



Office of Inspector General

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**United States Department of State  
and the Broadcasting Board of Governors  
Office of Inspector General**

**Office of Audits**

**Improved Contract Documentation and  
Monitoring by the Regional Procurement  
Support Office Are Needed for Construction  
Projects Associated With the President's  
Emergency Plan for AIDS Relief (PEPFAR)**

**Report Number AUD/IP-12-03, November 2011**

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## Spotlight: Improved Contract Documentation by the Regional Support Office Are Needed for Construction Projects Associated With the Presidents Emergency Plan for AIDS Relief (PEPFAR)

Office of Inspector General  
AUD/IP-12-03 October 2011

### Why OIG Conducted This Audit

The Department of State OIG is required, under the Tom Lantos and Henry J. Hyde United States Global Leadership Against HIV/AIDS, Tuberculosis, and Malaria Reauthorization Act of 2008, to conduct financial audits, inspections, and performance reviews of PEPFAR. This review focused on 100 of 145 contracts and task orders that the Regional Procurement Support Office in Frankfurt, Germany (RPSO) awarded for PEPFAR construction projects between FY 2003 and the first quarter of FY 2010. The 100 procurements totaled \$39,207,381 and were for the design, construction, and monitoring of construction of clinics, labs, and other health facilities throughout Africa.

### Objective

The primary objective of this review was to determine whether RPSO appropriately awarded and monitored PEPFAR construction contracts. The results of the OIG's work are being reported in two reports. In June 2011, OIG issued AUD/IP-11-14 *Audit of Construction and Transfer of Ownership of the President's Emergency Plan for AIDS Relief (PEPFAR) Overseas Construction Projects*, a report that focused on the Department's Office of the U.S. Global AIDS Coordinator's oversight of PEPFAR properties

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### What OIG Found

OIG found that RPSO did not comply with requirements in the *Federal Acquisition Regulation* or the Department's Contracting Officer's Representative (COR) Handbook for maintaining contract files to demonstrate performance of required actions in awarding and monitoring PEPFAR construction contracts. Specifically, contract files OIG reviewed were missing evidence of one or more of the following required contract award actions: obtaining Independent Government Cost Estimates, publicizing the solicitation and requirements, and delegating COR responsibilities. In 38 of the 100 contracts and task orders reviewed by OIG, RPSO also inappropriately included contingency costs of \$2,126,148. After the contracts were awarded, contract files in Tanzania and Uganda did not always contain adequate documentation showing required monitoring actions: including obtaining inspection reports or ensuring inspection reports received met contract requirements; conducting site visits; and reviewing progress payments.

RPSO did not always document essential contract award actions, so the Department cannot be assured these actions were always performed for PEPFAR construction contracts. Because of inadequate monitoring, the Department cannot be assured that PEPFAR buildings were properly constructed and that payments to contractors were for work actually completed. Since RPSO contracting officers are ultimately responsible for ensuring adequate monitoring, RPSO should have ensured that qualified personnel were available to monitor contracts, as was done in Ethiopia with the employment of a civil engineer.

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### OIG Recommended

RPSO should instruct its staff to determine whether required contract award actions for PEPFAR construction contracts were properly performed and documented; stop including contingency costs in PEPFAR construction contracts and task orders; review existing PEPFAR construction contracts and reclaim contingency costs inappropriately included in any contracts, as practicable; instruct its procurement staff to fully document contract monitoring to assess whether contractor performance is satisfactory; and require posts with substantial planned costs for PEPFAR construction projects to obtain an advisor with construction expertise to monitor contracts. The Department agreed with all five of the report's recommendations and has taken actions to address them. As a result, OIG closed one recommendation and considers the other four recommendations resolved, pending evidence that further actions have been taken.



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PREFACE

This report was prepared by the Office of Inspector General (OIG) pursuant to the Inspector General Act of 1978, as amended, and Section 209 of the Foreign Service Act of 1980, as amended. It is one of a series of audit, inspection, investigative, and special reports prepared by OIG periodically as part of its responsibility to promote effective management, accountability and positive change in the Department of State and the Broadcasting Board of Governors.

This report is the result of an assessment of the strengths and weaknesses of the office, post, or function under review. It is based on interviews with employees and officials of relevant agencies and institutions, direct observation, and a review of applicable documents.

The recommendations therein have been developed on the basis of the best knowledge available to OIG and, as appropriate, have been discussed in draft with those responsible for implementation. It is my hope that these recommendations will result in more effective, efficient, and/or economical operations.

I express my appreciation to all of those who contributed to the preparation of this report.

A handwritten signature in black ink, appearing to read "H. W. Geisel", written in a cursive style.

Harold W. Geisel  
Deputy Inspector General

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**Acronyms**

AIDS	acquired immune deficiency syndrome
A/LM/AQM	Office of Acquisitions Management, Bureau of Administration
CDC	Centers for Disease Control and Prevention
CMS	construction monitoring services
COR	contracting officer's representative
Department	Department of State
FAH	<i>Foreign Affairs Handbook</i>
FAR	<i>Federal Acquisition Regulation</i>
HHS	Department of Health and Human Services
HIV	human immunodeficiency virus
IGCE	Independent Government Cost Estimate
OIG	Office of Inspector General
PEPFAR	President's Emergency Plan for AIDS Relief
RPSO	Regional Procurement Support Office
S/GAC	Office of the U.S. Global AIDS Coordinator

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**Executive Summary**

In 2003, the Regional Procurement Support Office (RPSO) in Frankfurt, Germany, began awarding and monitoring President's Emergency Plan for AIDS Relief (PEPFAR) construction contracts for the Department of State (Department) and the Centers for Disease Control and Prevention (CDC). The contracts, including associated task orders, were awarded for the design, construction, and monitoring of the construction of hospitals, clinics, and laboratories supporting the treatment of patients with human immunodeficiency virus/acquired immune deficiency syndrome (HIV/AIDS) in nine countries in Africa.<sup>1</sup> The primary objective of this review was to determine whether RPSO appropriately awarded and monitored PEPFAR construction contracts. The results of the Office of Inspector General's (OIG) work are being reported in two reports. OIG's previous report focused on the Department's Office of the U.S. Global AIDS Coordinator's oversight of the construction and transfer of PEPFAR properties.<sup>2</sup>

OIG found that RPSO did not comply with requirements in the *Federal Acquisition Regulation* (FAR) or the Department's Contracting Officer's Representative (COR) Handbook, which is contained in the *Foreign Affairs Handbook* (FAH), for maintaining contract files to demonstrate performance of required actions in awarding and monitoring PEPFAR construction contracts. (Details of the methodology of OIG's review are shown in Appendix A, "Scope and Methodology.") Specifically, 34 PEPFAR construction contracts<sup>3</sup> at RPSO were missing evidence of one or more of the following required contract award actions for three of eight categories OIG reviewed:<sup>4</sup> obtaining Independent Government Cost Estimates (IGCE), publicizing the solicitation and requirements, and delegating COR responsibilities. During this review, OIG also found that RPSO inappropriately included contingency costs in these contracts and task orders totaling \$2,126,148. Because Tanzania, Ethiopia, and Uganda were awarded most of the contracts and task orders, OIG selected these countries for review and found that at two of the three posts—Tanzania and Uganda—contract monitoring files did not always contain adequate documentation showing required monitoring actions, including: obtaining inspection reports or ensuring inspection reports received met contract requirements; conducting site visits; and reviewing progress payments. However, OIG found that in Ethiopia, an engineer with technical construction expertise took responsibility for most of the monitoring functions for the U.S. Government, which resulted in better recordkeeping and more effective oversight.

