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Office of Inspector General  
United States Department of State

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AUD-CGI-25-15

Office of Audits

March 2025

# **Audit of Selected Contractor Requests for Equitable Adjustment Related to Bureau of Overseas Buildings Operations' Construction Projects**

CONTRACTS, GRANTS, AND INFRASTRUCTURE DIVISION

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# HIGHLIGHTS

Office of Inspector General  
United States Department of State

AUD-CGI-25-15

## What OIG Audited

The Bureau of Overseas Buildings Operations (OBO) directs the worldwide overseas building program for the Department of State (Department). Requests for equitable adjustment (REA) are contractor requests seeking an adjustment to a contract's time or price. The Department reported that contracting officials coordinated REAs totaling \$418 million from October 1, 2020, through June 30, 2023, on overseas construction projects.

The Office of Inspector General (OIG) conducted this audit to determine whether the process used by the Department to reach equitable adjustments with selected construction contractors responsible for large construction contracts complied with the Federal Acquisition Regulation (FAR) and Department guidance. From a universe of 440 REAs processed from October 1, 2020, through June 30, 2023, OIG selected 30 REAs from 5 overseas construction projects for review.

## What OIG Recommends

OIG made 20 recommendations to address the issues identified in this report, including 6 recommendations to recover questioned costs. On the basis of management's response to a draft of this report, OIG considers 7 recommendations resolved, pending further action, and 13 recommendations unresolved. A synopsis of management's comments and OIG's reply follow each recommendation in the Audit Results section of this report. OBO's and the Bureau of Administration's responses to a draft of this report are reprinted in their entirety in Appendices C and D. A summary of OBO's technical comments and OIG's replies are presented in Appendix E.

March 2025

## OFFICE OF AUDITS

CONTRACTS, GRANTS, AND INFRASTRUCTURE DIVISION

### Audit of Selected Contractor Requests for Equitable Adjustment Related to Bureau of Overseas Buildings Operations' Construction Projects

#### What OIG Found

The Department's process to reach equitable adjustments with selected construction contractors did not fully comply with the FAR and Department guidance. Specifically, of the 30 REAs reviewed for this audit, OIG found 14 constructive changes made by Project Directors (PD) or other OBO officials. Constructive changes occurred when the government expressly or impliedly ordered work outside the scope of the contract. Moreover, these constructive changes led to REAs and ultimately resulted in unauthorized commitments that were not properly ratified.

In addition, OIG found that PDs and Contracting Officers (CO) did not evaluate and resolve selected REAs in accordance with the FAR and Department guidance. Specifically, OIG found that PDs did not always comply with requirements to determine the merit of REAs, prepare sufficient independent government cost estimates, prepare negotiation memoranda or receive CO authorization before beginning to negotiate, and perform required cost analyses. Additionally, OIG found that the Department allowed contractors to improperly use two different bases for indirect cost allocation and did not resolve REAs in a timely manner.

These deficiencies occurred primarily because PDs and COs did not follow established policies and procedures for evaluating and resolving REAs. Additionally, OBO and the Bureau of Administration, Office of the Procurement Executive, Office of Acquisitions Management (AQM), had not developed and implemented a sufficient process to determine whether PDs and COs adhered to requirements. In addition, AQM did not have specific procedures for evaluating and resolving REAs, and the Department did not have sufficient guidance related to allocating overhead costs to construction projects. Until the Department fully complies with REA requirements, it cannot be assured that REAs are settled in a fair and reasonable manner. As a result, OIG is questioning \$837,172 in unsupported costs and \$3,251,891 in unallowable costs associated with 17 of the 30 REAs reviewed for this audit.

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## OBJECTIVE

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The Office of Inspector General (OIG) conducted this audit to determine whether the process used by the Department of State (Department) to reach equitable adjustments with selected construction contractors responsible for large construction contracts complied with the Federal Acquisition Regulation (FAR) and Department guidance.

## BACKGROUND

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### **Contract Administration Responsibilities**

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

The Bureau of Overseas Buildings Operations (OBO) directs the worldwide overseas building program for the Department and the U.S. government community serving abroad under chief of mission authority. It does so in concert with other Department bureaus, foreign affairs agencies, and Congressional mandates.<sup>1</sup> From FY 2016 through FY 2021, the Department awarded 24 New Embassy Compound (NEC) and New Consulate Compound (NCC) construction contracts valued at \$6 billion.

