation for this project states that the Government will award construction phase services⁵ to the successful offeror through a GMP with fee. Hence, the solicitation plans on the award of the construction project as a whole through the exercise of the construction option at a fully negotiated firm-fixed price. In effect, PBS awarded construction work piecemeal and on a cost basis, instead of as a complete project with a pre-determined GMP for the construction option.

³ Some cost increase may have been the result of changes to the project scope. However, the contract file did not identify or quantify the cost increases resulting from the scope changes.

⁴ A "cardinal change" occurs when the Government effects an alteration in the work that effectively requires the contractor to perform duties materially different from those originally bargained for. While there is no absolute definition of a cardinal change, the following factors are generally considered when determining whether one has taken place: (i) whether there is a significant change in the magnitude of work to be performed; (ii) whether the change is designed to procure a totally different item or drastically alter the quality, character, nature or type of work contemplated by the original contract; and (iii) whether the cost of the work ordered greatly exceeds the original contract cost.

⁵ Construction phase services are defined as “all work and services, including general conditions, necessary for the construction of the project described by the plans.”

Additionally, awarding the CMc contract in this manner is contrary to Recovery Act guidance issued by the Office of Management and Budget. This guidance states, “to the maximum extent practicable, contracts using Recovery Act funds shall be awarded as fixed price contracts (see FAR Subpart 16.2) using competitive procedures.”

Recommendations

We recommend that the Commissioner of the Public Buildings Service:

1. Develop and implement a system of management controls to ensure that contracts using the construction manager as constructor methodology meet competition requirements and provide adequate incentives for this type of procurement.

We appreciate the support that has been provided throughout this review. If you have any questions about this memorandum, please contact me at (202) 219-0088.

Sincerely,



R. Nicholas Goco
Deputy Assistant Inspector General for Real Property Audits (JA-R)

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Management Comments



GSA Public Buildings Service

FEB 23 2011

MEMORANDUM FOR R. NICHOLAS GOCO
DEPUTY ASSISTANT INSPECTOR GENERAL FOR RFAI
PROPERTY (JA-R)

FROM: ROBERT A. PECK
COMMISSIONER
PUBLIC BUILDINGS SERVICE (P)

SUBJECT: Recovery Act Report: Peace Arch U.S. Port of Entry
Redevelopment Construction Contract
Review of PBS’s Major Construction and Modernization Projects
Funded by the American Recovery and Reinvestment Act of 2009
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The Public Buildings Service (PBS) appreciates the opportunity to comment on the subject draft audit report. The Peace Arch U.S. Port of Entry redevelopment project was originally awarded in March 2007. In April 2009, a modification was awarded under the American Recovery and Reinvestment Act to fund an escalation to the project. The project is meeting the intent of the Act in putting people back to work and strengthening the economy.

The draft report includes one recommendation to develop and implement a system of management controls to ensure that contracts using the construction manager as constructor methodology meet competition requirements and adequately incentivize the procurement.

In response to this recommendation, PBS has developed and is currently implementing a corrective action plan in response to similar concerns raised in recent audit reports on the Austin Courthouse, 50 UN Plaza, Richard H. Poff, Huntington, and Edith Green/Wendell Wyatt building modernization projects. This corrective action plan, as designed by the PBS management and approved by your office, is intended to strengthen the system of internal controls surrounding the CMc delivery method so that actions noted in these audit reports are not repeated. Accordingly, we believe the actions set forth in this plan will satisfy this recommendation.

Please note that a more comprehensive response may follow upon issuance of the final audit report or as further information comes to our attention. Should you or your staff have any questions, please contact Jennifer Smith on (202) 501-4994.

U.S. General Services Administration
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**Recovery Act Report –
Peace Arch U.S. Port of Entry Redevelopment, Blaine, Washington
Review of PBS’s Major Construction and Modernization
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Background, Objectives, Scope, and Methodology

Background

The American Recovery and Reinvestment Act of 2009 (Recovery Act) provides the General Services Administration (GSA) with \$5.55 billion for the Federal Buildings Fund. In accordance with the Recovery Act, the GSA Public Buildings Service (PBS) is using the funds to convert federal buildings into High-Performance Green Buildings as well as to construct federal buildings, courthouses, and land ports of entry. The Recovery Act mandates that \$5 billion of the funds must be obligated by September 30, 2010, and that the remaining funds be obligated by September 30, 2011. The GSA Office of Inspector General (OIG) is conducting oversight of the projects funded by the Recovery Act.

The work on the Peace Arch project began prior to the passage of the Recovery Act. Site and design funding of \$9,812,000 was provided by Congress in fiscal year 2004, and additional funding of \$46,534,000 for design, construction management, and inspection was provided by Congress in fiscal year 2006. Further, Congress approved a PBS request to reprogram \$15,706,000 in additional funds to the project in fiscal year 2008. As a result, the project had received \$72,052,000 in funding prior to the Recovery Act.

PBS determined further additional funds would be required to complete this project. After the Recovery Act was enacted, PBS selected this project as one of the Border Stations and Land Ports of Entry projects to be constructed using Recovery Act funding. PBS allocated an additional \$26,284,708 to the Peace Arch project to cover escalation costs.

Objectives

The objective of the OIG’s Recovery Act oversight is to determine if PBS is planning, awarding, and administering contracts for major construction and modernization projects in accordance with prescribed criteria and Recovery Act mandates. The work for this report was performed while evaluating the award for the construction of the Peace Arch U.S. Port of Entry Redevelopment, Blaine, Washington.

Scope and Methodology

To accomplish the objective we conducted fieldwork in the Northwest Arctic Region, reviewed the contract file and other pertinent project documents, met with project staff, and reviewed

applicable guidance and regulations. The work for this report was performed between February 2010 and October 2010.

We conducted this performance audit in accordance with generally accepted government auditing standards except as noted below. 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.

The planning for this review is based on the audit plan for oversight of the Recovery Act projects as well as audit guidance being applied to all Recovery Act projects. A separate audit guide was not prepared for this project.

As this work was performed under the continuing oversight of all GSA Recovery Act projects, management controls are currently under assessment. Only those management controls discussed in the report have been assessed.

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