U.S. General Services Administration
Office of Inspector General

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MEMORANDUM FOR SHAPOUR EBADI
DIRECTOR, OFFICE OF INFRASTRUCTURE AND CAMPUS DEVELOPMENT (WPS)

FROM: PAUL MALATINO
DIRECTOR, OFFICE OF SPECIAL PROJECTS (JA-P)

SUBJECT: Analytical Procedures for Evaluating Cost Proposals Received Under a Utility Energy Services Contract at Saint Elizabeths
Memorandum Number A090168-06

This memo concerns current and planned use of a utility energy services contract (UESC) to design and construct a central utility plant at Saint Elizabeths. Our observations derive from a review of UESC task order GS-P-11-10-MM-006 awarded to Washington Gas Light Company under the GSA areawide utility contract.[1] We found neither a basis for determination of price reasonableness, nor justification for use of other than full and open competition. Additionally, funds were inappropriately "borrowed" from this task order to accomplish other work, understating actual obligations - a violation of appropriations law.

At a minimum, the non-competitive nature of these contracts mandates adoption of the price analysis techniques described in the Federal Acquisition Regulation (FAR) 15.404-1. However, we would also urge reconsideration of the selected contract type. The advantages of a UESC contract are both unrealized and outweighed by its disadvantages in this application.

As with prior contract actions examined in the course of monitoring the DHS headquarters consolidation at Saint Elizabeths, our objectives were to review compliance with relevant procurement and appropriations law, and to determine whether the selected procurement approach was reasonable and advantageous to the Government. Our work does not constitute an audit and contains no formal recommendations.

[1] *This fixed price task order, valued at $33,330,327, provides for design and construction of the electrical distribution system for the first phase of Saint Elizabeths West Campus. American Recovery and Reinvestment Act of 2009 funds were used. Additional task orders are planned to accomplish the overall scope, which is to provide design-build services for the adaptive reuse and expansion of the existing central utility plant and associated energy infrastructure/utility distribution system at the St. Elizabeth's West Campus. A combined heat and power component capable of cogeneration is envisioned.*

Price Reasonableness and Other Matters Concerning Task Order GS-P-11-10-MM-006

GSA did not develop methods or procedures to determine price reasonableness under this fixed price, UESC task order. Contrary to the proposal analysis techniques prescribed by FAR 15.404-1, GSA conducted only limited cost analysis and no price analysis. As a result, the Government may have substantially overpaid for this task. Additionally, funds were inappropriately "borrowed" from this task order to accomplish other work, understating actual obligations, a violation of appropriations law. Finally, the justification for other than full and open competition, as required by FAR 6.303-1, was absent from the contract record.

Task order GS-P-11-10-MM-006, referred to as Task Order #2, was awarded on September 10, 2010, to Washington Gas Light Company under the GSA areawide utility contract. Valued at $33,330,327, this fixed price task provides for design and construction of the electrical distribution system for the first phase of Saint Elizabeths West Campus. As is permitted under a UESC, the requirement was not competed. Two utilities hold GSA areawide contracts in the DC metropolitan area. The procurement team solicited proposals from both under Task Order #1, which covered initial design and coordination functions related to the overall central utility plant project. Washington Gas was awarded Task Order #1 which was valued at $3,782,500, on December 28, 2009. Nine months later, Task Order #2 was negotiated with and awarded directly to Washington Gas. Scope and pricing for all subsequent task orders under this UESC will also be negotiated contract actions. The objective of each negotiation is to arrive at a finding of fair and reasonable pricing. The process is subject to the provisions of FAR 15, Contracting by Negotiation.

The tradeoff with a sole-source action is that, while it dispenses with a cumbersome and time consuming source selection process, it challenges the buyer to develop an effective substitute for price competition in establishing price reasonableness. FAR 15.404-1 addresses this matter and discusses various proposal analysis techniques. These include comparisons with previous project costs and application of parametric estimating techniques,[2] neither of which is in evidence here. In addition, there was no evidence of outreach to knowledgeable sources such as the energy experts within GSA, or external sources, such as the Department of Energy, which maintains government-wide benchmarking data. Further, given that this task was concerned solely with design and construction of the electrical distribution system, and contained no energy savings component, PBS's own historical construction project data likely offered the

[2] *Mathematical relationships, usually based on statistical analysis, between price as the dependent variable and one or more physical characteristics of the item or system purchased as independent variables. According to* FAR 15.404-1(b)(2)(iii): "*Use of parametric estimating methods/application of rough yardsticks (such as dollars per pound or per horsepower, or other units) to highlight significant inconsistencies that warrant additional pricing inquiry.*"

best comparative data source. None of these potential sources or techniques was used. Accordingly, price analysis, as defined by FAR, was not performed in support of this award.