As the overseas real property manager for the Department, OBO has the lead role in acquiring, designing, building, operating, and maintaining Department facilities worldwide.<sup>2</sup> OBO's Construction and Security Management Directorate, Office of Construction Management (CM), provides management, oversight, and construction supervision of overseas construction projects.<sup>3</sup> CM has five branches based on region: (i) Africa; (ii) East Asia and Pacific; (iii) Europe; (iv) Near Eastern, South, and Central Asia; and (v) the Western Hemisphere.<sup>4</sup> Senior Construction Executives, who lead each branch,<sup>5</sup> assign Construction Executives to projects in their respective region.<sup>6</sup> Each major overseas construction project is assigned an onsite Project Director (PD),<sup>7</sup> who also serves as the Contracting Officer's Representative (COR)<sup>8</sup> for the construction contract. Each PD reports to the assigned Senior Construction Executive.<sup>9</sup> CM

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<sup>1</sup> 1 FAM 281.1(2), (7), and (15), "Responsibilities."

<sup>2</sup> 1 FAM 281.1(5) and (10).

<sup>3</sup> 1 FAM 286.1(2), "Office of Construction Management (OBO/CSM/CM)."

<sup>4</sup> OBO, "Construction Management Guidebook," 1.3.4.2, "Construction Operations Division (CFSM/CM/CO)," page 1-12.

<sup>5</sup> Ibid., 1.3.5.4, "Senior Construction Executives," page 1-13.

<sup>6</sup> Ibid., 1.3.5.5, "Construction Executive," page 1-17.

<sup>7</sup> Ibid., 1.3.5.6, "Project Director," page 1-19.

<sup>8</sup> According to OBO's "Construction Management Guidebook," 3.1.2, "Project Director (PD)," the PD is the COR, page 3-2.

<sup>9</sup> OBO, "Construction Management Guidebook," 1.3.5.6, page 1-19.

manages construction contracts in conjunction with the Office of the Procurement Executive (OPE).<sup>10</sup>

The PD, as the COR, is responsible for enforcing the terms and conditions of the construction contract. This responsibility entails reviewing all proposals for contract changes. In instances in which the estimated cost of a proposed change exceeds the PD's warrant authority,<sup>11</sup> the PD makes a recommendation for action to the Contracting Officer (CO).<sup>12</sup> The PD, acting as the COR, is not authorized to make any commitments or changes that affect the price, quality, quantity, delivery, or other terms and conditions of the contract.<sup>13</sup>

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

OPE is responsible for providing Department-wide acquisition policies and services, including developing, issuing, and maintaining acquisition regulations, procedures, and guidance.<sup>14</sup> Under the leadership of OPE, the Office of Acquisitions Management (AQM) manages, plans, and directs the Department's acquisition programs and conducts contract operations in support of activities worldwide.<sup>15</sup> According to the Department's Foreign Affairs Manual (FAM), AQM provides a full range of contract management services, including acquisition planning, contract negotiations, and cost and price analyses.<sup>16</sup>

The Foreign Affairs Handbook (FAH) states that the CO is the U.S. government's authorized agent for working with contractors and has sole authority to solicit proposals and negotiate, award, administer, modify, or terminate contracts.<sup>17</sup> The CO is also responsible for ensuring the performance of all necessary actions for effective contracting, ensuring compliance with the terms of the contract, and safeguarding the interests of the United States in its contractual relationships.<sup>18</sup> The CO is an employee of the Bureau of Administration and performs duties at the request of the bureau or office that requires the contract, relying on that bureau or office for technical support concerning the products or services being acquired.<sup>19</sup>

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<sup>10</sup> Ibid., 1.3.3.1, "Office of Construction Management (CFSM/CM)," page 1-10.

<sup>11</sup> According to OBO's "Construction Management Guidebook," 3.1.3, "COR Responsibilities," the PDs for overseas construction projects may be granted limited CO authority by A/OPE, page 3-3.

<sup>12</sup> Ibid., 3.1.2, page 3-2.

<sup>13</sup> FAR 1.602-2(d)(5).

<sup>14</sup> 1 FAM 212.2(b), "Office of the Procurement Executive (A/OPE)." During the audit, this requirement was moved to 1 FAM 212.1.

<sup>15</sup> After the completion of audit fieldwork, the Bureau of Administration implemented a reorganization of its offices and realigned their acquisitions expertise within OPE under the Deputy Assistant Secretary for Global Acquisitions.

<sup>16</sup> 1 FAM 212.2-2(a), "Office of Acquisitions Management (A/OPE/AQM)." During the audit, this requirement was moved to 1 FAM 212.1-2.

<sup>17</sup> 14 FAH-2 H-141(a), "Responsibilities of the Contracting Officer."

<sup>18</sup> FAR 1.602-2, "Responsibilities."

<sup>19</sup> 14 FAH-2 H-141(a).