RPSO did not always document essential contract award actions, so the Department cannot be assured that these actions were always performed for PEPFAR construction contracts. Also, because of inadequate monitoring, the Department cannot be assured that PEPFAR buildings were properly constructed and that payments made to contractors were for work actually completed. Since RPSO contracting officers are ultimately responsible for ensuring

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<sup>1</sup> The nine countries are Tanzania, Ethiopia, Uganda, Namibia, Zambia, Mozambique, Kenya, Botswana, and Malawi.

<sup>2</sup> *Audit of Construction and Transfer of Ownership of the President's Emergency Plan for AIDS Relief (PEPFAR) Overseas Construction Projects* (AUD/IP-11-14, June 2011).

<sup>3</sup> There are 66 task orders associated with the 34 contracts for a total of 100 procurement actions.

<sup>4</sup> The remaining five award categories reviewed include: providing justification for other than full and open competition, obtaining proper funding authorization, evaluating technical proposals, ensuring full and open competition, and reviewing cost proposals.

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adequate monitoring, RPSO should have ensured that qualified personnel were available to monitor contracts, as was done in Ethiopia with the employment of an engineer.

In September 2011, OIG provided a draft of this report with five recommendations to improve RPSO operations to the director of the Office of Acquisitions Management in the Bureau of Administration (A/LM/AQM). Specifically, OIG recommended that RPSO instruct its procurement staff to determine whether required contract award actions for PEPFAR construction contracts were properly performed and documented; stop including contingency costs in PEPFAR construction contracts and task orders unless identified contingencies arise from presently known and existing conditions, as described in the FAR<sup>5</sup>; review existing PEPFAR construction contracts and reclaim contingency costs inappropriately included in any contracts as practicable; fully document contract monitoring to assess whether contractor performance is satisfactory; and require posts with substantial planned costs for PEPFAR construction projects to obtain a technical advisor with construction expertise to monitor construction contracts.

In its October 7, 2011, response to the draft report, presented in Appendix B, A/LM/AQM agreed with all recommendations and stated it had already taken steps to address some of the recommendations. Based on A/LM/AQM's response, OIG considers Recommendation 1 resolved and closed. The four remaining recommendations are considered resolved because steps are being taken to implement them; however, they will remain open until A/LM/AQM provides evidence that they have been fully implemented.

### **Background**

RPSO Frankfurt<sup>6</sup> acquires supplies and services for U.S diplomatic posts throughout the world. RPSO's procurement personnel manage all stages of the procurement process, including soliciting quotations, processing task orders, and executing and administering contracts. RPSO has developed a specialized program for the acquisition of construction contracting services in which it awards security upgrades, designs and builds projects, and acquires architectural and engineering services.

From FY 2003 through the first quarter of FY 2010,<sup>7</sup> RPSO awarded 145 overseas construction procurements (contracts and associated task orders) for the CDC in support of PEPFAR. These 145 procurements, with a value totaling \$56,009,736, were awarded to construction companies in nine African countries and included laboratories, hospitals, and clinics, as well as construction monitoring and architect and engineering services, as shown in Figure 1.

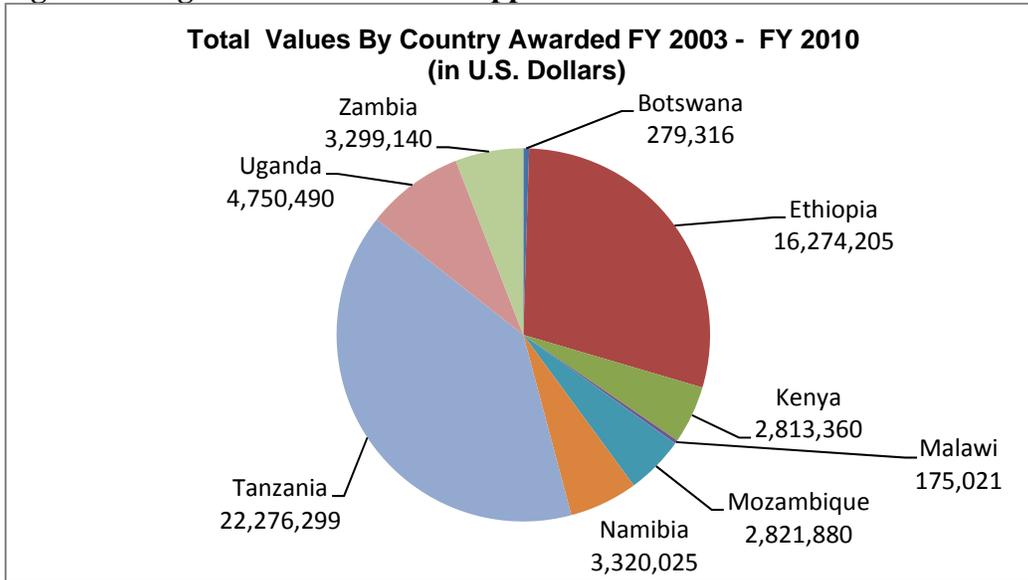
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<sup>5</sup> FAR 31.205-7, "Contingencies."

<sup>6</sup> Another RPSO, located in Fort Lauderdale, FL, acquires supplies and services for diplomatic posts in Latin America, the Caribbean, and Canada.

<sup>7</sup> At the beginning of FY 2010 (Nov. 4, 2009), the CDC sent a cable to posts advising the posts' staffs to "cease and desist" from participating in the award of contracts for PEPFAR construction (Cable 09 CDC ATLANTA GA 7821, "CDC Officials – Requisitioning Procurements Using State Department Funds"). This cable is detailed further in OIG's report AUD/IP/11-14, June 2011.

**Figure 1. Regional Procurement Support Office Construction Procurements**



Source: OIG-generated from RPSO contract files.

Of the 145 contracts and task orders RPSO awarded from FY 2003 through the first quarter of FY 2010, OIG reviewed files at RPSO for 100 contracts and task orders,<sup>8</sup> valued at a total of \$39,207,381: 34 contracts,<sup>9</sup> valued at \$17,492,381, and 66 associated task orders, valued at \$21,715,000. Of these 100 contract files, 59 files covered construction activities in the countries OIG visited: 38 in Tanzania, 7 in Uganda, and 14 in Ethiopia. Of these 59 files, 29 were for construction monitoring services or design services, and 30 were for construction activities, as shown in Table 1. (The contract files reviewed are further detailed in Appendix A.)

**Table 1. Construction Activities for Three Posts Visited**

Country	Total	Actual Construction	A & E Services and CMS Services *
Tanzania	38	18	20
Uganda	7	4	3
Ethiopia	14	8	6
<b>Total</b>	<b>59</b>	<b>30</b>	<b>29</b>

Source: OIG-generated from COR contract monitoring files.

\*Inspection reports and site visits are not required for architectural and engineering (A&E) services and contract monitoring services (CMS). Therefore, for these types of procurements, OIG reviewed only progress payments.

<sup>8</sup> Ninety-five of the 100 contracts and task orders OIG reviewed were awarded between FYs 2007 and 2009. The remaining five contracts were awarded outside this period: two contracts were awarded in FY 2005, two contracts were awarded in FY 2006, and one contract was awarded in FY 2010.

<sup>9</sup> The 34 contracts consisted of 21 firm-fixed-price contracts and 13 indefinite delivery/indefinite quantity contracts.

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Contracting officers at RPSO issued firm-fixed-price contracts and indefinite-delivery/indefinite-quantity contracts with fixed-price task orders for these construction procurements. With firm-fixed-price contracts or task orders, contractors receive a fixed cost for supplies or services not subject to any cost adjustment based on the contractor's actual experience.<sup>10</sup> According to the FAR, indefinite-delivery/indefinite-quantity contracts are used "to acquire supplies and/or services when the exact times and/or exact quantities of future deliveries are not known at the time of contract award,"<sup>11</sup> and individual task orders are then issued as separate awards for individual requirements.<sup>12</sup>

The FAR further states that the head of an office performing contracting functions must establish files that contain the records of all contractual actions.<sup>13</sup> The documentation should adequately represent a complete history of transactions, showing the complete background of decisions made at each step of the acquisition process and provide support for actions taken. The documentation is also essential to ensure that information is available "in the event of litigation or congressional inquiries."

