

DOCUMENT RESUME

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[Review of Negotiation by GSA's Boston Region of Contracts for A-E and Construction Services]. LCD-78-304; B-95136. January 17, 1978. 2 pp. + enclosure (10 pp.).

Report to Sen. Charles H. Percy, Ranking Minority Member, Senate Committee on Governmental Affairs: Permanent Subcommittee on Investigations; by Elmer B. Staats, Comptroller General.

Issue Area: Internal Auditing Systems (200); Federal Procurement of Goods and Services (1900).

Contact: Logistics and Communications Div.

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Organization Concerned: Department of Justice; General Services Administration; Boston Regional Office, MA.

Congressional Relevance: Senate Committee on Governmental Affairs: Permanent Subcommittee on Investigations. Sen. Charles H. Percy.

A 1975 General Services Administration (GSA) internal audit report found violations of Federal procurement regulations in contracts awarded by GSA's Boston Region (Region I) Construction Management Division. The circumstances and adequacy of the internal audit report and the effectiveness of Region I's actions to implement improvements recommended in the internal audit report were examined. In addition, Federal Bureau of Investigation (FBI) reports on allegations by a GSA employee of fraud and collusion in Region I's procurements were examined. Findings/Conclusions: The internal audit report noted six deficient areas in architecture and engineering (A-E) procurement: selection of A-E firms, GSA estimates for A-E services, records of price negotiations, submission of cost or pricing data, overpayment to contractor, and certifications of A-E's qualifications. The audit report's findings were well founded and indicated management control weaknesses requiring corrective action. However, the auditor did not determine how widespread the deficiencies were. The allegations of fraud by the GSA employee were based on alleged false justifications for using negotiated contracts. These allegedly false justifications appeared to be primarily an internal GSA management matter. It appears that the restrictive solicitations and reports detailed in the audit report are not now prevalent in either advertised or negotiated contracts. (RRS)



COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

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The Honorable Charles H. Percy
Ranking Minority Member
Permanent Subcommittee on
Investigations
Committee on Governmental Affairs
United States Senate

JAN 17 1978

Released 1/19/78

Dear Senator Percy:

RESTRICTED - Not to be released outside the General Accounting Office except on the basis of specific approval by the Office of Congressional Relations

Your letter of February 17, 1977, requested that we review certain management practices of the General Services Administration (GSA). Of concern were allegations of fraud and mismanagement in GSA's procurement practices. Specific interest was directed at a GSA internal audit report dated June 13, 1975, and its findings of violations of Federal procurement regulations in contracts awarded by GSA's Boston Region (Region I) Construction Management Division.

We and your representative agreed that we would examine (1) the circumstances and adequacy of the internal audit report and (2) the effectiveness of Region I's actions to implement improvements recommended in the internal audit report. We also agreed to examine Federal Bureau of Investigation (FBI) reports on allegations by a GSA employee of fraud and collusion in Region I's procurements in order to establish the relationship to and impact on the internal audit. It was also agreed that your requested nationwide statistical profile, as modified to show GSA's use of advertised and negotiated contracts for (1) new construction and (2) major repair and alterations, would be the subject of a separate information report.

We reviewed the internal audit report, supporting working papers, and FBI reports on the allegations the GSA employee made. We also tested Region I's current procurement practices by examining selected contracts--negotiated and advertised.

We found that the GSA Boston Field Audit Office, which issued the June 1975 report, was not restricted in its determination of audit scope and methods. The report was adequate in that its findings were well founded. It did inform management of numerous examples of procurement deficiencies, including insufficient documented support for

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the method of contracting--negotiating rather than formally advertising for contractor selection--and for the estimated costs and negotiated prices.

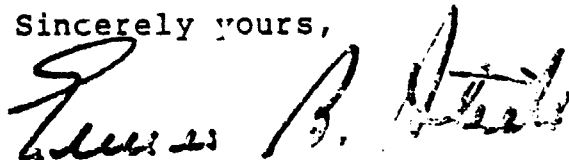
Although the scope of the internal audit did not provide for the additional work needed to more precisely show the extent of these deficiencies, it did establish that the procurement controls needed management attention. These findings were consistent with FBI's conclusions on its examination of the same or similar evidence; it did not find criminal wrongdoing, but the evidence indicated internal GSA management weaknesses.

