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Office of Inspector General  
United States Department of State

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Office of Audits

January 2024

# **Audit of Select Contract Administration Processes Related to the Construction of New Embassy Compound Mexico City, Mexico**

## **CONTRACTS, GRANTS, AND INFRASTRUCTURE DIVISION**

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# HIGHLIGHTS

Office of Inspector General  
United States Department of State

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## What OIG Audited

The Bureau of Overseas Buildings Operations (OBO) directs the worldwide overseas building program for the Department of State (Department) and sets worldwide priorities for the design and construction of projects under its purview. In coordination with OBO, the Bureau of Administration, Office of the Procurement Executive, Office of Acquisitions Management (AQM), is responsible for contract administration and oversight of the New Embassy Compound (NEC) Mexico City, Mexico, construction contract and modifications, with a total approved construction budget of \$632.4 million.

The Office of Inspector General (OIG) conducted this audit to determine whether OBO and the Bureau of Administration administered processes involving contract modifications, construction quality management, and progress payment reviews and approvals for the NEC Mexico City construction project in accordance with the Federal Acquisition Regulation (FAR) and Department guidance.

## What OIG Recommends

OIG made six recommendations to OBO and the Bureau of Administration to improve contract modification execution, project reporting, and contract administration for OBO construction projects. Based on the Department's responses to a draft of this report, OIG considers three recommendations resolved, pending further action, and three recommendations unresolved. A synopsis of management's responses to the recommendations offered and OIG's replies follow each recommendation in the Audit Results section of this report. Responses received from OBO and the Bureau of Administration are included in their entirety in Appendices B and C, respectively. A summary of OBO's technical comments with OIG's replies are presented in Appendix D.

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OFFICE OF AUDITS

CONTRACTS, GRANTS, AND INFRASTRUCTURE DIVISION

## Audit of Select Contract Administration Processes Related to the Construction of New Embassy Compound Mexico City, Mexico

### What OIG Found

Neither OBO nor AQM executed contract modifications for the NEC Mexico City construction contract in accordance with requirements. Specifically, the Project Director (PD) did not assess the impact that the contract modifications would have on the overall construction project timeline. In addition, the Department did not always perform required prenegotiation and negotiation activities to determine fair and reasonable pricing. Finally, the Contracting Officer did not always obtain required contractor release statements to avoid exposing the Department to increased financial risk. The deficiencies occurred, in part, because OBO and AQM management did not sufficiently oversee and enforce adherence to requirements. As a result, the Department executed contract modifications without full awareness of potential consequences to the construction project timeline and associated project costs.

OIG also found that the PD did not comply with construction quality management for project reporting. Specifically, the PD did not complete required daily logs and did not develop the required project procedures manual to guide project administration. The deficiencies occurred, in part, because OBO management failed to ensure that the PD fully complied with requirements. By failing to complete the daily logs and project procedures manual for a large, multimillion-dollar construction project, OBO limited its ability to protect the Department's interests and coordinate project administration.

Lastly, the PD approved progress payments for the NEC Mexico City construction project in accordance with requirements. Specifically, OIG found that the 15 selected progress payments reviewed for this audit contained an itemization of the amounts requested by the contractor and the contractor's certification, as required. In addition, the PD conducted monitoring activities to support the approval of progress payments. Because of the approval structure and the monitoring activities performed, the PD reasonably ensured that the contractor's requests for progress payments were valid and processed in a timely manner, thereby avoiding late payment penalties.

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## OBJECTIVE

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The Office of Inspector General (OIG) conducted this audit to determine whether the Bureau of Overseas Buildings Operations (OBO) and the Bureau of Administration administered processes involving contract modifications, construction quality management,<sup>1</sup> and progress payment reviews and approvals for the New Embassy Compound (NEC) Mexico City, Mexico, construction project in accordance with the Federal Acquisition Regulation (FAR) and Department of State (Department) guidance.

## BACKGROUND

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As the overseas real property manager for the Department, OBO has the lead role in acquiring, designing, building, operating, and maintaining Department facilities worldwide. In September 2017, the Bureau of Administration, Office of the Procurement Executive, Office of Acquisitions Management (AQM), on behalf of OBO, awarded Caddell Construction Co, LLC (Caddell), a firm-fixed-price,<sup>2</sup> design-bid-build<sup>3</sup> contract (Contract SAQMMA17C0287) for the construction of an NEC to be located in the Nuevo Polanco neighborhood of Mexico City, Mexico. The contract required Caddell to build a chancery, Marine Security Guard residence, underground parking structure, utility building, police barracks, and four campus access pavilions. The original substantial completion date<sup>4</sup> that was included in the contract for all required work was April 13, 2022. As of June 2023, the contract completion date was July 1, 2024, with an estimated substantial completion date of October 31, 2024. Figure 1 provides architectural renderings of NEC Mexico City.

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<sup>1</sup> Construction quality management includes all quality control and quality assurance activities instituted to achieve the quality established by the contract requirements.

<sup>2</sup> FAR 16.202-1, "Description," states that "a firm-fixed price contract provides for a price that is not subject to any adjustment based on the contractor's cost experience in performing the contract."

<sup>3</sup> FAR 36.102, "Definitions," defines design-bid-build as the traditional delivery method in which design and construction are sequential and contracted separately, with two contracts and two contractors.

<sup>4</sup> Substantial completion is the point at which the OBO project director determines that work is sufficiently complete and satisfactory for the Department to occupy the structure, with only minor items remaining to be completed or corrected.



Figure 1: Architectural renderings of NEC Mexico City.

**Source:** Architectural firm (Davis Brody Bond) website, <davisbrodybond.com>.

## **Contract Administration Responsibilities**

### ***Bureau of Administration***

The Office of the Procurement Executive is responsible for providing Department-wide acquisition policies and services, including developing, issuing, and maintaining acquisition regulations, procedures, and guidance.<sup>5</sup> Under the leadership of the Procurement Executive, AQM manages, plans, and directs the Department’s acquisition programs and conducts contract operations in support of activities worldwide. According to the Department’s Foreign Affairs Manual (FAM), AQM provides a full range of contract management services, including acquisition planning, contract negotiations, and cost and price analyses.<sup>6</sup> The Department’s Foreign Affairs Handbook (FAH) states that Contracting Officers (CO) have sole authority to negotiate, award, administer, modify, or terminate contracts.<sup>7</sup> The CO is also responsible for ensuring the performance of all necessary actions for effective contracting, ensuring compliance with the terms of the contract, and safeguarding the interests of the United States in its contractual relationships.<sup>8</sup>

### ***Bureau of Overseas Buildings Operations***

OBO’s Construction, Facility, and Security Management Directorate, Office of Construction Management (CM), provides management, oversight, and construction supervision of overseas construction projects. OBO’s CM office has five branches based on region: Africa, East Asia and Pacific, Europe, Near Eastern Asia, South and Central Asia, and Western Hemisphere. Senior Construction Executives, who lead each branch, assign Construction Executives to projects in their respective region. Each major overseas construction project is assigned an onsite Project

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<sup>5</sup> 1 FAM 212.2(b), “Office of the Procurement Executive (A/OPE).”

<sup>6</sup> 1 FAM 212.2-2(a), “Office of Acquisitions Management (A/AOPE/AQM).”

<sup>7</sup> 14 FAH-2 H-141(a), “Responsibilities of the Contracting Officer.”

<sup>8</sup> FAR 1.602-2, “Responsibilities.”

Director (PD),<sup>9,10</sup> who also serves as the Contracting Officer's Representative (COR)<sup>11</sup> for the construction contracts. Each PD reports to the assigned Senior Construction Executive.

The PD is responsible for all aspects of the construction project, including safety, security, quality assurance (QA), reporting, and reviewing and approving progress payment requests.<sup>12</sup> CM manages construction contracts in conjunction with the Bureau of Administration's Office of the Procurement Executive and monitors construction contractors' quality control (QC) in accordance with policies and standards.<sup>13</sup>

The PD, as the COR, is responsible for enforcing the terms and conditions of the construction contract and ensuring that all materials, equipment, and standards of workmanship comply with the contract requirements. This responsibility entails reviewing and obtaining approval of all required documents and reports and ensuring that the required documents and reports are prepared in a timely manner and are complete and accurate. The PD is also responsible for ensuring that all work is inspected and appropriately tested in accordance with the approved QA program and for rejecting any materials, equipment, or workmanship that does not comply with requirements. Additionally, the PD is responsible for reviewing all proposals for contract changes. In instances in which the estimated cost of a proposed change exceeds the PD's warrant authority, the PD is supposed to make a recommendation for action to the CO. When requested, the PD should prepare an independent government cost estimate<sup>14</sup> (IGCE) for proposed changes and negotiate and execute contract modifications on behalf of the CO. In addition, the PD is responsible for confirming pay requests from contractors based on submitted schedules of values. Furthermore, the PD approves and monitors the contractor's construction schedule to ensure that a project is completed in a timely manner and that the contractor's requests for progress payments are valid.<sup>15</sup>

The FAH states that the PD, as the COR, "is expected to advise and assist the [CO] in administering the business aspects of the contract by reviewing vouchers, invoices, reports, and deliverables."<sup>16</sup> However, it is important to note that the PD, as the COR, is not authorized to make any commitments or changes that affect the price, quality, quantity, delivery, or other terms and conditions of the contract.<sup>17</sup>

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<sup>9</sup> 1 FAM 286.1, "Office of Construction Management (OBO/CFSM/CM)."

<sup>10</sup> Each major overseas construction project has one PD assigned at a time. Because of the length of construction projects, multiple PDs may be assigned over the life of a project.

<sup>11</sup> According to the OBO, Construction Management Guide, 3.1.2, "Project Director (PD)," the PD is the COR.

<sup>12</sup> OBO, Construction Management Guide, 3.1.2.

<sup>13</sup> 1 FAM 286.1(7) and (11).

<sup>14</sup> The terms IGCE and independent government estimate are used interchangeably in the documents referenced in this report.

<sup>15</sup> OBO, Construction Management Guide, 3.1.2.

<sup>16</sup> 14 FAH-2 H-513(c)(1), "The Contracting Officer's Representative's (COR) Role In Contract Administration."

<sup>17</sup> FAR 1.602-2(d)(5).