### **Contracting Officer's Representative**

RPSO delegates the day-to-day monitoring of these procurements to personnel in the field by issuing a COR delegation memorandum, which the COR is required to sign and return to the contracting officer. The COR's signature certifies that he or she has read and understands the contents of the COR Handbook.

CORs are responsible for maintaining adequate records that document the performance of their duties. COR contract files should contain the COR delegation memorandum, a copy of the contract, correspondence and memoranda for the record on contractor performance, records related to the contractor's quality control plan and results of quality control activities, the surveillance schedule, and documentation pertaining to the COR's acceptance of performance of services.

### **Construction Monitoring Services**

For the three posts OIG visited, RPSO also awarded contracts to architectural and engineering firms to perform construction monitoring services (CMS) for PEPFAR construction projects.<sup>14</sup> These CMS contracts refer to the CMS contractor as the "on-site Government Representative." However, the contracts OIG reviewed caution that the CMS contractor does not have the authority to direct the activity of the construction contractor.

According to the contracts, the CMS contractor is responsible for construction contract monitoring and reporting on all aspects of construction, including structural, electrical,

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<sup>10</sup> FAR 16.202-1, "Firm-Fixed-Price Contracts – Description."

<sup>11</sup> FAR 16.501-2(a), "Indefinite-Delivery Contracts."

<sup>12</sup> FAR 16.504, "Indefinite-Quantity Contracts."

<sup>13</sup> FAR 4.801(a) and (b)(1)(2)(3)(4), "Government Contract Files – General."

<sup>14</sup> CMSs were included in 36 of the 145 construction procurements awarded by RPSO.

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mechanical, and security work. Specific required CMS actions include, but are not limited to, the following:

- Visiting the site periodically and monitoring the performance of the construction contractor.
- Observing, inspecting, and evaluating the construction work.
- Enforcing quality control requirements.
- Identifying and notifying the COR of potential schedule slippages.
- Reviewing the construction contractor's monthly progress payment requests and recommending appropriate action to the COR.
- Preparing and submitting timely and accurate weekly and monthly progress reports to the COR.
- Providing clear and comprehensive photographs that depict the entire property with the date and location (no fewer than five pictures to be taken and submitted with each report).

CMS contractors are required to submit written reports that must include date and time of the visit, weather conditions and temperatures, persons met on-site the day of inspection, workers present, and any item found deficient, along with a recommended corrective action.

### **Objective**

The results of OIG's work are being reported in two reports. The primary objective of this review was to determine whether RPSO followed applicable Federal regulations in awarding and monitoring PEPFAR construction contracts. The previous report focused on the Office of the U.S. Global AIDS Coordinator's oversight of PEPFAR construction projects and the transfer of these projects to host governments.<sup>15</sup>

### **Results of Review**

#### **Contract Files for PEPFAR Construction Contract Award Actions Were Incomplete**

RPSO did not comply with FAR or COR Handbook requirements for maintaining contract files<sup>16</sup> to demonstrate that required actions were performed in awarding PEPFAR construction contracts for three of eight award categories that OIG reviewed. For the 34 contract files reviewed,<sup>17</sup> OIG determined that 18 files were missing required documentation for one or more of the following award actions:

- Eleven files did not include an IGCE.
- Eight files contained no evidence that the solicitation or requirements were publicized.

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<sup>15</sup> *Audit of Construction and Transfer of Ownership of the President's Emergency Plan for AIDS Relief (PEPFAR) Overseas Construction Projects*, AUD/IP-11-14, June 2011.

<sup>16</sup> FAR 4.801(a) and (b)(1)(2)(3)(4).

<sup>17</sup> Sixty-six task orders are associated with the 34 contracts.

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- Ten files did not include a COR delegation memorandum.

Because RPSO did not always document these contract award actions, the Department cannot be assured that it obtained a fair and reasonable price from the bidder or offeror or that the solicitation was adequately publicized to ensure full and open competition. In addition, the failure to document the delegation of COR duties provides the Department no assurance that the COR understands his or her responsibilities.

### **Missing Contract Award Documentation**

RPSO contracting officers did not consistently adhere to the FAR or the COR Handbook in awarding PEPFAR construction contracts on behalf of the CDC for the following required actions: preparing an IGCE, publicizing the solicitation and requirements, and delegating COR responsibilities by memorandum.

Of the 34 contracts OIG reviewed, totaling \$17,492,381, OIG found 18 contracts, valued at \$8,464,199 (or 48.4 percent of the total value), that had documentation missing for one or more required award actions described as follows:

Independent Government Cost Estimate – RPSO procurement officials did not ensure that an IGCE was prepared for nearly one-third (11 of 34) of the PEPFAR construction contracts they awarded. The FAR<sup>18</sup> requires that the COR prepare an IGCE for supplies and services over the simplified acquisition threshold of \$150,000.<sup>19</sup> The Department’s guidance in the COR Handbook states that an IGCE should be prepared by the contracting officer and the COR. IGCEs are important in establishing a fair price for U.S. Government contracts. The COR Handbook states that IGCEs are the basis for reserving funds for the contract as part of acquisition planning and for comparing costs or prices proposed by offerors. It further states that IGCEs are an objective basis for determining price reasonableness in cases in which one bidder or offeror responds to a solicitation.

Publicizing Solicitations and Requirements – OIG found no evidence that RPSO contracting personnel publicized requirements for eight (24 percent) of 34 contracts awarded, as required by the FAR.<sup>20</sup> Acquisitions between \$25,000 and \$5 million are subject to some form of public notification appropriate to local conditions at the overseas post. RPSO procurement officials stated that they had sent Standard Forms 330, *Architect-Engineer Qualifications*, to architects recommended by the post. However, this form is used as part of the evaluation process and does not constitute proper notification. Sending information only to certain companies could be viewed as favoring specific vendors and is more likely to subject the Department to legal action by companies. For public notification, RPSO should have used the embassy Web site, local advertisement, notification to trade associations, or other methods appropriate for the post.

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<sup>18</sup> FAR 36.203, “Government Estimates of Construction Costs.”

<sup>19</sup> FAR 2.101 defines the simplified acquisition threshold as \$150,000, as of October 1, 2010. The simplified acquisition threshold at the time of OIG fieldwork was \$100,000.

<sup>20</sup> FAR 5.101(b), “Dissemination of Information – Methods of Disseminating Information.”

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COR Delegation – OIG found that RPSO contracting officers had not properly delegated COR duties for 10 (29 percent) of 34 PEPFAR construction contracts they awarded. Contracting officers are required to prepare and issue a COR delegation memorandum as part of the award process in accordance with the COR Handbook.<sup>21</sup> CORs are to act as the contracting officers' authorized representatives for these PEPFAR construction projects, assisting in the administration of the contract. As such, they should receive a delegation memorandum outlining their responsibilities at the same time the requirements are initiated, as required by the COR Handbook.<sup>22</sup> However, Department contracting personnel did not always issue delegation memoranda to the CORs and, in some cases, did not follow up with CORs to ensure signed memoranda were returned to RPSO for inclusion in the contract files. Properly documenting the delegation of duties for CORs is important because it certifies that CORs understand their responsibilities.

### **Conclusion**

Because RPSO did not always document contract award actions, the Department cannot be assured that required contract actions were taken for the PEPFAR construction contracts. Specifically, documentation of procurement actions that establish price, promote competition and contract transparency, and delineate contract administration roles and responsibilities are essential to demonstrate the adequacy of the contract award.