In supporting OBO construction projects, AQM is responsible for providing centralized contracting services and administering each contract.<sup>20</sup>

## **Constructive Changes and Requests for Equitable Adjustment**

A “constructive change” arises when, by informal action or inaction by the U.S. government, the contractor’s situation is so altered that the effect is as though a change order had been issued.<sup>21</sup> A constructive change may occur due to various reasons, including inadequate specifications, improperly interpreted specifications, overly strict inspection, or improper technical direction.<sup>22</sup> Constructive changes can lead to requests for equitable adjustment (REA).<sup>23</sup>

REAs are documents submitted by a contractor seeking an adjustment to the contract time or price. REAs can be submitted on projects regardless of fund source, project type, dollar amount, or contract office.<sup>24</sup> A contractor may also submit an REA if, without the fault or negligence of the contractor, the performance of all or any part of the work is suspended, delayed, or interrupted for an unreasonable period of time by acts of the CO or the COR in the administration of the contract or by the U.S. government’s failure to act within the time specified in the contract documents.<sup>25</sup>

## **REA Resolution Process**

For a contractor-originated change, the contractor should notify the PD in writing of the need for a constructive change, usually within 20 days of the occurrence of the circumstances leading to the request, through an REA.<sup>26</sup>

## ***Determination of Merit Process and Responsibilities***

In instances in which the estimated cost of a proposed change exceeds the PD’s warrant authority, upon receiving an REA, the PD should prepare a written analysis of the REA and make a recommendation of merit or no merit. The written analysis must include contract references and backup documentation.<sup>27</sup> For REAs determined to have merit, the PD should prepare an independent government cost estimate<sup>28</sup> (IGCE).<sup>29</sup> The PD provides the Construction Executive

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<sup>20</sup> 1 FAM 212.2-2(a). During the audit, this requirement was moved to 1 FAM 212.1-2.

<sup>21</sup> 14 FAH-2 H-535(a), “Constructive Changes.”

<sup>22</sup> 14 FAH-2 H-535(b).

<sup>23</sup> FAR 52.243-5, “Changes and Changed Conditions.”

<sup>24</sup> OBO, “Construction Management Guidebook,” 2.4.8.7, “Request for Equitable Adjustment,” page 2-99.

<sup>25</sup> Ibid., 3.2.12.6, “Suspension of Work,” page 3-46.

<sup>26</sup> Ibid., 3.2.12.12, “Contractor-Originated Changes (Requests for Equitable Adjustment [REA]),” page 3-55.

<sup>27</sup> Ibid., 3.2.12.13(B)(5), “Contractor-Originated Changes (Requests for Equitable Adjustment [REA]),” page 3-56.

<sup>28</sup> The terms IGCE and independent government estimate are used interchangeably in the documents referenced in this report.

<sup>29</sup> Ibid., 3.2.12.15, “Execution of Change,” page 3-59.

with the written analysis and recommendation.<sup>30</sup> The Construction Executive should then review the PD's analysis and IGCE, conduct a time analysis if required, and provide the CO with the technical analysis and recommendation.<sup>31</sup> The CO is required to inform the contractor by letter if the REA has merit or no merit or that a decision has not been made and a decision is expected by a certain date.<sup>32</sup>

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

An IGCE is the U.S. government's estimated cost or price of a proposed acquisition and is prepared by the COR. Its purpose is to serve as a basis for comparing costs or prices proposed by offerors and as an objective basis for determining price reasonableness.<sup>33</sup> According to the Department's "Overseas Procurement Guide," the government must prepare an IGCE for proposed contract modifications and assess any time extension that may be justified.<sup>34</sup> Furthermore, the FAH states that when a modification is necessary, the COR must prepare a procurement request to document the need for the modification, including "[t]he estimated total time necessary to accomplish the required services, if the time must be extended."<sup>35</sup>

For construction contracts, the FAR<sup>36</sup> requires an IGCE for each contract modification anticipated to exceed the simplified acquisition threshold.<sup>37</sup> However, the CO may require an IGCE even when the cost of required work is not anticipated to exceed the simplified acquisition threshold.<sup>38</sup> OBO guidance requires an IGCE for construction contract modifications that exceed \$25,000.<sup>39</sup> For OBO construction projects, the PD is responsible for preparing the IGCE using input from OBO's staff or resources assigned to the project. The PD should certify the IGCE prior to proceeding with subsequent steps in the change process.<sup>40</sup>

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<sup>30</sup> Ibid., 3.2.12.13(B)(5), page 3-56.

<sup>31</sup> Ibid., 3.2.12.13(B)(6), page 3-56; and 3.2.12.14, "Prenegotiation Responsibilities," page 3-59.

<sup>32</sup> Ibid., 3.2.12.13(B)(7), page 3-56.

<sup>33</sup> 14 FAH-2 H-351(a) and (b), "General."

<sup>34</sup> OPE, "Overseas Procurement Guide," Chapter 8, "Contract Modification/Contract Closeout," Section VI, "Backup Supporting Contract Modifications/Delivery Orders/Task Orders," C, "Pricing of Adjustments." As of October 1, 2023, the "Overseas Procurement Guide" was canceled and rescinded, and contracts personnel are now required to use the Department of State Acquisition Manual. This audit references the "Overseas Procurement Guide," as that was what was in effect during the period of review.