The technique that was used was labeled as an independent government estimate. It consisted of a single page spreadsheet with no narrative, containing data that mirrored the contractor's high-level cost proposal including identical line items. It contained some unit of measure and unit cost data, where the contractor proposed a lump sum, but did not explore potential cost redundancies, such as the application of overhead to what appear to be fully burdened labor rates. It did not challenge the appropriateness of any of the proposed cost elements. All allowances, contingencies, layers of oversight, and markups were accepted and incorporated into the government estimate. Still, the government estimate totaled about $1.1 million less than the cost proposal. This variance is not discussed in the contract document which serves as the price negotiation memorandum (PNM). The award was made at Washington Gas's proposed price.

If cost analysis is to function as a means of determining price reasonableness, the PNM should have discussed why price analysis was not possible; i.e., why external measures could not be applied. This should, in turn, have necessitated a request for supporting documentation in the form of "other than certified cost or pricing data" as required by FAR 15.403-1. The proposal as submitted does not, for example, identify any of the components of a lump sum line item for electrical equipment and installation, valued in excess of $7 million. It does not, as submitted, provide support for the $175 labor rate for an engineer, a rate then subject to additional overhead (15%), profit (10%) and markup (5%), which would equate to billable rate of $232.44 per hour.

Because this task is awarded under a UESC contract (described in more detail below), GSA must contract with a utility company. In this case, the actual work will be performed by Honeywell Building Solutions, which will serve as a first tier subcontractor to Washington Gas. Under this arrangement, Washington Gas charges both a project management fee to cover its costs plus a 5 percent markup on Honeywell's total cost of $29,606,493. Combined, the Washington Gas project management fee and markup add approximately 13 percent, bringing the total to $33,330,327. Here again, a question should arise as to whether this arrangement yields value or redundancy.

In additional to pricing concerns, we also noted a funding irregularity related to this task. The task was modified in March 2011, via Modification No. PC01. While the file documentation was incomplete, it did contain a copy of the SF30 (standard form used for modification of contract) which stated:

THIS IS A NO-COST MODIFICATION WHICH HAS NO EFFECT ON CONTRACT VALUE.

This Modification is for the Reallocation of Construction Funds in the amount of $1,632,674 from Task Order No.2 to fund the following critical projects under the Central Utility and Heating Plant, St Elizabeths West Campus, SE, Wash., DC:

1. Natural Gas Infrastructure;
2. Design and Construction of Electrical Ductbanks to Provide Normal Power to FEMA, Bldg 71, and Guard Shacks 5-11;
3. Phase I Central Utility Plant Design and Coordination (a), PJM Interconnection Coordination for the Campus (b), and Review of the new central utilities plant design by Clark Construction.

You are hereby directed to perform the scopes of work for the critical projects listed above. The scopes of work for the reallocated portions from Task 2 to be set aside for future funding consist of the following: Complete Wiring Terminations, Commissioning, Electrical Service to CGHQ & Adaptive Reuse Buildings and retention. All terms and conditions remain in full force and effect.

There is no authority under appropriations law to borrow from a fixed price obligation with a promise to repay with future funding so that additional work can be accomplished in the current period. The net effect of this action was to under-record current period obligations, overstate the available fund balance, and create the potential for an Antideficiency Act[3] violation. The work to be set aside is, in fact, not severable from the whole of Task Order #2; it is work that must be completed in order to bring electrical power to the USCG building, which was the point of the initial task. The modification is not a substitution but an increase in the scope of work. The implied value of the new tasks is $1,632,674. If Washington Gas is indeed compelled to complete this new work, then this change should be reflected as an additional obligation.

Finally, we note that the file does not contain written justification for the use of other than full and open competition, a requirement of FAR 6.303-1. GSA's own guidance covering the use of its areawide utility contracts emphasizes this requirement. It is a significant omission, because, as we discuss below, there were other options available, and the decision to procure under a UESC does not appear, in this instance, to be in the best interests of the Government.

Comparison of Alternative Contract Types

The law affords special treatment to the acquisition of utility services, in part, to make it easier for agencies to implement energy conservation and demand side management measures, such as the cogeneration plant contemplated for Saint Elizabeths. For example, an agency can enter into direct negotiations for energy management services with a public utility, an exception to the requirement to obtain full and open competition. It can also claim exemption from the full funding requirements of the Antideficiency Act, permitting it to enter into a long-term contract with private sector financing while obligating only its current year costs. The various provisions

[3] *Agencies may not spend, or commit themselves to spend, in advance of or in excess of appropriations; 31 U.S.C. § 1341 (Antideficiency Act).*

share a common prerequisite: reasonable expectation that the project will produce a direct reduction in energy usage.