### Management Comments to the Finding and OIG Analysis

A/LM/AQM, in its October 7, 2011 response, disagreed that an IGCE was necessary in establishing a fair price. A/LM/AQM stated that price reasonableness was established by contacting three or more contractors and therefore an IGCE was not necessary.

FAR 36.203 requires that “[a]n independent Government estimate of construction costs shall be prepared and furnished to the contracting officer at the earliest practicable time for each proposed contract and for each contract modification anticipated to exceed the simplified acquisition threshold.” Because the PEPFAR contracts exceeded the simplified acquisition threshold, IGCEs should have been prepared.<sup>23</sup> Further, Department regulations<sup>24</sup> require that an IGCE be prepared “to serve as a basis for comparing costs or prices proposed by offerors” and the Department’s *Overseas Contracting and Simplified Acquisition Guidebook* states that one of the purposes of the IGCE is to determine price reasonableness.

**Recommendation 1.** OIG recommends that the Regional Procurement Support Office in Frankfurt, Germany, issue instructions for its procurement staff to review active PEPFAR construction contract files to determine whether required contract award actions for PEPFAR construction contracts were properly performed and documented, including

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<sup>21</sup> 14 FAH-2 H-143.2(2), “Appointment Procedures.”

<sup>22</sup> 14 FAH-2 H-142, “Responsibilities of the Contracting Officer’s Representative.”

<sup>23</sup> FAR 2.101 defines the simplified acquisition threshold as \$150,000, as of October 1, 2010. The simplified acquisition threshold at the time of OIG fieldwork was \$100,000.

<sup>24</sup> 14 FAH-2 H-351 a (2) and c.

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obtaining an Independent Government Cost Estimate, publicizing contract solicitations, and delegating a contracting officer's representative. If documentation supporting any of these actions is found, it should be included in the respective file.

**Management Response:** A/LM/AQM agreed with the recommendation and stated it had conducted a complete review of PEPFAR files in January 2011, in response to OIG's preliminary findings, and has added missing documentation to the files.

**OIG Analysis:** OIG considers this recommendation resolved and closed because of the actions taken by RPSO to implement the recommendation, along with evidence that PEPFAR construction contract files have been reviewed and deficiencies pertaining to documentation addressed.

### **Contingency Costs Were Inappropriately Included in Firm-Fixed-Price Contracts**

Contingency costs of about \$2 million were inappropriately included in eight firm-fixed-price contracts and 30 task orders valued at nearly \$30 million out of the 100 contracts and task orders awarded by RPSO and reviewed by OIG. Because these contingency costs were part of the overall value of the contract, the funds could be spent without pre-approval from the Department. As a result, the Department could pay for goods or services it would otherwise not approve.

### **Construction Procurements With Contingency Costs**

Of the 100 PEPFAR construction procurements (contracts and task orders) awarded between FY 2005 and the first quarter of FY 2010 reviewed, OIG found that 38 contracts and task orders, valued at \$29,926,033, inappropriately included contingency costs totaling \$2,126,148. The contracts and tasks orders with inappropriate contingency costs are shown by country and dollar amount in Table 2.

**Table 2. Contracts and Task Orders With Inappropriate Contingency Costs (in U.S. Dollars)**

<b>Country</b>	<b>Contingency Cost</b>	<b>PEPFAR Amount</b>
Tanzania	964,668	10,027,924
Ethiopia	708,931	13,635,953
Uganda	8,265	204,817
Namibia	29,348	711,511
Zambia	118,748	934,984
Mozambique	194,250	2,500,000
Kenya	101,938	1,910,844
<b>Total</b>	<b>\$ 2,126,148</b>	<b>\$ 29,926,033</b>

Source: OIG-generated from RPSO contract files.

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A contingency, as described in the FAR 31.205-7, is “a possible future event or condition arising from presently known or unknown causes, the outcome of which is indeterminable at the present time.” According to the FAR, contingencies may be included in estimates of future costs if they “arise from presently known and existing conditions, the effects of which are foreseeable within reasonable limits of accuracy.” However, effects that cannot “be measured so precisely as to provide equitable results to the contractor and to the Government” are to be excluded from cost estimates.

### **Contingency Costs and Firm-Fixed-Price Contracts**

The director of RPSO stated that the office added funds on contracts for contingencies to streamline the administrative process, because if additional funds were needed after contract award, it could take months to get a modification approved. Some contract terms stated that the contingency funds were to “cover any additional construction effort that is required but could not be identified in time for inclusion in the solicitation package.” In addition, some task orders included language about contingency funds, stating that they were for possible construction revisions during the performance period and were placed in the contract for obligation purposes only. The contingency cost amount for some contracts was estimated as a percentage of the total contract value because, at the time of contract award, RPSO contracting officials could not determine the amount that would be needed. Further, the contract terms did not require any additional information from the contractor in order for the contractor to request payments for these contingency funds. For the contract files OIG reviewed that included either contingency costs or “provisional funds,” OIG found no evidence that, at the time of contract award, the contingency costs for the PEPFAR construction contracts were for known and existing conditions.

According to the FAR,<sup>25</sup> a firm-fixed-price contract “provides for a price that is not subject to any adjustment on the basis of the contractor’s cost experience in performing the contract. This contract type places upon the contractor maximum risk and full responsibility for all costs and resulting profit or loss.” The COR Handbook<sup>26</sup> states that payment for satisfactory completion of work is fixed and the contractor receives the pre-negotiated, fixed amount, regardless of actual costs incurred.” Adding funds to the contract for unknown future costs or contingencies in essence negates the purpose of a firm-fixed-price contract. In addition, the contractor may spend contingency funds on goods and services without approval from the U.S. Government, which could result in the Department paying for goods and services it would otherwise not approve. Ending the practice of adding contingency costs to firm-fixed-price PEPFAR construction contracts and reclaiming \$2 million in contingency costs inappropriately included in previous contracts and task orders are appropriate and prudent actions to ensure the effective use of PEPFAR funding.

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<sup>25</sup> FAR 16.202-1.

<sup>26</sup> 14 FAH-2 H-232, “Fixed-Price Contracts.”

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### Management Comments to the Finding and OIG Analysis

In its response to OIG's draft report, A/LM/AQM stated that RPSO required modification to PEPFAR contracts before contingency funds could be released and this information was clearly stated in RPSO's contract documents. However, in some of the contracts OIG reviewed, the language was unclear regarding how to handle contingencies. For example, in Tanzania, the language in the contract related to contingencies was confusing to the COR, technical advisor, and contractor. The technical advisor for the projects OIG reviewed said the language regarding contingencies was ambiguous and the COR responsible for overseeing the project said that RPSO procurement staff provided conflicting guidance about how to treat contingency costs. The contractor on the project was also unclear about how contingencies should be handled believing that they were entitled to the full amount of the award, including contingencies, because the award was fixed price.

**Recommendation 2.** OIG recommends that the Regional Procurement Support Office in Frankfurt, Germany, issue instructions for its personnel to stop the practice of including contingency funds in PEPFAR construction contracts unless identified contingencies arise from presently known and existing conditions, as described in section 31.205-7 of the *Federal Acquisition Regulation*.

**Management Response:** A/LM/AQM agreed with the recommendation and stated RPSO issued informal guidance to staff about contingencies after OIG's visit to RPSO.

**OIG Analysis:** OIG considers this recommendation resolved because RPSO has taken steps to address the recommendation; however, this recommendation will remain open until RPSO provides evidence that personnel have received guidance about the proper application of contingency costs.

**Recommendation 3.** OIG recommends that the Regional Procurement Support Office in Frankfurt, Germany, review existing PEPFAR construction contracts and reclaim any contingency costs inappropriately included in contracts as practicable.

