

Audit Report

AUDIT OF GSA'S ACQUISITION OF SERVICES
FOR THE INTERNATIONAL TRADE CENTER
AT THE RONALD REAGAN BUILDING
REPORT NUMBER A080106/P/W/R10004

May 3, 2010

**Office of Inspector General
General Services Administration**



Office of Audits

U. S. General Services Administration

OFFICE OF INSPECTOR GENERAL

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U.S. GENERAL SERVICES ADMINISTRATION
Office of Inspector General

Date: May 3, 2010

Reply to: Regional Inspector General for Auditing
Attn of: National Capital Region Field Audit Office

Subject: Audit of GSA's Acquisition of Service for the International
Trade Center at the Ronald Reagan Building
Report Number A080106/P/W/R10004

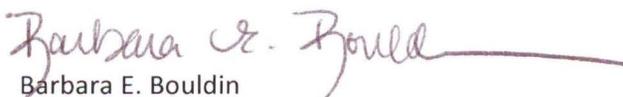
To: Sharon Banks
Acting Regional Administrator (WA)
National Capital Region

Bart Bush
Public Buildings Service Regional Commissioner (WP)
National Capital Region

This report presents the results of our audit of GSA's Acquisition of Services for the International Trade Center at the Ronald Reagan Building. The audit objective was to assess whether the extensive changes to the contract should have been made, with particular attention given to the potential procurement irregularities. Our audit identified numerous procurement irregularities and lack of oversight. The initial decisions to expand the scope of the contract created a flawed platform with an intense administrative workload. Although this contract spanned more than a decade and involved multiple contracting officers and Ronald Reagan Building and International Trade Center directors, the situation did not improve. We found that GSA executed contract actions contrary to FAR regulations, ignored statutes, and abandoned policies and sound business practices. Subsequently, GSA awarded another contract for up to 10 years to the incumbent without the benefit of competition and the assurance that the contract costs are fair and reasonable.

We recommend that the Acting Regional Administrator correct the type of contracting oversight deficiencies identified in this report for current and future contract actions; address the inherent conflict of interest that results from TCMA as both trade center manager and owner/manager of the Aria restaurant; evaluate and perform analyses of the contract to determine the best course of action to ensure GSA is obtaining fair and reasonable pricing, before awarding additional extensions/option years; and establish and support an independent line of authority for the contracting officer and ensure transparency in the management of the contract.

If you have any questions regarding this report, please contact me on (202) 708-5340.



Barbara E. Bouldin
Regional Inspector General for Auditing
National Capital Region Field Audit Office



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EXECUTIVE SUMMARY

PURPOSE

This audit was initiated in response to a request from the former Regional Administrator, concerned over the absence of adequate support to justify a proposed modification to extend the trade center management contract by 26 months beyond its final option year, at an estimated cost of \$50 million dollars. The audit objective was to assess whether the extensive changes to the contract should have been made, with particular attention given to the potential procurement irregularities¹. Specifically, we reviewed conditions surrounding the expansion of the contract to include commercial facility management services and operation of a parking garage, reliance on a cost reimbursable contract structure, and the substantial risk of overpayment² as well as payment of questionable expenses.

BACKGROUND

The Federal Triangle Development Act, Public Law 100-113, dated August 21, 1987, authorized the development of a Federal office complex and international cultural and trade center on the Federal Triangle site at 14th Street and Pennsylvania Avenue, NW, in Washington, D.C. The Act anticipated the development, maintenance and use to be a joint effort of the General Services Administration (GSA), the Pennsylvania Avenue Development Corporation (PADC), and the International Cultural and Trade Center Commission (Commission)³.

¹ Also see Appendix C for an alert report issued on this subject.

² The determination of an 'overpayment' is based on the modifications to the contract, not the payment history. However, the modifications establish the right to payment conditioned upon performance unless rescinded.

³ The sections of the Federal Triangle Development Act Public Law 100-113 pertaining to the establishment and operation of a commission were codified as 40 U.S.C. section 1106 – 1107. These sections are omitted from the current version of the U.S. Code due to "limited interest", but have not been repealed.

This vision of a joint effort, however, did not come to fruition and in 1995 GSA awarded a contract to Trade Center Management Associates (TCMA) to provide all International Trade Center management, operations and maintenance. TCMA was given the exclusive right to develop, operate and manage the more than 500,000 occupiable square feet dedicated to the International Trade Center in the Ronald Reagan Building in what is considered a prestigious area for federal tenant agencies housed in Washington, D.C. In December 2008, after an unsuccessful attempt to compete a new contract for a trade center manager, GSA awarded the contract to the incumbent, TCMA.

RESULTS IN BRIEF

In evaluating the changes and administration of GSA contract GS-11P-02-ZGC-0160⁴, awarded to TCMA in March 1995, and in effect through March 2009, this audit identified numerous and substantial procurement irregularities. In particular, we found:

1. The addition of commercial facility management services greatly and improperly expanded TCMA's contractual scope of work. The action was highly favorable to TCMA, and contrary to the Federal Acquisition Regulation (FAR), was non-competitive and cost-based.
2. A GSA decision that modified the TCMA contract to incorporate parking garage management and operations resulted in an excessive and unwarranted compensation arrangement, inappropriate risk assumption, unnecessary incurrence of taxes, penalties and interest, and improper payment of overhead on those taxes, penalties and interest.
3. The contractual compensation arrangement as it relates to marketing expenses inappropriately shifted all cost and performance risk to the government. GSA also inappropriately reimbursed TCMA for in-house labor costs and incurred the marketing expense for the Aria restaurant.
4. GSA's use of the TCMA contract to acquire construction services resulted in a series of non-competitive award actions, some of which were outside the scope of the contract. Deliverables were unspecified. Terms and conditions required for federal construction contracts were absent and multiple levels of cost mark-ups and fees were permitted.
5. There were 13 separate modifications since June 2002, valued in excess of \$4.5 million, to compensate TCMA for costs for up to 10 additional administrative positions. Administrative positions are typically included in

⁴ The contract was initially awarded as contract number GS-11P-94-AQC-0006. Contract Modification PA02 subsequently changed it to GS-11P-02-ZGC-0160 with no explanation.

contractual general and administrative (G&A) rates and should not have been reimbursed separately.

6. GSA improperly reimbursed TCMA in excess of \$10.6 million for 12 additional sales and sales management positions for work that was included in the fixed-price portion of the contract.
7. TCMA's operation of the Aria restaurant presents an inherent conflict of interest with TCMA's primary role as trade center manager. The terms of agreement are extraordinary in their transfer of costs and risk to the Government.
8. GSA's lack of oversight and enforcement of contract terms permitted TCMA to occupy at no cost substantially more International Trade Center space than provided for under the contract. We estimate the value of unauthorized occupancy at about \$651,398 per year.
9. Related program management deficiencies were also evident in that GSA:
 - a. Did not require the contractor to report on matters relevant to program success;
 - b. Failed to enforce existing audit rights; and,
 - c. Permitted International Trade Center operations to be heavily subsidized by the Federal Buildings Fund.

There was a significant breakdown in management controls. The contracting officers' ability to render independent, professional judgment was impaired by the organizational chain of command. The contracting officers were also hampered by the contract itself in that it was unwieldy and presented a particularly steep learning curve for any newly assigned administrative contracting officer. According to the contracting officers we interviewed, the vendor appears to enjoy unusual, direct access to management. The Ronald Reagan Building and International Trade Center staff also informed us that using the vendor to perform additional services aided in the smooth operations of a highly visible facility which was important to them.

RECOMMENDATIONS

We recommend that the Acting Regional Administrator:

- 1) Correct the type of contracting and oversight deficiencies identified in this report for current and future contract actions, including:
 - a) Non-compliance with all applicable Government contract laws and regulations;
 - b) Uncompensated use of space by TCMA;
 - c) Lack of meaningful performance measures for the contractor;

- d) Improper accounting treatment for assets including allocation of expenses and capitalization; and
 - e) Lack of effective acquisition planning for any contract modifications and awards.
- 2) Address the inherent conflict of interest that results from TCMA as both trade center manager and owner/manager of the Aria restaurant.
 - 3) Evaluate and perform analyses of the contract to determine the best course of action to ensure GSA is obtaining fair and reasonable pricing, as envisioned at the time of the award of the second contract, before awarding additional extensions/option years. Included in this evaluation would be a review of the International Trade Center mission as it affects the stewardship of the asset.
 - 4) Establish and support an independent line of authority for the contracting officer and ensure transparency in the management of the contract.

INTRODUCTION

BACKGROUND

The Federal Triangle Development Act, Public Law 100-113, dated August 21, 1987, authorized the development of a Federal office complex and international cultural and trade center on the Federal Triangle site at 14th Street and Pennsylvania Avenue, NW, in Washington, D.C. The Act anticipated the development, maintenance and use to be a joint effort of the General Services Administration (GSA), the Pennsylvania Avenue Development Corporation (PADC), and the International Cultural and Trade Center Commission (Commission)⁵.

Effective April 1, 1996, Congress transferred all responsibilities formerly held by PADC to GSA⁶, and the independent Commission was to oversee what was initially conceived as an international cultural and trade center. The legislation granted the Commission the authority to establish, operate and maintain an international cultural and trade center from space leased from GSA not to exceed 500,000 occupiable square feet in the building, which at that point was yet to be constructed. The Commission was in turn authorized to sublease to foreign missions and international cultural and trade organizations, including domestic organizations and State and local governments. The space was to be made available for the establishment of trade centers and exhibitions, offices, commercial establishments, a foreign trade reference facility, conference and event facilities and audio-visual facilities for translating foreign languages. The Commission was allowed to permit cultural events and other activities to be held in a portion of such space. The Commission was short lived and has apparently not played a role in what has evolved from the International Cultural and Trade Center to the International Trade Center at the Ronald Reagan Building⁷.

The arrangement initially envisioned has been superseded by a single contract providing all International Trade Center operations and maintenance. GSA made a competitive award to *Trade Center Management Associates* (TCMA). TCMA has been given the exclusive right to develop, operate and manage the more than

⁵ See Note 3.

⁶ The PADC was terminated in accordance with Public Law 104-134 and transferred its rights, title and interest in all property to the GSA on April 1, 1996. Also see 40 U.S.C. Chapter 67.

⁷ GSA's written response to a question that resulted from the Trade Center Manager pre-proposal conference indicated that the Commission was not currently funded and is inactive.

500,000 occupiable square feet dedicated to the International Trade Center in what is considered a prestigious area for federal tenant agencies housed in Washington D.C. The complex, with a value estimated by GSA at \$1.5 billion, is within two blocks of the White House, is within walking distance of the U.S. Capitol Building and has frontage on two arterial roadways with nearby access to the interstate highway system. It has a 1,950 space parking garage under the complex and a Great Plaza with outside seating and landscaping that serves as a gateway to the National Mall. National monuments, historic landmarks, hotels, theaters, restaurants, entertainment centers and sports arenas are also in close proximity to the site.

The International Trade Center has been acknowledged by a variety of associations and the recipient of several awards over the last 10 years, including Office Building of the Year in 2001 (BOMA) and the INNER CIRCLE award winner for conference centers in 2008.

BASE CONTRACT

On March 7, 1995, GSA awarded TCMA a firm, fixed-price contract⁸ comprised of a base year plus nine one-year options. An additional two years were added to compensate for construction delays, pushing the expiration date to March 7, 2007. Not ready with a successor contract, GSA extended TCMA's contract two additional years. It expired on March 7, 2009.

The purpose of the trade center manager contract was to develop, manage and operate the International Trade Center at the Ronald Reagan Building. The contract cites the government's planning goals for the creation of the International Trade Center, which were to:

- I. Facilitate and support a federal trade program to enhance the exchange of American goods and services in the international marketplace;
- II. Enhance the vitality of Pennsylvania Avenue and environs;
- III. Create a pedestrian link between the National Mall and the central business district;
- IV. Create a facility that provides visual testimony to the dignity, enterprise, vigor and stability of the American Government; and,
- V. Maximize the financial return on the Government's investment to support the center's activities.

⁸ See Note 4.

The contract was divided into two phases:

Phase I – Program Development – TCMA was tasked to perform market analysis and program development; and produce a marketing plan, leasing plan, and operating plan in support of the stated planning goals, subject to GSA approval. The fixed-price award was valued at \$590,029.

Phase II – Program Implementation – Following the approval of the final program under Phase I, TCMA was tasked with providing the services necessary to implement the program. Compensation was comprised of:

- a fixed-price payment of \$1,753,151⁹ per year, plus annual price escalation in accordance with a prescribed wage price index;
- commissions for office, retail and food service lease awards;
- a fee for event room-rentals; and
- reimbursement for certain anticipated expenses, such as covering added security for events, event production costs, marketing, advertising, publications, and costs of a similar nature.

The vendor was also permitted to provide catering services, but a specific revenue sharing arrangement was not specified under the base contract.

The Phase II base contract services tasked TCMA to:

1. Market space;
2. Secure tenants;
3. Develop lease terms and conditions;
4. Coordinate tenant space build-out;
5. Administer leases;
6. Reconcile utilities cost allocations;
7. Coordinate security requirements;
8. Provide all staffing needs relative to accounting and administrative support;
9. Provide an annual audit at contractor's expense;
10. Provide concierge services;
11. Provide International Trade Center budgeting and financial reporting;

⁹ As noted in the questions and answers for the Best and Final Offer, the price of the Phase II options fluctuates in years 1-3 (\$1,753,151, \$1,668,744 and \$1,749,006 respectively) due to some variations in TCMA's annual budget as a result of a phased hiring program, initial set-up costs and the provisions of required services during lease-up. Option year 3 pricing was in effect for the balance of the contract.

12. Promote the venue;
13. Coordinate required commercial facility management services; and
14. Manage events, conferences and exhibits to include soliciting, scheduling, collecting fees, catering, production, and cleaning. (We note that the base contract implies that event management will generate fees but does not describe a revenue sharing formula.)

The base contract **specifically excluded** two key areas: parking and commercial facility management. Per the Request for Proposal (RFP), parking was to be managed by GSA under a separate contract, and the International Trade Center was allocated 350 spaces to support its operations. Commercial facility management services were also to be procured under a separate contract. GSA envisioned a single-source contract providing commercial facility management services to the entire complex to include event support.

CONTRACT MODIFICATIONS

GSA exercised its first option for “Phase II – Program Implementation” services on March 8, 1996. As outlined above, the base contract contemplated an annual fixed-price payment (plus escalation), commissions and fees, catering, and certain reimbursable expenses. Contract modifications were initiated to fund these actions. In addition to these anticipated items, the contract was modified to include a comprehensive range of services outside the original scope of the contract. In the earliest and ultimately most expensive of these changes, TCMA was awarded operation of the parking garage and certain commercial facility management responsibilities.¹⁰ Construction projects were also awarded through this contract vehicle, as were additional administrative and sales positions, and restaurant startup costs and management. [Table 1](#) lists contract modifications by value through contract modification C197, effective May 9, 2008.

¹⁰ GSA awarded a separate commercial facility management contract that covered building operation, maintenance, operation and repair of mechanical, electrical, utility systems and structural maintenance and repairs for the entire Ronald Reagan Building and International Trade Center complex. The facilities management tasks awarded to TCMA cover services such as cleaning (including windows), custodial services, landscaping, and pest control for ITC space.

| Modification Category | Funded Amount |
|------------------------------|----------------------|
| CFM Services* | \$71,865,325 |
| Parking Garage | \$24,739,979 |
| Exercise Option | \$22,362,991 |
| Marketing/Promotion | \$12,273,975 |
| Additional Sales Staff | \$10,615,003 |
| Construction | \$10,104,471 |
| DC Tax | \$9,515,083 |
| Leasing Commissions | \$7,885,000 |
| Extension Mod | \$5,020,512 |
| Additional Admin Staff | \$4,548,379 |
| Restaurant | \$4,311,554 |
| Reimbursable - Misc | \$2,542,810 |
| Reimbursable – CFM Services* | \$2,086,701 |
| Signage | \$1,002,960 |
| Event Fees | \$953,000 |
| Linens | \$907,126 |
| Audit Services | \$785,900 |
| Studies/Consultants | \$724,907 |
| Wi-Fi | \$550,599 |
| Legal | \$520,000 |
| Program Development | \$493,485 |
| Fitness Center | \$374,413 |
| Phase I Increase | \$84,600 |
| Security Check | \$59,000 |
| Grand Total | \$194,327,775 |

Table 1 - Value of Contract Modifications through May 9, 2008

*Commercial Facility Management Services

SUCCESSOR CONTRACT ACTION

In May 2008, GSA conducted a competitive solicitation for offers, receiving only one response, that of the incumbent. As a result, GSA's management established a task force, assembled with GSA's legal counsel and procurement experts, to determine whether its new solicitation for a trade center manager for the International Trade Center in effect, prevented competition. The task force identified that the "limited historical data provided by GSA to the offerors, together with the substantial risks placed on offerors by the solicitation", prevented full and open competition. However, the November 25, 2008 memorandum to the Senior Procurement Advisor from the former Acting Regional Administrator stated that the region would proceed with contract award and the Senior Procurement Advisor concurred with that decision. On December 2, 2008, the new contract was awarded to the incumbent,

TCMA. The contract consists of a base period, nine optional one-year periods and a close out period.

OBJECTIVES, SCOPE AND METHODOLOGY

This audit was initiated in response to a request, in December 2007, from the former Regional Administrator, concerned over the absence of adequate support to justify a proposed modification to extend the current trade center management contract by 26 months beyond its final option year, at an estimated cost of \$50 million dollars. The audit objective was to assess whether the extensive changes to the contract should have been made¹¹, with particular attention given to potential procurement irregularities. Specifically, we reviewed conditions surrounding the expansion of the contract to include operation of a parking garage and commercial facility management, reliance on a cost reimbursable contract structure, and the potential for overpayment and payment of questionable expenses. An alert report was issued to the former Regional Administrator on May 29, 2008.

Fieldwork was performed from May 2008 to January 2009 and included contract, financial, and program activity from March 1995, contract award, through the end of fieldwork. The audit methodology included the following:

LAWS, REGULATIONS, GUIDANCE AND BUILDING HISTORY

- Reviewed authorizing legislation and Committee Reports;
- Reviewed the Public Buildings Service (PBS) accounting and construction guidance, and agency policies and procedures;
- Reviewed all Asset Business Plans for the building and parking garage;
- Reviewed and documented a news article related to the Ronald Reagan Building and International Trade Center;
- Reviewed the information on the Ronald Reagan Building and International Trade Center website.

CONTRACT AND RELATED RECORDS

- Analyzed the Trade Center Manager contract terms and conditions;

¹¹ The operations of the facility were not evaluated as part of our objective.

- Reviewed and analyzed documents provided by the former Regional Administrator including contract history, modification summary, and pre-award and solicitation files to obtain a more complete understanding;
- Analyzed the award documents (including amendments), the Technical Proposal, and the Best and Final Offer;
- Reviewed the contracting officers' correspondence files, and the 321 contract modifications spanning a 13-year period to ascertain the contract's history, major funding activities, and to determine the subject areas for review;
- Obtained a copy of the new awarded contract and related correspondence. Subsequent to fieldwork, we performed a limited review of aspects of the follow-on contract's Request for Proposal.