<sup>35</sup> 14 FAH-2 H-534(5), "Processing Contract Modifications."

<sup>36</sup> FAR 36.203(a), "Government estimate of construction costs."

<sup>37</sup> According to FAR 2.101, "Definitions," the simplified acquisition threshold is \$250,000.

<sup>38</sup> FAR 36.203(a).

<sup>39</sup> OBO, "Construction Management Guidebook," 3.2.12.8, "Change Orders and Claims Management," page 3-50.

<sup>40</sup> Ibid.

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

The prenegotiation objectives<sup>41</sup> establish the government's initial negotiation position and assist in the CO's determination of a fair and reasonable price.<sup>42</sup> According to OBO's "Construction Management Guide," upon receiving and reviewing the contractor's response to the request for proposal or the REA, the PD must prepare and forward a prenegotiation memorandum to the Construction Executive. The prenegotiation memorandum is required for modifications over \$25,000. The Senior Construction Executive should then review the PD's prenegotiation memorandum and coordinates with the PD. The Construction Executive should then transmit the coordinated response to the CO for decision. Lastly, the CO should issue a decision on the prenegotiation memorandum to the PD through the Construction Executive.<sup>43</sup> According to the FAR, the CO should establish prenegotiation objectives before the negotiation of any pricing action.<sup>44</sup>

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

According to the FAR, the purpose of performing a cost or price analysis is to develop a negotiation position that permits the CO and the offeror an opportunity to reach agreement on a fair and reasonable price.<sup>45</sup> The FAR requires the CO to document in the contract file the principal elements of the negotiated agreement and provides specific information that must be included in this documentation.<sup>46</sup>

According to the OBO "Construction Management Guidebook," in instances in which the estimated cost of a proposed change exceeds the PD's warrant authority, if the REA has merit, the PD, if authorized by the CO in writing, will negotiate the cost with the contractor. Following the negotiations, the PD should send the negotiation memorandum to the CO with the results of the negotiations.<sup>47</sup> Furthermore, the PD is required to document the negotiations and report the results of the negotiations to the Construction Executive.<sup>48</sup> The CO executes the contract modification based on the negotiated agreement.<sup>49</sup> If the REA is denied, the CO must inform the contractor in writing about the reason for denial.<sup>50</sup> A summary of the determination of merit, prenegotiation, and negotiation processes and responsibilities is shown in Figure 1.

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<sup>41</sup> The terms prenegotiation objectives, prenegotiation memorandum, and prenegotiation plan were used interchangeably in the documents referenced in this report. For consistency, OIG uses the term prenegotiation memorandum throughout the report.

<sup>42</sup> FAR 15.406-1(a), "Prenegotiation objectives."

<sup>43</sup> OBO, "Construction Management Guidebook," 3.2.12.14, page 3-59.

<sup>44</sup> FAR 15.406-1(b).

<sup>45</sup> FAR 15.405(a), "Price negotiation."

<sup>46</sup> FAR 15.406-3, "Documenting the negotiation."

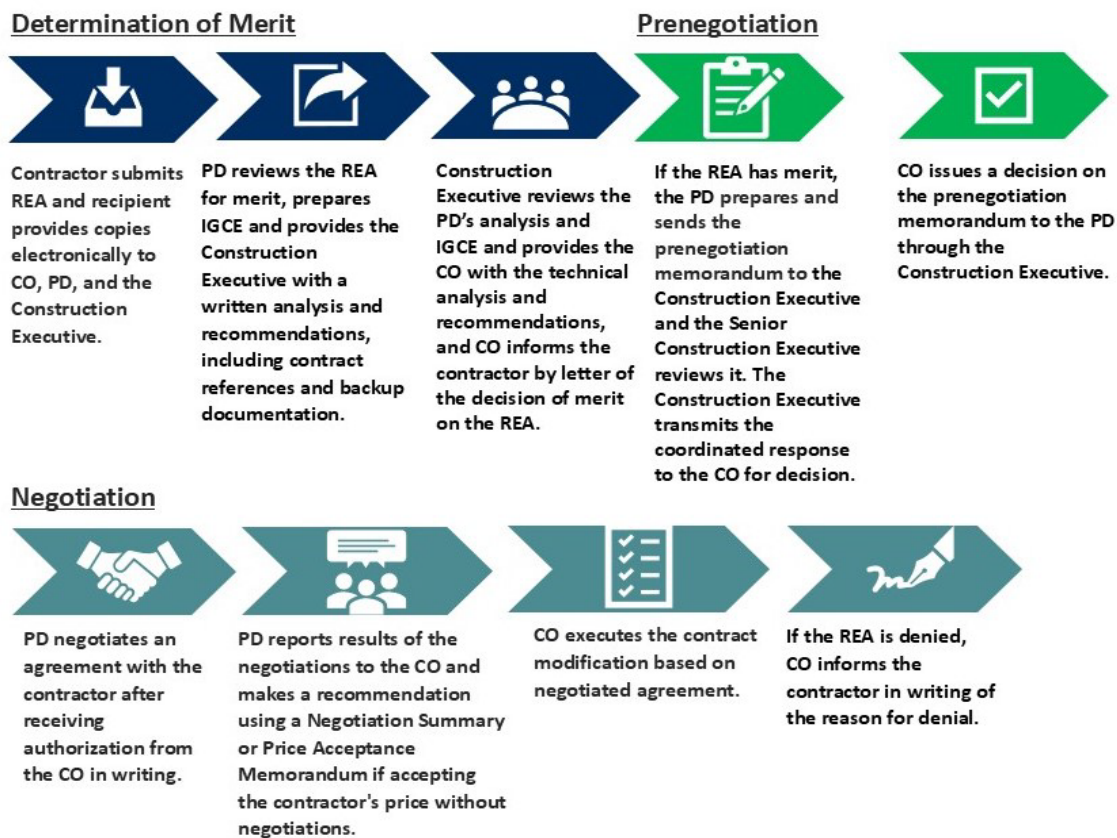
<sup>47</sup> OBO, "Construction Management Guidebook," 3.2.12.13(B)(8), page 3-56.