**Management Response:** A/LM/AQM agreed with the recommendation and stated RPSO Frankfurt has used change orders to modify contracts that contained contingency costs or has deobligated the contingency costs from PEPFAR construction contracts.

**OIG Analysis:** OIG considers this recommendation resolved because RPSO has taken steps to implement it; however, this recommendation will remain open until RPSO provides evidence that PEPFAR construction contracts containing contingency costs have been modified or contingency costs deobligated for the award actions OIG reviewed.

### **Incomplete Contract Monitoring Leaves PEPFAR Construction Projects at Risk**

At two of the three posts OIG visited—Tanzania and Uganda—OIG reviewed 22 PEPFAR contract files related to actual construction, 18 in Tanzania and four in Uganda, that did

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not always contain adequate documentation of required monitoring actions.<sup>27</sup> Specifically, eight of the 18 COR contract files reviewed in Tanzania lacked evidence to show that CORs obtained inspection reports from independent CMS contractors. Additionally, the inspection reports that were included in the files in Tanzania and Uganda did not always include the detailed information required by the contract terms. In Tanzania, three of 18 files also did not contain evidence showing that site visits were being conducted. OIG also found that 12 of the 38 construction and construction-related contract files OIG reviewed in Tanzania (see Table 1) did not contain evidence showing that progress payments had been reviewed. In Ethiopia, however, an engineer with technical construction expertise was hired to handle most of the monitoring functions for the U.S. Government, which resulted in better recordkeeping and more effective oversight.

The FAR<sup>28</sup> requires that contract files contain all pertinent contract actions. Therefore, the contracting officers at RPSO were ultimately responsible for ensuring that contract files contained evidence of monitoring efforts, but they did not always provide adequate oversight of CORs to ensure these activities were documented. As a result, the U.S. Government cannot be assured that construction always followed design specifications and met quality standards.

### **Monitoring Requirements**

The COR Handbook<sup>29</sup> states:

To assure performance of a contract in the manner most beneficial to the U.S. Government, the U.S. Government has the responsibility to actively watch and follow the contractor's performance and take prompt, affirmative action to correct problems. This is one of the most vital elements of what is called 'contract administration,' i.e., making sure that the terms and conditions agreed upon when the contract was awarded are actually carried out.

As part of contract administration, CORs are required to "maintain a file documenting significant actions and containing copies of trip reports, correspondence, and reports and deliverables received under the contract."<sup>30</sup>

### **Contract Monitoring in Ethiopia**

OIG found that Ethiopia had proper documentation to show consistent monitoring, including very detailed records of monitoring activities for the eight construction files reviewed. For example, the CMS contractor monitored construction by employing a resident employee, or "resident engineer," who was on-site and worked the same hours as the construction contractor.<sup>31</sup> On a daily basis, the resident engineer monitored and recorded the number and type

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<sup>27</sup> Of the 100 PEPFAR construction contract files OIG reviewed, 14 were in Ethiopia, 38 were in Tanzania, and seven were in Uganda. Of these files, 29 were for CMS or design services, and 30 were for construction activities.

<sup>28</sup> FAR 4.801(a) and (b)(1)(2)(3)(4).

<sup>29</sup> 14 FAH-2 H-511(a), "Administration."

<sup>30</sup> 14 FAH-2 H-513c(2), "The Contracting Officer's Representative's (COR) Role in Contract Administration."

<sup>31</sup> A resident engineer is an on-site monitor employed by the CMS contractor.

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of workers, on-site equipment, type and amount of work performed, and other information and activities. Reports that included this information were prepared daily and signed by the resident engineer and construction contractor. Daily reports were subsequently incorporated into monthly progress reports provided to the COR.

In addition, the COR in Ethiopia had an engineer with technical construction expertise to oversee and work closely with the CMS contractor to ensure that the contract requirements were met and construction project progressed as expected.

### **Contract Monitoring in Tanzania and Uganda**

At two posts OIG visited—Tanzania and Uganda—OIG found that CORs did not obtain adequate documentation from CMS contractors of construction monitoring activities. Specifically, eight of 18 PEPFAR construction contract files reviewed in Tanzania contained no evidence that inspection reports were obtained, and the remaining files often did not include all of the elements required under the terms of the contract. Although the four construction contract files reviewed in Uganda contained one inspection report for each project under construction, the files did not include all of the required monthly reports, and the single report obtained for each project did not include the detailed information required under the terms of the contract. Three of 18 contract files reviewed in Tanzania did not contain evidence to show that CORs had conducted site visits. In addition, 12 of the 38 construction and construction-related contract files OIG reviewed in Tanzania contained no evidence showing that progress payments had been reviewed.

Inspection Reports – Although required, CMS contractors did not provide inspection reports to the COR for eight of 18 construction contract files in Tanzania. OIG also found that the inspection reports were received sporadically, although the contract terms generally required reports to be submitted monthly. The inspection reports that the CORs received in Tanzania and Uganda did not always address inspection elements required by the contract, such as the date and time of the inspection, individuals met on-site the day of inspection, workers present, and any items found to be deficient. Each deficient item should include a description and explanation (cause) of the deficiency, the impact or consequences, recommended corrective action, and potential hazards.

CMS contractors were required to carry out and document inspections to determine whether services were performed according to the contract requirements and provide copies of inspection reports to the COR. In accordance with the COR Handbook,<sup>32</sup> the COR must ensure that the contractor complies with reporting provisions in the contract. The COR Handbook also states that the “COR must read and understand the progress reports to identify and initiate steps to deal with any threats to performance that they may disclose.”

However, in Uganda, the COR received only one combined inspection report for all four ongoing projects from the CMS contractor in March 2010, even though the CMS contractor should have been monitoring the projects for 5 months beginning in October 2009 and sending

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<sup>32</sup> 14 FAH-2 H-522.2, “Reports.”

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monthly reports to the COR. Prior to OIG's site visit to Tanzania, the COR made a special effort to obtain CMS inspection reports for the construction contract files but received reports for only six of 18 contracts.

Site Visits – OIG found that three of 18 construction procurement files in Tanzania did not contain evidence of any COR site visits. Although Uganda's files showed at least one COR site visit report for each of the four ongoing projects, the files were missing reports for dates site visits were indicated to have occurred, as noted in the files. In accordance with the COR Handbook,<sup>33</sup> CORs are required to conduct site visits to check a contractor's actual performance against the contractor's reported performance. In addition, physical on-site visits provide assurance that the contractor is performing work as expected.

Progress Payment Reviews – OIG found that 12 of 38 construction and construction-related COR contract files in Tanzania did not contain evidence that CORs were reviewing progress payment requests. CORs are required to review contractor invoices prior to payment to ensure that costs are valid and to compare claimed costs against actual progress. According to the COR Handbook<sup>34</sup> CORs are responsible for "monitoring the contractor's technical progress and the expenditures of resources relating to the contract."

### **Responsibility for Contract Monitoring**

In practice, RPSO contracting officers are primarily involved in the solicitation and award of procurements; CORs perform day-to-day contract monitoring after the award. However, RPSO contracting officers are ultimately responsible for contract monitoring because they are required to assess whether contractor performance is satisfactory.<sup>35</sup>

RPSO contracting officers stated that they are not responsible for ensuring that CORs properly monitor construction projects, but rather this is the responsibility of program officials or the CMS contractor. RPSO contracting officers said they tend to get involved with CORs only when specifically requested or when the contract needs to be modified. Some of RPSO's contract files that OIG reviewed included copies of progress reports and site visits for PEPFAR construction projects. However, these documents were not always included in RPSO's contract files or the COR's contract files at post.