FINANCIAL DATA

- Analyzed and created a database for the TCMA submitted invoices from January 2005 through May 2008 and analyzed the September 2007 detailed invoice binder (Note: The invoices from January 2005 through May 2008 were the only available electronic invoices.);
- Reviewed the budgets related to marketing, parking and commercial facility management ;
- Reviewed revenue generating activities under the contract and their respective expenses;
- Reviewed GSA's modification tracker and expense tracker;
- Obtained and reviewed the Ronald Reagan Building and International Trade Center profit/loss statement, and analyzed Pegasys reports for the TCMA contract.

CONFERENCES AND MEETINGS

- Held entrance conference and periodic briefings with the former Regional Administrator, and his senior executive staff including the Deputy Assistant Regional Administrator (ARA) for PBS Business Services and Support, Deputy ARA PBS Operations, Regional Counsel, and Triangle Services Center Director;
- Held discussions with GSA regional officials responsible for the day-to-day operations of the Ronald Reagan Building and International Trade Center, including Ronald Reagan Building and International Trade Center Directors, International Trade Center Director, contracting officers, International Trade Center program analyst, and International Trade Center budget analyst for the TCMA contract,

and Ronald Reagan Building and International Trade Center GSA building manager and staff;

- Held discussions with regional and central office Chief Financial Officer officials, regional PBS officials, GSA competition advocate utilized for the new procurement, GSA's space management personnel, GSA Regional Appraiser, Asset Manager, GSA Office of Inspector General legal personnel, and the 3H Technology contractor.

PROGRAMMATIC REVIEW

- Reviewed audits performed by an independent auditing firm of the parking garage, and conference center events and the related management letters;
- Toured the International Trade Center facilities including the North Tower, conference and event space, food preparation areas, parking garage and loading dock areas, restaurant, and exterior perimeter of the building to verify tenant occupancy, parking operations, TCMA occupancy, and observe the general control environment;
- Analyzed office and retail tenant license agreement files;
- Analyzed licenses, amendments, and corresponding meeting notes for the three restaurant tenants;
- Reviewed and analyzed TCMA submitted Room Commission sheets and 21-day event reports.

The audit was conducted in accordance with generally accepted government auditing standards (GAGAS) for performance audits. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

RESULTS OF AUDIT

RESULTS IN BRIEF

In evaluating the changes and administration of the General Services Administration (GSA) contract GS-11P-02-ZGC-0160¹², awarded to Trade Center Management Associates (TCMA) in March 1995, and in effect through March 2009, this audit identified numerous and substantial procurement irregularities. In particular, we found:

1. The addition of commercial facility management services greatly and improperly expanded TCMA's contractual scope of work. The action was highly favorable to TCMA, and contrary to the Federal Acquisition Regulation (FAR), was non-competitive and cost-based.
2. A GSA decision that modified the TCMA contract to incorporate parking garage management and operations resulted in an excessive and unwarranted compensation arrangement, inappropriate risk assumption, unnecessary incurrence of taxes, penalties and interest, and improper payment of overhead on those taxes, penalties and interest.
3. The contractual compensation arrangement as it relates to marketing expenses inappropriately shifted all cost and performance risk to the government. GSA also inappropriately reimbursed TCMA for in-house labor costs and incurred the marketing expense for the Aria restaurant.
4. GSA's use of the TCMA contract to acquire construction services resulted in a series of non-competitive award actions, some of which were outside the scope of the contract. Deliverables were unspecified. Terms and conditions required for federal construction contracts were absent and multiple levels of cost mark-ups and fees were permitted.
5. There were 13 separate modifications since June 2002, valued in excess of \$4.5 million, to compensate TCMA for costs for up to 10 additional administrative positions. Administrative positions are typically included in the contractual general and administrative (G&A) rates and should not have been reimbursed separately.
6. GSA improperly reimbursed TCMA in excess of \$10.6 million for 12 additional sales and sales management positions for work that was included in the fixed-price portion of the contract.

¹² See Note 4.

7. TCMA's operation of the Aria restaurant presents an inherent conflict of interest with TCMA's primary role as trade center manager. The terms of agreement are extraordinary in their transfer of costs and risk to the Government.
8. GSA's lack of oversight and enforcement of contract terms permitted TCMA to occupy at no cost substantially more International Trade Center (ITC) space than provided for under the contract. We estimate the value of unauthorized occupancy at about \$651,398 per year.
9. Related program management deficiencies were also evident in that GSA:
 - a. Did not require the contractor to report on matters relevant to program success;
 - b. Failed to enforce existing audit rights; and,
 - c. Permitted ITC operations to be heavily subsidized by the Federal Buildings Fund.

There was a significant breakdown in management controls. The contracting officers' ability to render independent, professional judgment was impaired by the organizational chain of command. The contracting officers were also hampered by the contract itself in that it was unwieldy and presented a particularly steep learning curve for any newly assigned administrative contracting officer. According to the contracting officers we interviewed, the vendor appears to enjoy unusual, direct access to management. The Ronald Reagan Building and International Trade Center staff also informed us that using the vendor to perform additional services aided in the smooth operations of a highly visible facility which was important to them.

1. COMMERCIAL FACILITY MANAGEMENT SERVICES

Although explicitly excluded from the original contract solicitation and award, commercial facility management services were nevertheless added to TCMA's contract. The addition of these services greatly and improperly expanded TCMA's contractual scope of work. The action was highly favorable to TCMA and, in contravention of the Competition in Contracting Act, 41 U.S.C. § 253, as well as FAR requirements, was non-competitive and cost based. As a result, GSA had no means to determine whether the proposal represented a realistic, market-based solution, and the vendor community was denied a competitive opportunity. Further, aspects of the compensation arrangement resulted in duplication of G&A type costs.

A no-bid, cost-plus-percentage-of-cost compensation arrangement was used from July 1997 through October 1999. From that point forward, the compensation

arrangement changed to what the official contract file characterizes as fixed-price. In fact, it was a highly unusual cost-derived compensation arrangement plus G&A, plus a management fee, plus escalation. The entire amount was reset at three-year intervals. The total value funded through May 2008 was \$74 million.

1.1. COMMERCIAL FACILITY MANAGEMENT SERVICES PHASE 1 – COST REIMBURSABLE

Within its base contract Request for Proposal (RFP), including specific questions and answers documented in amendments to the RFP, GSA advised bidders that commercial facility management services would be procured independently, and competitively, under a separate, future contract action. Contrary to its explicit statement of exclusion and without a stated justification, GSA modified the TCMA contract soon after award to allow for janitorial and facility management services. This initial modification stated that the action was “In accordance with discussions and representations by the Government...” While a former director of the facility stated that discussions did occur, she did not participate in them and we found no evidence of these discussions or specific Government representations, and no justifications as to how or why the decision was reached. This initial modification added, un-priced and only generically scoped, both 1) janitorial and facility management services and 2) operation and management of the parking garage. The specific language as it pertains to commercial facility management services was limited to the following:

Provide janitorial and facility management services for p[r]ogram areas related to the International Trade Center. (These areas generally included office space through the 9th floor, ground, concourse, mezzanine and below grade ancillary spaces and the parking garage.) which [sic] will include the following services:

1. *Janitorial/cleaning*
2. *Exterior of building cleaning (doors, all exterior glass and metal trim)*
3. *Snow removal*
4. *Trash collection and removal, recycling*
5. *All exterior building window washing*
6. *Landscape maintenance*
7. *Pest and rodent control*
8. *Reimbursable building alterations*
9. *Security support services*
10. *Coordination with other building maintenance and construction contractors ...*

YOU ARE REQUESTED TO SUBMIT A PROPOSAL FOR THIS ADDED WORK. NO COSTS SHALL BE INCURRED NOR THE GOVERNMENT LIABLE FOR ANY COSTS RELATING TO THIS MODIFICATION UNTIL THE FINAL SCOPE OF WORK, PERFORMANCE PERIOD AND PRICING ARE RECONCILED AND DEFINITIZING MODIFICATION ISSUED ACCORDINGLY. (Contract modification PC07, signed July 18, 1996)

On June 30, 1997, TCMA's contract was modified to add the final scope of work and to fund the initial task. Compensation for these services, for the start-up period (July 1, 1997 to September 30, 1998, extended to October 31, 1999), was a cost-plus-fee type arrangement, where TCMA received cost reimbursement, plus a (PROPRIETARY INFORMATION – REDACTED) G&A fee, plus a management fee based on square footage. The management fee, per the modification estimate, added (PROPRIETARY INFORMATION – REDACTED) per year to the contract. From data presented in the latest invoices (September and October 1999) for this initial commercial facility management services compensation arrangement, the fee represents an implied profit as high as (PROPRIETARY INFORMATION – REDACTED) over costs, with most cost risk absorbed by GSA. We note that FAR 16.301-3(b)¹³ prohibits the use of cost reimbursable contracts to acquire commercial services, a point also included in FAR 12.207¹⁴. Further, the cost-plus-percentage-of-cost pricing structure, which has been applied in this instance in the form of a predetermined (PROPRIETARY INFORMATION – REDACTED) G&A fee, is prohibited without exception by 41 U.S.C. § 254 (b), as well as FAR 16.102(c).

1.2. COMMERCIAL FACILITY MANAGEMENT SERVICES PHASE 2 – FIXED PRICE

At the end of this “start-up” period, the contract was modified to what the contract file characterizes as a fixed-price arrangement, supplemented by reimbursable and variable components, but intended to be primarily fixed-price. The following problems were present in this second phase. First, there was no full and open competitive process.¹⁵ TCMA submitted a cost budget, including substantial subcontracting, which served as the basis of award. Second, the fixed-price contract arrangement was in fact not fully fixed. It contained an annual price escalation provision, but in addition, was actually reset to cost after three years. In effect,

¹³ FAR 16.301-3(b): *“The use of cost-reimbursement contracts is prohibited for the acquisition of commercial items ...”*

¹⁴ FAR 12.207: *“... (a) Except as provided in paragraph (b)... agencies shall use firm-fixed-price contracts or fixed-price contracts with economic price adjustment for the acquisition of commercial items... (e) Use of any contract type other than those authorized by this subpart to acquire commercial items is prohibited.”* The exception cited, paragraph (b), is for time-and-materials or labor-hour contracts.

¹⁵ FAR 6.101: *“(a) 10 U.S.C. 2304 and 41 U.S.C. 253 require, with certain limited exceptions (see Subpart 6.2 and 6.3), that contracting officers shall promote and provide for full and open competition in soliciting offers and awarding Government contracts. (b) Contracting officers shall provide for full and open competition through use of the competitive procedure(s) contained in this subpart that are best suited to the circumstances of the contract action and consistent with the need to fulfill the Government's requirements efficiently ([10 U.S.C. 2304](#) and [41 U.S.C. 253](#)).”*

TCMA incurred no significant cost or performance risk; the arrangement was devoid of the hallmarks of a fixed-price contract. Third, the pricing arrangement left the contract vulnerable to cost duplication and violated aspects of FAR. To its budgeted direct cost, TCMA added (PROPRIETARY INFORMATION – REDACTED) G&A plus a (PROPRIETARY INFORMATION – REDACTED) management fee¹⁶ as a percentage of total cost. For example, based on its 2003 price proposal, the price was set at not to exceed (PROPRIETARY INFORMATION – REDACTED). The proposal provided line items for the direct costs such as uniforms, payroll and payroll taxes, telephone, and office supplies. To this TCMA added a G&A fee¹⁷ (PROPRIETARY INFORMATION – REDACTED); and management fee (PROPRIETARY INFORMATION – REDACTED). The budgeted direct costs include many indirect type expenses that would normally be associated with G&A. Permitting these costs as both direct and indirect elements is contrary to FAR cost rules¹⁸ and results in duplication. Additionally, this type of arrangement has more in common with cost-reimbursement than fixed-price contracting and a cost-based compensation arrangement for this type of service is not permitted under FAR.

2. PARKING GARAGE MANAGEMENT AND OPERATIONS

The GSA decision to modify the TCMA contract to incorporate parking garage management and operations resulted in an excessive compensation arrangement, inappropriate risk assumption, unnecessary incurrence of taxes, penalties and interest, and improper payment of overhead on those taxes, penalties and interest. From January 1999 through May 2008, TCMA earned fees of approximately (PROPRIETARY INFORMATION – REDACTED)¹⁹ on fully reimbursed parking garage

¹⁶ Fee was derived from a rate per square foot methodology that equated to (PROPREITARY INFORMATION – REDACTED) of the total proposed cost.

¹⁷ Under the contract, the vendor is provided space in the facility at no cost. Office space would also generally be part of G&A costs.

¹⁸ FAR 31.203(b): “After direct costs have been determined and charged directly to the contract or other work, indirect costs are those remaining to be allocated to intermediate or two or more final cost objectives. No final cost objective shall have allocated to it as an indirect cost any cost, if other costs incurred for the same purpose, in like circumstances, have been included as a direct cost of that or any other final cost objective.”

¹⁹ An estimate based on available audited TCMA revenue schedules from 1999 through 2006, and invoiced amounts for the remainder through May 2008.

operating expenses of (PROPRIETARY INFORMATION – REDACTED)²⁰, a (PROPRIETARY INFORMATION – REDACTED) rate of return with no cost or performance risk borne by TCMA. In addition, TCMA received an unallowable payment of (PROPRIETARY INFORMATION – REDACTED), equivalent to (PROPRIETARY INFORMATION – REDACTED) G&A²¹ improperly paid on taxes, penalties and interest of \$6.2 million. GSA, in turn, has had to assume the entire tax, penalty, and interest liability without recourse. Contract modifications to fund the tax and related liabilities exceeded \$9 million, costs that would have been avoided in their entirety had the facility been government operated. At a minimum, under a more appropriate contract structure, the contractor would have borne responsibility to identify and mitigate such risks, and it is arguable that TCMA, in its broader role as ITC manager, should have done so. In addition, there were no stated or measured performance goals.

2.1. IMPROPER CONTRACT ACTION

The contract was modified concurrently to include both the commercial facility management services (as discussed in the previous section of this report) and the parking garage operation and management. In both instances, it was GSA's original intention to procure the services under a contract separate from the TCMA contract. Pre-proposal conference minutes and Amendment 2 of the Solicitation noted that parking services would be contracted for separately by GSA. As with the commercial facility management services, we found no documentation of GSA's rationale for changing position to include parking as part of the contract. In discussions with a former director of the facility, we were told that her understanding was that including these services allowed for better coordination of operations within the facility. The contract was modified and the specific language as it pertains to parking was limited to the following:

Provide management and operation services for the entire parking garage for the Ronald Reagan Building and International Trade Center including parking designated for FOB tenants and ITC.

²⁰ This is an estimate based on funding documents. We also performed this analysis using electronic invoices and it yielded approximately the same rate of return.

²¹ A memo to the modification file says the amount was offset by (PROPRIETARY INFORMATION – REDACTED) previously reimbursed for legal expenses incurred. The purported legal fees incurred would have been elements of the G&A pool. FAR 31.202 precludes direct cost recovery of cost elements otherwise treated as indirect costs. Legal fees are either excluded from the G&A pool in their entirety, and billable to GSA only as direct cost elements of a contract specified final cost objective, or recoverable exclusively through application of the G&A rate allocable to an otherwise allowable final cost objective.

Services include but are not limited to: (A full scope of services will be developed and attached at a later date)

1. *Collect revenues from hourly, daily and monthly parkers*
2. *Provide all labor and materials for parking*
3. *Provide all labor to collect revenues and provide valet parking as needed designated [sic]*
4. *Ensure parking areas are cleaned and ready for monthly FOB employees by 6AM, Monday through Friday.*

YOU ARE REQUESTED TO SUBMIT A PROPOSAL FOR THIS ADDED WORK. NO COSTS SHALL BE INCURRED NOR THE GOVERNMENT LIABLE FOR ANY COSTS RELATING TO THIS MODIFICATION UNTIL THE FINAL SCOPE OF WORK, PERFORMANCE PERIOD AND PRICING ARE RECONCILED AND DEFINITIZING MODIFICATION ISSUED ACCORDINGLY. (Contract modification PC07, signed July 18, 1996)

Approximately one year later the TCMA contract was modified to supplement the contract action cited above by providing full terms, conditions, scope and pricing. The file did not address the exception to FAR competition requirements²², the use of a cost reimbursable contract structure to acquire commercial services²³, FAR-required profit analysis²⁴, nor Service Contract Act provisions²⁵.

2.2. PRICE STRUCTURE

Under the agreed upon contract terms, parking garage operating expenses were fully reimbursed to TCMA. Operating expenses included costs of personnel, materials, subcontracts, liability insurance for property and persons, utilities, valet parking, cleaning, supplies, uniforms, and laundry. Salaries included a general manager,

²² FAR 6.301(a): *"...Contracting without providing for full and open competition or full and open competition after exclusion of sources is a violation of statute, unless permitted by one of the exceptions in [6.302](#). (b) Each contract awarded without providing for full and open competition shall contain a reference to the specific authority under which it was so awarded...."*

²³ See Note 13.

²⁴ FAR 15.404-4(d): *"...unless it is clearly inappropriate or not applicable, each factor outlined in...this subsection shall be considered by agencies in developing their structured approaches and by contracting officers in analyzing profit, whether or not using a structured approach."*

²⁵ FAR 22.1002-1: *"Service contracts over \$2,500 shall contain mandatory provisions regarding minimum wages and fringe benefits, safe and sanitary working conditions, notification to employees of the minimum allowable compensation, and equivalent Federal employee classifications and wage rates. Under [41 U.S.C. 353\(d\)](#), service contracts may not exceed 5 years."*

facility manager, valet manager, assistant managers, bookkeeper, and receptionist. Through May 2008, estimated cumulative operating expense reimbursements were (PROPRIETARY INFORMATION – REDACTED).

In addition to recovering its cost, TCMA was paid a fee based on generated gross parking revenue. It earned (PROPRIETARY INFORMATION – REDACTED) on monthly permit parking revenue, and (PROPRIETARY INFORMATION – REDACTED) on transient parking fees for gross monthly transient parking revenue. A (PROPRIETARY INFORMATION – REDACTED) incentive payment was also available on operating expense savings, but the triggering condition was never met. Through May 2008, we estimated that TCMA earned parking fees totaling (PROPRIETARY INFORMATION – REDACTED).

The net result was a cost reimbursable contract structure that permitted profit averaging (PROPRIETARY INFORMATION – REDACTED) of operating costs. To earn this fee, TCMA assumed no cost risk. Any unanticipated expense or cost increase was passed on to GSA. For example, the costs associated with the failure to anticipate or mitigate a substantial tax liability were passed through to GSA.