## **Contract Modifications**

A contract modification means any written change in the terms of a contract.<sup>18</sup> Only COs, acting within the scope of their authority, are empowered to execute contract modifications on behalf of the government.<sup>19</sup> Modifications to a contract affect the interests, rights, and obligations of two independent parties—the U.S. government and the contractor. The responsibility of the CO is to preserve the integrity of the relationship between these two parties. The CO reviews the action in the modification to determine whether the action is consistent with the existing contract and to ensure that the equities of the existing relationship are preserved and will be continued when a modification is issued and negotiated.<sup>20</sup> The contract modification process advances from the PD, through the assigned OBO Construction Executive,<sup>21</sup> to the CO.<sup>22</sup>

### ***Independent Government Cost Estimates and Time Extensions***

An IGCE is the U.S. government’s estimated cost or price of a proposed acquisition and is prepared by the COR. Its purpose is to serve as a basis for comparing costs or prices proposed by offerors and to serve as an objective basis for determining price reasonableness.<sup>23</sup> According to the Bureau of Administration’s Overseas Procurement Guide, the government must prepare an IGCE for proposed contract modifications and assess any time extension that may be justified.<sup>24</sup> Furthermore, the FAH states that when a modification is necessary, the COR must prepare a procurement request to document the need for the modification, including “[t]he estimated total time necessary to accomplish the required services, if the time must be extended.”<sup>25</sup>

The FAR requires an IGCE for each contract modification anticipated to exceed the simplified acquisition threshold.<sup>26,27</sup> The CO may also require an IGCE when the cost of required work is not anticipated to exceed the simplified acquisition threshold.<sup>28</sup> OBO guidance requires an IGCE

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<sup>18</sup> FAR 2.101, “Definitions.”

<sup>19</sup> FAR 43.102, “Policy.”

<sup>20</sup> 14 FAH-2 H-531 (a) and (d), “General.”

<sup>21</sup> According to the OBO, Construction Management Guide, 1.3.5.5, “Construction Executive,” the Construction Executive is the responsible manager and point of contact once the project is awarded. The Construction Executive is accountable for all technical, administrative, and project budget matters for the project and reports directly to the Senior Construction Executive leading the responsible branch.

<sup>22</sup> OBO, Construction Management Guide, Table 3.2-1, “Change Order Execution above PD’s Authority/Warrant.”

<sup>23</sup> 14 FAH-2 H-351(a) and (b), “General.”

<sup>24</sup> Office of the Procurement Executive, Overseas Procurement Guide, Chapter 8, “Contract Modification/Contract Closeout,” Section VI, “Backup Supporting Contract Modifications/Delivery Orders/Task Orders,” C, “Pricing of Adjustments.”

<sup>25</sup> 14 FAH-2 H-534(5), “Processing Contract Modifications.”

<sup>26</sup> FAR 36.203(a), “Government estimate of construction costs.”

<sup>27</sup> As of 2023, the simplified acquisition threshold was \$250,000.

<sup>28</sup> FAR 36.203(a).

for construction contract modifications that exceed \$25,000.<sup>29</sup> For OBO construction projects, the PD is responsible for preparing the IGCE using input from OBO's staff assigned to the project. The PD should review and certify the IGCE prior to proceeding with subsequent steps in the change process.<sup>30</sup>

In the first notification to the CO of a potential change to the contract the IGCE is included. This initial package consists of the justification for the change, the statement of work involved, and the PD's IGCE to execute the change. The purpose is to provide a complete package of the change consisting of justification, description, and cost.<sup>31</sup>

### ***Type of Modifications***

A bilateral modification (supplemental agreement) is a contract modification that is signed by the contractor and the CO that can be used to make negotiated equitable adjustments resulting from a change order.<sup>32</sup> A unilateral modification is a contract modification that is signed only by the CO. Unilateral modifications can be used to make administrative changes, issue change orders, and make changes authorized by clauses other than a changes clause.<sup>33</sup> The CO may execute a unilateral modification without the prior agreement of the contractor pursuant to the Changes clause of the contract.<sup>34</sup> According to the Construction Management Guide, a unilateral modification by the U.S. government ensures that the contractor receives some payment for the change, but it will probably result in the contractor filing a claim. A unilateral modification must clearly be in the best interest of the U.S. government and must be fully justified by the existing circumstances.<sup>35</sup>

### ***Origination of Changes***

The contractor is notified, in writing, by the PD of the new requirement and is provided with a request for proposal (RFP) for a U.S. government-originated change. The contractor is asked to provide a price proposal to implement the change described in the RFP to the PD.<sup>36</sup> For a contractor-originated change request, the contractor notifies the PD in writing of the need for a constructive change,<sup>37</sup> usually within 20 days of the occurrence of the circumstances leading to the request, through a request for an equitable adjustment (REA).

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<sup>29</sup> OBO, Construction Management Guide, 3.2.12.8, "Change Orders and Claims Management."

<sup>30</sup> Ibid.

<sup>31</sup> OBO, Construction Management Guide, Table 3.2-1.

<sup>32</sup> FAR 43.103(a), "Types of contract modifications."

<sup>33</sup> FAR 43.103(b).

<sup>34</sup> OBO, Construction Management Guide, 3.2.12.8.

<sup>35</sup> Ibid.

<sup>36</sup> OBO, Construction Management Guide, 3.2.12.11, "USG-Originated Changes (Change Order)."

<sup>37</sup> Office of the Procurement Executive, Overseas Procurement Guide, Chapter 8, Section II, "Original Signed Contract and Modifications," E, "Constructive Changes."

### ***Prenegotiation Process and Responsibilities***

According to OBO's Construction Management Guide, upon receiving and reviewing the contractor's response to the RFP or an REA, the PD prepares a prenegotiation memorandum.<sup>38</sup> The prenegotiation memorandum provides a description of the change and a description of OBO's cost analysis and negotiation target positions using prices from the prepared IGCE.<sup>39</sup> The memorandum is reviewed by the responsible Senior Construction Executive, who will confer with the PD and other OBO officials. The Construction Executive transmits the coordinated response to the CO for a decision. Additionally, according to the FAR, the CO "shall establish prenegotiation objectives before the negotiation of any pricing action."<sup>40</sup> The FAR states that the prenegotiation objectives establish the government's initial negotiation position and assist in the CO's determination of a fair and reasonable price.<sup>41</sup> The CO establishes the prenegotiation objectives based on information from the prenegotiation memorandum and issues a negotiation decision to the PD through the Construction Executive.<sup>42</sup>

### ***Negotiation Process and Responsibilities***

According to the FAR, the purpose of performing a cost or price analysis is to develop a negotiation position that permits the CO and the offeror an opportunity to reach agreement on a fair and reasonable price.<sup>43</sup> The CO's primary concern is the overall price that the government will pay.<sup>44</sup> The FAR requires the CO to document the principal elements of the negotiated agreement in the contract file and provides specific information that must be included in this documentation.<sup>45</sup> According to the Construction Management Guide, the PD is required to document the negotiations and report the results of the negotiations to the Construction Executive and makes a recommendation through a negotiation summary document and price acceptance memorandum.<sup>46</sup> The CO is advised of the results of the negotiation and executes the modification based on the negotiated agreement.

A summary of the prenegotiation and negotiation process and responsibilities is shown in Figure 2.

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<sup>38</sup> According to the OBO Construction Management Guide, 3.2.12.14, "Pre-Negotiation Responsibilities," the prenegotiation memorandum is required for modifications of more than \$25,000.

<sup>39</sup> For RFPs, the IGCE is prepared before the RFP is issued, and for REAs, the IGCE is prepared after the REA has been received.

<sup>40</sup> FAR 15.406-1(b), "Prenegotiation objectives."

<sup>41</sup> FAR 15.406-1(a).

<sup>42</sup> OBO, Construction Management Guide, 3.2.12.14.

<sup>43</sup> FAR 15.405(a), "Price negotiation."

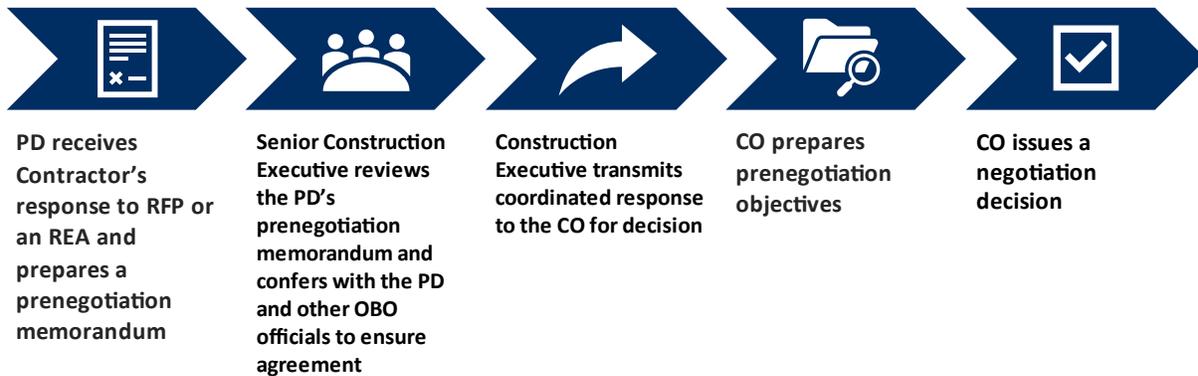
<sup>44</sup> FAR 15.405(b).

<sup>45</sup> FAR 15.406-3, "Documenting the negotiation."

<sup>46</sup> The Construction Management Guide provides a negotiation summary template and price acceptance memorandum in the appendices.

**Figure 2: Prenegotiation and Negotiation Process and Responsibilities**

**Prenegotiation**



**Negotiation**



Source: Generated by OIG using the OBO Construction Management Guide and the FAR.

**Construction Quality Management**

***Project Reporting Responsibilities***

One of the main responsibilities of the PD, as the COR, is the preparation and maintenance of daily logs, weekly activity reports, and monthly progress reports. The daily logs and reports serve as the project chronology or written abstracts of the PD's personal project logs. Specifically, the documents are contemporaneous recordings of facts concerning the project management information that provide a means of maintaining detailed knowledge of the project. OBO requires that the logs and reports be routinely prepared. In addition, OBO requires that the reports be accurate and presented in a logical format with sufficient detail to enable the reconstruction of project events by individuals whose familiarity with the project is limited.<sup>47</sup> The required documents should include the following information:

<sup>47</sup> Ibid., 3.2.9, "Project Reporting Responsibilities."