RPSO contracting officers stated that many CORs monitoring PEPFAR construction contracts were CDC medical professionals who often were not experienced in monitoring construction contracts. However, because RPSO contracting officers and contract specialists were aware of this limitation, they should have been even more involved with the CDC-designated CORs to ensure that proper procedures were followed. The director of RPSO acknowledged that CORs from the CDC would benefit from hiring engineers to confirm before payment whether buildings were completed according to specifications. However, at two posts with substantial construction (Tanzania and Uganda), there was no engineer on-site to perform this task.

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<sup>33</sup> 14 FAH-2 H-522.3, "Site Visits."

<sup>34</sup> 14 FAH-2 H-142b(7).

<sup>35</sup> 14 FAH-2 H-513a.

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The U.S. Government cannot be assured that PEPFAR facilities in Tanzania and Uganda were properly constructed or monitored. At one location in Tanzania, a site where a PEPFAR facility was to be built had previously been a trash dump. The original design contractor did not perform an environmental scan of this location, which would have likely been uncovered through effective monitoring. At another PEPFAR–constructed facility in Uganda, the contractor had completed renovating a laboratory to be used for treating tuberculosis patients but did not install a key piece of equipment required to operate the laboratory—a negative air pressure system. This system is required to meet international accreditation standards and is used to prevent the dispersion of microbial pathogens from contaminated areas. CDC personnel told OIG that, before they could open the lab, they would require an additional \$70,000 to \$80,000 to obtain and install the system. In addition, without evidence of progress payment reviews, contractors may be paid for work that may not have been actually completed, and the U.S. Government is not assured that constructed facilities meet design specifications.

**Recommendation 4.** OIG recommends that the Regional Procurement Support Office in Frankfurt, Germany, issue instructions for its procurement staff to fully document contract monitoring to assess whether contractor performance is satisfactory.

**Management Response:** A/LM/AQM agreed with the recommendation and stated RPSO Frankfurt “...will provide additional guidance to CORs emphasizing the need to maintain adequate contract files on contract monitoring.”

**OIG Analysis:** OIG considers this recommendation resolved because A/LM/AQM has agreed to take necessary steps to implement it; however, this recommendation will remain open until RPSO provides evidence that CORs responsible for PEPFAR construction contracts have received additional guidance about maintaining contract monitoring files.

**Recommendation 5.** OIG recommends that the Regional Procurement Support Office in Frankfurt, Germany, require posts with substantial planned costs for PEPFAR construction projects to obtain a technical advisor with construction expertise for monitoring construction contracts.

**Management Response:** A/LM/AQM agreed with “...the concept of posts obtaining a technical advisor with construction expertise for monitoring construction contracts” but stated that RPSO Frankfurt cannot require CORs to hire a technical advisor. However, A/LM/AQM stated that RPSO Frankfurt will augment guidance to its customers, emphasizing ways to improve contract monitoring.

**OIG Analysis:** OIG considers this recommendation resolved because A/LM/AQM has agreed to take steps to improve technical oversight of PEPFAR construction contracts; however, this recommendation will remain open until RPSO provides evidence that that additional guidance emphasizing ways to improve contract monitoring has been disseminated.

## **Best Practice – Standard Design for PEPFAR Construction**

At the outset of his administration, President Obama stated that the U.S. Government needed to work better, faster, and more efficiently. The *Tom Lantos and Henry J. Hyde United States Global Leadership Against HIV/AIDS, Tuberculosis, and Malaria Reauthorization Act of 2008*<sup>36</sup> reauthorized PEPFAR funding for FY 2009 and required, among other items, that a best practices report be disseminated. In addition, on September 14, 2010, the President’s Management Council—a group of Federal agency Deputy Secretaries overseeing the President’s efficiency goals—stated that the Council is “pursuing a management agenda that embraces technological innovations and management best practices to improve effectiveness, efficiency, and customer service.”<sup>37</sup>

OIG noted a best practice of using standard design to construct PEPFAR facilities in Tanzania and Ethiopia. If implemented more widely, this best practice could reduce costs and project completion times for PEPFAR construction.

### **Standard Design**

The CDC has plans to construct approximately 90 medical facilities. Most buildings constructed for PEPFAR are medical facilities, including laboratories and outpatient health clinics. In Tanzania, the CDC hired consultants to analyze planned projects, and these consultants recommended using standard design. In Ethiopia, the CDC is building seven regional laboratories using the same design. The advantages of using standard design are described in “Best Practice – Standard Design.”

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<sup>36</sup> Section 205 of the *Tom Lantos and Henry J. Hyde United States Global Leadership Against HIV/AIDS, Tuberculosis, and Malaria Reauthorization Act of 2008* (Pub. L. No. 110-293 § 205).

<sup>37</sup> Memorandum for the Senior Executive Service, “The Accountable Government Initiative – an Update on Our Performance Management Agenda,” Office of Management and Budget, September 14, 2010.

**Best Practice - Standard Design**

In Tanzania, the Centers for Disease Control and Prevention (CDC) currently has five standard designs ranging from small to supersize. CDC Tanzania has engaged architectural services to use standard design to build four care and treatment centers with 13 rooms and three care and treatment centers with 11 rooms. These clinics have standardized layout, roofing, walls, security, plumbing, and electrical requirements. CDC Tanzania also engaged architectural services to use a standard design to renovate 11 one-room tuberculosis clinics. This standard design turned the one-room clinics into six-room clinics, with installed plumbing; wiring for computers, phones, and fans; and a layout to accommodate patient confidentiality and patient flow.

In Ethiopia, the CDC is building seven regional laboratories using the same design. The design requirements include safety protection, radio frequency shielding, seismic consideration, utility and drainage systems, and water treatment. The standard design makes it easier to modify existing laboratories and easier to transfer modifications to future project designs. Even where standard design is not used, such as for outpatient annexes in various sizes, project materials come from a standardized set of specifications. To further its standard design efforts, CDC Ethiopia issued a scope of work order for design work at medical facilities seeking an integrative prototype outpatient department model.

Using standard design includes the following advantages:

- Cost savings from minimizing architectural services.
- Shortened time of project from site selection to project completion because individual project architectural analyses and drawings are not needed. The Department recorded a 34 percent shorter project duration in its first year using standard design for embassies.
- Reduction in project error because approved designs are repeated.
- Incorporation of specific expertise that might not be available through local architects into standard design.
- Ease of monitoring and assessing the progress and quality of construction.
- Shorter learning curve for contractors bidding to build the facilities.
- Ability to standardize laboratory equipment—changing the design of the laboratories makes it more difficult to coordinate the various types and location of equipment in laboratories.

## **List of Recommendations**

**Recommendation 1.** OIG recommends that the Regional Procurement Support Office in Frankfurt, Germany, issue instructions for its procurement staff to review active PEPFAR construction contract files to determine whether required contract award actions for PEPFAR construction contracts were properly performed and documented, including obtaining an Independent Government Cost Estimate, publicizing contract solicitations, and delegating a contracting officer's representative. If documentation supporting any of these actions is found, it should be included in the respective file.

**Recommendation 2.** OIG recommends that the Regional Procurement Support Office in Frankfurt, Germany, issue instructions for its personnel to stop the practice of including contingency funds in PEPFAR construction contracts unless identified contingencies arise from presently known and existing conditions, as described in section 31.205-7 of the *Federal Acquisition Regulation*.

**Recommendation 3.** OIG recommends that the Regional Procurement Support Office in Frankfurt, Germany, review existing PEPFAR construction contracts and reclaim any contingency costs inappropriately included in contracts as practicable.

**Recommendation 4.** OIG recommends that the Regional Procurement Support Office in Frankfurt, Germany, issue instructions for its procurement staff to fully document contract monitoring to assess whether contractor performance is satisfactory.

**Recommendation 5.** OIG recommends that the Regional Procurement Support Office in Frankfurt, Germany, require posts with substantial planned costs for PEPFAR construction projects to obtain a technical advisor with construction expertise for monitoring construction contracts.