<sup>48</sup> Ibid.

<sup>49</sup> Ibid., 3.2.12.13(B)(9), page 3-56.

<sup>50</sup> Ibid., 3.2.12.13(B)(10), page 3-56.

**Figure 1: REA Process: Determination of Merit, Prenegotiation, and Negotiation Steps and Responsibilities**



Source: Generated by OIG using the OBO "Construction Management Guidebook."

**Contract Modifications**

During the life of a contract, it may become necessary to alter the contract terms to incorporate new requirements or resolve problems that develop after the contract has been awarded. In such cases, the CO must prepare and issue a contract modification.<sup>51</sup> A contract modification means any written change in the terms of a contract.<sup>52</sup> Only COs, acting within the scope of their authority, are empowered to execute contract modifications on behalf of the government.<sup>53</sup> Modifications to a contract affect the interests, rights, and obligations of the U.S. government and the contractor, and it is important for the CO to preserve the integrity of the relationship between these two parties. The CO reviews the action to determine whether it is consistent with the existing contract and to ensure that the equities of the existing relationship are preserved and will be continued when a modification is issued and

<sup>51</sup> 14 FAH-2 H-531(a), "General."

<sup>52</sup> FAR 2.101.

<sup>53</sup> FAR 43.102, "Policy."

negotiated.<sup>54</sup> The contract modification process advances from the PD, through the assigned Construction Executive,<sup>55</sup> to the CO.<sup>56</sup>

### ***Construction Projects and REAs Selected for Testing***

AQM reported that contracting officials coordinated REAs totaling \$418 million from October 1, 2020, through June 30, 2023, on overseas construction projects. OIG selected a sample of REAs associated with five OBO construction projects for review. The five construction contracts were for NEC Asuncion, Paraguay; NEC Beirut, Lebanon; NCC Hyderabad, India; NCC Lagos, Nigeria; and NEC Tegucigalpa, Honduras. Table 1 provides details on the five selected construction projects.<sup>57</sup>

**Table 1: Construction Projects Selected for Review**

<b>Construction Project</b>	<b>Contract</b>	<b>Contract Award Amount</b>	<b>Number of REAs Submitted</b>	<b>Amount of REAs Submitted</b>
NEC Asuncion	SAQMMA17C0082	\$165,823,000	115	\$12,363,443
NEC Beirut	SAQMMA17C0079	\$586,061,860	31	\$39,571,642
NCC Hyderabad	SAQMMA16C0274	\$203,114,000	29	\$11,773,568
NCC Lagos	19AQMM21C0156	\$319,027,389	7	\$13,564,440
NEC Tegucigalpa	19AQMM18C0223	\$244,544,274	98	\$14,534,201
<b>Total</b>		<b>\$1,518,570,523</b>	<b>280</b>	<b>\$91,807,294</b>

**Source:** OIG-generated based on data obtained from OBO and AQM.

### ***NEC Asuncion***

In January 2017, the Department awarded a \$165.8 million firm-fixed-price,<sup>58</sup> design-bid-build<sup>59</sup> contract (Contract SAQMMA17C0082) to Cadell Construction Co., LLC, (Cadell) for the construction of NEC Asuncion. The construction project included a chancery building, a U.S. Marine security guard residence, a support annex, a utility building, and parking. From October 1, 2020, through June 30, 2023, Caddell submitted 115 REAs valued at \$12,363,443. OIG reviewed seven of these REAs valued at \$6,847,781. The NEC Asuncion construction project was completed in December 2023. Figure 2 provides an exterior rendering of NEC Asuncion.