Region I has substantially implemented the audit recommendations. As discussed in greater detail in enclosure I, our tests of the current contracts indicated improvements in the procurement controls.

We trust that this report satisfies your request and are prepared to answer questions you may have. As agreed with your representative, we did not obtain formal comments from GSA and are sending a copy of this report to the Administrator of General Services. We expect to provide the nationwide statistical profile by March 1978.

Copies of this report are also being sent to Senators Edward M. Kennedy and Edward W. Brooke pursuant to their joint letter request and agreements with your representative, and to Congressman Gerry E. Studds.

Sincerely yours,



Comptroller General
of the United States

Enclosure

INTERNAL AUDIT REPORT ON REGION I AND
IMPLEMENTATION OF RECOMMENDED IMPROVEMENTS

CIRCUMSTANCES AND ADEQUACY OF
GSA'S INTERNAL AUDIT REPORT ON
CONSTRUCTION MANAGEMENT DIVISION
ACTIVITIES, BOSTON REGION

Normally, GSA internal audits are programed by the headquarters office in Washington. The audit reported on June 13, 1975, was initiated by the Boston Field Audit Office to replace a scheduled audit because there was insufficient activity to warrant a review in the area of the scheduled audit. The Boston Field Audit Office requested permission to audit Boston's Construction Management Division (CMD) activities from GSA's Director of Audits in Washington because (1) of indications that insufficient cost or pricing data was being submitted by contractors and (2) Boston's CMD activities had not been audited for several years.

GSA's Director of Audits approved the audit and mandated a comprehensive review of Boston's CMD procurement procedures. Field work started in November 1974 and was completed in March 1975, with the report being issued in June 1975. The audit was interrupted between November and December 1974 because of an FBI investigation into allegations by a GSA employee of fraud, collusion, and kickbacks in contract awards.

The Boston Field Audit Office auditor determined the scope of the audit and selected the contracts for review. He reviewed negotiated procurements, including change orders, but did not review advertised contracts.

The auditor examined 9 of 43 negotiated construction contracts active as of January 1975. The selection generally included contracts awarded for more than \$100,000 and was not based on statistical sampling. He also reviewed 5 of the 6 most recent architect-engineer (A-E) contracts and change orders.

Because this was a regionally generated audit, a written program was not prepared. The field auditor referred to GSA audit guides and reports, and used judgment regarding areas for review. The audit was originally scheduled for 250 hours and later increased to 400 hours; it actually took about 600 hours.

The auditor found many procurement areas lacking in the required controls, including instances where (1) the documentation in the contract files did not justify negotiating instead of formal advertising and (2) the amounts awarded for negotiated contracts did not appear reasonably close to GSA estimates.

The auditor discussed some of the findings with personnel of GSA's Field Investigations Office, which investigates violations of Federal statutes covering criminal activities. He was aware that the GSA Field Investigations Office had FBI reports on the employee allegations.

The objective of internal auditing is to assist management by furnishing information, analyses, appraisals, and recommendations pertinent to management's responsibilities. The purpose of internal audit reports is to communicate information and to focus attention on conditions or events that require action of some kind by management officials. It is essentially a management tool; the report is not designed for public distribution. The audit reported

"* * * a number of practices used by the CMD that do not comply with GSA regulations or Federal Procurement Regulation guidance. Many of the CMD practices compromise the necessary safeguards of negotiated procurement established in these guidelines."

The report recommended that the method of selection and the negotiation of fee for A-E awards follow the written directives and be appropriately documented in the official contract files. For negotiated construction contracts, the report recommended improved controls to insure more formal advertising and competition.