## **Scope and Methodology**

The purpose of this review was to assess Department of State (Department) effectiveness in awarding and monitoring contracts supporting President's Emergency Plan for AIDS Relief (PEPFAR) projects. The primary objective of this review was to determine whether the Department followed applicable policies, regulations, and procedures in awarding and monitoring PEPFAR construction projects.

To obtain an understanding of laws and regulations related to the award and monitoring of overseas construction and construction-related activities, the Office of Inspector General (OIG) reviewed the *Federal Acquisition Regulation (FAR)*, the *Foreign Affairs Manual*, the *Foreign Affairs Handbook*, *Department of State Acquisition Regulations*, and the *Overseas Contracting and Simplified Acquisition Guidebook*.

OIG also searched the Internet and the Department's Web site for information relevant to the construction industry, Federal construction contracting, and the construction of health care facilities. OIG obtained and reviewed documents from the Department and the Centers for Disease Control and Prevention that explained the PEPFAR overseas construction process and procedures, as well as information about issues affecting the procurement process.

OIG met with key personnel from the Office of the U.S. Global AIDS Coordinator and the Bureau of Administration to discuss their roles and understanding of PEPFAR overseas construction projects.

OIG's Office of Audits conducted this review from January 2010 to January 2011 in accordance with the *Quality Standards for Inspections*, issued in January 2005 by the Council of the Inspectors General on Integrity and Efficiency.

### **Contract Files Reviewed and Sites Visited**

During this review, OIG visited the Regional Procurement Support Office (RPSO) in Frankfurt, Germany, from January to February 2010 to obtain an understanding of RPSO's contract award and monitoring processes. OIG also developed a list, using contract files, of all PEPFAR overseas construction projects awarded by RPSO from FY 2003 through the first quarter of FY 2010 to nine African countries: Tanzania, Ethiopia, Uganda, Namibia, Zambia, Mozambique, Kenya, Botswana, and Malawi. OIG's list showed that RPSO awarded 145 contracts and task orders, valued at \$56,009,736, during the period to these nine countries. Of the 145 contracts and task orders, 99 contracts and task orders (68 percent), totaling \$43,300,994, were awarded to Tanzania, Ethiopia, and Uganda. OIG focused its review on contracts and task orders that were awarded from FYs 2007–2009, although five of the 100 contracts reviewed were not awarded during that time period,<sup>1</sup> thereby narrowing the scope from 145 contracts and

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<sup>1</sup> These five contracts consisted of two contracts awarded in FY 2005, two contracts awarded in FY 2006, and one contract awarded in FY 2010.

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task orders to 100, as shown in Table 1. These 100 files contained 34 contracts (21 firm-fixed-price contracts and 13 indefinite delivery/indefinite quantity contracts) and 66 associated task orders, all of which totaled \$39,207,381.

**Table 1. Total PEPFAR Overseas Construction Procurements, FY 2003 – FY 2010**

Country	Awarded by RPSO		Reviewed by OIG at RPSO		Reviewed by OIG at Post	
	Number of Items*	Value in U.S. Dollars	Number of items	Value in U.S. Dollars	Number of items	Value in U.S. Dollars
Tanzania	58	22,276,299	52	11,991,137	38	7,275,944
Ethiopia	22	16,274,205	14	15,865,597	14	15,865,597
Uganda	19	4,750,490	17	2,980,433	7	2,475,443
<b>Subtotal</b>	<b>99</b>	<b>43,300,994</b>	<b>83</b>	<b>30,837,167</b>	<b>59</b>	<b>25,616,984</b>
<b>Percent of Totals</b>	<b>68</b>	<b>77</b>	<b>83</b>	<b>79</b>	<b>100</b>	<b>100</b>
Namibia	12	3,320,025	5	1,805,691	-	-
Zambia	12	3,299,140	3	1,141,687	-	-
Mozambique	3	2,821,880	3	2,821,880	-	-
Kenya	11	2,813,360	4	2,321,640	-	-
Botswana**	6	279,316	2	279,316	-	-
Malawi	2	175,021	-	-	-	-
<b>Subtotal</b>	<b>46</b>	<b>12,708,742</b>	<b>17</b>	<b>8,370,214</b>	-	-
<b>Percent of Totals</b>	<b>32</b>	<b>23</b>	<b>17</b>	<b>21</b>	-	-
<b>Totals</b>	<b>145</b>	<b>\$ 56,009,736</b>	<b>100</b>	<b>\$ 39,207,381</b>	<b>59</b>	<b>\$ 25,616,984</b>
<b>Percent of Totals</b>	100	100	69	70	59	65

Source: OIG-generated from RPSO contract files.

\*The number of items includes contracts and task orders.

\*\* Although OIG verified that RPSO awarded six contracts for Botswana, OIG was unable to determine the funding source for four of the contracts. Therefore, the dollar amounts for those four contracts have not been included.

At RPSO, OIG reviewed the 100 files to determine whether the files contained the required documentation to show that procurement personnel followed Federal laws and policies in awarding and monitoring these contracts and their associated task orders. In addition, OIG assessed whether the contract files contained documentation to show that RPSO provided oversight for the PEPFAR construction projects.

OIG then selected Tanzania, Ethiopia, and Uganda for site visits conducted in April and May 2010 because these three countries were the chief beneficiaries of PEPFAR construction procurements, as indicated above in Table 1. They had 83 procurements related to PEPFAR construction projects valued at \$30,837,167 (or 79 percent of the total \$39,207,381) for the period FY 2007 through FY 2009. At these three posts, OIG reviewed 59 of the 83 (or 71 percent) COR files, valued at \$25,616,984, to determine whether the files contained adequate evidence of monitoring, such as inspection reports, site visit reports, and progress payments with required acceptance and approval.

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OIG interviewed contracting officer’s representatives, construction monitoring services personnel hired by RPSO, and host country officials overseas to gain an understanding of their procedures for monitoring construction projects and to determine the extent of coordination with contracting officers at RPSO. OIG also visited nine construction sites in various phases of construction, including two completed facilities. At these sites, OIG observed the level of progress on construction projects and methods used to monitor construction. OIG also gained an understanding of the services to be provided and any problems or delays encountered. The construction sites OIG visited in each country are shown in Table 2.

**Table 2. PEPFAR Construction Sites Visited**

Tanzania	National Headquarters and Zonal Blood Transfusion Center
	Temeke Hospital Ward
	Tandale Care and Treatment Clinic
Ethiopia	Zewditu Hospital Health Clinic, ART Treatment
	Adama Hospital Regional Blood Bank Laboratory
	Armed Forces Hospital Health Clinic, VCT/ART
Uganda	Uganda Blood Transfusion Services
	Mukono Health Center IV
	National TB & Referral Laboratory

Source: OIG-generated.

After its site visits, OIG reviewed and materials obtained from RPSO and COR files to determine whether these files were complete and to identify discrepancies needing resolution. Subsequently, in January 2011, OIG requested and obtained from RPSO additional information and responses that addressed contract award issues and answers to its questions resulting from its review of procurement documents. OIG analyzed the additional information provided and adjusted its results accordingly.

**Data Reliability and Use of Computer-Processed Data**

OIG obtained from RPSO’s database a list of PEPFAR construction procurements. RPSO developed this database as a separate log to track procurements by year. OIG compared the list generated from the RPSO database with information contained in RPSO files to verify the completeness of the list. OIG believes that the data was sufficiently reliable for purposes of its report and that the evidence obtained provides a reasonable basis for the findings and conclusions based on the review objective.