<sup>54</sup> 14 FAH-2 H-531(d).

<sup>55</sup> According to the OBO, "Construction Management Guidebook," 1.3.5.5, the Construction Executive is the responsible manager and point of contact once the project is awarded. The Construction Executive is accountable for all technical, administrative, and project budget matters for the project and reports directly to the Senior Construction Executive leading the responsible branch, page 1-17.

<sup>56</sup> OBO, "Construction Management Guidebook," Table 3.2-1, "Change Order Execution above PD's Authority/Warrant," page 3-60.

<sup>57</sup> Appendix A provides details on how the construction projects and REAs were selected for review.

<sup>58</sup> FAR 16.202-1, "Description," states that "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."

<sup>59</sup> FAR 36.102, "Definitions," defines design-bid-build as the traditional delivery method in which design and construction are sequential and contracted separately, with two contracts and two contractors.



**Figure 2:** Exterior rendering of NEC Asuncion.  
**Source:** OBO Project Fact Sheet.

### *NEC Beirut*

In June 2016, the Department awarded a \$586 million firm-fixed-price, design-bid-build contract (Contract SAQMMA17C0079) to B.L. Harbert International LLC (B.L. Harbert) for the construction of NEC Beirut. The complex included a chancery building, a U.S. Marine security guard residence, representational spaces, staff housing, facilities for the community, and associated support facilities. From October 1, 2020, through June 30, 2023, B.L. Harbert submitted 31 REAs valued at \$39,571,642. OIG reviewed eight of these REAs valued at \$5,523,698. The NEC Beirut construction project is scheduled to be completed in October 2025. Figure 3 provides an exterior rendering of NEC Beirut.



**Figure 3:** Exterior rendering of NEC Beirut.  
**Source:** OBO Project Fact Sheet.

### *NCC Hyderabad*

In September 2016, the Department awarded a \$203 million firm-fixed-price, design-build<sup>60</sup> contract (Contract SAQMMA16C0274) to Cadell for the construction of NCC Hyderabad. The compound included a new office building, a U.S. Marine security guard residence, an entry pavilion, a new support annex and warehouse, and a utility building. From October 1, 2020, through June 30, 2023, Caddell submitted 29 REAs valued at \$11,773,568. OIG reviewed four of

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<sup>60</sup> FAR 36.102 defines design-build as combining design and construction in a single contract with one contractor.

these REAs valued at \$1,130,463. The NCC Hyderabad construction project was completed in November 2022. Figure 4 provides an exterior rendering of NCC Hyderabad.



**Figure 4:** Exterior rendering of NCC Hyderabad.  
**Source:** OBO Project Fact Sheet.

### *NCC Lagos*

In September 2021, the Department awarded a \$319 million firm-fixed-price, design-build contract (Contract 19AQMM21C0156) to Pernix Federal, LLC, (Pernix) for the construction of NCC Lagos. The complex will include a consulate building, a U.S. Marine security guard residence, a warehouse, a utility building, a recreation facility, a staff parking garage, a pedestrian bridge, and a boat dock, as well as perimeter and site improvements. From October 1, 2020, through June 30, 2023, Pernix submitted seven REAs valued at \$13,564,440. OIG reviewed four of these REAs valued at \$4,713,630. The NCC Lagos construction project is scheduled to be completed in March 2027. Figure 5 provides an exterior rendering of NCC Lagos.



**Figure 5:** Exterior rendering of NCC Lagos.  
**Source:** OBO Project Fact Sheet.

### *NEC Tegucigalpa*

In September 2018, the Department awarded a \$244.5 million firm-fixed-price, design-bid-build contract (Contract 19AQMM18C0223) to B.L. Harbert for the construction of NEC Tegucigalpa. The complex will include a chancery building, a U.S. Marine security guard residence, a utility building, a warehouse, a support annex, community facilities, a parking structure, and other support buildings and site improvements. From October 1, 2020, through June 30, 2023, B.L. Harbert submitted 98 REAs valued at \$14,534,201. OIG reviewed seven of these REAs valued at

\$3,213,420. The NEC Tegucigalpa construction project is scheduled to be completed in November 2024. Figure 6 provides an exterior rendering of NEC Tegucigalpa.



**Figure 6:** Exterior rendering of NEC Tegucigalpa.  
**Source:** OBO Project Fact Sheet.

## AUDIT RESULTS

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### **Finding A: The Department Did Not Reach Equitable Adjustments in Accordance With Federal Requirements and Department Guidance**

OIG found that the Department's process to reach equitable adjustments with selected construction contractors did not fully comply with the FAR and Department guidance. Specifically, of the 30 REAs reviewed for this audit, OIG found 14 constructive changes made by PDs or other OBO officials. Constructive changes occurred when the government expressly or impliedly ordered work outside the scope of the contract. Moreover, these constructive changes led to REAs and ultimately resulted in unauthorized commitments that were not properly ratified.