- Daily Log: The PD must prepare a daily log of construction for each project workday, even if no work is performed that day. This log provides details of the daily work and efforts performed. It should include daily hours worked and weather conditions, contractor supervisory and tradesmen personnel, safety items of inspections and serious injuries that could result in lost time, major materials deliveries, and major equipment used. According to OBO, it has found that the daily log is the most important job record in dealing with litigation. The data are essential in resolving future problems, disputes, and claims, because the log represents the only OBO-recorded source of information regarding performance by all project parties on a day-by-day basis.<sup>48</sup>
- Weekly Activity Report: The PD prepares a weekly activity report for review and use by all Construction Executives (this is not limited to the Construction Executive responsible for the project) and CM staff.<sup>49</sup>
- Monthly Progress Reports: The PD is required to prepare monthly progress reports that should contain detailed statements describing the project status and the results of field activities occurring during the reporting period. This report is intended to provide OBO with an in-depth, periodic analysis and statement of the construction contractor's performance.<sup>50</sup>

### ***Project Procedures Manual***

The PD is responsible for developing the initial project procedures manual and updating it as required. The purpose of the project procedures manual is to explain all the procedures that are to be followed by the various parties in the administration of the project. When the project manual has been completed, copies of the manual should be distributed to the OBO project staff and management and supervisory personnel for all firms and organizations participating in the project. When developing the project procedures manual, the PD should identify all major parties and their relationships and provide instructions and forms covering the procedures. The following topics should be addressed in the project procedures manual: communications, OBO project office staff, equipment and supplies, construction project files index, the CM office budget, standard procedures, project meetings, details of the QA and QC program, inspections and tests, scheduling, and the safety and health program.<sup>51</sup>

### ***Quality Assurance and Work Progress Inspections***

The PD should review the contractor's invoice and determine whether the charged costs are commensurate with the progress made and if the work for which the contractor is requesting payment has been satisfactorily performed. Completion of the contractor's work entails many inspections to determine that all the work has been completed as required.<sup>52</sup>

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<sup>48</sup> Ibid., 3.2.9.1, "Daily Log."

<sup>49</sup> Ibid., 3.2.9.2, "Weekly Activity Report (WAR)."

<sup>50</sup> Ibid., 3.2.9.3, "Monthly Progress Reports."

<sup>51</sup> Ibid., "Project Procedures Manual."

<sup>52</sup> OBO, Construction and Commissioning Guidebook, Section 4.3.17, "Schedule of Defects."

According to OBO field staff, to determine the percentage of completion and the status of an NEC project, OBO technical personnel should conduct inspections to determine the percentage of individual schedule activities completed. To determine whether the work has been completed and conforms to the technical requirements of the contract, OBO personnel should conduct QA inspections.<sup>53</sup> During these inspections, OBO personnel are required to walk through the work site and document the project's progress, including identifying issues with meeting technical specifications and the quality of building materials. The PD should discuss any concerns or discrepancies identified during the work progress and QA inspections with the contractor. Once the parties agree that the contractor's proposed costs are commensurate with the work progress described and the work is deemed satisfactory based on QA inspections, the contractor sends an updated invoice back to the PD for signature and for processing and payment.

### **Progress Payment Review and Approval Process**

The FAR states that "the Government shall make progress payments monthly as the work proceeds, or at more frequent intervals as determined by the [CO], based on estimates of work accomplished which meets the standards of quality established under the contract as approved by the [CO]."<sup>54</sup> The source of information related to work completed should be based on the contractor's cost-loaded critical path method schedule.<sup>55</sup> The critical path method schedule is used in monitoring the construction progress and costs, and can serve as a valuable basis for evaluating delay claims.<sup>56</sup> The PD is responsible for ensuring that progress payments are processed in a timely manner, thereby avoiding any additional costs to the U.S. government in the form of interest payments or late payment penalties.<sup>57</sup>

## **AUDIT RESULTS**

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### **Finding A: Contract Modifications Were Not Executed in Accordance With Federal Regulations and Department Guidance**

OIG found that neither OBO nor AQM executed contract modifications for the NEC Mexico City construction contract in accordance with requirements. Specifically, the PDs did not assess the impact that the contract modifications would have on the overall construction project timeline. In addition, the Department did not always perform required prenegotiation and negotiation activities to determine fair and reasonable pricing. For example, the Department did not always prepare prenegotiation memoranda and objectives and did not always negotiate changes with

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<sup>53</sup> According to 14 FAH-2 H-523.2(b), "Inspection," the COR may perform QA inspections "at such times and places as may be necessary to determine conformance with contract requirements.

<sup>54</sup> According to FAR 52.232-5(b), "Progress Payments," progress payments are requested by the contractor. For the purposes of this report, OIG considers them to be invoices for payment.

<sup>55</sup> OBO, Construction and Commissioning Guidebook, Section 4.6.26, "Payments to General Contractor."

<sup>56</sup> OBO, Construction Management Guide, 3.2.10, "Construction Schedule – Project Execution Schedule (PES)."

<sup>57</sup> OBO, Construction and Commissioning Guidebook, Section 4.6.26.

the contractor. Furthermore, OIG found that OBO field staff revised 13 of the 15 IGCEs reviewed for this audit to align with the proposals received from the contractors rather than perform required negotiations. Finally, the CO did not always obtain required contractor release statements to avoid exposing the Department to increased financial risk. The deficiencies occurred, in part, because OBO and AQM management did not sufficiently oversee and enforce adherence to requirements. As a result, the Department executed contract modifications without full awareness of the consequences to the construction project timeline and associated project costs.

### ***Schedule Impacts Were Not Considered When Estimating the Cost of Modifications***

An IGCE is the U.S. government's estimate of the cost of a proposed acquisition, including direct and indirect costs,<sup>58</sup> that is prepared by the COR<sup>59</sup> (for construction contracts, the PD is the COR). The government must prepare an IGCE for proposed contract modifications<sup>60</sup> and assess any time extension that may be justified.<sup>61</sup> Furthermore, the FAH states that when a modification is necessary, the COR's procurement request should include "the estimated total time necessary to accomplish the required services, if the time must be extended."<sup>62</sup> An assessment of time is needed to ensure that all direct and indirect costs are included in the cost estimate.

OIG obtained IGCEs prepared by the PDs for the 15 RFPs<sup>63</sup> that related to the 8 contract modifications reviewed for this audit and found that the Department did not assess the impact that the executed contract modifications would have on the overall construction project timeline for the NEC Mexico City when preparing the IGCEs.<sup>64</sup> Instead, OBO field staff located in Mexico City stated that they would assess scheduling impacts when the construction contractor asked for an extension in a proposal submitted in response to an RFP. In addition, OBO field staff stated that the construction contractor would submit a time impact analysis<sup>65</sup> when it believed that additional time would be needed to complete the project because of the modification. Furthermore, if the contractor submitted a time impact analysis in response to an RFP, OBO would review the document internally or use a separate contractor to analyze the

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<sup>58</sup> OBO, Office of Cost Management Guide, Section 1.7.2, "Independent Government Estimates and Bid Evaluation."

<sup>59</sup> 14 FAH-2 H-351(b).

<sup>60</sup> OBO's Construction Management Guide, 3.2.12.11, "USG-Originated Changes (Change Order)," and 3.2.12.12, "Contractor-Originated Changes (Requests for Equitable Adjustment [REA])," states that an IGCE should be prepared by the PD as part of the RFP and REA process.

<sup>61</sup> Office of the Procurement Executive, Overseas Procurement Guide, Chapter 8, Section VI, C.

<sup>62</sup> 14 FAH-2 H-534(5), "Processing Contact Modifications."

<sup>63</sup> The 15 RFPs were associated with 8 modifications. Some modifications were related to multiple RFPs. Appendix A provides details on the items selected for review.

<sup>64</sup> A similar issue was reported in OIG, *Management Assistance Report: Actions to Address Ongoing Construction Schedule Delays at New Embassy Compound Mexico City Are Needed* (AUD-CGI-23-16, April 2023).

<sup>65</sup> Contract Specification, Section 013205, "Project Scheduling," Paragraph 3.6, states that the contractor should prepare a time impact analysis to identify and evaluate the impact of a particular event or situation on the completion of the project.

proposed modification. For example, the contractor submitted time impact analyses in response to two of the RFPs reviewed during this audit. OIG found evidence that OBO reviewed the documents provided by the contractor after the contractor requested time extensions. However, this approach is contrary to Department guidance because OBO failed to assess time as part of its IGCE in order to determine whether time extensions were justified.

***OBO Did Not Always Perform Required Prenegotiation and Negotiation Activities***

According to OBO's Construction Management Guide, upon receiving the contractor's response to an RFP or a contractor's REA, the PD prepares a prenegotiation memorandum for modifications of more than \$25,000. The prenegotiation memorandum is reviewed by the responsible Senior Construction Executive, who confers with the PD and other OBO officials. The coordinated response is transmitted to the CO for decision. Additionally, the CO must establish prenegotiation objectives before the negotiation of any pricing action. According to the FAR, "the scope and depth of the analysis supporting the objectives should be directly related to the dollar value, importance, and complexity of the pricing action."<sup>66</sup> The FAR also states that the prenegotiation objectives establish the government's initial negotiation position and assist in the CO's determination of fair and reasonable price.<sup>67</sup>

After the CO approves the prenegotiation documents, the PD proceeds with negotiations on the proposed change. The PD is required to document the negotiations conducted and recommendations regarding acceptance or rejection and report the results of the negotiations to the Construction Executive with a recommendation.<sup>68</sup> The Construction Management Guide provides a negotiation summary template and price acceptance memorandum.<sup>69</sup> According to the FAR, the CO shall document in the contract file the principal elements of the negotiated agreement.<sup>70</sup> OBO policy states that contractor prices within 10 percent of the IGCE are considered reasonable<sup>71</sup> and no negotiations are conducted; therefore, prenegotiation documents would not be needed.

***Prenegotiation and Negotiation Activities Related to Requests for Proposals***

OIG reviewed 15 RFPs and found that the Department did not always prepare prenegotiation documents (i.e., prenegotiation memorandum and prenegotiation objectives) or document negotiations with the contractor as required for responses to RFPs.<sup>72</sup> The contractor's proposals related to 7 of 15 RFPs selected for review were more than \$25,000 and more than 10 percent different than the original IGCE amount, meaning that OBO was required to negotiate with the

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<sup>66</sup> FAR 15.406-1, "Prenegotiation objectives."

<sup>67</sup> Ibid.

<sup>68</sup> OBO, Construction Management Guide, Table 3.2-1, "Change Order Execution above PD's Authority/Warrant."

<sup>69</sup> Ibid.

<sup>70</sup> FAR 15.406-3, "Documenting the negotiation."

<sup>71</sup> OBO, Policy and Procedures Directive COST 01: Cost Estimate Preparation and Review (April 2015), at 3.1.2.

<sup>72</sup> For government-originated changes, the contractor is notified in writing of the new requirement using an RFP.

contractor. However, OIG found that the Department did not create prenegotiation documents related to these eight proposals and did not conduct negotiations with the contractor.

For example, for RFP 16, the contractor's proposal included a 52-calendar day extension (non-compensable) and a \$108,597 price. The price acceptance memorandum prepared by OBO stated that the proposed price was considered fair and reasonable;<sup>73</sup> however, OBO disagreed with the claim for time. The Department did not conduct negotiations with the contractor with the intent of achieving a mutually acceptable change to the project schedule. Instead, the CO issued a unilateral modification<sup>74</sup> for \$108,597 with no time extension.