**Prior OIG Reports**

In June 2011, OIG reported<sup>2</sup> that the Department’s Office of the U.S. Global AIDS Coordinator (S/GAC) coordinated, provided oversight for, and transferred PEPFAR overseas

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<sup>2</sup> *Audit of Construction and Transfer of Ownership of the President’s Emergency Plan for AIDS Relief (PEPFAR) Construction Projects*, AUD/IP-11-14, June 2011.

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construction projects on an ad hoc basis. In addition, S/GAC did not establish effective internal controls for PEPFAR construction projects and did not properly transfer completed construction projects to host governments. OIG made four recommendations for S/GAC (1) to develop an interagency memorandum of agreement to address the PEPFAR overseas construction projects, (2) to seek resolution about the legal dispute on construction authority with senior-level management within the Department of Health and Human Services (HHS), (3) to appoint a senior-level official with the requisite experience in construction and authority to make decisions related to PEPFAR overseas construction projects, and (4) to establish guidance for all agencies involved with PEPFAR overseas construction projects that clearly describes procedures for construction and property management.

The second recommendation, which pertained to the legal dispute, was closed because S/GAC immediately took action to reclaim and redistribute \$51 million in PEPFAR construction funds provided to HHS and the U.S. Agency for International Development—thus eliminating the need for resolution of the legal dispute with HHS. The remaining three recommendations are resolved because S/GAC has taken action to implement them. They can be closed when OIG receives and accepts documentation showing that they have been implemented.



United States Department of State

Washington, D.C. 20520

October 7, 2011

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**MEMORANDUM**

TO:           OIG/AUD – Evelyn R. Klemstine

FROM:        Cathy Read *[Signature]* A/LM/AQM

SUBJECT:     Response to Draft Report on Improved Contract Documentation and Monitoring by the Regional Procurement Support Office Are Needed for Construction Projects Associated with the President's Emergency Plan for AIDS Relief (PEPFAR)

The following are the Office of Acquisitions Management (A/LM/AQM) comments on Recommendations 1 through 5 and technical comments of the subject Audit Report.

**Recommendation 1.** OIG recommends that the Regional Procurement Support Office in Frankfurt, Germany, issue instructions for its procurement staff to review active PEPFAR construction contract files to determine whether required contract award actions for PEPFAR construction contracts were properly performed and documented, including obtaining an Independent Government Cost Estimate, publicizing contract solicitations, and delegating a contracting officer's representative. If documentation supporting any of these actions is found, it should be included in the respective file.

**A/LM/AQM's Response:** A/LM/AQM concurs with this recommendation. RPSO Frankfurt issued informal guidance and discussed repeatedly in staff meetings to review active PEPFAR construction contract files for completeness. RPSO Frankfurt publicizes construction contracts on the Berlin embassy website and with local construction companies that are recommended by the client. For A & E contracts, restricting advertisement to the Berlin embassy website will exclude notifying qualified and registered companies in the country where work is going to be performed. Competition was sought and achieved through wide distribution to known architecture firms in the applicable countries. Based on OIG findings, a

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complete review of all PEPFAR files was conducted in January 2011 and appropriate missing documentation has been added to the file.

**Recommendation 2.** OIG recommends that the Regional Procurement Support Office in Frankfurt, Germany, issue instructions for its personnel to stop the practice of including contingency funds in PEPFAR construction contracts unless identified contingencies arise from presently known and existing conditions, as described in section 31.205-7 of the *Federal Acquisition Regulation*.

**A/LM/AQM's Response:** A/LM/AQM concurs with this recommendation. RPSO Frankfurt issued informal guidance repeatedly in staff meetings since the OIG's original visit. RPSO Frankfurt will periodically remind staff about contingency funds in construction contracts. RPSO Frankfurt notes that in a firm-fixed contract, the inclusion of risk in a contractor's proposal (sometimes referred to as a contingency) is allowable. In cases where risk is already priced and a separate line item for contingencies is identified, RPSO staff will not include these costs unless they are in accordance with FAR 31.205-7.

**Recommendation 3.** OIG recommends that the Regional Procurement Support Office in Frankfurt, Germany, review existing PEPFAR construction contracts and reclaim any contingency costs inappropriately included in contracts as practicable.

**A/LM/AQM's Response:** RPSO Frankfurt employed this practice prior to OIG's audit and will continue this practice. All such costs identified from the PEPFAR construction contracts were modified via valid change orders (including requests for equitable adjustments) or deobligated from the contract.

**Recommendation 4.** OIG recommends that the Regional Procurement Support Office in Frankfurt, Germany, issue instruction for its procurement staff to fully document contract monitoring to assess whether contractor performance is satisfactory.

**A/LM/AQM's Response:** RPSO Frankfurt will provide additional guidance to CORs emphasizing the need to maintain adequate contract files on contract monitoring. RPSO Frankfurt documents the Contracting Officer's file for past performance as required by the FAR.

**Recommendation 5.** OIG recommends that the Regional Procurement Support Office in Frankfurt, Germany, require posts with substantial planned costs for

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PEPFAR construction projects to obtain a technical advisor with construction expertise for monitoring construction contracts.

**A/LM/AQM's Response:** A/LM/AQM agrees with the concept of posts obtaining a technical advisor with construction expertise for monitoring construction contracts. RPSO Frankfurt recommends to all PEPFAR clients to hire a technical advisor and issues IDIQ contracts to A&E firms to perform construction monitoring services to assist posts. RPSO Frankfurt cannot require that customers obtain a technical advisor if the COR believes sufficient expertise is already available to monitor the program. RPSO Frankfurt will augment guidance to construction customers to emphasize various ways to improve contract monitoring to include better monitoring documentation and more effective use of technical support.

**A/LM/AQM's technical corrections to the draft OIG report:** RPSO Frankfurt respectfully submits the following recommended changes to the draft report text:

**Page 6** – “the Department cannot be assured that it obtained a fair and reasonable price from the bidder or offeror” –

**A/LM/AQM's comments:** RPSO Frankfurt submits that adequate competition was always received. Three or more contractors were contacted in all cases for all contracts awarded. Price reasonableness is then established by competitive price comparison.

**Page 6** – “IGCEs are important in establishing a fair price for U.S. Government contracts.”

**A/LM/AQM's comments:** RPSO Frankfurt submits that in accordance with FAR 15.402 and 15.404-1 adequate price competition establishes price reasonableness. Therefore, in cases where an IGCE was not provided by post, adequate price competition was received by three or more firms and thus price reasonableness was established. IGCEs are useful to perform price analysis when competition is lacking.

**Page 7** – “Because these contingency costs were part of the overall value of the contract, the funds could be spent without pre-approval from the Department.”

**A/LM/AQM's comments:** RPSO Frankfurt submits that the above statement is inaccurate. Obligated dollars that were placed on the contract in this capacity were

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specifically excluded from the firm fixed price. Additionally, in order for the contractor to utilize these funds a formal modification, authorizing specific work to the contract, was required.

**Page 8** – “Further, the contract terms did not require any additional information from the contract in order for the contractor to request payments for these contingency funds.”

**A/LM/AQM’s comments:** RPSO Frankfurt submits when a contingency or provisional sum was placed on an award it was specifically written in the award that the funds associated with those line items could only be utilized upon a formal contract modification that incorporated them into the firm fixed price.

**Page 9** – similar statement about the contractor being able to spend these monies without prior approval.

**A/LM/AQM’s comments:** RPSO Frankfurt reasserts our above two comments which are applicable to this portion of the report.

**Page 12** – “RPSO contracting officers stated that they are not responsible for ensuring the CORs properly monitor construction projects”

**A/LM/AQM’s comments:** A/LM/AQM advises that Contracting Officers appoint CORs and are responsible to ensure they fulfill their duties. RPSO Frankfurt relies heavily on the CORs to monitor their projects.

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Drafted: A/LM: Mark Bohac x5-5840

Cleared: A/LM/AQM/RPSO: [REDACTED]  
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