2.3. AVOIDABLE INTEREST AND PENALTIES ON D.C. SALES AND USE TAX

The District of Columbia imposes a 12% sales and use tax on commercial parking revenues. The tax liability issue first surfaced as the result of an audit in 2002 by the District of Columbia Office of Tax and Revenue. The audit found unpaid taxes of \$2.9 million for the period January 1, 1998 through December 31, 2001. The taxes remained unpaid until 2005, by which time the penalty plus interest had increased the amount by \$3.3 million to \$6.2 million. That amount, plus an additional \$1.8 million, per a settlement agreement between TCMA and the District, resolved the tax liability through calendar year 2006. Since that time, taxes have been remitted as required, and since May 2007, TCMA is collecting tax from the parking patrons, so the cost burden to GSA has, finally, been alleviated. Monthly taxes average approximately \$55,000.

The District's position was as follows. Because the ITC parking garage is vendor operated, and that vendor was most accurately defined as an independent contractor and not an agent or instrumentality of the Federal Government, all parking revenue (except that which represents a direct intergovernmental transfer from a tenant agency to GSA) is subject to the tax. If the Government itself were operating the garage, the District acknowledges, it would be without authority to collect the tax.

The failure to identify the liability is a responsibility shared by both GSA and TCMA. GSA ultimately lost nearly \$10 million. Proper acquisition planning, a suitable

contract structure with appropriate risk sharing, accounting for results of operations - all of these were absent on GSA's part. A GSA operated facility, or one deemed under GSA control, would have avoided the cost altogether. TCMA failed to identify the potential liability in the first place, and changes to offset the cost to GSA took years to implement. A vendor that recognized the liability and properly collected the tax would also have avoided the cost to GSA, shifting it more appropriately to the parking patrons. Within the scope of this audit, we did not explore the reasons why the original taxes remained unpaid while interest charges accrued, or whether the payment by GSA was proper and justified.

2.4. TCMA MARK-UP ON D.C. SALES AND USE TAX PAYMENT

TCMA received an unallowable payment of (PROPRIETARY INFORMATION – REDACTED), equivalent to (PROPRIETARY INFORMATION – REDACTED) G&A, applied to the taxes, penalties and interest totaling \$6.2 million and covering taxes through calendar year 2001. No G&A mark-up was applied to subsequent tax payments. There was no justification for a G&A mark-up based on an uncollected tax liability. It was improper to compensate TCMA for overhead associated with taxes it failed to assess or collect, and for interest charges paid by GSA. Further, the G&A allocation base, never defined under the contract, could not have included taxes. These are not expenses that TCMA would incur; these are instead liabilities that TCMA was obligated to collect from parking patrons on behalf of the District Government.

3. MARKETING

The contractual compensation arrangement as it related to marketing expenses inappropriately shifted all cost and performance risk to the government. GSA also inappropriately reimbursed TCMA for in-house labor costs for an additional position, and incurred the marketing expense for the Aria restaurant. In addition, an asset acquired in support of outdoor events, with an original purchase price in excess of \$50,000, was incorrectly accounted for as a reimbursable marketing expense and improperly sold.

3.1. BASE CONTRACT

GSA tasked TCMA under Phase II of the base contract to *“...aggressively promote the ITC and all of its programs”* and *“prepare an annual plan outlining promotional activities, promotional costs and calendar of events. The programmed events shall be accompanied by budget estimates and presented to the Government for approval.”* The fee structure was such that all personnel costs related to

programming and promotional activities would be covered by the base contract fee. All other costs related to marketing would be paid on a reimbursable basis as approved by GSA as the yearly budget.

3.2. COST AND PERFORMANCE RISK

The contract established no measurable performance goal or cost constraint relative to marketing and promotion. While funding through May 9, 2008 exceeded \$12 million, the effectiveness of marketing relative to these expenditures was never evaluated by GSA. We reviewed the composition of the outlays for the period from January 2005 through May 2008. Summary data is provided in [Table 2](#):

| Marketing Categories | Invoiced Jan 05-May 08 | % |
|---------------------------------------|---------------------------|-------------|
| General | \$2,352,756 | 58% |
| Woodrow Wilson Plaza (Outdoor Events) | \$1,077,011 | 26% |
| Aria Restaurant | \$316,914 | 8% |
| Complementary Food Court Vouchers | \$170,604 | 4% |
| Additional TCMA Payroll | \$117,688 | 3% |
| Other | \$35,298 | 1% |
| Total | \$4,070,271 | 100% |

Table 2 - Marketing Expense Invoiced Jan 2005 through May 2008

We developed the table using electronic invoices submitted to GSA for payment. Unusual outlays included reimbursed labor costs and tenant marketing, as discussed below.

3.3. LABOR

Although TCMA labor associated with marketing is unambiguously made part of the fixed-price portion of the base contract, TCMA submitted and GSA approved for payment costs associated with a TCMA employee identified as a marketing assistant. There is no apparent reason for GSA to permit additional compensation of this type, as GSA did not change the nature or extent of marketing already required as a deliverable under the base contract.

3.4. ARIA RESTAURANT

As developed more fully in the Restaurant section of this report, Aria Restaurant, an ITC tenant, is owned and operated by the same individuals who comprise TCMA. The Aria marketing expenses are borne by GSA and this arrangement was not included in the terms of the licensing agreement. The effects of this arrangement were that an

unauthorized rent concession accrued to Aria/TCMA, and the viability of the restaurant as a going concern is artificially bolstered.

3.5. MOBILE PERFORMANCE STAGE

In September 2001, TCMA was authorized to purchase a mobile performance stage at a delivered price not to exceed \$55,730. It did so, invoicing GSA as a marketing expense line item. GSA reimbursed TCMA for the entire amount. While TCMA prepared a “schedule” of government furnished equipment (GFE), and that schedule was subject to audit, the schedule presented only aggregate data. As such, without additional inquiry, it was not possible for GSA to determine whether the stage or any specific GFE had been captured and controlled as inventory.

In March 2008, TCMA sold the stage for (PROPRIETARY INFORMATION – REDACTED) and deposited the proceeds into a TCMA account used for the ITC activities. A Ronald Reagan Building (RRB) and ITC Director stated that since TCMA revenue collection and deposits were subject to audit, he was confident that the amount was remitted, but this was not verifiable. GSA’s oversight was lacking. GSA did not screen the property for possible reutilization (as required by FAR 45-602) and did not comply with Federal Management Regulations Part 102-38 with regards to the sale of personal property, disposition of proceeds, and reporting requirements.

4. CONSTRUCTION MANAGEMENT

GSA's use of the TCMA contract to acquire construction services, which totaled \$10 million, resulted in a series of inappropriate award actions. Terms and conditions required for federal construction contracts were absent. Deliverables were unspecified. Multiple levels of cost mark-ups and fees were permitted. Further, if independent government cost estimates or other forms of price analysis were performed, these were not generally documented in the contract file. We found only limited examples of multiple quotes secured by TCMA’s general construction subcontractor, and no evidence of full and open competition. The process, to the extent documented, does not establish a basis for the determination of price reasonableness. Further, these actions received inappropriate accounting treatment. Construction projects well above the capitalization threshold were expensed as incurred rather than capitalized and depreciated as required under generally accepted accounting principles.

4.1. INAPPROPRIATE AWARD ACTIONS

The base contract did not clearly include actual construction services or construction management for the ITC, and subsequent actions to include these services did not comply with regulations and guidelines designed to protect the interests of the government. TCMA was required to provide “coordination services” relative to building construction projects:

At times, particularly after the building is completed, the Government may elect to have the tenant construction documents and buildout provided by other contractors. The TCM will provide coordination services for programming, blocking and stacking, design, construction documents, construction, construction management, inspection coordination of tenant's outside vendors such as, telephone, data, security, furniture, and move-in. Final acceptance of the space for occupancy will be by the Government. (TCMA Contract; Section (C)(6)(b), page I-C-18; emphasis added)

These coordination services were part of the fixed-price requirement; there was no contract provision for additional compensation, and there were no additional construction related services specified under the contract. TCMA’s staffing proposal included a full-time position staffed by an individual with the requisite skills and experience to satisfy this requirement. Inexplicably, GSA read this clause to exclude construction coordination services in the case of retail space, an interpretation it cited in Modification SA34 as justification to add compensation for coordination of design and construction build-out for food court tenants. In contrast, GSA also interpreted the above-cited clause to include construction management services, architectural and engineering services, and actual construction services for event space such as the atrium, although these services were outside the scope of the contract.

Many of the necessary safeguards for federal construction projects were absent as a result of awarding this work as modifications to the contract. First, the work was given to TCMA non-competitively, which has some important implications. For the work that was not within the scope of the base contract, there were potential Competition in Contracting Act violations. Also, fair and reasonable prices were not established through competition. Second, the potential for a conflict existed, since TCMA could not serve as an independent check in its capacity as GSA’s ITC manager on the work it did as construction coordinator. Third, the arrangement did not provide contractual assurances of compliance with federal construction requirements, including federal design standards, a fire and life safety program, and labor laws, since these specifications and clauses were absent from the contract modifications. Lastly, the modification language was typically vague, rarely defined a specific procurement outcome and did not specify deliverables.

An additional effect of this approach is that it interjected multiple levels of mark-up on construction work. An example from the file for Modification 58B shows TCMA contracting with a construction vendor. The vendor submitted a proposal to TCMA that delineated costs by trade, plus a general conditions (overhead) factor of (PROPRIETARY INFORMATION – REDACTED), plus a fee of (PROPRIETARY INFORMATION – REDACTED). To this, TCMA added (PROPRIETARY INFORMATION – REDACTED) G&A, plus (PROPRIETARY INFORMATION – REDACTED) profit. In addition, TCMA billed GSA directly for construction coordination as well as construction management, plus overhead, plus profit.

4.2. IMPROPER ACCOUNTING

With respect to accounting treatment, GSA's practice was to book the entire contract cost, inclusive of actual construction and related capital costs, as a lump sum administrative expense each month as billed. In accordance with generally accepted accounting principles, where the outlay represents a tenant improvement allowance, the cost should have been recorded as a reduction to rent revenue. Where the outlay represents a non-leasehold capital improvement, the cost should have been capitalized. Further, some of the modifications were worded vaguely which increases the risk that some tasks might have been more accurately viewed as parts of a single procurement, possibly valued above the dollar threshold that requires advance congressional authorization.

See [Appendix D](#) for a list and summary of the contract modifications relative to construction and construction management.

5. ADDITIONAL ADMINISTRATIVE POSITIONS

From June 2002 to March 2008, there were 13 separate modifications, valued in excess of \$4.5 million, to compensate TCMA for costs associated with up to 10 additional administrative positions. These modifications were not compensation for contract changes that added new services or deliverables; these were direct compensation for costs that are either not compensable under this firm, fixed-price type contract²⁶, or costs already compensated in prior modifications where new

²⁶ FAR 16.202-1: "A firm-fixed-price contract provides for a price that is not subject to any adjustment on the basis of the contractor's cost experience in performing the contract. This contract type places upon the contractor maximum risk and full responsibility for all costs and resulting profit or loss. It provides maximum incentive for the contractor to control costs and perform effectively and imposes a minimum administrative burden upon the contracting parties..."

contract requirements were actually added. In addition, these modifications improperly added G&A costs plus profit, further inflating the amounts paid.

Per the justification documents, the modifications were intended to provide TCMA compensation for additional costs of record-keeping, accounting, payroll, and management information services. These costs are usually referred to as overhead or indirect expenses and considered to be G&A, not direct cost. G&A is usually expressed as a percentage of direct costs. TCMA's original contract price proposal included a G&A rate of (PROPRIETARY INFORMATION – REDACTED) applicable to a direct labor base. Subsequently, a (PROPRIETARY INFORMATION – REDACTED) G&A rate applied to any direct costs, including subcontracting costs, was routinely proposed by TCMA and accepted by GSA, as seen throughout the contract modification file history.

A change in the G&A rate itself would not be a compensable event. However, when the Government changes a contract requirement, the contract provides for an equitable adjustment. It is through the application of the G&A rate on the additional compensable direct costs that a company is reimbursed for an increase to its G&A costs, not through an increase to the rate itself.

6. ADDITIONAL SALES POSITIONS

TCMA proposed and GSA funded in excess of \$10.6 million in contract modifications to reimburse TCMA for 12 additional sales and sales management positions related to conference center and event activities. As with the additional administrative positions discussed above, modifications to the contract granting compensation for costs associated with additional sales positions represent an overpayment²⁷. Unlike the administrative positions, these sales positions are not G&A cost components but represent a direct function for which TCMA is already compensated through the fixed-price payment under its base contract. Had GSA required TCMA to market an additional venue or more events than originally contemplated, an equitable adjustment to the contract price would be appropriate. But GSA has not added an additional requirement. Under the terms of its contract, TCMA was already bound to provide the sales staffing level necessary to fill the venue with events.

²⁷ See Note 2.

The justification documentation in the contract file, as it relates to the initial modification to add additional sales positions, Modification SC82 (April 24, 2001), seems to recognize this distinction, as it states in part that:

The TCM base contract was executed on March 9, 1996. Since that time there have been numerous modifications to the Contract base services adding additional responsibilities and tasks for the TCM and providing for additional compensation. This modification does not add an additional service but provides for additional compensation {auditor's emphasis} for extra resources provided by the TCM to perform the base Contract service of sales and sales management.

Absent an additional service requirement, there is no provision in this or any fixed-price contract for additional compensation due to a contractor's increased costs. Performance and cost risk under a fixed-price arrangement rest with the contractor²⁸.

The only payment constraint imposed by Modification SC82 was the following:

The Government will continue to provide this additional annual compensation so long as the annual sales of food, beverages, and room rentals is at least \$10,000,000 for the preceding calendar year.

In effect, the modification redefined the compensation model and transferred substantial cost risk from the vendor to the Government. Above \$10 million in sales, the Government now agreed to pay the cost of 12 additional sales positions in addition to the fixed-price. There is no such arrangement contemplated or permitted under the FAR, which discusses fixed-price and cost reimbursable type contracts in mutually exclusive terms.

In soliciting for this contract, GSA evaluated the technical competency of its offerors. TCMA cited and GSA accepted the experience of its TCMA's employees as evidence of its ability to translate the ITC requirement into a realistic staffing plan and price proposal. The technical proposal submitted by TCMA detailed its anticipated sales staffing plan, which included a Director of Conference Exhibition and Banquet Sales with three sales representatives. Its proposal states that:

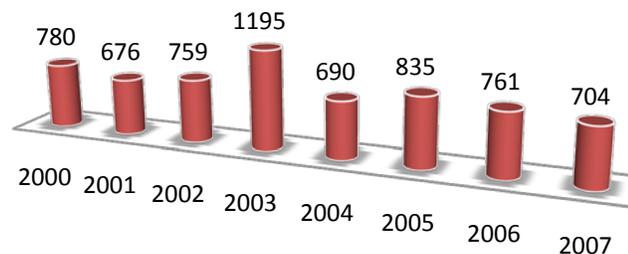
The offeror's experience at World Trade Center Boston shows that for a facility of this size to be a financial success, it will need to ultimately reach some (PROPRIETARY INFORMATION – REDACTED) customers and host

²⁸ See Note 26.

approximately (PROPRIETARY INFORMATION – REDACTED) meetings or events per week. This means that each salesperson will have to book (PROPRIETARY INFORMATION – REDACTED) events annually.

That totals (PROPRIETARY INFORMATION – REDACTED) events per year, which the proposal clearly contemplates accomplishing with a sales staff of (PROPRIETARY INFORMATION – REDACTED) ((PROPRIETARY INFORMATION – REDACTED) events each). Whether or not that was a reasonable and realistic assumption is another matter, but it is clearly the assumption stated by TCMA and accepted by GSA. There were no additional requirements that would have added to this maximum figure of (PROPRIETARY INFORMATION – REDACTED) events annually. By comparison, and as seen below, the actual number of events to date has ranged between 600 and 1,200 per year with an average of 800.

Event Count



As the chart indicates, only one contract year reached the number of events estimated in TCMA's proposal, which presented a range of (PROPRIETARY INFORMATION – REDACTED) events per year. TCMA may indeed have needed more than the (PROPRIETARY INFORMATION – REDACTED) sales people proposed, but this was not due to a change in the requirement. As such, its additional costs, \$10.6 million, were not properly compensable.

7. RESTAURANT

Operation of the Aria restaurant presents an inherent conflict of interest with TCMA's primary role as trade center manager. The terms of agreement are extraordinary in their transfer of costs and risk to the Government. Our review of the file, and discussion with GSA management, indicated that the restaurant was viewed as an essential element of the ITC retail tenant mix, and that GSA was willing to accept less than favorable terms to avoid the negative impression of an extended vacancy. In our view, this explanation did not justify the situation.

By way of brief background, the TCMA base contract specified that a full service dining operation was contemplated for the ITC and the trade center manager would be responsible for securing tenants. To date, there have been three restaurants at the same location. The first, Palomino Euro Bistro, was licensed for 10 years plus three 5-year options to RUI One Corp on December 9, 1998. However, after 27 months, it gave termination notice. The contract was amended to shift certain responsibilities and expenses to GSA through TCMA who managed the transition/termination, earning a fee of (PROPRIETARY INFORMATION – REDACTED) per month. On September 12, 2001, TCMA executed a new license for 10 years plus two 5-year options with Jump Higher, Washington DC, LLC, to house a new restaurant, Jordan's. In May 2003, Jump Higher gave termination notice, but agreed to continue operations under amended terms that again shifted certain responsibilities and expenses to GSA through TCMA, which again managed the transition/termination. Under these terms, TCMA earned (PROPRIETARY INFORMATION – REDACTED) per month plus reimbursement for the cost of a restaurant manager and bookkeeper. On June 3, 2004, TCMA executed a license agreement with Aria Management, LLC for the current restaurant, Aria, again with a 10-year fixed term plus two 5-year options - an agreement that remains in effect to date.

7.1. CONFLICT OF INTEREST

Aria Management, LLC, is a TCMA affiliate. The entities share identical ownership and common management. The dual roles given to TCMA, wherein it functions as both GSA's ITC manager and ITC restaurant owner, create an inherent conflict of interest. As GSA's ITC manager, TCMA is responsible for evaluating the tenant mix and space use to help achieve the goals of promoting international trade while also striving to maximize GSA's return on investment. As a profit driven business, Aria/TCMA would logically look to earn the maximum return with the least risk to itself. The party that GSA has entrusted with protecting the government's interest has a financial incentive to transfer costs and risks normally borne by the tenant to GSA. That is in fact what occurred.

7.2. PREFERENTIAL TERMS

Aria/TCMA is granted extraordinarily preferential terms, terms not found in the agreements covering the two previous restaurant operators. Aria is charged no fixed rent, only a percentage of gross sales with no minimum revenue requirement. Unlike the other retail tenants, Aria pays no utility costs and no common area maintenance fee. Further, during the term of the Aria license, the restaurant space

was renovated to provide new kitchen equipment, furniture and artwork as a non-competitive modification to the TCMA contract²⁹ at the Government's expense. Modification PC126 authorized \$2,044,416, including (PROPRIETARY INFORMATION – REDACTED) G&A and (PROPRIETARY INFORMATION – REDACTED) profit to TCMA. Similar inappropriate, non-competitive procurement actions were a common practice under this contract. Additional subsidies include reimbursement for the cost of employing an accountant/bookkeeper, and reimbursement for all Aria marketing expenses, which were covered as reimbursable costs under TCMA's contract. No other tenant received such consideration.