OIG also found that instead of developing prenegotiation objectives and conducting negotiations with the contractor as required, the PDs prepared price acceptance memoranda for the CO to execute modifications without negotiations for these eight RFPs. Furthermore, the PDs prepared price acceptance memoranda even when OBO did not agree with the contractor's proposed price or time extensions. Additionally, OBO field staff generally revised IGCEs to be within 10 percent of the contractor's proposals after receiving the contractor's proposals. OBO field staff stated that when contractor proposals are more than 10 percent different than the IGCE estimate, OBO field staff would discuss the differences with the contractor and potentially go back and forth several times and then revise the IGCE to reflect any agreements reached with the contractor. According to OBO field staff, the goal is to be "fair and reasonable." However, revising the IGCE is not in accordance with the FAR and the Construction Management Guide. In fact, revising an IGCE is not discussed in the FAR or the Construction Management Guide.

IGCE's are intended to inform the development of prenegotiation objectives and subsequent negotiations. Those negotiations may result in an agreement to a fair and reasonable price that varies from the IGCE, but adjusting the IGCE after receiving the contractor's proposal is not part of the process included in the FAR or Construction Management Guide. Such adjustments are inconsistent with the purpose of an IGCE and create a misleading record of the modification. Table 1 provides details of the changes made to 13 of 15 IGCEs reviewed during this audit after proposals were received from the contractor.

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<sup>73</sup> OBO considered the proposed price as fair and reasonable even though the proposed price was not within 10 percent of the original IGCE.

<sup>74</sup> OBO, Construction Management Guide, Table 3.2-1, states that if agreement is not reached on an equitable adjustment in a timely fashion, and if the CO finds the contractor's proposal unacceptable and further negotiations are not productive, the CO can issue a unilateral modification reflecting the Department's determination of an equitable adjustment of the contract price and the time required for performance of the contract.

**Table 1: Revisions to IGCEs After Receipt of Proposal**

RFP	OBO's Initial IGCE	Contractor's Proposed Price	OBO's Revised IGCE	Modification Executed Amount
RFP 2	\$172,029.00	\$185,726.00	Not Revised	\$185,726.00
RFP 14	\$3,836.26	\$1,377.00	\$1,328.68	\$1,377.00
RFP 16	\$46,571.90	\$108,597.00	\$104,198.14	\$108,597.00
RFP 17	\$5,084.55	\$7,860.00	\$7,446.21	\$7,860.00
RFP 29	\$135,927.00	\$983,275.00	\$770,136.00	\$798,755.00
RFP 33	\$92,406.84	\$126,704.00	\$127,096.00	\$126,704.00
RFP 39	-\$284,372.61*	\$593,474.00	\$559,945.00	\$593,474.00
RFP 50	\$12,292.22	\$115,470.80	\$109,245.14	\$115,470.80
RFP 54	\$3,296.40	\$0.00	\$0.00	\$0.00
RFP 60	\$200,676.00	\$216,879.00	Not Revised	\$216,879.00
RFP 61	\$3,755.00	\$642.00	\$651.00	\$642.00
RFP 80	\$6,102.00	\$27,844.00	\$26,849.00	\$27,844.00
RFP 82	\$309,613.00	\$241,866.00	\$236,476.00	\$241,866.00
RFP 88	\$51,832.00	\$30,299.00	\$30,345.00	\$30,299.00
RFP 87	\$319,295.00	\$527,352.00	\$518,374.00	\$527,352.00

\* The IGCE initially included an estimate that the amount would decrease because of expected materials reduction.

Source: OIG generated based on construction project data obtained from OBO.

### ***Prenegotiation and Negotiation Activities Related to Requests for Equitable Adjustments***

For the eight REAs reviewed for this audit,<sup>75</sup> OBO complied with prenegotiation and negotiation requirements for two of three REAs meeting the criteria for such requirements. Specifically, three of eight REAs reviewed during this audit (REAs 3, 4, and 17.1) deviated more than 10 percent from the IGCE amount. OIG found that OBO negotiated with the contractor on two of those three REAs. Specifically, OBO established prenegotiation objectives for REAs 3 and 4 and negotiated a collective resolution for these two REAs, which was approved by the CO and documented in the contract file.<sup>76</sup> Although OBO complied with prenegotiation and negotiation requirements for REAs 3 and 4, OIG found that OBO and AQM elected to extend the contractor performance period by 257 days (172 noncompensable days and 85 compensable days) in one modification and, 3 months later, issued a separate modification with the amount of additional funding that would be provided (\$3,253,715) for the 85 compensable days. By issuing the modifications in this manner, the CO's execution of the first modification created an undefinitized contract action.<sup>77</sup> Although dividing the modification into two parts was

<sup>75</sup> REAs are contractor-originated changes in which the contractor notifies the government in writing of a constructive change.

<sup>76</sup> OBO, Construction Management Guide, Section 3.2.12.13, "Requests for Equitable Adjustment (REA) Policy and Procedures Guidelines."

<sup>77</sup> Undefinitized contract actions are actions in which the contract terms and conditions, specifications, or prices have not been agreed upon before performance is begun under the action.

problematic, OIG found that the PD prepared a price negotiation memorandum for REAs 3 and 4 and, overall, prepared price negotiation memoranda or price acceptance memoranda for six of eight REAs selected for review.

OIG found that the Department did not negotiate with the contractor for REA 17.1. Specifically, the contractor submitted an REA for a 128-calendar day extension, compensable at \$5.596 million. OBO determined that the schedule extension should be in the range of 112-128 noncompensable calendar days. The CO provided the contractor a letter explaining the rationale. However, the Department did not have evidence that it had negotiated with the contractor to reach an agreement about compensable versus noncompensable days. Ultimately, the Department issued a unilateral modification<sup>78</sup> for this change.

In addition, OBO field staff stated that they prepared IGCEs after receipt and review of the contractor's proposals. OBO did not have a process to ensure that the IGCE was prepared independently. Although most of the IGCE amounts for the eight REAs reviewed for this audit were generally different than the contractor's request, as shown in Table 2, there was no evidence to demonstrate that the IGCEs were prepared independent of the contractor's REA.

**Table 2: REA and IGCE Amounts**

REA	Contractor's Request	OBO's IGCE	Modification Executed
REA 3 and 4*	257 calendar days (167 compensable)	257 calendar days (54 compensable)	257 calendar days (85 compensable)
REA 3 and 4*	\$7,214,934.40	\$1,844,550.00	\$3,253,715.00
REA 6	\$9,787.62	\$9,861.16	\$9,787.62
REA 9	\$4,823.21	\$4,837.19	\$4,823.21
REA 10	\$6,054.90	\$5,832.67	\$6,054.90
REA 16	61 calendar days	61 calendar days	61 calendar days
REA 17.1	128 compensable calendar days	125 noncompensable calendar days	128 noncompensable calendar days
REA 46	\$9,112.00	\$9,206.00	\$9,112.00

\* REAs 3 and 4 were combined for resolution and modification.

**Source:** OIG generated based on construction project data obtained from OBO.

### ***Insufficient Contractor's Release Statement***

FAR 43.204 states that to avoid subsequent controversies that may result from a supplemental agreement containing an equitable adjustment, the CO should include a statement releasing "the Government from any and all liability under this contract for further equitable adjustments."<sup>79</sup> Also, to prevent further claims for bilateral modifications, the Department's

<sup>78</sup> OBO, Construction Management Guide, Table 3.2-1, states that if agreement is not reached on an equitable adjustment in a timely fashion, and if the CO finds the contractor's proposal unacceptable and further negotiations are not productive, the CO can issue a unilateral modification reflecting the Department's determination of an equitable adjustment of the contract price and the time required for performance of the contract.

<sup>79</sup> FAR 43.204(c)(2), "Administration."

Overseas Procurement Guide directs the CO to insert a statement reading, “the Contractor agrees that this is a complete and equitable adjustment for the changes identified in this modification. No further claims or requests for equitable adjustment will be submitted or considered.”<sup>80</sup>

Of the 14 contract modifications reviewed for this audit, 10 modifications were bilateral, meaning that the contract modification was signed by the contractor and the CO.<sup>81</sup> Of those 10, OIG found that the CO did not obtain the required release statement from the contractor for 1 of the 10 bilateral modifications, which are necessary to avoid exposing the Department to increased financial risk. For the other nine bilateral modifications, the CO inserted the statement of release from the FAR.<sup>82</sup> The CO did not use the required wording from the Overseas Procurement Guide to prevent further claims.<sup>83</sup>

### ***Department Officials Did Not Monitor Adherence to Federal Regulations and Department Guidance***

The *Standards for Internal Control in the Federal Government* states that management should monitor internal controls “as part of the normal course of operations.”<sup>84</sup> The standards also state that “ongoing monitoring should be “built into the entity's operations, performed continually, and responsive to change”<sup>85</sup> to sustain internal controls. To comply with these internal control requirements, OBO and AQM management should monitor their internal control systems consistently by assessing the effectiveness of each control and determine whether personnel implemented the established controls. The deficiencies identified during the audit occurred, in part, because OBO and AQM management did not ensure that the PDs and the CO adhered to requirements and processes outlined in the FAR, the FAH, the Overseas Procurement Guide, and the Construction Management Guide. Specially, OBO did not have a process to ensure that IGCEs included an assessment of the impact that the proposed modification would have on the completion time for the project. Additionally, OBO did not have a process to keep staff who receive REA pricing separate from staff who develop IGCEs. Furthermore, AQM and OBO did not have a process to ensure that COs prepared prenegotiation objectives and PDs conducted negotiations to reach agreement on a fair and reasonable price on executed modifications for RFP and REA proposed changes.

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<sup>80</sup> Office of the Procurement Executive, Overseas Procurement Guide, Chapter 8, Section II, C.

<sup>81</sup> FAR 43.103, “Types of contract modifications.”

<sup>82</sup> For five of nine release statements, AQM added the word “compensation” to the standard FAR language. According to AQM, the Department’s Office of the Legal Adviser requested the addition of the word “compensation” to the contractor’s release statement in 2019 in response to litigation.

<sup>83</sup> A similar issue was reported in OIG report *Audit of the Bureau of Overseas Buildings Operation’s Process To Identify and Apply Best Practices and Lessons Learned to Future Construction Projects* (AUD-MERO-20-39, September 2020). That report included a recommendation to the Bureau of Administration to consistently include a contractor release statement to avoid exposing the Department to increased financial risk.

<sup>84</sup> Government Accountability Office, *Standards for Internal Control in the Federal Government* (GAO-14-704G, September 2014), §16.05.

<sup>85</sup> *Ibid.*, §16.04.

***Impact of the Deficiencies Identified During the Audit***

Because of the deficiencies identified during the audit, the Department executed contract modifications without full awareness of potential consequences to the construction project's timeline and associated project costs, including increasing the risk of constructive acceleration<sup>86</sup> that could result in additional REAs and cost to the government. Additionally, the deficiencies identified increase the difficulty for OBO and AQM to address the impact of changes to the construction project timeline and to hold the contractor accountable for completing the project as agreed to in the contract documents. Therefore, OIG is offering the following recommendations to address the identified conditions:

**Recommendation 1:** OIG recommends that the Bureau of Overseas Buildings Operations, in coordination with the Bureau of Administration, develop, implement, and communicate a process to ensure that Project Directors for construction projects prepare independent government cost estimates that consider the impact that the modification will have on the overall schedule of the project to determine if extensions are justified. At a minimum, the process should include clarification of individual responsibilities and accountability.