The audit report's findings were well founded and indicated management control weaknesses requiring corrective action. However, the auditor did not determine how widespread the deficiencies were. For example, the report noted a lack of documentation of reasonable safeguards of fair competition in extensions of the bid-opening dates for two of the nine construction contracts reviewed. No comment was made on the remaining contracts.

In commenting on the audit recommendations, the Regional Administrator generally agreed but emphasized that CMD's practices generally complied with the procurement regulations

and that these practices have not compromised the negotiated procurement practices. He did, however, acknowledge the lack of documentation and, as detailed in later sections of this enclosure, substantially implemented the audit recommendations.

Examination of FBI reports on
allegations made by GSA employee

In November 1974, a GSA employee approached FBI with GSA documents which he alleged involved fraud, collusion, and kickbacks. The allegations concerned nine contracts. FBI investigated the allegations from November 1974 through January 1975.

We examined the FBI reports on the results of its investigation to (1) see if there was any adverse impact on the scope of GSA's internal audit and (2) compare these results with the audit findings. We also discussed the investigation with a Boston FBI official who said that the charges were based on rumor.

FBI needed specific information to investigate the alleged kickbacks, but the complainant could only provide rumor. Concerning the alleged collusion, FBI interviewed GSA and contractor officials and examined contractor financial records, but did not uncover evidence of criminal wrongdoings.

Most of the allegations of fraud concerned what the employee believed were false justifications for awarding negotiated instead of advertised contracts. Another charge was that a GSA employee had illegally filled in the price on a contractor's bid. In this case, FBI interviewed a former employee of the contractor who stated that she had filled in the bid amount; this was verified by laboratory handwriting analysis.

In summary, FBI did not uncover evidence of criminal wrongdoing regarding the allegations made by the GSA employee. It was concluded that the alleged false justifications for using negotiated contracts appeared to be primarily an internal GSA management matter.

REVIEW OF CURRENT CONSTRUCTION MANAGEMENT
DIVISION PROCUREMENT PROCEDURES

Our review of the current practices focused on deficiencies noted in the internal audit report. The report noted six deficient areas in A-E procurement, eight in negotiated construction procurement, and two common to both.

We examined all negotiated construction contracts (total of 9) and A-E contracts (total of 4) awarded from January 1975 through March 31, 1977, and selected change orders approved during that time. We also examined an A-E contract awarded in August 1977 because the A-E contracts that fell between January 1975 and March 1977 were awarded before or shortly after Region I's response to the internal audit. In addition, we examined 15 advertised construction contracts. Our review, therefore, included 5 A-E contracts and 24 construction contracts.

Our review shows that CMD has substantially implemented the audit recommendations, and there have been improvements in the procurement controls. The following sections detail our observations.

Negotiated A-E contracts

The six reported deficiencies in A-E procurement involved the adequacy of the documented support for

- selection of A-E firms,
- GSA estimates for A-E services,
- records of price negotiations,
- submission of cost or pricing data,
- overpayment to contractor, and
- certifications of A-E's qualifications.

The auditor (1) found that the selection and negotiation practices did not provide adequate records of the basis for CMD actions and determinations and (2) recommended that the applicable regulations and agency instructions be followed, and that such compliance be documented in the official contract files.

In the five A-E contracts we examined, GSA substantially satisfied the internal audit recommendations. The four contracts awarded between January 1975 and March 1977 had most of the required documentation. The other contract, awarded in August 1977, had none of the documentation deficiencies cited in the audit report. Our more specific observations follow.

Documentation for selection criteria and evaluation and rationale of award

One of the five contracts was awarded before the issuance of the audit report, and three were within 6 months after the report. These four contracts reflected an improvement in documentation supporting the evaluation and rationale for the contract award. The remaining contract--awarded August 17, 1977--was well documented, showing the selection criteria used, and the evaluation process and rationale for award.

Independent GSA estimates

The GSA estimates in the five contract files contained statements showing that (1) overhead rates were derived from historical data based on recent regional A-E contracts and Government audits, and (2) the profit rates were based on consideration of such factors as the high degree of specialization, complexity, and risk. However, they did not show which recent A-E contracts GSA used to develop the historical data, and did not explain the high degree of specialization, complexity of the project, or risk involved.