One consequence of this arrangement is that GSA did not know how much rent revenue it received from the tenant, Aria. As GSA's trade center manager, TCMA was charged with ensuring that GSA was receiving a fair market rent, and that the utilization of space helped optimize its return on investment. However, under the terms of the Aria license agreement, the restaurant revenue is pooled with the TCMA catering revenue and remitted as a combined total under the catering remittance schedule. TCMA did not separate restaurant revenue from other TCMA catering revenue in arriving at the total "percentage rent" it owes GSA and GSA did not require them to differentiate.

8. TCMA OCCUPANCY OF INTERNATIONAL TRADE CENTER SPACE

GSA's lack of oversight and enforcement of contract terms permitted TCMA to occupy, at no cost, substantially more ITC space than provided for under the contract. GSA also permitted TCMA partners and subcontractors to occupy space free of rent. GSA's failure to enforce, in effect, changed the terms of the contract, granting TCMA a valuable concession in exchange for nothing at all, an action not permitted under a government contract. We estimated the value of unauthorized occupancy at about \$651,398 per year.

TCMA exceeded its occupancy limit of space authorized in the contract by about 15,170 rentable square feet (RSF) valued at approximately \$651,398³⁰ annually. Projected over 10 years since contract award, this space could have potentially yielded revenue valued at close to \$6.5 million. The contract authorizes TCMA to

²⁹ The issue is discussed in depth under the Construction Management section of this report.

³⁰ Calculation based on the average rent rate for ITC office tenants during fiscal year 2008.

locate its staff within the ITC not to exceed about 3,000 RSF³¹ at no cost to the contractor. Space measurements taken in accordance with the standards approved by the American National Standards Institute, Inc., and Building Owners and Managers Association International (ANSI/BOMA) showed that TCMA occupies 18,170 RSF.

There were no modifications or formal correspondence authorizing the contractor to exceed the prescribed allotted space. Leasing strategies prescribed in the Leasing Plan section of the contract establishes a goal to have the ITC space 100% leased with the exception of TCMA's allotted space. Although the RRB/ITC Director and ITC Director were knowledgeable of and responsible for TCMA's occupancy of ITC space, no action has been taken to correct the issue. The following are two examples of how TCMA exceeded its allowable space allotment. We found no formal license or rental agreement in these arrangements to compensate GSA for use of this space.

- TCMA had a joint venture with Washington Link, an event planning and management company. TCMA's partner in this arrangement specialized in event planning, convention activities, conference planning, corporate events, fund-raising support services, and event facilities management, with a client list of associations and corporations across the United States. The office space used for their operations, 2,423 RSF, equates to a rental value of \$104,044 per year based on the average office rental space rate in the building.
- TCMA's subcontractors for audio/visual and conference/event services were housed, at the time of our review, in 2,122 and 758 RSF, respectively, in the ITC.

An additional consideration is liability insurance; without an executed lease, there is no apparent requirement for the tenant to carry commercial general liability insurance, as would be required of all other retail and commercial tenants housed in the ITC. The insurance would protect the landlord, in this case GSA, from claims for bodily injury or death, property damage or destruction.

³¹ The base contract prescribed 2,000 occupiable square feet (OSF) whereby we applied a 1.5 rentable/usable factor. The follow-on contract increased the amount of space provided TCMA.

9. CONTRACT OVERSIGHT

The fiscal operations of the ITC also lacked oversight. Contract provisions designed to provide some insight into TCMA operations were either not enforced or absent. Further, arbitrary accounting treatment of ITC expenses caused the Federal Office Building component of the complex to absorb costs, thereby supplementing the operations of the ITC. These issues are discussed in more detail below.

9.1. AUDITS

A primary source missing from the oversight equation was the audited financial statements for TCMA. The base contract called for an annual audit of the contractor's "books and records" at TCMA's expense. A reasonable interpretation would be that TCMA was to provide audited annual financial statements sufficient to demonstrate compliance with relevant contract requirements. The requirement was never enforced.

Instead, starting in fiscal year 2001 (FY01), the contract was modified to fund limited scope audits, with "breadth and extent of the desired audit" to be defined by GSA. The areas agreed upon were the following:

1. Schedules of Conference Center Event Rates and Revenues and Monies remitted to the Government under Contract;
2. Schedule of Parking Revenues and the Commissions Earned by TCMA;
3. Schedule of Furniture and Support Equipment Used in Connection with the Contract; and
4. Schedules of Individuals Employed and Compensated by TCMA and Aria.

For these audited schedules, which provide only limited assurances and no insight into TCMA operational results, the contract value was increased by \$785,900. In return, GSA received appreciably less than what was already required under the base contract. Further, it does not appear that GSA used these reports. For example, we observed audit cover letters that frequently made reference to a *management letter*, a vehicle for communicating internal control related matters. It is cited by the external auditor as an integral part of the audit to be read in conjunction with the report. GSA claimed not to have, nor to have been entitled to receive, these letters. The letters cited recurring control deficiencies, unaddressed by TCMA. GSA should have insisted not only that TCMA provide the management letters, a component of the audit work for which GSA paid, but also that TCMA take the recommended corrective actions, considering the high dollar value, and substantially cost-reimbursable nature, of the contract.

9.2. PROGRAM PERFORMANCE MEASUREMENT

As it relates to the contract, GSA did not collect nor require the contractor to report on matters relevant to program success. For example, GSA did not possess statistics relative to room utilization rates for events, nature of events, or average room rental rate. It did not require that TCMA differentiate its percentage rent, which includes both catering revenue and restaurant revenue. It did not evaluate rent earned in aggregate for its retail and office space. It had no established measure of overall productivity. It did not utilize an accounting system to allocate contract outlays by expense category. Finally, GSA neither measured nor compared results of operations to permit informed management decisions. Much of this information should have been provided by the contractor in the form of monthly deliverables.

9.3. FUNDING

GSA considers the ITC self-sufficient from a funding perspective in that the ITC operations should not be supplemented outside of the ITC budget. Its measure of solvency, however, is skewed heavily in favor of the ITC. The ITC, as an organizational unit (a budgetary/accounting entity), consists of two of the three Ronald Reagan complex buildings: **DC0515AF** (the International Trade Center, exclusive of 80,546 RSF of space occupied by Federal tenants) and **DC0516AF** (the parking garage). The Reagan complex also includes **DC0459AF** (the Federal Office Building - FOB). Nearly all of the complex expenses are booked against the FOB. In FY07, for example, there was debt service of \$46.8 million, depreciation of \$30.9 million and operations and maintenance of \$19.7 million. The ITC's share of these expenses is borne by the FOB, which operates at a net loss (\$36.7 million loss in FY07). Further, indirect costs, while "allocated" to the ITC buildings (\$4.3 million in FY07), are not counted against the ITC budget, meaning those costs are left to be absorbed by the Federal Buildings Fund. The net result is that the ITC operations are heavily subsidized by the Federal Buildings Fund.

OBSERVATIONS

The multiple procurement irregularities noted throughout this report attest to the breakdown of vital management controls. In our interviews we questioned why these conditions were allowed to evolve. Several of the major decisions affecting the contract were not supported by a documented rationale or justification. According to the contracting officers, TCMA had access to GSA management and the contracting officers perceived this access as a coercive force. Additionally, a contracting officer was for some time directly reporting to the director of the Ronald

Reagan Building and International Trade Center, which meant that the contracting officer was to approve actions generated or justified by his supervisor. According to the Ronald Reagan Building and International Trade Center staff, there was a concern that since this was a unique and highly visible property, operations should run smoothly, and modifying the contract to incorporate the additional services facilitated that.

On December 2, 2008, a new contract, with a value in excess of \$220 million, was awarded to the sole bidder, TCMA. According to the former Acting Regional Administrator, after award and as sufficient information becomes available, GSA's National Capitol Region will conduct a more complete evaluation of the contract, contractor performance, and overall business case in order to decide the future direction of the Ronald Reagan Building and International Trade Center and whether the options will be exercised.

As GSA evaluates the contract and contractor performance as well as other data to determine the best course of action, it should consider whether the ITC program mission, as envisioned in the original legislation for the facility, should be addressed as well.

CONCLUSION

This audit was primarily a review of the single complex contract that provided the International Trade Center management and nearly all related services through March 2009. We identified multiple procurement irregularities and lack of oversight throughout the report. The initial decisions to expand the scope of the contract to include commercial facility management services, parking garage operations and even some construction services, all under cost reimbursable compensation arrangements, created a flawed platform with an intense administrative workload that was inherited by each succeeding contracting officer. Although this contract spanned more than a decade and involved multiple contracting officers and Ronald Reagan Building and International Trade Center directors, the situation did not improve.

In its approach to this contract, GSA ignored statutes, regulations, policies and sound business practices. Subsequently, GSA awarded another contract for up to 10 years to the incumbent without the benefit of competition and the assurance that the contract costs are fair and reasonable. GSA's oversight must improve.

RECOMMENDATIONS

We recommend that the Acting Regional Administrator:

- 1) Correct the type of contracting and oversight deficiencies identified in this report for current and future contract actions, including:
 - a. Non-compliance with all applicable Government contract laws and regulations;
 - b. Uncompensated use of space by TCMA;
 - c. Lack of meaningful performance measures for the contractor;
 - d. Improper accounting treatment for assets including allocation of expenses and capitalization;
 - e. Lack of effective acquisition planning for any contract modifications and awards.
- 2) Address the inherent conflict of interest that results from TCMA as both trade center manager and owner/manager of the Aria restaurant.
- 3) Evaluate and perform analyses of the contract to determine the best course of action to ensure GSA is obtaining fair and reasonable pricing, as envisioned at the time of the award of the second contract, before awarding additional extensions/option years. Included in this evaluation would be a review of the International Trade Center mission as it affects the stewardship of the asset.
- 4) Establish and support an independent line of authority for the contracting officer and ensure transparency in the management of the contact.

MANAGEMENT CONTROLS

Management controls over administering this contract need strengthening. We tested controls over reporting, separation of duties, and management oversight. Results showed that these specific controls could be improved to allow for enhanced input to the acquisition planning process. Specifically, we evaluated various management controls over commercial facility management, parking garage management and operations, marketing, construction management, additional administrative and sales positions, the restaurant, and TCMA occupancy of International Trade Center space. The related control issues are discussed in the context of our results and findings. The application of the audit recommendations should address the issues within the management structure of the International Trade Center program.

MANAGEMENT COMMENTS

The National Capital Region's (NCR) Acting Regional Administrator and the Public Buildings Service (PBS) Regional Commissioner have provided comments to this report and they are included in their entirety as Appendix A. In its response, NCR primarily focused its discussion on programmatic issues and the new contract awarded to the incumbent, TCMA, for a Trade Center Manager of the International Trade Center (ITC) at the Ronald Reagan Building. They summarize several reasons for modifying the previous TCMA contract. NCR's discussion begins with the transfer of this unique asset from the Pennsylvania Avenue Development Corporation to GSA and the accompanying goal that its "statutory vision", both physically and financially, must be made to succeed. Based on that goal, NCR's response repeatedly concludes that all managements' contract actions were sound business decisions. With regard to those contract actions, NCR contends that its modifications to the previous TCMA contract were appropriate in order to achieve quality level building services, create a visual attraction, and maintain revenue and programmatic operations growth. NCR also contends that the audit report's findings have been addressed in the new contract to TCMA.

AUDITOR RESPONSE

The comments provided by the NCR Acting Regional Administrator and PBS Regional Commissioner warrant a response that is included as Appendix B. The Region's comments misdirect the reader when they focus on the facility's performance resulting from its business decisions rather than discuss the legality and cost to taxpayers of those decisions. To illustrate, we identified a conflict of interest in the dual roles of TCMA as both GSA's ITC restaurant owner, Aria, and as GSA's ITC manager, responsible for negotiating the license with the restaurant. In its response, NCR explained that GSA hired an outside attorney to negotiate the license in order to mitigate any conflict. As support, NCR provided a letter between a law firm and TCMA, not GSA. The letter contradicts the point that NCR was making since the letter clearly identifies that the law firm represents TCMA and that no attorney/client relationship exists with GSA. As another example, the comments cite a "sole source justification" to explain the rationale for adding the commercial facilities management services and parking garage operations to the contract. While the comments note that the justification was attached to a specific modification in

the contracting officer representative's file, they fail to note that the justification did not comport with FAR requirements and that it was not signed.

We did not evaluate the new contract or the performance of the facility as those issues were outside the scope of this review. Instead, we identified and stressed numerous and substantial procurement irregularities in the administration of the previous TCMA contract. We also identified areas where improved information would allow for contract performance measurement. The OIG positions stated in the audit report remain unchanged.

APPENDIX A

APPENDIX A – MANAGEMENT COMMENTS



GSA National Capital Region

MAR 22 2010

MEMORANDUM FOR BARBARA E. BOULDIN
REGIONAL INSPECTOR GENERAL FOR AUDITING
WASHINGTON FIELD OFFICE (JA-W)

FROM: SHARON J. BANKS *Sharon J. Banks*
ACTING REGIONAL ADMINISTRATOR
NATIONAL CAPITAL REGION (WA)

BART BUSH *BB*
REGIONAL COMMISSIONER
PUBLIC BUILDINGS SERVICE (WP)

SUBJECT: Response to Draft Audit Report: International Trade Center at
the Ronald Reagan Building

We appreciate the opportunity to review the Office of Inspector General (OIG) Draft Report, entitled "Audit of GSA's Acquisition of Services for the International Trade Center at the Ronald Reagan Building Report Number A080106/P/W/XXXXXX (the "Audit Report")," dated February 18, 2010.

For the reasons set forth in this memorandum, we believe that the Audit Report fails to fully appreciate the statutory framework and the statutory vision under which the International Trade Center (ITC) was created and fails to take into account business perspectives and management decisions made to ensure that the ITC is managed in a way that will ensure its success as measured by all five planning goals developed jointly by the GSA and the Pennsylvania Avenue Development Corporation ("PADC") :

(1) facilitate and support a Federal Trade Program to enhance the exchange of American goods and services in the international marketplace; (2) enhance the vitality of Pennsylvania Avenue and its environs; (3) create a pedestrian link between the National Mall and the central business district; (4) create a facility that provides visual testimony to the dignity, enterprise, vigor and stability of the American government; and (5) maximize the financial return on the Government's investment to support the Center's activities. Indicators of the phenomenal success of the ITC include a number of awards that are not fully captured in the Audit Report.

The Audit Report summarizes the Federal Triangle Development Act, Public Law 100-113, dated August 21, 1987, and the expectation that GSA, the Pennsylvania Avenue Development Corporation (PADC), and the International Cultural and Trade Center Commission (Commission) would jointly develop, maintain, and use the ITC. See Audit

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Report, p. 1. It notes, too, that the joint effort did not come to fruition. See Audit Report, p. 2. However, it inadequately captures the unenviable position GSA was placed in when this unique property earlier described by Sen. Daniel Patrick Moynihan as a "parking lot of surpassing ugliness"¹ became the sole responsibility of GSA.

In January 1992, the government determined that the proposed cultural trade center would not be economically viable and eliminated it from the project, resulting in a partial project redesign. After the cultural trade center was eliminated, the Commission did not receive funding and became dormant in March 1992. There remained continuing controversies during this time regarding the planned federal tenancy for the building, as well as the planned elimination of the cultural trade center. A final housing plan for the project was approved in December 1993. Under the housing plan, the major federal agency occupants for the building were the U.S. Customs Service, the Environmental Protection Agency, the Agency for International Development, and the Woodrow Wilson Center. The housing plan also proposed the reallocation of 500,000 square feet for an international trade center, which the plan described as having a "greater potential for marketability than that originally contemplated." In 1996, Congress passed legislation dissolving PADC and transferring many of its assets and liabilities to GSA.²

In the face of consistent and often extreme opposition, GSA was left with the sole responsibility to ensure the ITC met the statutory vision under which it was created. GSA has succeeded in creating a facility that provides visual testimony to the dignity, enterprise, vigor and stability of the American government and GSA is proud of its stewardship of this critical asset which so positively reflects on our Nation's capital.

We also believe that identified concerns have been addressed in the new contract. We take exception to the Audit Report's characterization of the new contract, including the purpose the GSA task force was created and the conclusions it reached. *Audit Report*, p. 9. The clearly stated purpose of the GSA task force was to assess whether concerns addressed in the Regional Inspector General's Alert Report No. A080106/P/W/W08001 ("Alert Report"), dated May 29, 2008, have been addressed sufficiently through solicitation number GS-11P-08-YAC-0012. *Task Force Report*, p. 1. The GSA task force determined that the new solicitation effectively addressed the concerns in the Alert Report. *Task Force Report*, p. 6.

The Alert Report did not address competition for the new contract nor should it have since GSA was in the acquisition process for this new contract when the Alert Report was issued. The GSA task force clearly stated that this was an issue beyond the scope of its review. *Task Force Report*, p. 6. While the GSA task force noted that "the limited historical data provided by GSA to the offerors, together with the substantial risks placed on offerors by the solicitation *may* result in a lack of full and open competition" [emphasis added], the GSA task force further stated that "[c]onversely, it could be argued that the entities potentially qualified to perform the services described in the solicitation would be able, based on general market data and their historical knowledge

¹ S.Rep.No. 100-139, at 7 (1987).

² Pub. L. 104-134, Title III, Gen. Provisions, Sec. 313, 110 Stat. 1321, 1321-198 (1996).

of the services to be provided, to prepare and submit an informed proposal taking into consideration the relative risks and opportunities presented by the solicitation." *Task Force Report*, p. 6. The GSA task force noted that no protests regarding the solicitation were filed prior to the closing date for receipt of proposals, "thus potentially indicating some degree of comfort within the marketplace with the terms and conditions upon which GSA has solicited these services." *Task Force Report*, p. 6.

Contrary to the suggestion in the Audit Report that the new contract was awarded to TCMA after an unsuccessful attempt to compete a new contract, the new contract was awarded under full and open competition. See Audit Report, p. 2. The agency made a good faith effort to obtain competition by publicizing the requirement, mailing solicitations to potential offerors and conducting a pre-proposal conference. Therefore, GSA obtained full and open competition under the Competition in Contracting Act of 1984 (CICA), even if only one proposal was received in response to the solicitation.

The GSA task force concluded that the new solicitation effectively addressed the Alert Report concerns. *Task Force Report*, p. 6. With the concurrence of the Senior Procurement Advisor, GSA appropriately proceeded to award of the new contract on December 2, 2008.

I. RESPONSE TO DRAFT AUDIT REPORT RESULTS

A. COMMERCIAL FACILITIES MANAGEMENT SERVICES

The Audit Report concludes that the addition of commercial facility management (CFM) services greatly and improperly expanded TCMA's contractual scope of work. The Audit Report maintains that this action was highly favorable to TCMA, and contrary to the Federal Acquisition Regulation (FAR), was non-competitive and cost-based.