**Management Response:** OBO concurred with the recommendation, stating that it is drafting an update to its standard independent government estimate form to consider potential changes in project schedule. OBO also stated that "the accumulation of many discrete modifications may impact the critical path timeline" and "discrete modifications might have only negligible time impacts (or none at all) on the critical path of the project to justify an extension of the period of performance. Therefore, it is not always possible to determine if each individual contract modification will impact the overall project schedule."

**OIG Reply:** OIG acknowledges that discrete modifications might have only a negligible impact on the critical path; however, OIG believes that any time determined to be owed to the contractor should be included in the executed modification. OIG also believes that it is possible for OBO to determine if each contract modification will impact the overall project schedule. On the basis of OBO's concurrence with the recommendation and planned actions, OIG considers this recommendation resolved, pending further action. This recommendation will be closed when OIG receives documentation demonstrating that OBO, in coordination with the Bureau of Administration, has developed, implemented, and communicated a process to ensure that PDs for construction projects prepare IGCEs that consider the impact that any proposed modification will have on the overall schedule of the project to determine if extensions are justified.

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<sup>86</sup> Constructive acceleration is when the government requires the contractor to meet the current delivery schedule in the face of excusable delays.

**Recommendation 2:** OIG recommends that the Bureau of Overseas Buildings Operations (OBO) develop, implement, and communicate a process to ensure a separation of duties between OBO staff who receive the price proposal for a request for equitable adjustment related to a construction project and OBO staff who develop the independent government cost estimate for the construction project. At a minimum, the process should include clarification of individual responsibilities and accountability.

**Management Response:** OBO stated that although the methodology OIG recommended may be applicable for RFPs, it would not be a feasible approach for a fair and expedient analysis of an REA. OBO stated that the OBO and the Bureau of Administration Service Level Agreement provides detailed procedures for both REAs and RFPs, including clarification of individual responsibilities and accountability, as well as procedures for reviewing IGCEs.

**OIG Reply:** On the basis of OBO's response to the recommendation, OIG considers this recommendation unresolved. OIG acknowledges that the OBO and Bureau of Administration Service Level Agreement outlines procedures and individual responsibilities for the construction modification process. However, the Service Level Agreement does not develop, implement, and communicate a process to ensure a separation of duties between OBO staff who receive the price proposal for an REA related to a construction project and OBO staff who develop the IGCE for the REA. This recommendation will be considered resolved when OBO provides a plan of action for addressing this recommendation or an acceptable alternative that fulfills the intent of the recommendation. This recommendation will be closed when OIG receives documentation demonstrating that OBO has developed, implemented, and communicated a process to ensure a separation of duties between OBO staff who receive the price proposal for an REA related to a construction project and OBO staff who develop the IGCE for the REA.

**Recommendation 3:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, develop, implement, and communicate a process to ensure that Contracting Officers prepare prenegotiation objectives for modifications to construction projects of more than \$25,000 and that Project Directors do not revise independent government cost estimates during or after negotiations in accordance with the Federal Acquisition Regulation and Department of State policy. At a minimum, the process should include guidance on documenting fair and reasonable pricing and any schedule extensions for the modification and a clarification of individual responsibilities and accountability.

**Management Response:** The Bureau of Administration concurred with the intent of the recommendation; however, it requested that the recommendation be modified to increase the threshold to \$250,000 for each RFP to align with the simplified acquisition threshold in the FAR. The Bureau of Administration stated that, in coordination with OBO, it will review its Service Level Agreement and responsibility matrix to ensure adherence to the FAR, Department of State Acquisition Regulation, and Department of

State Acquisition Manual guidance on negotiations, IGCEs, and documentation of fair and reasonableness of pricing and scheduling modifications.

**OIG Reply:** On the basis of the Bureau of Administration's response to the recommendation, OIG considers this recommendation unresolved. Although the Bureau of Administration stated that it concurred with the intent of the recommendation, its response did not demonstrate that it would address the recommendation. OIG agrees that the Service Level Agreement and the responsibility matrix should adhere to procurement regulations. However, as presented in the Audit Results section of this report, the FAR and OBO guidance already outline requirements. The deficiencies identified in this report relate to non-adherence with the requirements. Additionally, although the FAR's simplified acquisition threshold is \$250,000, the OBO Construction Management Guide defines a more stringent threshold of \$25,000. Therefore, OIG is not revising this recommendation as requested by the Bureau of Administration.

This recommendation will be considered resolved when the Bureau of Administration provides a plan of action for addressing this recommendation or an acceptable alternative that fulfills the intent of the recommendation. This recommendation will be closed when OIG receives documentation demonstrating that the Bureau of Administration, in coordination with OBO, has developed, implemented, and communicated a process to ensure that COs prepare prenegotiation objectives for modifications to construction projects of more than \$25,000 and that PDs do not revise IGCEs during or after negotiations in accordance with the FAR and Department policy.

**Recommendation 4:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, develop, implement, and communicate a process to ensure that Project Directors for construction projects conduct and document price negotiations in accordance with the Federal Acquisition Regulation and Department of State policy. At a minimum, the process should include guidance on documenting fair and reasonable pricing and any schedule extensions for the modification and a clarification of individual responsibilities and accountability.

**Management Response:** The Bureau of Administration did not concur with the recommendation, stating that current federal and Department regulations and policies direct that fair and reasonable price determinations and contractual modifications be made and executed by a warranted CO. The Bureau of Administration proposed the recommendation be modified to state, "OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, develop, implement, and communicate a process to ensure that Project Directors for construction projects provide support to the Contracting Officer to ensure that price negotiations are conducted and documented in accordance with the Federal Acquisition Regulation and Department of State policy."

**OIG Reply:** On the basis of the Bureau of Administration's response to the recommendation, OIG considers this recommendation unresolved. OIG acknowledges

that federal and Departmental regulations and policies direct that fair and reasonable price determinations and contractual modifications be made and executed by a warranted CO. However, the deficiencies identified in this report related to non-adherence with the requirements. Therefore, OIG is not revising this recommendation as requested by the Bureau of Administration.

This recommendation will be considered resolved when the Bureau of Administration provides a plan of action for addressing the recommendation or an acceptable alternative that fulfills the intent of the recommendation. This recommendation will be closed when OIG receives documentation demonstrating that the Bureau of Administration, in coordination with OBO, has developed, implemented, and communicated a process to ensure that PDs for construction projects conduct and document price negotiations in accordance with the FAR and Department policy. At a minimum, the process should include guidance on documenting fair and reasonable pricing and any schedule extensions for the modification and a clarification of individual responsibilities and accountability.

## **Finding B: OBO Did Not Comply With Guidance for Project Reporting and Contract Administration**

OIG found that the PDs did not comply with construction quality management for project reporting. Specifically, the PDs did not complete required daily logs and did not develop the required project procedures manual to guide project administration. The deficiencies occurred, in part, because OBO management failed to ensure that the PDs fully complied with requirements. By failing to complete the daily logs and project procedures manual for a large, multimillion-dollar construction project, OBO limited its ability to protect the Department's interests and coordinate project administration.

### ***OBO Daily Logs Were Not Completed***

The Construction Management Guide requires Department officials who are involved in construction projects to prepare several types of reports to inform senior officials about the status of construction projects, including daily logs, weekly activity reports, and monthly progress reports.<sup>87</sup> The Construction Management Guide states that the reports are contemporaneous recordings of facts concerning project management and that the reports provide a means for OBO to maintain detailed knowledge of a project.<sup>88</sup> According to the Construction Management Guide, the PD is the primary recorder of facts and events as they occur for a project.<sup>89</sup> The PD must prepare a daily log of construction for each project workday,

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<sup>87</sup> The daily reports, weekly activity reports, and monthly progress reports are prepared by OBO's onsite PD.

<sup>88</sup> OBO, Construction Management Guide, 3.2.9, "Project Reporting Responsibilities."

<sup>89</sup> Ibid., 3.2.9.1, "Daily Log."

even if no work has been performed that day.<sup>90</sup> OBO issued a bulletin<sup>91</sup> to remind “Construction Executives, PDs, and project managers” of the “importance of consistent and accurate reporting.”

OIG found that the PDs completed the weekly activity reports and monthly progress reports for the NEC Mexico City construction project. However, the PD stated that he had not prepared the required daily logs since he was designated the PD on October 28, 2020. The PD stated that he did not prepare the daily logs because there were other logs and meetings that could be used for the same purpose. However, the daily logs are required and are intended to be the basis for the PDs’ monthly progress reports . Additionally, recording the daily log data is essential to help resolve future problems, disputes, and claims, because the log represents the only OBO-recorded source of information regarding performance by all project parties on a day-by-day basis.

### ***OBO Did Not Develop a Project Procedures Manual for the NEC Mexico City Project***

According to the Construction Management Guide, the purpose of the project procedures manual is to explain all the procedures that are to be followed by the various parties in the administration of a construction project.<sup>92</sup> When developing the project procedures manual, the PD should identify all major parties and their relationships and provide instructions and forms covering all of the procedures.<sup>93</sup>

The PD stated that he had not developed a project procedures manual for the NEC Mexico City construction project. Instead, the PD used the Construction Management Guide<sup>94</sup> and Division 01 specifications<sup>95</sup> for guidance. Therefore, the PD did not have a project-specific guide that provided the OBO staff working on the project with instructions and information for the specific administration of this construction project. For example, a project procedures manual would provide project-specific processes related to communication requirements; OBO project office staff responsibilities, equipment, supplies, construction project files, standard procedures, project meetings, QA and QC programs, inspections and tests, and scheduling; and the project’s safety and health program.

### ***Department Officials Did Not Ensure Adherence to Department Policies***

The deficiencies identified occurred, in part, because of insufficient OBO management oversight. According to the Government Accountability Office, organizations should establish

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<sup>90</sup> Ibid.

<sup>91</sup> OBO, Office of Construction Management Bulletin, CB-2020-002, “Consistent and Accurate Reporting in the Monthly Cables” (August 2020).

<sup>92</sup> OBO, Construction Management Guide, 3.2.12.2, “Project Procedures Manual.”

<sup>93</sup> Ibid.

<sup>94</sup> The Construction Management Guide is an internal OBO guidebook that describes the roles, responsibilities, and relationships of the project staff managing site operations.