Price negotiation meetings

Two of the five A-E contracts had some of the deficiencies relating to price negotiation records noted in the audit report.

A contract awarded in March 1975 did not have a detailed summary of the negotiations. The record included a list of unidentified personnel, A-E's and GSA's estimates, and the final negotiated price. A GSA official told us that it was one of the first A-E contracts he negotiated, and he did not know what details to include in the record.

A contract awarded in August 1975 had a summary of price negotiations but did not reflect the extent to which factual cost or pricing data was used in the negotiations. It also did not summarize the pertinent advisory audit report recommendations. A GSA official stated that he did not know why this information was not included in the record.

For the remaining three contracts, the official files appropriately showed the details of the negotiations.

Cost or pricing data submitted by contractors

Only one of the five A-E contracts exceeded \$100,000 and required cost or pricing data. The contract file contained the A-E cost estimate, cost breakdown of staff-hours for each stage of the contract, and the employees' salaries.

However, A-E did not furnish financial statements for the 3 previous years, as required by regulations, or supporting statements to explain the method of estimating the proposed labor-hours and the techniques used in arriving at proposed labor rates. A-E also did not explain the basis for other direct costs and the method used to compute overhead rates.

Negotiated construction contracts

As a general policy, the Government purchases goods and services by soliciting supplies and services from qualified sources with full and free competition using public advertising. However, in certain cases, such as where the product is peculiar in nature or when time is critical, contracts may be negotiated and awarded after soliciting offers from one or more qualified sources.

Negotiated construction contracts awarded by GSA reflect some of the principles applicable to advertised contracts. Instead of soliciting bids through public advertising, a limited number of contractors are asked to submit offers, which may be accepted or rejected. Normally, the contract is awarded to the contractor submitting the lowest offer. However, the option of price negotiation is left open where all offers exceed GSA cost estimates.

At the time of our review, nine negotiated construction contracts totaling \$347,349 were active. We examined all of these contracts, which were awarded in the period January 1975 through March 1977.

As previously noted, 8 of the 16 GSA audit findings addressed negotiated contracting practices. The principal findings involved

- inadequate justification for negotiated rather than advertised contracts,
- restricted solicitation of bids indicating favoritism, and
- deficiencies in the timing and pricing of change orders.

Improvements have been made in the region's management of construction contracts. In addition, the recommendations suggested in the internal audit report have been substantially implemented. Since the GSA audit, there has been a change in emphasis from negotiated to advertised contracts. The number of negotiated contracts decreased from 43 at the time of internal audit to only 9 out of 153 construction contracts active at the time of our review.

The nine contracts showed the following reasons for negotiation:

- Three contracts were negotiated on the basis that they were authorized by other legislation. Two were in conjunction with the Small Business Act. The third contract--for repaving at a U.S. Border Station located on a highway that a State was resurfacing--was in accord with provisions of the Federal Property and Administrative Services Act permitting reimbursement to a State.
- Two were negotiated on the basis of "public exigency" where emergency or dangerous conditions prevailed. For example, the sea wall at the GSA motor pool was collapsing, thus requiring immediate attention.
- Three were negotiated on a "sole source" basis, where experience or unique expertise was required. For example, an elevator company received a contract for about \$167,000 to repair escalators which it had installed in the John F. Kennedy Federal building.
- The final contract was negotiated after all advertised bids exceeded GSA cost estimates. In this case, those contractors who had submitted bids under formal advertising were asked to submit offers under the negotiated process. Also, other contractors were solicited to make offers.

The internal audit had also found that several firms were being repeatedly solicited for bids and selected for most negotiated contracts, indicating unfair advantages and favoritism. However, we found no indication of favoritism. In the case of the nine contracts we examined, Region I used various methods of solicitation, including contractors previously awarded contracts, classified pages of telephone directories, and contractors expressing interest. No contractor bid on more than one project. As a result, nine different firms received the nine negotiated awards.