CFM services were not excluded from the original contract for the specific purpose of having them competed separately. Rather, CFM services were not addressed at the time of the RFP because the most effective manner for executing the program was still being developed and the building itself was still under construction for another three years. GSA recognized that business decisions would be made after the developmental period to address additional requirements when the need arose.

The addition of CFM services was appropriately made as a sole source selection to Trade Center Management Associates' (TCMA) because TCMA was already assisting in the development of the center programs and operations for the government, and was responsible for providing a venue for trade tenants, retail services, and conference center spaces that would enhance business and trade activity at the complex. Attracting clients to the trade center and conference center event performance are interdependent with the cleaning requirements in these spaces. If an incident occurred during an event, TCMA needed to have the ability and be immediately responsible for meeting client needs during setup, take down, and cleaning calls. In order for TCMA to manage space effectively, they likewise needed the ability to control cleaning in tenant spaces in order to be held responsible for total customer service, the highest quality

standard event service, and expedient event setup, takedown, and cleaning. TCMA was required to provide services for GSA's operation, different in nature and level than other buildings and this award was made to enhance quality and efficiency of the overall operation of the trade center and to be responsive to visitors and tenants.

The decision to add CFM services to the contract was a sound business decision, properly made after review of the legislative goals, TCMA's contract requirements, and the best interest of the government. Rationale included in a sole source justification³ was:

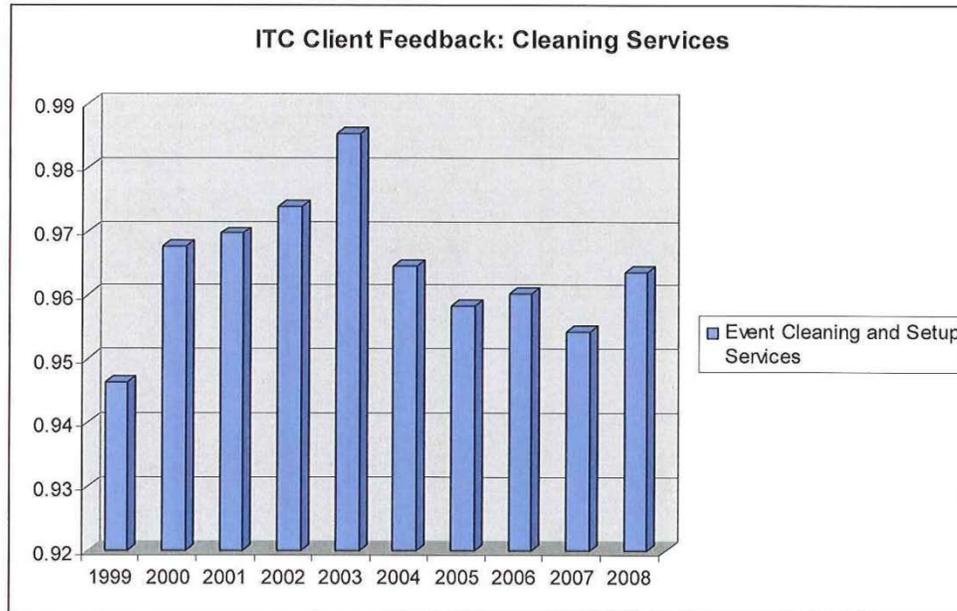
TCMA must have close control over services and costs to serve the unique mix of visitors and customers to maintain the viability of the center. The TCM must ensure customer satisfaction and sanitary conditions due to the extensive food service and large groups anticipated for seminars, conventions and visitors which it is expected to attract.

Contract Modification PC07, dated July 18, 1996.⁴

The effectiveness of this arrangement and the quality level of cleaning achieved is apparent when reviewing the conference center event questionnaires collected over the past decade. A total of 1,367 Client Surveys were collected from event holders. When asked three CFM-related questions that impact the ITC conference center events, including whether their event was "set up properly," "set up on time," and "clean and working" a total of 97% responded "yes". These superior ratings support the decision that TCMA should control CFM services that impact all of conference center event and associated areas in the building. TCMA was motivated to ensure all interior and exterior public facing elements were cleaned on a responsive basis because any limitations in the CFM services would negatively impact leasing and conference center business. A separate contractor would not have this same motivation to ensure responsive and high quality performance.

³ The Sole Source Justification attached to Modification PC07, maintained by the Contracting Officer's Representative, recognizes that this modification is outside the scope of the original contract and presents a basis for the sole source award. See Attachment 1.

⁴ See also Modification SA17, dated June 30, 1997, which supplements PC07, by providing further definition of responsibilities and the fee structure for these additional services; Modification SA45, dated October 20, 1998, which extended the start-up period to track expenses for a base-line before a fixed fee pricing structure was to take effect due to delay in building opening until May 1998; Modification 60, dated October 28, 1999, which established a fixed fee method of payment for the vast majority of services.



B. PARKING

The Audit Report concludes that a GSA decision that modified the TCMA contract to incorporate parking garage management and operations resulted in an excessive and unwarranted compensation arrangement, inappropriate risk assumption, unnecessary incurrence of taxes, penalties and interest, and improper payment of overhead on those taxes, penalties and interest. The Audit Report further states that these are "costs that would have been avoided in their entirety had the facility been government operated." See Audit Report, pp. 17-18.

Parking management services were not excluded for the specific purpose of having them competed separately. They were not addressed at the time of the RFP because construction was not complete and the program was still being developed. It was recognized that business decisions would be made after the developmental period to address additional requirements when the need arose.

Similar to the CFM work performed by TCMA, it was essential that parking services were included under the TCMA contract because event, tenant and visitor management had to coordinate with the parking operation to achieve expected quality standards for each activity and to coordinate with the U.S. Secret Service for high profile participants at events. The Garage operation had to be prepared for increased fluctuations caused by the conference center and customer service provided to event attendees included valet parking for guests arriving throughout the day. It was important that these

services be provided at a class A level when guests entered and exited the space for their events.

The decision to add parking garage management services to the contract was a business decision, properly made after review of the legislative goals, TCMA's contract requirements, and the best interest of the government. Rationale in a sole source justification⁵ included:

The TCM has a contractual obligation to promote utilization of the parking garage at night and on weekends to enhance the government's return on its investments and support the center's programs. The availability and the condition of the parking areas is a critical factor in the success of the ITC in attracting the public to participate in the many activities at the Center.

Contract Modification PC07, signed July 18, 1996.

Whereas GSA would typically lease out the garage, collecting a marginal fee while the operator assumed certain risk and received all revenue, GSA decided to set up a fee structure through which TCMA operated the garage and GSA collected the revenue from this operation. GSA benefited from the efficiency achieved by TCMA and the revenue generated by the parking component of the contract.

GSA rightly determined that it was not in the best position to operate the largest underground parking garage with public access in Washington, DC. It was also necessary for GSA to require TCMA to carry private insurance coverage for the garage because it was not in the best interest of the government to self-insure for alleged negligence for garage related incidents, including damage to vehicles from bollard malfunction, slipping and falling accidents and other accidents that can occur in a large parking garage. TCMA was required to carry garage liability insurance for bodily injury and property damage with a limit of at least \$1M, Garage Keepers' liability insurance with a limit of at least \$1M, and umbrella excess liability coverage with a limit of at least \$5M. See Modification SA15, dated March 7, 1997.

While the Audit Report concluded that the modification to include parking garage management and operations "resulted in an excessive and unwarranted compensation arrangement", it does not support this conclusion with any analysis of the industry standard for similar parking garage operations in a facility similar to the ITC. The demands and the expectations for this garage are not standard. As noted, the availability and condition of the parking areas directly impacts the success of the ITC

⁵ The Sole Source Justification attached to Modification PC07, maintained by the Contracting Officer's Representative, recognizes that this modification is outside the scope of the original contract and presents a basis for the sole source award. See Attachment 1. See also Modification SA15, dated March 7, 1997, which supplements PC07, by providing further definition of responsibilities and the fee structure for these additional services.

activities, tenant satisfaction, and revenue. By all of these measures, the success of the ITC is considerable and the quality and responsiveness of its operation has won acclaim from both government and private sectors. For these same reasons, we also take exception to the Audit Report's assessment that the contract structure for these parking services was not suitable.

The Audit Report maintains that accounting for results of operations was missing without presenting any facts to support this conclusory statement. Audits of parking operations were conducted annually by an independent CPA firm.

Regarding the District's later enforcement of D.C. Code § 47-2002, which provides for the taxation of gross sales of vendors of tangible personal property and services, GSA's position at the time of the modification was that the District did not have authority, directly or indirectly, to tax the federal government. GSA believed that the parking revenue was not subject to local taxation because it was deposited directly into a U.S. Treasury account and so did not direct TCMA to collect the tax. The Audit Report is misguided in its presentation that there was legal clarity regarding whether this tax should be collected. DC initially taxed all revenue including intergovernmental transfers. This portion of the tax was challenged, GSA prevailed, and a portion of the imposed tax was removed. The Audit Report likewise demonstrates a complete lack of understanding regarding the decision-making process in delaying payment of this tax and acknowledges that the scope of the audit did not include review of the reasons for delay. The tax on the general public parkers has been collected from the parking patrons since May 2007 when GSA directed TCMA to begin collecting and remitting the tax.

C. MARKETING EXPENSES

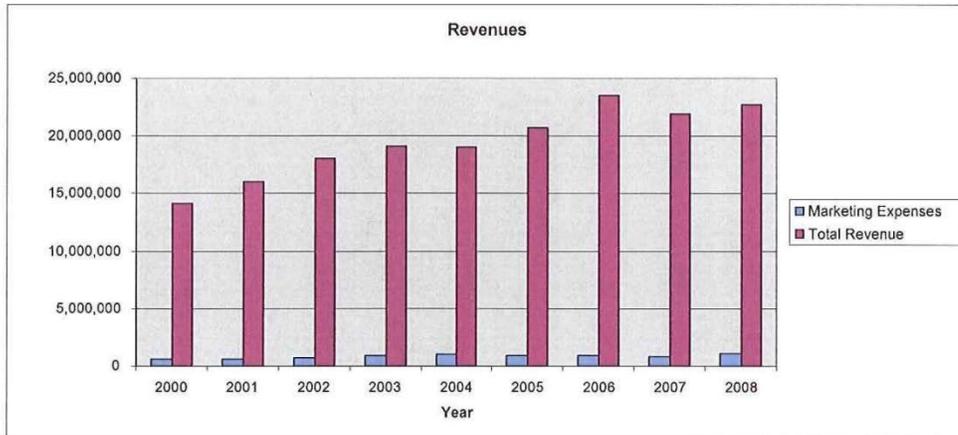
The Audit Report concludes that the contractual compensation arrangement as it relates to marketing expenses inappropriately shifted all cost and performance risk to the government.

As the program operations grew and several GSA-directed public marketing programs within the ITC were created, this budget grew. New programs such as the building's fitness center operation and LIVE! on Woodrow Wilson Plaza series of summer concerts required signage and directory visuals and GSA instructed TCMA to market these programs and to make them successful. While these events may or may not have directly created revenue, nonetheless, GSA decided that they were an important addition to meet an element of the legislative mandate for this building: to enliven Pennsylvania Avenue and its Environs as well as bring tourism to D.C.'s downtown business district. The food court tourism program, Doc Scantlin concert performances, capitol steps shows, and visitor packets and brochures are some examples of marketing expenses intended to activate the facility. These activities have been formally recognized by the DC Mayor, among others, and have been a major contributor to the program's success. These events also brought attention to the building with its attractive conference space options and expansive food court, revenue from which benefits GSA.

RONALD REAGAN BUILDING AND INTERNATIONAL TRADE CENTER
AWARDS AND RECOGNITION

| <u>AWARD</u> | <u>SPONSORING ORGANIZATION</u> | <u>YEAR</u> |
|---|--|--|
| "Certificate of Merit for Excellence in Construction" presented to GSA for the Ronald Reagan Building and International Trade Center | The Associated Builders and Contractors, Inc. (ABC) of Metropolitan Washington and Virginia Chapters | 1997, 1998 |
| "Silver Anvil Award" presented to GSA, Hill and Knowlton, Inc., and TCMA for excellence in Special Events and Observances: Government | Public Relations Society of America (PRSA) | 1999 |
| "Thoth Award" Honoring Excellence in Public Relations | Public Relations Society of America (PRSA) National Capital Chapter | 1999 |
| "Special Jury Award" | Meeting Professionals International (MPI) | 1999 |
| "Grand TOBY Winner" In Government Building Category and Grand Winner | Apartment and Office Building Association of Metropolitan Washington (AOBA) | 1999-2000 |
| "Office Building of the Year" In the Government Building Category | Apartment and Office Building Association of Metropolitan Washington (AOBA) | 1999-2000 |
| "Office Building of the Year" In the Government Building Category | Building Owners and Managers Association International (BOMA) | 2000-2001 |
| "Inner Circle Award" for Meetings and Groups | Association Meetings Magazine chosen by readers for Convention Center Excellence | 2002, 2003, 2004, 2005, 2006, 2007, 2008 |
| "Downtown DC Momentum Award" for activating public space | Downtown Business Improvement District | 2003 |
| "Addy" Citation of Excellence for Collateral | The Ad Club of Metropolitan Washington | 2005 |
| "Best Food Court" In Washington DC | Frommer's Travel Guides | 2006, 2007 |

Increasing marketing expenses, commensurate with the growth in the number and quantity of the program operations and consistent with the legislative goals, TCMA's contract requirements, and the best interest of the government, was a sound business decision.



Marketing expenses have been effectively managed by GSA over the course of the TCM contract. Marketing expense has averaged 4.2% of the program's annual revenue, evidencing a steady, strategic approach to the business where the budget has been programmed to concentrate the government's investment over time. The management of these annual expenditures has remained steady as revenue has steadily increased.

We disagree with the statement that the contract established no measurable performance goal or cost constraint relative to marketing and promotion. See Audit Report, p. 21. Marketing expenses were budgeted, approved or disapproved, and only reimbursed with proper documentation of payment. Any savings based on advertising frequency accrued to GSA. Again, the key performance measurement is the programmatic success in creating a facility that provides visual testimony to the dignity, enterprise, vigor and stability of the American government.

D. CONSTRUCTION SERVICES

The Audit Report concludes that GSA's use of the TCMA contract to acquire construction services resulted in a series of non-competitive award actions, some of which were outside the scope of the contract. Deliverables were unspecified. Terms and conditions required for federal construction contracts were absent and multiple levels of cost mark-ups and fees were permitted.

TCMA provided services including assisting in the selection and administration of contracts for the Government's architect, structural, mechanical, and electrical engineers and other additional consultants who were necessary to develop the ITC construction projects. For example, on November 3, 1997, TCMA was tasked with developing construction requirements, preparing bid documents, and soliciting competitive bids for construction based upon completed bid documents to assist GSA in completing the construction of the ITC's north office tower. See Modification SA25. TCMA was a preferred vendor to provide construction management services, ensuring these projects were coordinated around tenanted spaces and conference center events. For each project, GSA required that at least three bids were received. GSA reviewed and approved all solicitation documents, cost estimates, construction drawings, and approved the final selection decisions. Each phase of construction was inspected by GSA personnel.

The construction bidding process was augmented prior to the award of the new contract. The process was amended by the GSA to provide for more front-end GSA involvement, input and approvals. Under the revised process, GSA prepares the Independent Government Cost Estimate (IGCE) for each job and continues to either provide the scope of work, or if TCMA is to provide a recommended scope of work, GSA approves the scope of work prior to any Request for Proposal (RFP) being prepared for prospective offerors. Contractors (three to five) that can provide the required services are sent the RFP. TCMA reviews all proposals received and submits them to GSA, with comments and a copy of the IGCE and the approved scope of work. GSA performs the price reasonableness determination and makes the award.

Upon award of a construction contract, Certificates of Insurance and Bonds, if required, are obtained from the contractor. Prior to the start of construction, a pre-construction meeting is held with the contractor, GSA inspector, and TCMA. GSA inspects and accepts all work performed.

Regarding the concern that "construction projects well above the capitalization threshold were expensed as incurred rather than being capitalized and depreciated as required by generally accepted accounting principles," changes were made in fiscal year 2009 for all new obligations. See Audit Report, p. 23. Construction awards are established in IRIS and funded under BA54. Construction projects that meet the capitalization criteria are being capitalized.

E. ADMINISTRATIVE POSITIONS

The Audit Report concludes that there were 13 modifications since June 2002 to compensate TCMA for costs up to 10 additional administrative positions. Administrative positions are typically included in contractual and administrative (G&A) rates and should not have been reimbursed separately.

GSA was in the fortunate position of being able to add administrative positions to help manage the success of the ITC. Had the vision of this building not materialized, there would have been no need to expand the administrative staffing. Adding these positions

was a sound business decision, completely justified by the unexpected volume of business due to its successful operation.

These positions provided administrative services directly beneficial to the Government. The added positions included controller, accountant, financial administrative assistant, payroll clerk and management information services (MIS) director. These positions were responsible for record keeping, accounting, payroll and management information services functions of the contract. These personnel handled the markedly increased program activity and revenue generation experienced by the ITC program over the course of time. In terms of accounting alone, the number of checks processed annually by this group grew from 400 the first year to 3,400 in 2002 and this revenue benefitted GSA.

The government reviewed certified salary, bonus, and benefits cost to TCMA before any additions were made; GSA directed an independent outside accounting firm to audit these positions each year as part of the salaries audit and provide the results to the Government. GSA also imposed additional obligations on TCMA for audits and reporting since the contract award and these personnel helped directly to respond to the additional obligations.

F. SALES AND MANAGEMENT POSITIONS

The Audit Report concludes that GSA improperly reimbursed TCMA for 12 additional sales and sales management positions for work that was included in the fixed-price portion of the contract.

To help manage the success of the ITC, GSA was in the fortunate position of being able to add sales and sales management positions. The base contract provided for three sales people and one director of sales. This staff was unable to provide the necessary effort to keep up with the success of the conference center and so in 1998, 1999, and 2000, TCMA spent \$1,958,138 above the contract amount for these additional personnel. See Modification 82. Much of this was due to the fact that GSA had not previously operated a public event center and these capacities were unknown during the RFP and offer review process.

As the conference center activity increased, a Modification was issued in 2001 to provide for a significant change in the resources required. Compensation for additional sales personnel was contingent each year upon specified sales volume reached by the contractor (evidencing activity and benefit to the government via revenue generated). This compensation to TCMA for additional sales employees was made based upon gross sales revenue and \$10M was used as the base requirement for such compensation. TCMA bore these expenses during the year the revenue was generated and upon certification of achieving this required revenue, GSA compensated TCMA the following year. If, for instance, the revenues generated were \$10,050,001, TCMA could add an additional sales person the following year if the cost of adding that person was \$50,000. If gross sales revenue fell below the \$10M gate for two consecutive years, the Government and TCMA agreed to renegotiate the staffing level. This did not occur,

further exemplifying the program's success. The GSA determined that addition of these personnel was essential to maximize the revenue to the Government. See Memo for Modification 82 and Item 14, Description of Modification 82.