<sup>95</sup> Division 01 specifications are contractual requirements that explain procedures to execute the construction, commissioning, and closeout of the project.

and maintain an environment throughout the entity that sets a positive attitude toward internal control.<sup>96</sup> Additionally, management should evaluate performance and hold individuals accountable for their internal control responsibilities.<sup>97</sup> OIG found that OBO management did not ensure that the PDs prepared the daily logs according to OBO requirements. Additionally, the Department requires the development of internal controls, such as a project procedures manual, to explain all the procedures that are to be followed by various parties in the administration of the project. However, OBO management failed to ensure that a project procedures manual was developed and distributed as required.

***Improvements Could Protect the Department From Contractor Disputes***

As a result of these deficiencies, OBO missed opportunities to improve its ability to protect the Department's interests should a dispute or challenge arise from the construction contractor. The Construction Management Guide states that project records are the single most powerful tool in defending a course of action to resolve construction disputes.<sup>98</sup> The level of contextual information from daily logs provides more complete historical data through the course of a project than other types of reports. That detailed information would be directly aligned with day-to-day events. Furthermore, without sufficient guidance, oversight personnel may not fully understand their responsibilities in administering and overseeing the construction project, which could result in management failing to achieve its goals and objectives. Having a project procedures manual for large, multimillion-dollar and multi-year construction projects, such as the NEC Mexico City project, especially when oversight personnel periodically rotate over the life of a project, is important to ensure consistency and uniformity. For example, OBO field staff stated that three PDs had been assigned to the NEC Mexico City project. Therefore, OIG is offering the following recommendations to address the identified conditions:

**Recommendation 5:** OIG recommends that the Bureau of Overseas Buildings Operations develop, implement, and communicate a process to ensure that Project Directors comply with the Construction Management Guide's process for all reporting requirements, including daily logs. At a minimum, the process should include clarification of individual responsibilities and accountability.

**Management Response:** OBO concurred with the recommendation, stating that it will make relevant stakeholders aware through periodic alerts.

**OIG Reply:** On the basis of OBO's concurrence with the recommendation and planned actions, OIG considers this recommendation resolved, pending further action. This recommendation will be closed when OIG receives documentation demonstrating that OBO has developed, implemented, and communicated a process to ensure that PDs comply with the Construction Management Guide's process for all reporting requirements, including daily logs.

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<sup>96</sup> GAO-14-704G, page 21.

<sup>97</sup> Ibid.

<sup>98</sup> Ibid.

**Recommendation 6:** OIG recommends that the Bureau of Overseas Buildings Operations develop, implement, and communicate a process to ensure that Project Directors comply with the Construction Management Guide's requirement for developing and distributing a project procedures manual. At a minimum, the process should include clarification of individual responsibilities and accountability.

**Management Response:** OBO concurred with the recommendation, stating that it will make relevant stakeholders aware through periodic alerts.

**OIG Reply:** On the basis of OBO's concurrence with the recommendation and planned actions, OIG considers this recommendation resolved, pending further action. This recommendation will be closed with OIG receives documentation demonstrating that OBO has developed, implemented, and communicated a process to ensure that PDs comply with the Construction Management Guide's requirement for developing and distributing a project procedures manual.

### **Finding C: OBO Approved Progress Payment Requests in Accordance With Requirements**

OIG found that the PDs approved progress payments for the NEC Mexico City construction project in accordance with requirements. Specifically, OIG found that the 15 selected progress payments reviewed for this audit contained an itemization of the amounts requested by the contractor and the contractor's certification as required. In addition, the PDs conducted monitoring activities to support the approval of progress payments. Because of the approval structure and the monitoring activities performed, the PDs reasonably ensured that the contractor's requests for progress payments were valid and processed in a timely manner, thereby avoiding late payment penalties.

#### ***Progress Payment Requests and Reviews Complied With Requirements***

According to the FAR, for fixed-price construction contracts, "the Government shall make progress payments monthly as the work proceeds, or at more frequent intervals as determined by the [CO], on estimates of work accomplished which meets the standards of quality established under the contract, as approved by the [CO]."<sup>99</sup> The FAR also requires the contractor's request for progress payments to include certain substantiation, such as "an itemization of the amounts requested, related to the various elements of work required by the contract covered by the payment requested."<sup>100</sup> In addition, the FAR requires the contractor to provide a certification of payment to subcontractors with its request for a progress payment.<sup>101</sup> Furthermore, the contract requires the contractor to submit a monthly progress report and an updated project execution schedule with the progress payment request. The FAH requires the

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<sup>99</sup> FAR 52.232-5(b), "Payments under Fixed-Price Construction Contracts."

<sup>100</sup> FAR 52.232-5(b)(1)(i).

<sup>101</sup> FAR 52.232-5(c), "Contractor certification."

COR (who is the PD for construction projects) to review and approve the contractors' vouchers or invoices after adequately verifying the costs using supporting documentation.<sup>102</sup>

OIG found that each of the 15 progress payments reviewed during this audit<sup>103</sup> contained an itemization of the amounts requested by the contractor and the required contractor's certification. In addition, all 15 progress payments contained the contractor's name and address, invoice date and number, contract number, description of the work or services performed, name and address of the contractor official to whom payment was to be sent, a monthly progress report, and an updated project execution schedule. OIG also confirmed that all 15 progress payments included the signature of the PD approving the progress payment.<sup>104</sup>

### ***Monitoring and Evaluation Activities Conducted***

The FAH states that "it is the COR's responsibility to ensure that the Department gets what it pays for through good contractor performance. This responsibility requires the COR to develop a contract monitoring plan commensurate with the complexity and criticality of the contract and to ensure that the COR is performing, in a timely manner, U.S. Government contract administration responsibilities."<sup>105</sup> The FAH also states that the best method for monitoring the contractor's work is through actual inspection.<sup>106</sup> The COR may perform inspections by using several techniques and procedures including spot checks, scheduled inspections of functions performed by the contractor on a periodic basis, random sampling of routine functions, use of contract monitoring and user reports, and periodic review of the contractor's QC program and reports.<sup>107</sup> Furthermore, the contract states that "following receipt of the Contractor's request for payment, and on the basis of an inspection of the work, the [CO] or PD shall make a determination as to the amount which, in his or her opinion, is then due."

One reason that the progress payments were submitted in compliance with requirements was that the PDs conducted monitoring activities to support the approval of progress payments. According to OBO field staff, to determine the percentage of completion and the status of the NEC project, OBO technical personnel conduct work progress inspections. The technical personnel compare their estimate of the completion of the project with the contractor's estimate and either concur or make suggestions to revise the estimate. During the QA inspections, the PD or the OBO project engineer and contractor personnel perform a walkthrough of the work site and discuss the project's progress, including any issues with meeting technical specifications and the quality of building materials. In addition, the PD stated that he reviewed contractor-submitted daily and monthly progress reports, attended weekly QC meetings, and regularly communicated with the contractor's personnel. Because of the approval structure implemented and the monitoring activities performed, the PDs reasonably

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<sup>102</sup> 14 FAH-2 H-142(b)(15), "Responsibilities of the Contracting Officer's Representative (COR)."

<sup>103</sup> Appendix A provides details of the sample selected.

<sup>104</sup> All approved progress payment amounts matched the progress payment amounts requested by the contractor.

<sup>105</sup> 14 FAH-2 H-521, "Elements of Contract Administration."

<sup>106</sup> 14 FAH-2 H-522.1(b), "Progress or Status Reports."

<sup>107</sup> 14 FAH-2 H-522.1(c).

ensured that the contractor's requests for progress were valid and processed in a timely manner, thereby avoiding late payment penalties.

## RECOMMENDATIONS

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**Recommendation 1:** OIG recommends that the Bureau of Overseas Buildings Operations, in coordination with the Bureau of Administration, develop, implement, and communicate a process to ensure that Project Directors for construction projects prepare independent government cost estimates that consider the impact that the modification will have on the overall schedule of the project to determine if extensions are justified. At a minimum, the process should include clarification of individual responsibilities and accountability.

**Recommendation 2:** OIG recommends that the Bureau of Overseas Buildings Operations (OBO) develop, implement, and communicate a process to ensure a separation of duties between OBO staff who receive the price proposal for a request for equitable adjustment related to a construction project and OBO staff who develop the independent government cost estimate for the construction project. At a minimum, the process should include clarification of individual responsibilities and accountability.

**Recommendation 3:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, develop, implement, and communicate a process to ensure that Contracting Officers prepare prenegotiation objectives for modifications to construction projects of more than \$25,000 and that Project Directors do not revise independent government cost estimates during or after negotiations in accordance with the Federal Acquisition Regulation and Department of State policy. At a minimum, the process should include guidance on documenting fair and reasonable pricing and any schedule extensions for the modification and a clarification of individual responsibilities and accountability.

**Recommendation 4:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, develop, implement, and communicate a process to ensure that Project Directors for construction projects conduct and document price negotiations in accordance with the Federal Acquisition Regulation and Department of State policy. At a minimum, the process should include guidance on documenting fair and reasonable pricing and any schedule extensions for the modification and a clarification of individual responsibilities and accountability.

**Recommendation 5:** OIG recommends that the Bureau of Overseas Buildings Operations develop, implement, and communicate a process to ensure that Project Directors comply with the Construction Management Guide's process for all reporting requirements, including daily logs. At a minimum, the process should include clarification of individual responsibilities and accountability.

**Recommendation 6:** OIG recommends that the Bureau of Overseas Buildings Operations develop, implement, and communicate a process to ensure that Project Directors comply with the Construction Management Guide's requirement for developing and distributing a project procedures manual. At a minimum, the process should include clarification of individual responsibilities and accountability.

## APPENDIX A: PURPOSE, SCOPE, AND METHODOLOGY

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The Office of Inspector General (OIG) conducted this audit to determine whether the Bureau of Overseas Buildings Operations (OBO) and the Bureau of Administration administered processes involving contract modifications, construction quality management,<sup>1</sup> and progress payment reviews and approvals for the New Embassy Compound (NEC) Mexico City, Mexico, construction project in accordance with the Federal Acquisition Regulation (FAR) and Department of State (Department) guidance.

OIG conducted this audit from October 2022 to June 2023 in the Washington, DC, metropolitan area and Mexico City, Mexico. The scope of this audit was the administration and oversight of the NEC Mexico City construction contract from September 29, 2017, to August 25, 2022. OIG conducted this performance audit in accordance with generally accepted government auditing standards. These standards require that OIG plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for the findings and conclusions based on the audit objective. OIG believes that the evidence obtained provides a reasonable basis for the findings and conclusions based on the audit objective.

To obtain background information for this audit, OIG researched and reviewed federal laws and regulations and Department policies and procedures. Specifically, OIG reviewed the FAR, the Foreign Affairs Manual, the Foreign Affairs Handbook, the Department of State Acquisition Regulation, and applicable OBO guidance related to construction projects. During fieldwork, OIG also interviewed key personnel within OBO and the Bureau of Administration, Office of the Procurement Executive, Office of Acquisitions Management (AQM). Additionally, OIG reviewed and analyzed the NEC Mexico City construction contract AQMMA17C0287; contract modification documentation; quality assurance and quality control documentation; and progress payments, including supporting documentation.