Considered with respect to the specific requirement at Saint Elizabeths, these special provisions present GSA with three broad procurement alternatives: (1) a negotiated UESC task order awarded under the local GSA areawide utility contract; (2) a competitively awarded task order issued under an energy savings performance contract (ESPC); or (3) a stand-alone contract action(s) covering design and construction. The following briefly describes the typical advantages and disadvantages of each approach.

(1) Utility Energy Services Contract

A stand-alone UESC is an option, but for locations where GSA already has an areawide utilities contract in place, a UESC is executed as a task order under that contract. The areawide contract contains general terms and conditions. A separate authorization document details the utility service or project to be provided. Only regulated public utility firms are awarded an areawide contract. For the DC metropolitan area, there are in fact two contract holders: Washington Gas Light Company and Potomac Electric Power Company. According to the GSA user guide, prior to entering into an agreement for energy management services, a customer agency is required to competitively evaluate the capabilities of both companies and select the one that provides the best value.

Advantages:

- Speed and ease of use
- No formal source selection
- Flexible and severable by task
- Project can be financed over 10 years

Disadvantages:

- No price competition
- Challenging price analysis
- No savings guarantee
- Risk premium increases cost of money
- Utility company adds layer of markup

(2) Energy Savings Performance Contract

Similar to UESC as an alternative means of financing capital projects without direct appropriations. Contracts are with energy service companies (ESCOs), not public utilities. DOE has awarded indefinite delivery, indefinite quantity (IDIQ) contracts to 16 ESCOs under its Federal Energy Management Program (FEMP). An agency's requirements are competed, following fair opportunity rules per FAR 16.505(b)(1) - multiple award contracts. A DOEqualified project facilitator is mandatory. Savings guarantees are mandatory and must exceed payments in each year. Measurement and verification are mandatory.

Advantages:

- Project can be financed over 25 years
- Guaranteed cost savings
- Established contract vehicle
- Utility company markup is eliminated

Disadvantages:

- Leveraged project magnifies cost of schedule disruptions and changes
- Analysis of financing requires specialized knowledge
- Requires FEMP assistance and paid facilitator
- Formal procurement process
- Challenging price analysis
- Risk premium increases cost of money
- Increased contract administration and related costs over life of contract

(3) Stand-Alone Procurement

If alternative financing is not required, an agency can construct a combined heating and power plant, distribute electrical power, and acquire virtually any necessary energy management services via conventional procurement methods. Given the fact that construction is a primary business line at GSA, the tools, knowledge, and skills needed are already at its disposal. The contract or contracts would in effect be tailor-made to meet the priorities of this project. GSA may, for example, choose to award a design/build contract, or separate those functions to maximize price competition. It could structure its contract to include options for future phases, lessening the procurement workload for future periods and likely attracting additional bid interest. It can target all of the benefits intended from full and open competition.

Advantages:

- Project team controls contract terms and conditions
- Price subject to competition
- Entire process lies within GSA area of expertise

Disadvantages:

- Need to fully fund non-severable tasks at point of award
- More front-end effort and time
- Potential for bid protest

Conclusion

Under the procedures currently in place, the contracting officer will not receive adequate analytical support to arrive at a determination of price reasonableness. There are corrective measures to address the analytical shortcomings, such as implementing FAR 15.404-1 price analysis techniques, but the contract vehicle itself shifts considerable pricing leverage to the contractor. This will only intensify as the contract progresses. Further, the UESC appears to impose an unnecessary layer of management and cost. The project team has the discretion to use this contract vehicle, but it also has an obligation under each new award action to justify why it is advantageous to do so.

With only partially funded requests in the current period, and the expectation of an austerity budget going forward, this project faces significant challenges. The under-recorded obligation noted in this memo is one manifestation of such challenges, as the project team struggles to maintain critical path events. The modern and efficient central utility plant envisioned is placed at risk if future phases are deferred or eliminated. With increased uncertainty, contract flexibility is a critical attribute and should be incorporated into the design of whatever contract vehicle is selected for future tasks.

These observations are made in the course of our oversight and monitoring of the DHS headquarters consolidation project. They do not derive from nor have we conducted the tests and procedures that would be required under an audit. Accordingly, we are making no formal recommendations. However, this memo will be made available to the independent public accountant, and may trigger additional testing as part of its annual audit of GSA's financial statements. We hope these observations will assist you in evaluating your procurement options. If we can be of further assistance, please contact me at 202-208-0021.

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