The Audit Report maintains that because TCMA's proposal anticipated that a three person sales staff could accomplish sales of approximately 1500 events a year, which exceeds the average number of events at the ITC, GSA should not have provided additional compensation for sales staff. See Audit Report, p. 27. However, for the ITC, the number of events was not the best indicator of profitability or sales staff requirements due to the volume of activity taking place for each event and ancillary and other revenue trends associated with the marketplace or type of event being held. For instance, when reviewing events from September 2008, a marketing event provided over \$34,500 dollars for the government whereas a local consulting firm event provided only \$2,500 for use of the same space in the building. Also, an "event" could include a high value contract covering several days' use of the conference center and coordination with multiple high-level organizers.

Overall, revenue outperformed the event charts over this 7 year period (213% from 2000 to 2007) and is believed to be a more accurate indicator of success. Based on the revenue generated, the decision to add sales and sales management positions is amply supported and was a sound business decision.

G. ARIA RESTAURANT

The Audit Report concludes that TCMA's operation of the Aria restaurant presents an inherent conflict of interest with TCMA's primary role as trade center manager. The terms of the agreement are extraordinary in their transfer of costs and risk to the Government.

After two restaurant operations failed to complete the term of their licenses, PBS management considered all potential solutions for the best use of this space in terms of viability and achieving GSA's goal to activate the central outdoor plaza where this space is situated and provide a needed tenant amenity. See Discussion and Decision Points, February 17, 2004. GSA conducted a thorough analysis regarding the objectives for use of this space, the alternative uses of the space, the considerations, and the challenges and solutions. Additionally, the restaurant space was actively marketed seeking potential tenants. No other restaurant expressed interest in occupying this space. Before the decision was made to permit TCMA to execute a license agreement with Aria Management, LLC for the operation of Aria, a business decision was made that operation of this restaurant met the objectives for optimizing the use of this space. See Discussion and Decision Points, February 17, 2004.

If the Aria license had not been negotiated, there would not have been a restaurant in this space and GSA would have had to arrive at a different solution for less than optimal use of the space and eliminate the considerable amenity of proximate restaurant that federal and other tenants could use for business luncheons. The only other lunch

option would have been the food court and casual eateries, which cannot meet the various needs of all tenants and visitors.

GSA hired an outside real estate attorney to negotiate the license to mitigate any conflict of interest. The license requires Aria to remit a license fee based on a sliding percentage scale of 4% to 8% applied to the gross food and beverage receipts, less sales tax. To determine the gross amount of food and beverage receipts for this calculation, the revenue from the conference center is added to the revenue from Aria to reach the highest possible total revenue number which results in GSA receiving the greatest possible license percentage. See Modification 16A. From 2004 through 2009, Aria paid a license fee which averaged greater than 7 percent of its gross food and beverage receipts.

Importantly, the percentage of revenue from Aria due to GSA under the license is greater than the percentage of revenue from the other two restaurants who vacated the space – Jordans and Palomino Euro Bistro. For Jordans, the percentage of gross sales payable to GSA was 5 %. For Palomino Euro Bistro, the percentage of gross sales payable to GSA was 6%, not payable unless revenue reached \$5,327,466. Whereas, with Aria, the percentage of gross sales payable to GSA began at the \$2,000,000 revenue mark and climbed to 8% for revenues exceeding \$15,000,000. Also, for Aria, to reach each sales volume tier, all revenue from the conference center was combined. What that meant is that GSA would receive its revenue percentage at the highest possible tier for all food and beverage operations and since the revenue tier was determined based on gross revenue and not based on profit. Further, GSA would receive its revenue percentage even if Aria was not a financially successful business. In short, GSA reaped a significant financial benefit from the license with Aria and met its legislative goal to activate the central outdoor plaza of the RRB/ITC.

We disagree that the terms of the Aria license transfers the cost and risk to the government. As set forth above, Aria assumed and continues to possess considerable risk under this license. As noted, in its first year, Aria was required to pay and did pay GSA a percentage of revenue. This was an unusually favorable term for the government. Normally, it would be expected for a new restaurant to have a start-up year where these high revenue percentages would not be paid. Indeed, under the license with Palomino, for the first year, 0% of revenue was to be paid to GSA.

Now that Aria has been in operation for approximately five years, it is clear that the stated objectives have been met: integrating and cooperatively using Aria with the ITC conference center operations; stimulating and enhancing Wilson Plaza and the RRB/ITC; providing a necessary tenant amenity, and achieving greater financial success for GSA than achieved with the previous restaurants. Although difficult financially because it is isolated and not street-front property, the venue contributes to the plaza's activity and the overall appearance of this public space in the heart of the plaza.

The Audit Report notes that Aria does not pay utility costs or common area maintenance fees. That is correct; however, Aria is responsible for all repair and

maintenance of the internal space. In fact, Aria is currently spending considerable money to renovate the restaurant. This is consistent with the license terms to ensure a viable business in the space after two tenants broke their agreements before term expiration.

H. TCMA'S SPACE OCCUPANCY

The Audit Report concludes that GSA's lack of oversight and enforcement of contract terms permitted TCMA to occupy at no cost substantially more ITC space than provided for under the contract.

As existing activity grew substantially and additional requirements were added, GSA evaluated the need and provided additional space. All TCMA space was utilized exclusively for the direct performance of this contract, essential for servicing the building and operation. GSA believed it beneficial from a revenue standpoint to have TCMA staff on site to ensure a responsive, efficient operation of this flagship property. Subcontractor space was provided only for those directly servicing the building, including cleaning employees, CFM employees, direct management and parking operator employees, and direct management required to service the building on-site. This was a sound business decision, consistent with the normal practice for onsite contractors. GSA provides an adequate amount of space to on-site contractors depending upon staffing levels. The amount of space grew due to the programmatic success and the attendant increase in responsibility and operational complexity.

If this space were used to generate revenue, adequate space would not be available for TCMA to perform its contractual duties and GSA would expect to suffer a reduction in revenue. Too, the main occupied space is unmarketable due to the ceiling height. Since TCMA is not a tenant, there is no license or rental agreement for the use of this space – nor is there for any on-site contractor.

We note that the office space provided under the new contract is consistent with the space occupied. See Audit Report, footnote 31, p. 30.

I. PROGRAM MANAGEMENT

The Audit Report concludes that related program management deficiencies were also evident in that GSA: (a) did not require the contractor to report on matters relevant to program success; (b) failed to enforce existing audit rights; and (c) permitted ITC operations to be heavily subsidized by the FBF.

We find these conclusions unsupported and take exception to them. There were multiple and frequent on-going reports and meetings related to the program's success. The list of awards and recognition from numerous sources that highlight this success is extensive and impressive. The revenue steadily increased. We can see no basis upon which one could challenge the success of the ITC.

Audits were conducted. Three annual audits were conducted by independent CPA firm Vitale, Caturano & Company. GSA reviewed the independent auditor's reports to verify that revenues are appropriately collected and remitted. The audit ensures deposits are free of material misstatement. Audits are performed in accordance with GAAP standards. The internal management letter is submitted to TCMA for their internal process improvement and is available for GSA to review.

The ITC revenue cannot be used to pay the debt service. The Federal Triangle Development Act, provided, among other things, for the establishment of a separate account within the Treasury dedicated exclusively to trade center activities. See 40 U.S.C. 1107(d)(2). This separate account was to receive all rents and fees collected by the Commission and to be available to pay all expenses incurred by the Commission in carrying out its duties. The Act further specified the type of expenses the account would be available to pay. See 40 U.S.C. 1107(d)(3).

On March 31, 1992, the Commission ceased operations and became dormant. In 1996, Congress passed legislation dissolving PADC and transferring many of its assets and liabilities to GSA. GSA proceeded with the development of the trade center. Since GSA was left standing alone to ensure the success of the trade center, GSA's Fiscal Year 1996 Appropriations Act provided broad flexibility and authority in the level of support the FBF can offer to the ITC program. Also in 1996, Congress enacted legislation that dissolved the PADC and transferred many of its assets and liabilities to GSA. This legislation contained language similar to GSA's Fiscal Year 1996 Appropriations Act, granting GSA the authority:

To enter into and perform such leases, contracts, or other transactions with any agency or instrumentality of the United States, the several States, or the District of Columbia, or with any person, firm, association, or corporation as may be necessary to carry out the responsibilities of the Pennsylvania Development Corporation under the Federal Triangle Development Act.

Pub. L. 104-134, Title III, General Provisions, 313(c)(4), 110 Stat. 1321, 1321-199.

Following PADC's dissolution, additional language similar to the broad authority in this legislation was included in GSA's Fiscal Year 1997 Appropriations Act. Pub. L. 104-208, 110 Stat. 3009, 3009-335. The accompanying Conference Report stated: "[t]he intent is to provide GSA permanent authority to perform activities necessary to implement the trade center plan at the Federal Triangle." H.R. Conf. Rpt. No. 863, 104th Cong., 2nd Sess. 1996.

Due to the unique design and intent of the Ronald Reagan Complex, costs are shared between the ITC and the Federal Office Building. We acknowledge there are inconsistencies regarding the methodology for assigning some costs internal to GSA within the Ronald Reagan Building complex. We agree that the FBF covers some costs for utilities and some overhead components and the capital reinvestment to the FBF for the ITC and, conversely, that the ITC covers costs that are typically covered by the FBF

such as costs associated with federal tenants and common area use in and outside the building. Also, the revenue attributed to the ITC does not include \$61,225,743 that was deposited to the general FBF, and not the ITC's working fund, from 1998 to 2009, which included: (i) federal subsidized parking revenue of \$20,848,236 and (ii) revenue from federal office tenants in ITC space of \$40,377,506. We have begun a comprehensive review to ensure all material components are formally recognized and the allocation methodology is well documented. We also plan to develop specific financial statements that describe the full cost of the RRB and develop management reporting to highlight the source of funding for the costs. Discussions regarding the best way to assign the costs to the ITC versus FBF are ongoing.

II. RESPONSE TO DRAFT AUDIT REPORT OBSERVATIONS

The OIG makes two observations in the Audit Report. The first is that TCMA had access to GSA management which the contracting officers perceived as a coercive force. We have no information nor did the Audit Report provide us any information to support this observation. As discussed, without specific information, we cannot respond to this observation.

The other observation concerned the new contract, review of which was not included in the purpose of the Audit Report. See Audit Report, p. 1. We believe that identified concerns have been addressed in the new contract and take exception to the Audit Report's characterization of the new contract, including the purpose the GSA task force was created and the conclusions reached by this task force. See Audit Report, p. 9. The clearly stated purpose of the GSA task force was to assess whether concerns addressed in the Regional Inspector General's Alert Report No. A080106/P/W/W08001 ("Alert Report"), dated May 29, 2008, have been addressed sufficiently through solicitation number GS-11P-08-YAC-0012. *Task Force Report*, p. 1. The GSA task force determined that the new solicitation effectively addressed the concerns in the Alert Report. *Task Force Report*, p. 6.

The Alert Report did not address competition for the new contract nor should it have since GSA was in the acquisition process for this new contract when the Alert Report was issued. The GSA task force clearly stated that this was an issue beyond the scope of its review. *Task Force Report*, p. 6. Contrary to the suggestion in the Audit Report that the new contract was awarded to TCMA after an unsuccessful attempt to compete a new contract, the new contract was awarded under full and open competition. See Audit Report, p. 2. The agency made a good faith effort to obtain competition by publicizing the requirement, mailing solicitations to potential offerors and conducting a pre-proposal conference. Therefore, GSA obtained full and open competition under the Competition in Contracting Act of 1984 (CICA), even if only one proposal was received in response to the solicitation.

With the concurrence of the Senior Procurement Advisor, GSA appropriately proceeded to award of the new contract on December 2, 2008. *Audit Report*, p. 9. This action was entirely consistent with the GSA task force recommendations.

III. RESPONSE TO DRAFT AUDIT REPORT RECOMMENDATIONS

A. IDENTIFIED CONTRACTING AND OVERSIGHT DEFICIENCIES

The Audit Report recommends that GSA correct the type of contracting and oversight deficiencies identified in this report for current and future contract actions, including: (a) non-compliance with all applicable Government contract laws and regulations; (b) uncompensated use of space by TCMA; (c) lack of meaningful performance measures for the contractor; (d) improper accounting treatment for assets including allocation of expenses and capitalization; and (e) lack of effective acquisition planning for any contract modifications and awards.

Since the focus of the Recommendations is looking forward and we have already responded above with more specificity, our response will primarily focus on the new contract awarded to TCMA, GS-11P-09-ZGD-0064, on December 2, 2008.

(a) non-compliance with all applicable Government contract laws and regulations—New Contract

We complied with all applicable Government contract laws and regulations in the procurement of the new contract. NCR assembled an experienced, qualified, and dedicated team to prepare an entirely new contract structure for the replacement contract. This integrated project team represented a cross-section of NCR/PBS and included participants from procurement, finance, legal, operational, small business, and management. In addition, NCR/PBS obtained independent procurement experience from an outside consultant. Contract was awarded based on full and open competitive award.

(b) uncompensated use of space by TCMA

Under the new contract, the office space provided to TCMA is consistent with the space occupied. It is approximately the same amount of office space that they had occupied under the old contract and is needed for the efficient performance of the contract.

(c) lack of meaningful performance measures for the contractor

The performance measurement is the programmatic success of this unique facility. The revenues have steadily increased. The awards and recognition have multiplied. The ITC provides visual testimony to the dignity, enterprise, vigor and stability of the American government, consistent with the statutory framework and statutory vision under which it was created.

The new contract includes an Award Fee Plan (AFP) which will serve as the basis for the evaluation of the Contractor's performance and for presenting an assessment of that

performance to the Award Fee Determining Official (AFDO). It describes specific criteria and procedures used to assess the contractor's performance and to determine the amount of award fee earned. Actual award fee determinations and the methodology for determining award fee are unilateral decisions made solely at the discretion of the Government. Greatest performance measure is the success of the building.

(d) improper accounting treatment for assets including allocation of expenses and capitalization

Due to the unique design and intent of the Ronald Reagan Complex, costs are shared between the ITC and the Federal Office Building. We acknowledge there are inconsistencies regarding the methodology for assigning some costs within the Ronald Reagan Building complex. We agree that the FBF covers some costs for utilities and some overhead components and the capital reinvestment to the FBF for the ITC and, conversely, that the ITC covers costs that are typically covered by the FBF. We have begun a more comprehensive review to ensure all material components are formally recognized and the allocation methodology is well documented. In addition, we plan to develop specific financial statements that describe the full cost of the RRB and develop management reporting to highlight the source of funding for the costs. Discussions regarding the best way to assign the costs to the ITC versus FBF are ongoing.

(e) lack of effective acquisition planning for any contract modifications and awards.

The Federal Acquisition Regulation (FAR) Part 7 implements the statutory requirement for acquisition planning. While FAR section 7.102 requires planning on all acquisitions, *written* acquisition plans are not required for all acquisitions. See GSA Directive OGP 2800.1, Acquisition Planning, dated January 1, 2004.

Within the past year, GSA NCR has conducted Acquisition Planning training to ensure that all associates are aware that all acquisitions, regardless of dollar value, require acquisition planning and that all acquisitions over the SAT must have a written acquisition plan before a solicitation is issued, unless an exception exists.

B. ARIA RESTAURANT

The Audit Report recommends that GSA address the inherent conflict of interest that results from TCMA as both trade center manager and owner/manager of the Aria restaurant.

As presented more fully above, before the decision was made to permit TCMA to execute a license agreement with Aria Management, LLC, for the operation of Aria, a thorough analysis was conducted regarding the objectives for use of this space, the alternative uses of the space, the considerations, and the challenges and solutions. A business decision was made that operation of this restaurant met the objectives for optimizing the use of this space. Now that Aria has been in operation for approximately five years, it is clear that the stated objectives have been met: integrating and

cooperatively using Aria with the ITC conference center operations, stimulating and enhancing Wilson Plaza and the RRB/ITC, and achieving greater financial success for GSA than achieved with the previous restaurants.

C. FAIR AND REASONABLE PRICING IN NEW CONTRACT

The Audit Report recommends that GSA evaluate and perform analyses of the contract to determine the best course of action to ensure GSA is obtaining fair and reasonable pricing, as envisioned at the time of the award of the second contract, before awarding extensions/option years. Included in this evaluation would be a review of the ITC mission as it affects stewardship of the asset.

The regional procurement team, regional leadership, and the Senior Procurement Advisor agreed that the procurement should proceed to award. Further, “[a]s sufficient information becomes available during contract performance, NCR intends to review the requirements for this contract, assess the performance of the contractor, evaluate the business model under which the RFP was developed, conduct market research and assess market conditions, and generally evaluate the best course for the long run. . . [u]ntil this information is available and analysis of it is conducted, NCR remains supportive of awarding the contract and looks forward to the continuing success of this flagship building.” See Phelps’ Memo, November 25, 2008.

D. CONTRACTING OFFICER LINE OF AUTHORITY

The Audit Report recommends that GSA establish and support an independent line of authority for the contracting officer and ensure transparency in the management of the contract.

Since approximately May 2006, the Contracting Officer has reported to the Deputy Director of the Service Center responsible for the RRB/ITC.

We appreciate the opportunity we were provided to review this Draft Audit Report. If you have any questions or would like to discuss this further, please call me at (202) 708-9100.

| | | | | |
|--|-------------------|---|--------------------------------|---|
| AMENDMENT OF SOLICITATION/MODIFICATION OF CONTRACT | | | 1. CONTRACT ID CODE | PAGE OF PAGES 1 3 |
| 2. AMENDMENT/MODIFICATION NO. PC07 | 3. EFFECTIVE DATE | 4. REQUISITION/PURCHASE REQ. NO. | 5. PROJECT NO. (If applicable) | |
| ISSUED BY GSA, NCR Property Development Procurement Branch (WPCA) 7th & D Streets SW, Room 2634 Washington, D.C. 20407 | | 7. ADMINISTERED BY (If other than Item 6) CODE | | |
| 8. NAME AND ADDRESS OF CONTRACTOR (No., street, county, State and ZIP Code) John E. Drew, Chairman Trade Center Management Associates 1250 Eye Street, N.W. Suite 701 Washington, D.C. 20005 | | | (y) | 9A. AMENDMENT OF SOLICITATION NO. |
| | | | | 9B. DATED (SEE ITEM 11) |
| | | | | 10A. MODIFICATION OF CONTRACT/ORDER NO. GS1194AQC00g |
| | | | | 10B. DATED (SEE ITEM 13) 3/7/95 |
| CODE | FACILITY CODE | | | |

11. THIS ITEM ONLY APPLIES TO AMENDMENTS OF SOLICITATIONS

The above numbered solicitation is amended as set forth in Item 14. The hour and date specified for receipt of Offers is extended, is not extended.

