



Office of Audits
Office of Inspector General
U.S. General Services Administration

Improvement Needed in PBS's Use of Construction Manager as Constructor Contracts

Memorandum Number A220057
August 17, 2022



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SUBJECT: Improvement Needed in PBS's Use of Construction Manager as Constructor
Contracts
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The purpose of this memorandum is to convey our concerns regarding PBS's award and administration of capital construction contracts using the Construction Manager as Constructor (CMc) project delivery method. Of particular concern, contracting officers need to ensure that construction contractors appropriately accumulate and report project costs. Additionally, contracting officers need to avoid making improper adjustments to the CMc contract's guaranteed maximum price (GMP), and ensure that the CMc contract's GMP is not converted to a firm-fixed price prematurely. In light of PBS's significant current and anticipated CMc workload, failure to mitigate these concerns will put PBS at considerable financial risk for overpaying for construction work.

Background

PBS is the landlord for the federal government and acquires space on behalf of its tenants through new construction and leasing. PBS's Office of Design and Construction manages GSA's design and delivery of public buildings, from pre-planning through commissioning.¹ As of June 2022, PBS reported 94 capital construction projects, with an aggregate contract value of more than \$5.5 billion.² For eight of those projects, totaling approximately \$1.2 billion, PBS used the CMc project delivery method. PBS also plans to use CMc contracts for some projects funded by

¹ Commissioning is PBS's process to ensure that building systems and assemblies are planned, designed, installed, tested, operated and maintained to meet project requirements.

² Capital construction projects are projects that exceed the congressionally mandated prospectus threshold as referenced in Section 102-73.35 of the Federal Management Regulation, which is currently \$3.375 million in Fiscal Year 2022.

the 2021 Infrastructure Investment and Jobs Act, which provided GSA with \$3.4 billion for the construction and modernization of land ports of entry.

PBS uses CMc as one of its primary project delivery methods for its capital construction projects. PBS typically uses this delivery method for large, complex projects, such as courthouses or major modernizations, when construction expertise is essential during design. Using this approach, PBS first awards a contract to an architect-engineer firm for design services. Prior to design completion, PBS awards another contract to a construction contractor to serve as the CMc. The CMc contractor provides design-phase services, such as evaluating labor and material market conditions and identifying constructability issues and potential scheduling delays. By involving the CMc contractor during design, PBS expects to reduce the likelihood of costly changes that otherwise would not be identified until construction is underway.

PBS awards CMc contracts for design-phase services at a firm-fixed price. The CMc contracts include an option for construction at a GMP. The GMP is competed as part of the base contract award, and includes the estimated cost of work, a contingency allowance, and a fixed price for the CMc contractor's fee. Once the construction option is exercised, PBS reimburses the CMc contractor for its actual construction costs, plus its fee, up to the GMP amount. During construction, PBS and the CMc contractor may agree to convert the CMc contract to a firm-fixed price contract. This should occur after 100 percent of the construction documents are completed and after contingency risks have been sufficiently reduced.

Using the CMc project delivery method, the CMc contractor accepts a degree of risk, as it is responsible for completing the project even if costs exceed the GMP. As an incentive to complete projects under budget, CMc contracts often include a shared savings clause. Under this clause, the CMc contractor is entitled to a percentage of the cost savings if the project is completed for less than the GMP.

GSA Office of Inspector General Audits of CMc Contracts Awarded Under the Recovery Act

PBS used the CMc project delivery method extensively during its implementation of the American Reinvestment and Recovery Act of 2009 (Recovery Act). During our office's oversight of GSA's Recovery Act implementation, we found a number of deficiencies in PBS's execution of these contracts. For example, we found that PBS:

- Improperly obligated project contingency funds;³

³ *Recovery Act Report – Improper Obligation of Construction Contingency Funds, Review of PBS's Major Construction and Modernization Projects Funded by the American Recovery and Reinvestment Act of 2009* (Report Number A090172/P/R/R11016, September 30, 2011).

- Failed to establish project GMPs at contract award;^{4,5} and
- Failed to establish fair and reasonable pricing when exercising a construction option.⁶

These findings resulted in violations of the Federal Acquisition Regulation (FAR) and Competition in Contracting Act of 1984. In some cases, these violations resulted in excessive costs to GSA.

CMc Policy and Regulations

In response to our Recovery Act audit findings, PBS issued its February 2011 *Policy and Procedures for using the Construction Manager as Constructor (CMc) Project Delivery Method* (2011 CMc policy). This document established mandatory procedures for using the CMc project delivery method, including the use of templates for preparing the statement of work, solicitation, and agreement. PBS also developed and implemented mandatory training for awarding and administering CMc contracts.