In addition, OIG found that PDs and COs did not evaluate and resolve selected REAs in accordance with the FAR and Department guidance. Specifically, OIG found that PDs did not always comply with requirements to determine the merit of REAs, prepare sufficient IGCEs, prepare negotiation memoranda, receive CO authorization before beginning to negotiate, and perform required cost analyses. Additionally, OIG found that the Department allowed contractors to improperly use two different bases for indirect cost allocation and did not resolve REAs in a timely manner. These deficiencies occurred primarily because PDs and COs did not follow established policies and procedures for evaluating and resolving REAs. Additionally, OBO and AQM<sup>61</sup> had not developed and implemented a sufficient process to determine whether PDs and COs adhered to requirements. Finally, AQM did not have specific procedures for evaluating and resolving REAs, and the Department did not have sufficient guidance related to allocating overhead costs to construction projects. Until the Department

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<sup>61</sup> After the completion of audit fieldwork, the Bureau of Administration implemented a reorganization of its offices and realigned their acquisitions expertise within OPE under the Deputy Assistant Secretary for Global Acquisitions.

fully complies with REA requirements, it cannot be assured that REAs are settled in a fair and reasonable manner. As a result, OIG is questioning \$837,172 in unsupported costs and \$3,251,891 in unallowable costs associated with 18 of the 30 REAs OIG reviewed for this audit.

***Constructive Changes Led to REAs and Unauthorized Commitments***

According to the FAR, COs may, at any time, make changes in the work within the general scope of the contract via a change order.<sup>62</sup> The COR, however, “has no authority to make any commitments or changes that affect price, quality, quantity, delivery, or other terms and conditions of the contract nor in any way direct the contractor or its subcontractors to operate in conflict with the contract terms and conditions.”<sup>63</sup> “When a contractor performs work beyond the work required under the contract, but without a formal change order, and it is perceived that such work was informally ordered by the government or caused by fault on the part of the government, a constructive change can be found to have occurred.”<sup>64</sup>

Similarly, the FAH states that a “constructive change is a situation that can be construed as having the effect of a change order. A ‘constructive change’ arises when, by informal action or inaction by the U.S. government, the contractor’s situation is so altered that the effect is as though a change order had been issued.”<sup>65</sup> Similarly, the Department of State Acquisition Manual defines a constructive change as “oral or written communications, acts, or omissions by the CO or other authorized official that are construed as having the same effect as a written change order.”<sup>66</sup> Courts have held that a constructive change requires both the change component, or work outside the scope of the contract, and the order or fault component, which is the reason the contractor performed the work. For example, one court stated, “if the government either expressly or impliedly ordered work outside the scope of the contract, or if the government otherwise caused the contractor to incur additional work, a constructive change arises for that work performed outside of the scope of the contract.”<sup>67</sup> The Overseas Procurement Guide warns that “constructive changes are to be avoided. They are evidence of poor or inadequate administration of a contract. They consume administrative time that could better be spent on other matters, and they often cost the [g]overnment money.”<sup>68</sup>

Of the 30 REAs reviewed for this audit,<sup>69</sup> OIG found 14 constructive changes made by PDs or other OBO officials. In each instance, the PD or another OBO official provided oral or written communication to the contractor, and this was construed as having the same effect as a change

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<sup>62</sup> FAR 52.243-4(a), “Changes.”

<sup>63</sup> FAR 1.602-2(d)(5).

<sup>64</sup> *American Line Builders, Inc. v. United States*, 26 Cl. Ct. 1155, 1180 (1992).

<sup>65</sup> 14 FAH-2 H-535(a).

<sup>66</sup> “Department of State Acquisition Manual,” 643.103-80, “Constructive Changes,” page 162.

<sup>67</sup> *Miller Elevator Co. v. United States*, 30 Fed. Cl. 662, 678 (1994).

<sup>68</sup> OPE, “Overseas Procurement Guide,” Chapter 8, Section II, “Original Signed Contract and Modifications,” E, “Constructive Changes.”

<sup>69</sup> Appendix A provides details of the sample selected.

order. Subsequently, the contractors submitted REAs for these 14 constructive changes, and the Department paid the contractors for these constructive changes.