Offers must acknowledge receipt of this amendment prior to the hour and date specified in the solicitation or as amended, by one of the following methods:
 (a) By completing Items 8 and 15, and returning _____ copies of the amendment; (b) By acknowledging receipt of this amendment on each copy of the offer submitted; or (c) By separate letter or telegram which includes a reference to the solicitation and amendment numbers. FAILURE OF YOUR ACKNOWLEDGMENT TO BE RECEIVED AT THE PLACE DESIGNATED FOR THE RECEIPT OF OFFERS PRIOR TO THE HOUR AND DATE SPECIFIED MAY RESULT IN REJECTION OF YOUR OFFER. If by virtue of this amendment you desire to change an offer already submitted, such change may be made by telegram or letter, provided each telegram or letter makes reference to the solicitation and this amendment, and is received prior to the opening hour and date specified.

12. ACCOUNTING AND APPROPRIATION DATA (If required)

13. THIS ITEM APPLIES ONLY TO MODIFICATIONS OF CONTRACTS/ORDERS. IT MODIFIES THE CONTRACT/ORDER NO. AS DESCRIBED IN ITEM 14.

| | |
|-------------------------------------|---|
| <input checked="" type="checkbox"/> | A. THIS CHANGE ORDER IS ISSUED PURSUANT TO: (Specify authority) THE CHANGES SET FORTH IN ITEM 14 ARE MADE IN THE CONTRACT ORDER NO. IN ITEM 10A. |
| <input checked="" type="checkbox"/> | B. THE ABOVE NUMBERED CONTRACT/ORDER IS MODIFIED TO REFLECT THE ADMINISTRATIVE CHANGES (such as changes in paying office, appropriation date, etc.) SET FORTH IN ITEM 14, PURSUANT TO THE AUTHORITY OF FAR 43.103(b). |
| <input type="checkbox"/> | C. THIS SUPPLEMENTAL AGREEMENT IS ENTERED INTO PURSUANT TO AUTHORITY OF: |
| <input type="checkbox"/> | D. OTHER (Specify type of modification and authority) |

E. IMPORTANT: Contractor is not, is required to sign this document and return _____ copies to the issuing office.

14. DESCRIPTION OF AMENDMENT/MODIFICATION (Organized by UCP section headings, including solicitation/contract subject matter where feasible.)

See pages 2-3 of this document.

Except as provided herein, all terms and conditions of the document referenced in Item 9A or 10A, as heretofore changed, remains unchanged and in full force and effect.

| | |
|--|--|
| 15A. NAME AND TITLE OF SIGNER (Type or print) n/a | 16A. NAME AND TITLE OF CONTRACTING OFFICER (Type or print) William B. Owenby Contracting Officer |
| 15B. CONTRACTOR/OFFEROR (Signature of person authorized to sign) | 15C. DATE SIGNED |
| 15D. UNITED STATES OF AMERICA BY <i>William B. Owenby</i> (Signature of Contracting Officer) | 16C. DATE SIGNED 7/18/96 |

NSN 7540-01-152-8070
PREVIOUS EDITION UNUSABLE

30-105

STANDARD FORM 30 (REV. 10-83)
Prescribed by GSA
FAR (48 CFR) 33.243

**CONTRACT MODIFICATION NO. 7
TO CONTRACT NO. GS11P94AQ6006**

In accordance with discussions and representations by the Government, Contract No. GS11P94AQ6006 for program develop and management services for the International Trade Center at the Ronald Reagan Building and International Trade Center in Washington, DC is hereby modified as follows:

1. Janitorial and facility management

Provide janitorial and facility management services for pogram areas related to the International Trade Center. (These areas generally include office space through the 9th floor, ground, concourse, mezzanine and below grade ancillary spaces and the parking garage.) which will include the following services:

1. Janitorial/cleaning
2. Exterior of building cleaning (doors, all exterior glass and metal trim)
3. Snow removal
4. Trash collection and removal, recycling
5. All exterior building window washing
6. Landscape maintenance
7. Pest and rodent control
8. Reimbursable building alterations
9. Security support services
10. Coordination with other building maintenance and construction contractors

2. Operate and manage Parking Garage

Provide management and operation services for the entire parking garage for the Ronald Reagan Building and International Trade Center including parking designated for FOB tenants and ITC.

Services include but are not limited to: (A full scope of services will be developed and attached at a later date)

1. Collect revenues from hourly, daily and monthly parkers
2. Provide all labor and materials for parking
3. Provide all labor to collect revenues and provide valet parking as needed designated
4. Ensure parking areas are cleaned and ready for monthly FOB employees by 6AM, Monday through Friday.

YOU ARE REQUESTED TO SUBMIT A PROPOSAL FOR THIS ADDED WORK. NO COSTS SHALL BE INCURRED NOR THE GOVERNMENT LIABLE FOR ANY COSTS RELATING TO THIS MODIFICATION UNTIL THE FINAL SCOPE OF WORK, PERFORMANCE PERIOD AND PRICING ARE RECONCILED AND DEFINITIZING MODIFICATION ISSUED ACCORDINGLY.

Draft 7/18/96 - L. Brooks

**SOLE SOURCE JUSTIFICATION FOR CFM CONTRACT FOR THE TRADE
CENTER PORTION OF THE RRB/ITC BUILDING**

The International Trade Center part of the complex is a unique undertaking for the government. Legislation for the Federal Triangle directed that the complex now known as the Ronald Reagan and International Trade Center (ITC) be designed to have a discrete section of the complex devoted to a private/public partnership.

Pursuant to the legislation, dated August, 1987, approximately 500,000 square feet in the building is to accommodate office space leased to be leased to private associations and government entities who will be co-located to provide one stop shopping for information and networking to further US trade interests in the international marketplace. In addition, a US Center for World Trade to be co-sponsored by major government trade related agencies and private associations will provide training, trade related information and seminars for states, port authorities, trade associations, outbound trade missions, foreign buying delegations, small and medium sized firms as well as large industries.

The center is expected to provide private trade consultant assistance as well as services similar to regional export assistance centers. The ITC is designed to provide a venue for networking and matchmaking for business opportunities, foreign country briefings and a Trade Center Institute which, among other activities will organize conferences, educational programs, business forums, exhibits of US Products to further the center's mission.

In addition, the ITC will include a food court, restaurants, specialized retail space and a "showcase retail" center to promote the best and innovative US industry products. To facilitate seminars, meetings and conventions, the center includes conferencing and training spaces, an auditorium, and banquet facilities.

To carry out these activities, the government has procured the services of a joint venture, Trade Center Management Associates, to assist in the development of the center programs and operation of the center for the government. The ITC is a unique enterprise for the government and requires services for its operation which differ from federal office buildings in the nature and level of services necessary to enhance the quality and efficiency of operation of the Trade Center.

Trade Center Manager (TCM) must have close control over services and costs in order to serve the unique mix of visitors and customers and to maintain the viability of the center. The TCM must ensure customer satisfaction and sanitary conditions due to the extensive food service and large groups anticipated for seminars, conventions and visitors which it is expected to attract. In addition, the ITC is

expected to have extended hours of operation, which are anticipated to be as late as 2 A.M. when large conventions and seminars are scheduled.

Therefore, in order to provide the additional and special services required for the ITC facilities management, it is determined that the best interests of the government would be served if the TCM were required to provide Commercial Facility Management Services for the spaces allocated to the Trade Center Program and that a contractual arrangement be negotiated on a sole source basis with the TCMA. These services include janitorial, building window washing, pest control, exterior cleaning and snow removal, trash collection and removal. The contractual arrangement will be based on an initial one year contract with options for renewal on an annual basis for the duration of the TCMA contract (approximately 9 years).

B. Parking Garage Management

There are approximately 2,000 underground parking spaces associated with the complex. The majority of the parking spaces will be allocated to the major Federal Office tenants for daily, daytime parking. Approximately 350 parking spaces will be available for ITC use on a permanent basis and the entire garage facility will be made available to the ITC from 6PM through 2AM, Monday to Friday and twenty four hours on Saturday, Sunday and holidays.

The TCM has a contractual obligation to promote the utilization of the parking garage at night and on weekends to enhance the government's return on its investments and support the center's programs.

The availability and the condition of the parking areas is a critical factor in the success of the ITC in attracting the public to participate in the many activities at the Center. The ITC will share joint use of the total parking areas with the FOB tenants. The spaces must be efficiently managed and kept clean, well lighted and secured at all times, and the management of the parking spaces must be carefully coordinated in order to serve all uses of the RRB and ITC and the tenants.

Therefore, in view of the needs for financial control and the orderly management of the parking garage, it is determined to be in the best interests of the government to contract with the TCMA to provide parking management, collect monthly, daily and hourly parking revenues and provide cleaning, light bulb replacement and other services necessary to meet the center's program objectives in the most efficient and effective manner possible.

Contracting Officer

APPENDIX B

APPENDIX B – AUDITOR RESPONSE

In its response to the report, the National Capital Region (NCR) focused its discussion on programmatic issues and the new contract awarded to TCMA. NCR emphasized that the “statutory vision”, both physically and financially, for this unique asset must be made to succeed. Based on that goal, NCR’s response repeatedly concludes that management’s contract actions were sound business decisions and that the modifications to the previous TCMA contract were appropriate. NCR also contends that the audit report’s findings have been addressed in the new contract to TCMA. We disagree with NCR’s comments. We have included the following information to assist the reader in understanding why we do not agree with the comments. However, since NCR did not address the violations of contracting regulations, procedures and law in many cases, we did not repeat those findings here.

NCR’s General Comment: Contrary to the suggestion in the Audit Report that the new contract was awarded to TCMA after an unsuccessful attempt to compete a new contract, the new contract was awarded under full and open competition. (Appendix A, page 39)

OIG Response: In response to NCR’s answer to the sufficiency of competition regarding the new contract award, NCR misrepresented the actual results of the Agency’s own Task Force and Competition Advocate. Correspondence from the Task Force to the Former Acting Regional Administrator confirmed there existed a concern surrounding the Agency’s decision to reject a request for historical information related to the Trade Center’s business volume that may have resulted in a lack of full and open competition. The Task Force also concluded that the question regarding the access to procurement sensitive information would best be answered within the acquisition community and not by the Task Force itself. As such, it recommended and forwarded the issue to the GSA Competition Advocate who, after review, concluded “the decisions rendered by GSA effectively prevented full and open competition.”

RESPONSE TO DRAFT AUDIT REPORT RESULTS

COMMERCIAL FACILITIES MANAGEMENT SERVICES

- i. **NCR Comment:** “CFM services were not excluded from the original contract for the specific purpose of having them competed separately. Rather, CFM services were not addressed at the time of the RFP ...” (Appendix A, page 39)

OIG Response: In contrast to NCR’s response, we found the following statement within the base contract Request for Proposal (RFP): “The maintenance, operations, and facility

management for the FTB [Federal Trade Building] will be contracted by GSA to a private Commercial Facilities Manager (CFM).” This was further clarified through specific questions and answers documented in an amendment to the RFP where GSA advised bidders that commercial facility management services would be procured independently, and competitively, under a separate future contract action.

- ii. **NCR Comment:** The addition of CFM services was appropriately made as a sole source selection and sound business decision to TCMA. (Appendix A, page 39/40)

OIG Response: The addition of CFM services as a sole source action significantly funded the contract for an additional \$74 million and is in contravention of the Competition in Contracting Act, 41 U.S.C. § 253, as well as FAR requirements. This action constituted a material change that greatly expanded the contract beyond its original scope. In addition, NCR’s referenced sole source justification was unsigned and not part of the official contract file. Moreover, even if the document were signed, which it is not, the justification does not meet FAR 6.3 requirements. Finally, if NCR believed that the sole source justification document was critical to its argument, it is unclear why NCR did not accurately portray the document as unsigned in its response.

The OIG position stated in the audit report remains unchanged.

PARKING

- i. **NCR Comment:** “Parking management services were not excluded for the specific purpose of having them competed separately. They were not addressed at the time of the RFP...” (Appendix A, page 41)

OIG Response: See OIG Response to CFM Comment i.

- ii. **NCR Comment:** The addition of parking services was appropriately made as a sole source selection and sound business decision to TCMA. (Appendix A, page 42)

OIG Response: See OIG Response to CFM Comment ii. Additional funding for parking totaled approximately \$25 million.

- iii. **NCR Comment:** “Audits of parking operations were conducted annually by an independent CPA firm.” (Appendix A, page 43)

OIG Response: Our audit report accurately discusses the work performance by the CPA firm in the Section entitled “Contract Oversight”. The work was limited to reviews of schedules and provided only limited assurances, with no insight into TCMA operational

results. Further, regional personnel claimed not to have been entitled to management letters that cited recurring control deficiencies.

- iv. **NCR Comment:** “The Audit Report likewise demonstrates a complete lack of understanding regarding the decision-making process in delaying payment of this tax and acknowledges that the scope of the audit did not include review of the reasons for delay.” (Appendix A, page 43)

OIG Response: Within the scope of this audit, we did not explore the reasons why the original taxes remained unpaid while interest charges accrued, or whether the payment by GSA was proper and justified. Instead, the audit identifies that GSA ultimately lost nearly \$10 million due to the absence of proper acquisition planning, a suitable contract structure with appropriate risk sharing, accounting for results of operations by GSA and TCMA failure to identify the potential liability in the first place.

The OIG position stated in the audit report remains unchanged.

MARKETING EXPENSES

- i. **NCR Comment:** “We disagree with the statement that the contract established no measureable performance goal or cost constraint relative to marketing and promotion... Again, the key performance measurement is the programmatic success in creating a facility that provides visual testimony to the dignity, enterprise, vigor and stability of the American government.” (Appendix A, page 45)

OIG Response: In contrast to NCR’s comment, the overall programmatic success cannot be measured by “visual testimony.” TCMA’s contract lacks cost constraints and meaningful performance measures relative to providing insight on the rate of return on any investment of marketing and promotion expenses. The effectiveness of marketing relative to these expenditures was never evaluated by GSA. Instead, the TCMA contract inappropriately shifts all cost and performance risk to the government. NCR provides a comparison of marketing expenses as a percentage of annual program revenue. A more accurate analysis might consider a comparison of marketing outlays to the revenue generated for a specific activity or area.

GSA’s use of the awards and recognition chart to demonstrate its success is misleading. For at least one of these awards, GSA added more than \$300,000 to the TCMA contract “to prepare for the Government’s submission of the Ronald Reagan Building and International Trade Center (RRB/ITC) in The Office Building of the Year (TOBY) award competition.”

The OIG position stated in the audit report remains unchanged.

CONSTRUCTION SERVICES

- i. **NCR Comment:** “TCMA was a preferred vendor to provide construction management services, ensuring these projects were coordinated around tenanted spaces and conference center events. For each project GSA required that at least three bids were received.” (Appendix A, page 46)

OIG Response: There is no provision for vendor preference, as used by NCR, under FAR. GSA’s use of the TCMA contract to acquire construction services resulted in a series of inappropriate award actions. Terms and conditions required for federal construction contracts were absent. Deliverables were unspecified. Multiple levels of cost mark-ups and fees were permitted. Further, independent government cost estimates or other forms of price analysis were not generally documented in the contract file. We found only limited examples of multiple quotes secured by TCMA’s general construction subcontractor, and no evidence of full and open competition. The process, to the extent documented, does not establish a basis for determining price reasonableness.

The OIG position stated in the audit report remains unchanged.

ADMINISTRATIVE POSITIONS

- i. **NCR Comment:** “Adding these positions was a sound business decision, completely justified by the unexpected volume of business due to its successful operation.” (Appendix A, page 46/47)

OIG Response: There is no provision in this contract or any fixed-price contract for additional compensation due to a contractor’s increased costs. Under a firm-fixed-price type contract, actual costs whether higher or lower than anticipated have no effect on the price agreed to under the contract. Performance and cost risk under a fixed-price arrangement rest with the contractor.

Specifically, FAR 16.202-1 states: *“A firm-fixed-price contract provides for a price that is not subject to any adjustment on the basis of the contractor’s cost experience in performing the contract. This contract type places upon the contractor maximum risk*

and full responsibility for all costs and resulting profit or loss. It provides maximum incentive for the contractor to control costs and perform effectively and imposes a minimum administrative burden upon the contracting parties...”

The OIG position stated in the audit report remains unchanged.

SALES AND MANAGEMENT POSITIONS

- i. **NCR Comment:** “This staff was unable to provide the necessary effort to keep up with the success of the conference center ...” (Appendix A, page 47)

OIG Response: The additional sales positions are a direct function for which TCMA is already compensated through the fixed price payment under its contract. Under the terms of the contract, TCMA was already bound to provide the sales staffing level necessary to fill the venue with events. In soliciting for this contract, the Government evaluated the technical competency of its offerors. TCMA cites and GSA accepted the experience of its members as evidence of ability to translate the ITC requirement into a realistic staffing plan and price proposal. The technical proposal submitted by TCMA detailed its anticipated sales staffing plan. Absent an additional service requirement, there is no provision in this or any fixed-price contract for additional compensation due to a contractor’s increased costs. Performance and cost risk under a fixed-price arrangement rest with the contractor.

Specifically, FAR 16.202-1 states: *“A firm-fixed-price contract provides for a price that is not subject to any adjustment on the basis of the contractor’s cost experience in performing the contract. This contract type places upon the contractor maximum risk and full responsibility for all costs and resulting profit or loss. It provides maximum incentive for the contractor to control costs and perform effectively and imposes a minimum administrative burden upon the contracting parties...”*

The OIG position stated in the audit report remains unchanged.

ARIA RESTAURANT

- i. **NCR Comment:** “GSA hired an outside real estate attorney to negotiate the license to mitigate any conflict of interest.” (Appendix A, page 49)

OIG Response: NCR misrepresents the relationship between GSA and the attorney(s) used to negotiate this license. According to documentation provided by NCR, TCMA used its existing attorney(s) to assist in the negotiation of a license to itself (Aria), which would not mitigate the inherent conflict of interest or risk. While TCMA agreed to waive any privileges in order to expedite a GSA review, GSA did not have an attorney/client relationship with the law firm.

Aria Management, LLC is a TCMA affiliate. The entities share identical ownership and common management. As GSA's ITC manager, TCMA is responsible for evaluating the tenant mix and space use to help achieve the goals of promoting international trade while also striving to maximize GSA's return on investment. As Aria's owner, a profit driven business, TCMA/Aria would logically look to earn the maximum return with the least risk to itself. The party that GSA has entrusted with protecting the government's interest has a financial incentive to transfer costs and risk normally borne by the tenant to GSA.

The OIG position stated in the audit report remains unchanged.

TCMA'S SPACE OCCUPANCY

- i. **NCR Comment:** "As existing activity grew substantially and additional requirements were added, GSA evaluated the need and provided additional space. All TCMA space was utilized exclusively for the direct performance of this contract, essential for servicing the building and operation." (Appendix A, page 50)

OIG Response: NCR's lack of oversight and enforcement of contract terms permitted TCMA to occupy substantially more space than allowed under the contract, and NCR also allowed TCMA partners and subcontractors to occupy space free of rent. There were no modifications or formal correspondence authorizing the contractor to exceed the prescribed allotted space with an estimated value of \$651,398 annually. NCR has not initiated any effort prior to the audit to determine the extent to which TCMA expanded its space occupancy.

The OIG position stated in the audit report remains unchanged.