In 2016, GSA's Office of Acquisition Policy opened General Services Administration Acquisition Regulation (GSAR) Case 2015-G506, *Adoption of Construction Project Delivery Method Involving Early Industry Engagement—Construction Manager as Constructor (CMc)*, to incorporate the 2011 CMc policy into the GSAR. During review of the 2011 CMc policy and existing guidance, GSA identified several necessary changes and issued an October 2018 FAR and General Services Administration Acquisition Manual Class Deviation that was effective while the GSAR was being updated.⁷ These changes were formally adopted into the GSAR in January 2020.

Of particular note, the GSAR changes require that the contracting officer perform a price realism analysis prior to award to ensure the offeror's price reflects an accurate understanding of the contract requirements. Additionally, the GSAR requires an independent audit when a CMc contract is converted from GMP to firm-fixed price. The contracting officer must first request that the Office of Inspector General (OIG) perform all audit services. If the OIG declines, then the contracting officer may obtain the services from a certified public accountant.

⁴ *Recovery Act Report – Austin Courthouse Project, Review of PBS's Major Construction and Modernization Projects Funded by the American Reinvestment and Recovery Act of 2009* (Report Number A090172/P/R/R10001, March 12, 2010).

⁵ *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* (Report Number A090172/P/R/R11007, March 4, 2011).

⁶ *Recovery Act Report – Thurgood Marshall U.S. Courthouse Project, Audit of PBS's Major Construction and Modernization Projects Funded by the American Recovery and Reinvestment Act of 2009* (Report Number A090172/P/R/R11012, August 19, 2011).

⁷ Class Deviation CD-2019-02.

GSA OIG Construction Contract Audits

The GSA OIG performs several types of construction contract audits in response to requests from PBS's contracting officers and GSA's Office of General Counsel. For CMc contracts, these include, but are not limited to, audits of requests for equitable adjustment, claims, conversion proposals, and final settlement proposals. Since January 2017, we have issued 44 construction contract audit reports covering nearly \$467 million in project costs. Notably, 23 of these audits were of claims and requests for equitable adjustment totaling more than \$60.7 million through which we identified more than \$24.4 million in unallowable costs. Because these audit reports contain privileged or proprietary contractor information, they are not publicly available.

Concerns with PBS's Use of the CMc Project Delivery Method

Although PBS has taken steps to address prior concerns with the use of CMc contracts and implemented CMc policy and regulations, we continue to observe problems with PBS's award and administration of CMc contracts. In particular, we are concerned that PBS is:

- Not ensuring that construction contractors properly accumulate and record project costs;
- Improperly adjusting the contract's GMP; and
- Prematurely converting the GMP to a firm-fixed price.

These concerns are discussed below.

PBS is not ensuring that construction contractors properly accumulate and record project costs. On construction projects using the CMc methodology, contractor payments and shared savings calculations are determined based on actual construction costs incurred. Therefore, it is extremely important to ensure that construction contractors properly accumulate and record project costs.

However, during the course of our office's construction contract audit work, we have noted that contracting officers are not always fulfilling their responsibilities for ensuring contractors are properly accumulating and recording costs on CMc projects. As a result, the CMc contractor's project cost records cannot be relied on to ensure that contractor payments are correct or that shared savings calculations are accurate.

Pursuant to FAR 52.230-1, *Cost Accounting Standards Notices and Certification*, and GSAR 536.7105-3, *Accounting and Auditing Requirements*, CMc contracts are covered by cost accounting standards (CAS) unless an exemption applies or a waiver was granted.⁸ CAS are a set of 19 standards that require the contractor and its subcontractors to disclose their cost

⁸ 48 CFR 9903.201-1, *CAS applicability*, provides exemptions, such as contracts or subcontracts with small businesses.

accounting practices in writing and follow them consistently. This process ensures that the contractor accurately accumulates project costs and records them appropriately.

A contract may be subject to full or modified CAS, based on the value of the contract and whether the CMC contractor or its subcontractors have other CAS-covered contracts. Contracts or subcontracts of \$50 million or more are considered fully CAS-covered and are subject to all 19 standards. Contracts or subcontracts with values between \$7.5 million and \$50 million are subject to modified CAS, which requires adherence to 4 of the 19 standards. However, a contract or subcontract of less than \$7.5 million may be subject to full or modified CAS if the CMC contractor or its subcontractors have other CAS-covered contracts with GSA or other federal agencies.