Two of the GSA audit findings noted deficiencies in the awarding of contract change orders. The deficiencies were that

- contractors did not submit cost proposals in a timely manner,
- Government cost estimates were not always made,
- amounts negotiated appeared excessive when compared to Government estimates,
- change order negotiations were delayed, and
- changes were made that did not relate to the initial contract.

For four of the nine contracts, we found one change order each. None of the above deficiencies were noted. All four change orders were within the general provisions of the original contract and were done concurrently with the work required in the original contract. The contractor cost estimate and amount negotiated were higher than the Government cost estimate in two change orders, while the opposite was true for the other two. Two change orders resulted in reduced contract scope and a credit, and the remaining two increased the cost. The total cost increase was about \$2,100--about 3 percent of the contracts' total amount of about \$74,000.

Other internal audit findings showed the need for improvement in practices used by the negotiated contracting review committee; the use of fixed rates in contract estimating for profit, overhead, etc.; and, bid opening and review procedures. Our review of negotiated contracts and change orders indicated substantial correction of these conditions.

The findings on the need to improve contract files and maintain an updated bidders mailing list were also examined. Again, improvements over conditions cited in the audit report were noted.

Advertised construction contracts

The audit report considered only negotiated contracts. During the period covered by our review, negotiated procurements had been reduced to 9 out of a total of 153 active construction awards. The remaining 144 contracts were formally advertised. Since a number of the deficiencies cited in the audit report also could occur on advertised awards, we randomly selected 15 of the 144 contracts for review.

One aspect of advertised contracts we examined was the method of obtaining competition. We noted that the region used various types of advertising to solicit bids, such as posting advertisements in CMD and the GSA Business Service Center in Boston. Advertisements also are placed in the local newspaper where the projects are located and in trade journals, such as the Commerce Business Daily and Dodge Reports.

Contractors are also solicited from a bidders' mailing list. A contractor gets on this list by successfully completing a project or by submitting forms with data on type of business and work desired. The bidders' list is entered in a computer which, when a project arises, selects the names of those contractors who have indicated they are capable of performing the work. For a small project (under \$100,000), usually 40 or 50 names are selected and sent bid packages. For larger projects, all contractors who have indicated the capacity to perform such work and then respond affirmatively to preinvitation solicitations will be sent bid packages. The bidders' list is updated and purged annually, with contractors being queried as to whether they wish to remain on the list.

We believe that the region attempted to solicit an adequate number of contractors. Only one contract examined was for an amount over \$100,000. For this contract, 48 contractors were solicited or indicated interest to bid, and 6 contractors submitted bids. The number of contractors invited to bid on the remaining contracts ranged from 13 to 90, and the number of bids received per contract ranged from 2 to 15. While these figures reflect the analysis of only 15 of 144 advertised contracts, we believe that they are indicative of the region's current practices in soliciting competitive bids.

We were also interested in learning how change orders affected advertised contracts. Ten of the 15 advertised contracts had change orders. Five had one change order and five had two change orders. Six contracts were increased in cost by less than 10 percent by change orders. The remaining four contract costs were increased by 30 percent or more. Of these four, three contracts for painting were increased by 30, 31, and 62 percent. Costs increased in these contracts because after work had progressed, it was found that extra coats of paint were needed. The other contract, for electrical work, had its cost increased by 48 percent. The increase occurred because certain equipment was found to be faulty and, in correcting this problem, other alterations were needed.

All change orders were well-documented and in line with the intent of the original contract.

We were also interested in determining if the distribution of actual awards for the 144 advertised contracts--valued in excess of \$17 million--might also tend to show full and free competition rather than the indications of favoritism noted by the auditor for negotiated contracts. We found that awards were made to 103 different contractors; 84 contractors had single awards valued at about \$13.4 million or 75 percent of the total value of advertised contracts, and 19 contractors had been awarded two or more contracts valued at about \$4.3 million.

Based on our examination of the methods of obtaining competition and the distribution of awards, the restrictive solicitations and awards noted in the audit report are currently not prevalent in either advertised or negotiated contracts.