### **Data Reliability**

#### ***Contract Modifications***

OIG used data provided by OBO that was obtained from non-automated sources to identify the universe of issued contract modifications from the contract award date, September 29, 2017, through August 25, 2022. To assess the completeness and accuracy of the universe of issued contract modifications, OIG used computer-processed data from the Federal Procurement Data System.<sup>2</sup> Specifically, OIG compared the data obtained from the Federal Procurement Data System with the data provided by OBO. OIG did not identify any material discrepancies and concluded that the data from OBO were sufficiently reliable for the selection of contract modifications to review.

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<sup>1</sup> Construction quality management includes all quality control and quality assurance activities instituted to achieve the quality established by the contract requirements.

<sup>2</sup> The Federal Procurement Data System is a computer-based system used by the federal government for collecting, developing, and disseminating procurement data.

### ***Progress Payments***

OIG used electronically processed data from the Department’s Global Financial Management System (GFMS)<sup>3</sup> to determine the universe of progress payments made for the NEC Mexico City, Mexico, contract from the contract award date, September 29, 2017, through July 9, 2022. To assess the completeness and accuracy of the universe of progress payments, OIG compared data that it obtained from OBOLink<sup>4</sup> and the Invoice Processing Platform<sup>5</sup> with the GFMS data. OIG did not identify any material discrepancies and concluded that the data from GFMS were sufficiently reliable for the selection of progress payments to review.

### **Work Related to Internal Control**

During the audit, OIG considered a number of factors, including the subject matter of the project, to determine whether internal control was significant to the audit objective. Based on its consideration, OIG determined that internal control was significant for this audit. OIG then considered the components of internal control and the underlying principles included in the *Standards for Internal Control in the Federal Government*<sup>6</sup> to identify internal controls that were significant to the audit objective. Considering internal control in the context of a comprehensive internal control framework can help auditors determine whether underlying internal control deficiencies exist.

For this audit, OIG concluded that three of five internal control components from the *Standards for Internal Control in the Federal Government*—Control Environment, Control Activities, and Information and Communication—were significant to the audit objectives. The Control Environment component is the foundation for an internal control system. It provides the discipline and structure to help an entity achieve its objectives. The Control Activities component includes the actions management establishes through policies and procedures to achieve objectives and respond to risks in the internal control system, which includes the entity’s information system. The Information and Communication component relates to the quality information that management and personnel communicate and use to support the internal control system. OIG also concluded that five of the principles related to the selected components were significant to the audit objectives, as described in Table A.1.

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<sup>3</sup> GFMS is the Department’s accounting system of record, and all domestic accounting transactions are processed using GFMS.

<sup>4</sup> OBOLink is the official repository of OBO project records.

<sup>5</sup> The Invoice Processing Platform is a secure, web-based service that manages government invoicing from purchase order through payment notification.

<sup>6</sup> Government Accountability Office, *Standards for Internal Control in the Federal Government* (GAO-14-704G, September 2014).

**Table A.1: Internal Control Components and Principles Identified as Significant**

<b>Components</b>	<b>Principles</b>
Control Environment	Management should establish an organizational structure, assign responsibility, and delegate authority to achieve the entity's objectives.
Control Activities	Management should design control activities to achieve objectives and respond to risks.
Control Activities	Management should implement control activities through policies.
Information and Communication	Management should internally communicate the necessary quality information to achieve the entity's objectives.
Information and Communication	Management should externally communicate the necessary quality information to achieve the entity's objectives.

**Source:** OIG generated from the Government Accountability Office, *Standards for Internal Control in the Federal Government* (GAO-14-704G, September 2014).

OIG then interviewed Department officials and reviewed Department procedures and contract documentation to obtain an understanding of the internal controls related to the components and principles identified as significant for this audit. OIG performed procedures to assess the design of key internal controls. Specifically, OIG did the following:

- Analyzed contract modification documents to assess compliance with applicable regulations.
- Analyzed quality assurance and quality control procedures and documents to determine evidence of compliance with oversight requirements.
- Reviewed a sample of progress payments and supporting documentation to determine whether progress payments were properly supported and reviewed prior to approval.

Internal control deficiencies identified during the audit that are significant within the context of the audit objectives are presented in the Audit Results section of this report.

## **Sampling Methodology**

OIG's sampling objective was to select a sample of contract modifications and progress payments for testing.

### ***Contract Modifications***

To determine whether modifications were executed in accordance with federal regulations and Department guidance, OIG used judgmental sampling to select modifications for testing. The goal of the selection process was to judgmentally select a sample that was representative of the universe of modifications related to the NEC Mexico City construction project that were issued between the date of the contract award, September 29, 2017, and August 25, 2022. OIG obtained a list of 65 modifications from OBO. OIG removed 12 modifications that were related

to administrative changes<sup>7</sup> because administrative changes do not present a risk to the audit objective. From the remaining 53 modifications, OIG judgmentally selected 20 for testing. After testing 14 modifications, OIG determined that it was finding the same deficiencies for each modification tested. Therefore, OIG concluded that testing the remaining six modifications was not necessary because the additional information would not impact the audit results. Therefore, as shown in Table A.2, OIG judgmentally reviewed 14 modifications, valued at \$6,264,099, related to the NEC Mexico City construction contract. Also, as shown in Table A.2, some modifications related to multiple Requests for Proposal or multiple Requests for Equitable Adjustments. Therefore, OIG reviewed 15 Requests for Proposal and 8 Requests for Equitable Adjustment associated with the 14 contract modifications.

**Table A.2: Modifications, Requests for Proposal, and Requests for Equitable Adjustment Reviewed**

<b>Modification Number</b>	<b>Request for Proposal or Request for Equitable Adjustment Number</b>	<b>Date Signed</b>	<b>Executed Amount</b>
P0008	RFP 2	04/18/2019	\$185,726
P00012	RFP 14, 17	02/25/2020	9,237
P00013	RFP 16	02/26/2020	108,597
P00018	REA 3, 4	06/18/2020	0*
P00024	REA 6, 9, 10	09/15/2020	18,426
P00027	REA 3, 4	09/28/2020	3,253,715
P00031	REA 16	01/13/2021	0*
P00035	RFP 33, 50, 60, 61	02/24/2021	459,696
P00044	RFP 39	07/07/2021	593,474
P00046	REA 17.1	08/23/2021	0*
P00048	RFP 29	09/09/2021	798,755
P00051	RFP 54, 80, 82, 88	11/23/2021	300,009
P00063	REA 46	07/15/2022	9,112
P00064	RFP 87	08/16/2022	527,352
<b>Total</b>			<b>\$6,264,099</b>

\* Modification executed for a time extension, with no additional costs.

Source: OIG generated based on construction project data obtained from OBO.

### **Progress Payments**

To determine whether documentation was sufficient to support the approval for payments, OIG employed non-statistical judgmental sampling<sup>8</sup> to select progress payments for testing. The goal of the selection process was to judgmentally select a sample that was representative of progress payments made between October 1, 2018, and July 9, 2022. Specifically, OIG obtained

<sup>7</sup> FAR 43.101, "Definitions," states that an administrative change is a unilateral contract change that does not affect the substantive rights of the parties (e.g., a change in the paying office or the appropriation data).

<sup>8</sup> Nonstatistical sampling draws on the auditor's experience and professional judgment in selecting units for evidence from the sampling frame.

a list of 73 progress payments, valued at \$411,617,215, for the NEC Mexico City contract from GFMS. OIG removed 29 progress payments that were made before or after the audit scope period or that were unrelated to construction, for example payments that were COVID related or were for value added taxes. In addition, OIG removed one invoice that was listed as canceled. From the remaining 44 progress payments, valued at \$340,139,158, OIG judgmentally selected 15 progress payments for testing. As shown in Table A.3, OIG judgmentally selected 15 progress payments, valued at \$116,923,073, to include each fiscal year and quarter.

**Table A.3: Progress Payments Selected for Testing**

Invoice	Quarter and Fiscal Year	Invoice Amount
2030-011	Quarter 1, FY 2019	\$6,375,949
2030-013	Quarter 2, FY 2019	3,129,170
2030-017	Quarter 3, FY 2019	3,330,961
2030-020	Quarter 4, FY 2019	12,763,676
2030-023	Quarter 1, FY 2020	16,789,736
2030-027	Quarter 2, FY 2020	9,101,172
2030-030-R1	Quarter 3, FY 2020	6,939,140
2030-031	Quarter 4, FY 2020	5,381,020
2030-035	Quarter 1, FY 2021	3,495,860
2030-037-03	Quarter 2, FY 2021	8,498,417
2030-039	Quarter 3, FY 2021	7,325,846
2030-043	Quarter 4, FY 2021	9,614,951
2030-045	Quarter 1, FY 2022	9,217,362
2030-050	Quarter 2, FY 2022	9,718,144
2030-051	Quarter 3, FY 2022	5,241,669
<b>Total</b>		<b>\$116,923,073</b>

Source: OIG generated based on its analysis of invoice amounts from GFMS data.

### Prior Office of Inspector General Reports

In April 2023, OIG reported<sup>9</sup> that OBO and AQM did not assess time for the NEC Mexico City project as part of the independent government cost estimate process. Assessing time changes required during the independent government cost estimate process is important because the estimate must be prepared prior to receiving the proposal from the contractor. Without a complete independent government cost estimate that includes an assessment of time, the Department was not fully prepared to determine whether the contractor's proposal was fair and reasonable and whether a time extension, as presented in the time impact analysis prepared by the contractor, was justified. The related recommendation in this report remained resolved, pending further action, as of September 2023.

<sup>9</sup> OIG, *Management Assistance Report: Actions To Address Ongoing Construction Schedule Delays at New Embassy Compound Mexico City Are Needed* (AUD-CGI-23-16, April 2023).

In September 2020, OIG reported<sup>10</sup> that when executing award modifications for the Amman, Jordan, construction contract, the Contracting Officer did not include the estimated total time necessary to accomplish the required work. This deviation was contrary to federal and Department guidance for modifying construction contracts and occurred partly to expedite the issuance of the contract modifications. However, this practice made it difficult for OBO to hold the contractor accountable for completing the project on time. OIG closed the recommendation included in the report that was related to the award modification in September 2020.

In June 2018, OIG reported<sup>11</sup> that the invoice review and approval procedures used by OBO for the construction of the NEC and a housing project in Islamabad, Pakistan, generally complied with federal requirements and Department policy. However, OIG found that the Contracting Officer's Representative did not always document his inspection of the contractor's work to attest to the fact that the amount, in his opinion, was due to be paid for work performed. In addition, OIG found that OBO had not adopted a standard operating procedure for reviewing construction invoices associated with large, multimillion-dollar and multi-year construction projects. OIG closed the two recommendations included in the report that were related to invoice review and approval in March 2019 and November 2019, respectively.