FAR 30.202, *Disclosure requirements*, requires contracting officers to:

- Determine when a proposed contract is covered by CAS and ensure that the CMC contractor submits a Cost Accounting Standards Board Disclosure Statement (Disclosure Statement) during the procurement, when applicable.⁹
- Make a written determination that the Disclosure Statement is adequate prior to award, based on an auditor's review. Generally, this determination should be made within 30 days after the contracting officer receives the Disclosure Statement.
- Determine whether the disclosed practices comply with CAS and FAR Part 31, *Contract Cost Principles and Procedures*, before exercising the construction option. This determination is based on the auditor's detailed review.

However, contracting officers do not always follow these requirements. Our audits have shown that in some cases, contracting officers do not:

- Evaluate CAS applicability,
- Ensure that contractors complete required solicitation certifications and submit Disclosure Statements,
- Make required adequacy determinations prior to contract award, or
- Make required compliance determinations prior to exercising the GMP construction option.

In another case, PBS awarded a CMC contract to a small business that was exempt from CAS. However, the contracting officer erroneously modified the contract to remove all accounting requirements—not just the CAS requirement. In these instances, the contractor project cost records cannot be relied on for final settlement proposals and shared savings calculations, proposals to convert the GMP to firm-fixed price, or contractor claims. Due to the size of CMC contracts, which often exceed \$100 million, the government is at risk for significant overpayments if contractors do not accurately accumulate and report project costs.

⁹ 48 CFR 9903.202-8, *Subcontractor Disclosure Statements*, requires that the contractor or high-tier subcontractor be responsible for administering the CAS requirements contained in the subcontracts.

To ensure contractors properly record and allocate CMc project costs, contracting officers must follow FAR and GSAR requirements for CAS. This includes determining whether a contract is subject to CAS, and if so, whether full or modified CAS applies. If a contract is CAS-covered, the contracting officer must ensure that offerors submit required solicitation certifications and Disclosure Statements. The contracting officer must also obtain audit assistance in a timely manner for adequacy and compliance determinations, audits of CMc final settlement proposals, or proposals to convert the GMP to firm-fixed price.

PBS is improperly adjusting the contract's GMP. GSAR 536.7105-2, *Guaranteed Maximum Price*, allows changes to the GMP for conditions covered by certain contract clauses, including the changes clause, differing site conditions clause, and suspension of work clause. When adjustments to the GMP are made, the contracting officer must document support for any scope changes, including a separate analysis to document the rationale for any upward or downward adjustment to the GMP. However, during an audit of a construction contract, we noted that a contracting officer failed to properly track the GMP during construction, leading to errors in contract modifications. When contracting officers fail to properly track GMP changes, PBS is at risk for overpaying the CMc construction contractor for its work.

PBS is prematurely converting the GMP to a firm-fixed price. In accordance with GSAR 536.7105-8, *Conversion to Firm-Fixed Price*, the GMP for a CMc contract can be converted to a firm-fixed price that does not exceed the GMP. This can be done after the construction documents are complete and contingency risk has been reduced in the best interest of the government. However, through our construction contract and Recovery Act audits we have found that contracting officers attempted to convert the GMP to a firm-fixed price prematurely, even prior to completion of design. This is problematic because, in general, the government's risk of overpaying is not reduced until construction starts, the majority of subcontract agreements have been awarded, and the estimated project cost is verifiable.

If the GMP is converted to a firm-fixed price before the subcontract agreements are executed, CMc contractors may be able to attain excessive profits by negotiating with subcontractors to lower costs after converting to a firm-fixed price. This risk is exemplified by a construction contract that was funded by the Recovery Act. For this contract, the PBS contracting officer converted the construction GMP to a firm-fixed price prior to the execution of the subcontract agreements. The contracting officer relied upon subcontractor bid proposals provided by the CMc contractor as the basis for the conversion price. However, once PBS converted to firm-fixed price and exercised the construction option, the CMc contractor negotiated lower costs with subcontractors, or selected other lower cost subcontractors. By doing so, we estimated that the CMc contractor obtained a windfall of nearly \$25 million in additional profit.

Conclusion

When using the CMc project delivery method, PBS must: (1) ensure construction contractors properly accumulate and report project costs, (2) avoid improper adjustments to the GMP, and (3) ensure that the GMP is not converted to a firm-fixed price prematurely.

Given the size of PBS's CMc project workload, and the likelihood that PBS will use this project delivery method for a number of Infrastructure Investment and Jobs Act projects, PBS must take steps to improve its award and administration of CMc projects to ensure compliance with FAR and GSAR requirements. In particular, PBS contracting and project management staff must be cognizant of and adhere to CAS requirements and CMc policies and regulations. Therefore, PBS staff need to be properly trained and have adequate resources to oversee CMc contracts. Failure to do so may result in significant overpayments for construction work.

Compliance Statement

This memorandum complies with the Council of the Inspectors General on Integrity and Efficiency's Quality Standards for Federal Offices of Inspector General.

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