PROGRAM MANAGEMENT

- i. **NCR Comment:** “The ITC revenue cannot be used to pay the debt service.” (Appendix A, page 51)

OIG Response: Assuming that the ITC revenue could not be used for debt service, and debt service was required to be paid out of a different funding source, GSA would be able to include the expenses for debt service in its calculations of the ITC’s net profitability. The audit report is thus correct in its assertion that GSA’s accounting treatment creates an inaccurate impression of the ITC’s financial success.

The OIG position stated in the audit report remains unchanged.

APPENDIX C

APPENDIX C – ALERT REPORT

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Restricted Report

ALERT REPORT:
AUDIT OF GSA'S ACQUISITION OF SERVICES
FOR THE INTERNATIONAL TRADE CENTER
AT THE RONALD REAGAN BUILDING
REPORT NUMBER A080106/P/W/W08001

MAY 29, 2008

**Office of Inspector General
General Services Administration**



Office of Audits

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ALERT REPORT:
AUDIT OF GSA'S ACQUISITION OF SERVICES
FOR THE INTERNATIONAL TRADE CENTER
AT THE RONALD REAGAN BUILDING
REPORT NUMBER A080106/PM/W08001

MAY 29, 2008

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Office of Inspector General

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Date: May 29, 2008

Reply to: Paul Malatino
Attn of: Regional Inspector General for Auditing, Washington Field Audit Office (JA-W)

Subject: Alert Report: Audit of GSA's Acquisition of Services for the International Trade Center at the Ronald Reagan Building
Report Number A080106/P/W/W08001

To: Tony Reed
Regional Administrator
National Capital Region (WA)

This alert report is issued to bring to your attention matters that may impact your efforts to replace the expiring contract to provide trade center management services in support of the International Trade Center at the Ronald Reagan Building. As you know, we have in process an audit of PBS' efforts to administer that contract. The review was undertaken at your request, as you became concerned over the absence of support to justify a proposed modification to extend the current trade center management contract by 26 months at an estimated cost of \$50 million dollars. That contract was originally awarded on March 7, 1995, with a base year plus nine one-year options. An additional two years were added to compensate for construction delays. Total evaluated price at the time was \$18,071,371 plus economic price adjustment. The scope and size of that contract have been expanded through extensive modification; the contract value now exceeds \$220 million.

Our survey work indicates an absence of effective oversight of the International Trade Center and a compromised system of management control. Oversight responsibility that was originally intended to rest with a third party has been instead assumed by GSA. The relevant criterion appears to be obsolete legislation¹ that, for reasons which are not part of the record we have examined to date, was never fully implemented. Establishing the specific authority and limitations of ITC scope of operations and funding are logical

¹ Reference is made to the Federal Triangle Development Act, Public Law 100-113. Sections pertaining to the establishment and operation of a commission were codified as 40 U.S.C. §§ 1106-1107. These sections are omitted from the current version of the U.S. Code due to "limited interest", but have not been repealed.

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precursors to establishing the scope of any follow-on contract actions. At present, in lieu of a commission as originally contemplated, GSA is operating the ITC without a dedicated oversight body.

The authorizing legislation envisioned an independent commission to oversee what was initially conceived as an international culture and trade center. The commission was short lived and has apparently not played a role in what has evolved into the International Trade Center at the Ronald Reagan Building. The legislation granted the commission the authority to lease space from GSA not to exceed 500,000 square feet in the building, which at that point was yet to be constructed. The commission was in turn authorized to sublease to foreign missions, commercial establishment sponsored by foreign governments, and international cultural and trade organizations, including domestic organizations and State and local governments. The initial concept had the commission leasing from GSA at "cost" and generating operating revenue from its higher, market rate subleases. Higher than anticipated construction cost eliminated this funding option, congress authorized no alternative, and the commission expired².

Serving in place of the commission, GSA has awarded a contract to a single commercial entity, the Trade Center Management Associates (TCMA). TCMA has been given the exclusive right to operate, manage and profit from the more than 500,000 rentable square feet dedicated to the ITC in what is considered the most prestigious area for federal tenant agencies housed in Washington, DC. The building is within two blocks of the White House, is within walking distance to the U.S. Capitol Building and has frontage on two arterial roadways with nearby access to the interstate highway system. It has a 1,950 space parking garage under the building, a Great Plaza with outside seating and landscaping that serves as a gateway to the National Mall. National monuments, historic landmarks, hotels, theaters, restaurants, entertainment centers and sports arenas are within close proximity to the site.

The source of all ITC funding, which is in effect TCMA funding, is the revenue it generates. All non-federal tenant rent, venue rental, event management and support fees, and all non-federal tenant parking revenue, represent a dedicated funding source for ITC operations. While ITC funds are ultimately derived from a Federal Buildings Fund (FBF) asset, the ITC does not compete with other PBS priorities for a share of overall funding. We raise this as an issue because the specific authority that permits this funding arrangement is not evident. For example, when the parking garage operations were added to TCMA's contract, the associated non-federal tenant parking

² Barbara Gamarekian. "New Trade Center in Washington: Will it Help or Hurt the Kennedy?" New York Times. July 10, 1990.

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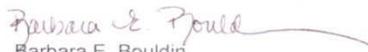
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revenue stream became part of the dedicated funding source. As parking garage operations were not part of the trade center management contract's original scope, the decision to award a sole source, cost reimbursable contract, and the decision to dedicate a portion of the revenue stream of the underlying asset are actions that require a Determination and Finding (FAR 1.7) with respect to the procurement and specific authorization from the Chief Financial Officer with respect to the funding. Our review to date has not produced a record of the source or authority for that action. That void is what we are raising to the level of a management alert.

As to the procurement in general, preliminary audit inquiries and documentary review made in the course of our survey work indicate a high likeliness of numerous and substantial procurement irregularities. The contract has been expanded to include, for example, the operation of a parking garage, facilities management services and a restaurant. The contract cost structure itself is ambiguous, with the distinction between fixed cost and cost reimbursable elements particularly blurred. There appears to be a substantial risk of cost duplication or payment of otherwise unreasonable, unallocable or unallowable expenses. The modification files also indicate a REDACTED *General and Administrative* cost factor applied to everything from indirect costs themselves to taxes and subcontracts. These and other issues have been identified as risk indicators and will be examined fully in the course of audit field work.

If you have any questions regarding this alert report, please contact me or Barbara Bouldin, Audit Manager, at (202) 708-5340.


Barbara E. Bouldin
Audit Manager
Washington Field Audit Office

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Regional Administrator, National Capital Region (WA)

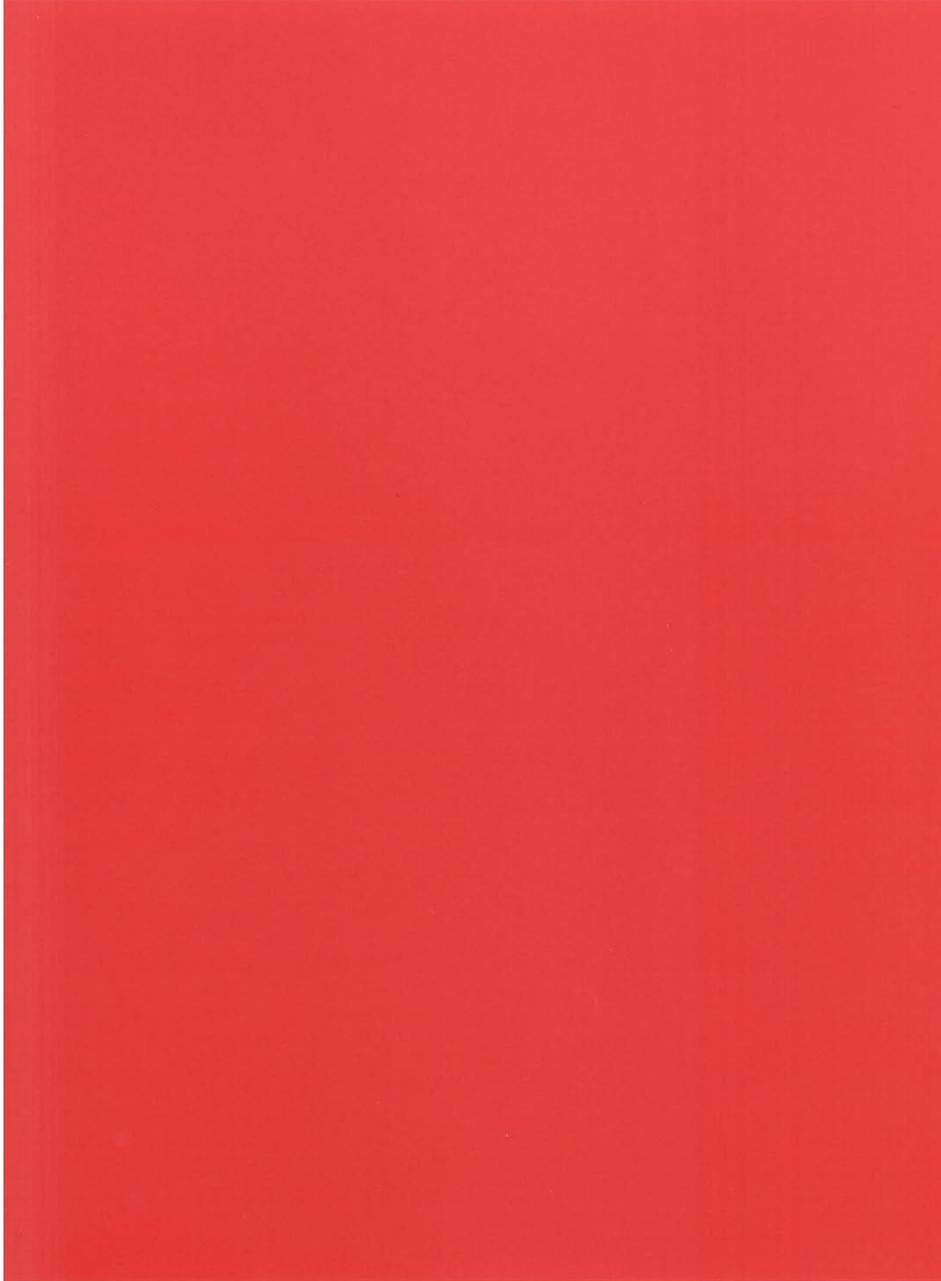
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APPENDIX D

APPENDIX D – CONSTRUCTION RELATED CONTRACT MODIFICATIONS

| Mod # | Mod Amt | Effective Date | Scope ³² |
|-------|---------------|----------------|---|
| SA25 | NTE \$143,000 | 11/1/97 | Adds construction management service for the build-out of the ITC North Office Tower, Phase One. This phase covers build-out of common areas plus 60,000sf tenanted office space. Compensation (PROPRIETARY INFORMATION – REDACTED) lump sum plus (PROPRIETARY INFORMATION – REDACTED) construction cost for above standard fit-out. ITC Director asserts that CM services fall within the scope of TCMA’s contract. |
| SA29 | NTE \$155,000 | 2/1/98 | Adds construction management of the build-out of the ITC North Office Tower, Phase Two. This phase covers build out of balance of tenanted office space, 100,000sf. Compensation (PROPRIETARY INFORMATION – REDACTED) lump sum plus (PROPRIETARY INFORMATION – REDACTED) construction cost for above standard fit-out. Overall construction budget was (PROPRIETARY INFORMATION – REDACTED) covering both Phases. |
| SA34 | NTE \$170,500 | ?/97 | Signed 6/98 to compensate TCMA for retail (food court) construction coordination services already rendered over past 12 months. TCMA claimed there had been an “agreement” to reimburse these expenses. ITC Director approved payment, claims that retail coordination services were not part of the contract. |
| SA42 | NTE \$ 45,000 | 11/97 | Signed retroactively on 9/98 for “hours expended and other direct costs” and to be provided “from November, 1997 through April, 1998.” TCMA is tasked “to make recommendations and work with the new architectural team to assure the ITC program and design integrity.” |
| SC58 | \$1,700,000 | 9/15/99 | Modification SC58 obligates funding for programming, design and implementation of the “America’s Showcase” retail space and for associated tenancy-related costs. No deliverable; modification simply locks in funding. Modification 58A, discussed next, indicates that these funds were intended for CM services as well as hard costs of tenant space build-out. |
| 58A | \$0 | 7/5/01 | Provides a partial scope of services with reference to Modification 58 for funding. Specifies amount NTE (PROPRIETARY INFORMATION – REDACTED) billed on a labor hour basis derived from <i>actual salary</i> times a multiplier of (PROPRIETARY INFORMATION – REDACTED) that includes overhead but no fee. Rates are as follows: <ul style="list-style-type: none"> • Vice President @ (PROPRIETARY INFORMATION – REDACTED) /hr • Construction Manager @ (PROPRIETARY INFORMATION – REDACTED) /hr • Support Staff @ (PROPRIETARY INFORMATION – REDACTED) /hr Specific Tasks include: <ul style="list-style-type: none"> • Review license form and exhibits. Also authorizes TCMA to engage A/E/s on reimbursable basis. |

³² Exclusive of restaurant construction modifications

| Mod # | Mod Amt | Effective Date | Scope ³² |
|-------|-------------|----------------|---|
| | | | <ul style="list-style-type: none"> Review deals for Licensor (GSA/TCMA) work requirements. Oversee selected A/E's and coordinate construction services. Coordination and Construction Management of Licensee (tenant) work. Implies oversight of construction contracts to be awarded by GSA. <p>Estimated budget for Licensee Work is (PROPRIETARY INFORMATION – REDACTED). Modification implies that construction coordination services were not a deliverable included under the fixed-price of the base contract, clause (C)(6)(b) cited on page 22.</p> |
| 58B | \$700,000 | 9/25/03 | <p>Funding increase for “continuing design, construction and construction management services to support the build-out of tenant spaces.” Memo to file explains that funds will also cover one full time CM plus one part time CM with rates based on “hourly rates taken from existing A/E and CM services contracts.” Scope of services simply points back to Modifications 58 and 58A. No additional details in this modification.</p> |
| 58C | \$1,250,000 | 9/24/04 | <p>Supplements funding to cover costs for “partial fiscal year 2004 and...some of the initial FY 2005 expenditures...” No specific project identified; funding was retroactive in part.</p> <p>Memo to file signed by Director states that:</p> <ul style="list-style-type: none"> Construction/Build-out – “costs...are based upon competitive pricing and the TCM will obtain and submit competitive pricing bids.” CM and A/E services are “based upon Government established hourly rates.” <p>Memo to file also discusses TCMA hiring the current CM, changing his status from subcontractor to employee of TCMA. Memo cites current rate (PROPRIETARY INFORMATION – REDACTED) /hr plus (PROPRIETARY INFORMATION – REDACTED) G&A plus (PROPRIETARY INFORMATION – REDACTED) profit.</p> |
| PC58D | \$1,500,000 | 1/10/05 | Additional funding. No specified deliverable. |
| PC58E | (\$350,000) | 6/21/05 | Decrease – new priorities for FY2005 |
| PC96 | \$1,100,000 | 9/19/02 | <p>Modification to convert Atrium to ballroom. Memo to file says that the funding and authority in this modification will “provide the Government...the ability to perform a design-build project...on a tight timeframe...” Actual scope of work and deliverables not specified in modification. File implies that TCMA solicited competing bids and ultimately awarded contract to (PROPRIETARY INFORMATION – REDACTED) valued at (PROPRIETARY INFORMATION – REDACTED) + A/E fees of (PROPRIETARY INFORMATION – REDACTED) + additional TCMA fees and profit totaling (PROPRIETARY INFORMATION – REDACTED). Email “approval” comes from COTR, who also agrees that GSA will cover any additional contingencies up to (PROPRIETARY INFORMATION – REDACTED), “not at the risk or expense of TCMA.”</p> |
| PC96a | \$18,582 | 9/22/03 | <p>Change order to Atrium conversion project. Replace defective sprinkler heads. Includes (PROPRIETARY INFORMATION – REDACTED) cost + (PROPRIETARY INFORMATION – REDACTED) (PROPRIETARY INFORMATION – REDACTED) fee + (PROPRIETARY INFORMATION – REDACTED) CM + (PROPRIETARY INFORMATION – REDACTED) G&A + (PROPRIETARY INFORMATION – REDACTED) Profit. Modification states that this work was not contemplated under original plan.</p> |
| PC96b | \$43,022 | 11/1/04 | Additional funding for Atrium conversion. No details provided in file. |
| PC101 | \$20,000 | 9/20/02 | <p>Authorization for TCMA to contract for a sound system in Pavilion reception room. Memo states that this feature was “value engineered” out of original</p> |

| Mod # | Mod Amt | Effective Date | Scope ³² |
|--------------|---------------------|----------------|---|
| | | | design for (PROPRIETARY INFORMATION – REDACTED). Significant estimated cost savings is attributed to GSA direction to “pursue the marketplace instead of summarily going to the in-house audio visual contractor”. Outcome not documented. |
| 101a | \$400,000 | 9/27/06 | “Supplemental” funding for sound system, at twenty times original estimate. Outcome not documented. |
| PC139 | \$500,000 | 12/?/05 | Additional funding for retail and office construction, CM, and A/E services. Vague reference to Modification 58E. No specified deliverable. |
| 139a | \$800,000 | 9/27/06 | Additional funding, as above. No specified deliverable. |
| C167 | \$1,800,000 | 9/11/07 | Additional funding, as above. No specified deliverable. |
| C193 | \$21,348 | 4/22/08 | This is the first of the construction modifications that fell within the audit time frame. There is a marked difference in modification structure, scope and analysis. This Modification 193 is for A/E services covering renovation of Suite 330. Three proposals are documented and compared. An IGE was prepared. A contracting officer’s determination of price reasonableness is documented. Analysis of A/E costs, a component of nearly all the preceding work, was not present in the prior modifications. Price analysis notwithstanding, there is no provision for obtaining A/E services through TCMA. This approach does not satisfy competitive procedures for A/E services as defined by FAR 36.6, and GSA incurs an unnecessary TCMA mark-up of (PROPRIETARY INFORMATION – REDACTED) G&A plus (PROPRIETARY INFORMATION – REDACTED) profit. |
| C195 | \$22,326 | 4/29/08 | Create an outdoor deli area for ARIA restaurant. Work includes 8 new electrical outlets and new drapery and track. As above, includes CO determination of price reasonableness, contains three bids, and references and an IGE. Same criticism as C193. |
| C196 | \$23,592 | 5/9/08 | Renovation of a current tenant’s space (PROPRIETARY INFORMATION – REDACTED). As with C193 and C195, modification contains a discrete scope, multiple bids, and an IGE. View as TI for a succeeding lease. |
| TOTAL | \$10,062,371 | | |

APPENDIX E

APPENDIX E – REPORT DISTRIBUTION

Acting Regional Administrator, National Capital Region (WA)

Public Buildings Service Regional Commissioner (WP)

Internal Control and Audit Division (BEI)

Assistant Inspector General for Auditing (JA)

Director, Audit Planning, Policy, and Operations (JAO)

Director, Administrative and Data Systems (JAS)

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