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<sup>10</sup> OIG, *Audit of the Bureau of Overseas Buildings Operation's Process To Identify and Apply Best Practices and Lessons Learned to Future Construction Projects* (AUD-MERO-20-39, September 2020).

<sup>11</sup> OIG, *Audit of the Bureau of Overseas Buildings Operation's Process for Reviewing Invoices for the Construction of the U.S. Embassy in Islamabad, Pakistan* (AUD-MERO-18-46, June 2018).

## APPENDIX B: BUREAU OF OVERSEAS BUILDINGS OPERATIONS RESPONSE

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United States Department of State

Washington, D.C. 20520

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December 19, 2023

### INFO MEMO FOR NORMAN BROWN – OIG/AUD

Elizabeth A. Slaughter  
Digitally signed by Elizabeth A. Slaughter  
Date: 2023.12.19 11:33:10 -05'00'

FROM: OBO/COMP– Elizabeth A.S. Slaughter

SUBJECT: Bureau of Overseas Buildings Operations (OBO) Response to OIG draft Audit of Select Contract Administration Processes Related to the Construction of the New Embassy Compound Mexico City, Mexico

OBO appreciates the OIG’s careful review of Mexico City project and would like to highlight the following comments and suggested edits:

- In the Highlights / What OIG Recommends section, OBO suggests that the OIG add the following text in bold:
  - “OIG made six recommendations to OBO and the Bureau of Administration to improve contract modification execution, project reporting, and contract administration for the **Mexico City New Embassy Compound project.**”
- Beginning on Page 4, and throughout the report, the emphasis is on contract modifications as proposals (wherein the government is requesting a change). The report does not address other modifications such as requests for equitable adjustment, wherein the contractor is asserting (or claiming) the government directed a change and compensation is owed. These two processes are different than a legal claim (i.e., certified claim), which goes beyond the contract modification framework.
- Beginning on Page 7, the section on Construction Quality Management, Project Reporting Responsibilities, discusses the importance of daily logs and includes the Office of Construction Management (CM) Guide. OBO acknowledges the importance of daily logs, and also uses other forms of

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documentation to include the General Contractor's daily logs and photographic documentation of project progress.

Please see the following responses to the four recommendations for which OBO is the action office.

**Recommendation 1:** OIG recommends that the Bureau of Overseas Buildings Operations, in coordination with the Bureau of Administration, develop, implement, and communicate a process to ensure Project Directors for construction projects prepare independent government cost estimates that consider the impact that the modification will have on the overall schedule of the project to determine if extensions are justified. At a minimum, the process should include clarification of individual responsibilities and accountability.

**OBO Response:** OBO concurs with the recommendation and is drafting an update to its standard Independent Government Estimate (IGE) form to take into account potential changes in project schedule.

**OBO notes to the OIG that the accumulation of many discrete modifications may impact the critical path timeline. However, discrete modifications might have only negligible time impacts (or none at all) on the critical path of the project to justify an extension of the period of performance. Therefore, it is not always possible to determine if each individual contract modification will impact the overall project schedule.**

**Further, OBO would like to confirm that its staff in Mexico City did conduct a schedule assessment when drafting the initial IGEs for several of the Requests for Proposal (RFPs) that the OIG reviewed and concluded that there was no schedule impact.**

**Recommendation 2:** OIG recommends that the Bureau of Overseas Buildings Operations (OBO) develop, implement, and communicate a process to ensure a separation of duties between OBO staff that receive the price proposal for a request for equitable adjustment related to a construction project and OBO staff that develop the independent government cost estimate for the construction

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project. At a minimum, the process should include clarification of individual responsibilities and accountability.

**OBO Response: Although the methodology the OIG recommends may be applicable for requests for proposals (RFP), OBO contends that it would not be a feasible approach for a fair and expedient analysis of a request equitable adjustments (REA). The OBO-AQM Service Level Agreement Attachment A (OBO can provide the OIG another copy, if requested, under separate cover) provides detailed procedures for both REAs and RFPs, including clarification of individual responsibilities and accountability, as well as procedures for reviewing independent government cost estimates, pre-negotiation and price acceptance.**

**Recommendation 5:** OIG recommends that the Bureau of Overseas Buildings Operations develop, implement, and communicate a process to ensure that Project Directors comply with the Construction Management Guide's process for all reporting requirements, including daily logs. At a minimum, the process should include clarification of individual responsibilities and accountability.

**OBO Response: OBO concurs with the OIG's recommendation that Project Directors comply with the CM Guidebook on all reporting requirements, including daily logs. OBO will make relevant stakeholders aware through periodic alerts.**

**Recommendation 6:** OIG recommends that the Bureau of Overseas Buildings Operations develop, implement, and communicate a process to ensure that Project Directors comply with the Construction Management Guide's requirement for developing and distributing a project procedures manual. At a minimum, the process should include clarification of individual responsibilities and accountability.

**OBO Response: OBO concurs with the OIG's recommendation that Project Directors comply with the CM Guidebook requirements for developing and distributing a project procedures manual for capital construction and major rehabilitation projects. OBO will make relevant stakeholders aware through periodic alerts.**

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## APPENDIX C: BUREAU OF ADMINISTRATION RESPONSE

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**United States Department of State**

**Washington, D.C. 20520**

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January 4, 2024

**MEMORANDUM**

TO: OIG/AUD – Norman Brown

FROM: A/OPE/AQM – Vincent Sanchez, Acting HCA Digital signed by Vincent J. Sanchez  
Date: 2024.01.04 09:20:07

SUBJECT: Draft Report - Audit of Select Contract Administration Processes Related to the Construction of New Embassy Compound Mexico City, Mexico, December 2023 (AUD-CGI-24-XX)

Thank you for the opportunity to provide a response to the subject report. The point of contact for this report is the A/OPE Front Office ([A-OPEFrontOfficeAssistants@state.gov](mailto:A-OPEFrontOfficeAssistants@state.gov)).

**Recommendation 3:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, develop, implement, and communicate a process to ensure that Contracting Officers prepare pre-negotiation objectives for modifications to construction projects of more than \$25,000 and that Project Directors do not revise independent government cost estimates during or after negotiations in accordance with the Federal Acquisition Regulation and Department of State policy. At a minimum, the process should include guidance on documenting fair and reasonable pricing and any schedule extensions for the modification and a clarification of individual responsibilities and accountability.

**Management Response to Draft Report (01/04/24):** The Bureau of Administration, Office of the Procurement Executive, Office of Acquisitions Management (A/OPE/AQM) concurs with the intent of the recommendation; however, request the threshold be increased to \$250K per Request for Proposal (RFP) to align with the simplified acquisition threshold defined in the Federal Acquisition Regulation (FAR). The FAR also outlines the requirements on documenting fair and reasonable pricing as well as CO and COR individual responsibilities and accountability. A/OPE/AQM in coordination with Bureau of Overseas Buildings Operations, will review its Service Level Agreement (SLA) and responsibility matrix to ensure adherence to FAR, DOSAR and DOSAM guidance on negotiations, independent government cost estimates and documentation of fair and reasonableness of any pricing and scheduling modifications.

**Recommendation 4:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, develop, implement, and communicate a process to ensure that Project Directors for construction projects conduct and document price negotiations in accordance with the Federal Acquisition Regulation and Department of State policy. At a minimum, the process should include guidance on documenting fair and reasonable

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pricing and any schedule extensions for the modification and a clarification of individual responsibilities and accountability.

**Management Response to Draft Report (01/04/24):** The Bureau of Administration, Office of the Procurement Executive, Office of Acquisitions Management (A/OPE/AQM) does not concur with the recommendation. Current federal and Departmental regulations and policies direct that fair and reasonable price determinations as well as contractual modifications are made and executed by a warranted Contracting Officer (CO). Therefore, it is proposed that the recommendation be modified to state:

OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, develop, implement, and communicate a process to ensure that Project Directors for construction projects provide support to the Contracting Officer to ensure that price negotiations are conducted and documented in accordance with the Federal Acquisition Regulation and Department of State policy.

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## APPENDIX D: OIG REPLIES TO TECHNICAL COMMENTS FROM THE BUREAU OF OVERSEAS BUILDINGS OPERATIONS

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In addition to responding to the recommendations offered in a draft of this report, the Bureau of Overseas Buildings Operations (OBO) provided technical comments regarding the audit findings that did not directly relate to the Office of Inspector General's (OIG) recommendations (see Appendix B). OBO's comments and OIG's replies are summarized as follows:

**OBO Comment:** OBO requested that OIG add text on the Highlights Page of the audit report to indicate that the six recommendations were "for the Mexico City New Embassy Compound project."

**OIG Reply:** OIG's recommendations were not limited to the Mexico City New Embassy Compound. Instead, OIG's recommendations were intended to improve contract modification execution, project reporting, and contract administration for all OBO construction projects. OIG modified the language on the Highlights Page to indicate that the six recommendations were "for OBO construction projects."

**OBO Comment:** OBO stated that the emphasis in the report is on contract modifications as proposals. OBO noted that the report does not address other modifications, such as requests for equitable adjustment when the contractor asserts that the government directed a change and owes compensation.

**OIG Reply:** OIG acknowledged and differentiated requests for proposal and requests for equitable adjustment in the Background and Audit Results section of this report. Therefore, OIG did not modify the report based on this comment.

**OBO Comment:** OBO stated that in the report, OIG identifies the importance of daily logs. OBO acknowledged the importance of daily logs, but also stated that it uses other forms of documentation, including the general contractor's daily logs and photographic documentation of project progress.

**OIG Reply:** OIG acknowledges OBO uses other forms of documentation in addition to daily logs. In fact, OIG detailed in this report that the Project Director used other logs and meetings to document project progress. However, OBO's Construction Management Guide states that "OBO has found that the daily log is the most important job record in dealing with litigation."

## ABBREVIATIONS

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AQM	Office of Acquisitions Management
CM	Office of Construction Management
CO	Contracting Officer
COR	Contracting Officer's Representative
FAH	Foreign Affairs Handbook
FAM	Foreign Affairs Manual
FAR	Federal Acquisition Regulation
GFMS	Global Financial Management System
IGCE	Independent Government Cost Estimate
NEC	New Embassy Compound
OBO	Bureau of Overseas Buildings Operations
OIG	Office of Inspector General
PD	Project Director
QA	Quality Assurance
QC	Quality Control
REA	Request for Equitable Adjustment
RFP	Request for Proposal

## OIG AUDIT TEAM MEMBERS

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Melissa Bauer, Division Director and Audit Manager  
Contracts, Grants, and Infrastructure Division  
Office of Audits

Eric Covington, Senior Management Analyst  
Contracts, Grants, and Infrastructure Division  
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Brian Jones, Senior Auditor  
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