However, the changes made to the contract requirements were never submitted as a request for proposal (RFP).<sup>70</sup> Instead, PDs or other OBO officials allowed the contractors to proceed in accordance with OBO's direction and without requiring the CO to prepare and issue a contract modification before the work occurred.<sup>71</sup> The contractors then submitted REAs after completing the work, and the Department paid the contractors for these constructive changes. For example, for the NEC Tegucigalpa construction project, the contractor submitted a request for information (RFI)<sup>72</sup> asking if the government wanted to include fire protection-related monitoring, which was not included in the contract requirements. In response, the PD stated in writing that the monitoring would be "a benefit for facilities maintenance and we also recommend this be incorporated." For three other RFIs submitted by the contractor for the NEC Tegucigalpa construction project, the PD responded that an RFP would be issued, which demonstrates that the PD recognized the response changed the contract requirements and understood the process for approving changes to projects. However, the CO did not issue RFPs or execute a contract modification for these changes before the work occurred, as required. Eventually, the contractor completed the work as described in the written communication in the RFIs because the contractor construed OBO's responses to the RFIs as having the effect of a change order and submitted REAs for compensation. The Department subsequently paid the contractor for those constructive changes.

In another example, for the NCC Hyderabad construction project, the contractor submitted requests for design clarification to OBO requesting the review and clarification of proposed design changes. OBO responded in writing to the requests for design clarification, concurring with the contractor's proposed changes. The contractor construed OBO's responses to the requests for design clarification as having the effect of a change order and submitted REAs for the costs of the additional work. However, the CO did not issue an RFP or execute a contract modification for these changes to the contract before the work occurred. Nonetheless, the Department paid the contractor for those constructive changes.

Additionally, the PD for the NCC Lagos construction project verbally instructed the contractor to provide internet service for the OBO construction office because internet service could not be obtained through government channels. However, the contract did not include this requirement. Again, the CO did not issue an RFP or execute a contract modification for this change to the contract before the work occurred. As a result, the contractor submitted multiple

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<sup>70</sup> According to OBO's "Construction Management Guidebook," 3.2.12.11, "For a U.S. government-originated change, the Contractor is notified by the COR in writing of the requirement of a change and is issued RFP," page 3-52.

<sup>71</sup> According to FAR 43.102(b), contract modifications, including changes that could be issued unilaterally, shall be priced before their execution if this can be done without adversely affecting the interest of the government. If a significant cost increase could result from a contract modification, and time does not permit negotiation of a price, at least a ceiling price shall be negotiated unless impractical.

<sup>72</sup> An RFI is a process that allows the contractor to obtain clarification about project requirements or intent.

REAs for the internet service, and the Department paid the contractor for those constructive changes.

#### *Lack of Oversight Caused Identified Issues*

One reason for the deficiencies identified was improper adherence to Department policy by PDs. In some cases, COs and PDs did not issue an RFP to a contractor when the government found it necessary to change contract requirements. In addition, OIG found that COs did not sufficiently review documents related to constructive changes. For example, a contractor for one project provided the PD with RFIs on various issues. The RFIs were added to ProjNet,<sup>73</sup> to which the CO had access. However, the CO was not able to demonstrate that they followed up on the RFIs to ensure that contractor requests were addressed in accordance with FAM requirements.

A contributing factor was the lack of a formalized process for COs to monitor PDs' actions when resolving issues to prevent constructive changes. According to the FAR, "[COs] are responsible for ensuring performance of all necessary actions for effective contracting, ensuring compliance with the terms of the contract, and safeguarding the interests of the United States in its contractual relationships."<sup>74</sup> However, OIG did not find evidence that the COs responsible for the selected projects questioned why the constructive changes occurred. Additionally, the COs should have determined whether the responsible PDs had knowingly or inadvertently created the constructive change by their actions. Furthermore, OBO management did not sufficiently oversee situations in which constructive changes occurred. Lastly, OIG found that the OBO management officials did not hold the PDs accountable for their actions that led to constructive changes.

#### *Constructive Changes Led to REAs*

Because of the constructive changes that occurred, contractors submitted REAs to cover increased costs related to construction activities. Reacting to contractor-submitted REAs resulting from constructive changes prevents the government from forward pricing the work and limits the government's ability to lessen schedule impacts and negotiate costs because the contractor has already performed the work.

#### *Constructive Changes Led to Unauthorized Commitments*

According to the FAR, "an unauthorized commitment is an agreement that is not binding solely because the government representative who made it lacked the authority to enter into that agreement on behalf of the government."<sup>75</sup> As noted previously, the FAR also states that "the COR has no authority to make any commitments or changes that affect price, quality, quantity, delivery, or other terms and conditions of the contract nor in any way direct the contractor or

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<sup>73</sup> According to the Foreign Affairs Manual (15 FAM 661.8), ProjNet is a web service that allows the secure exchange of design and construction information among project stakeholders.

<sup>74</sup> FAR 1.602-2.

<sup>75</sup> FAR 1.602-3(a), "Ratification of unauthorized commitments."

its subcontractors to operate in conflict with the contract terms and conditions.”<sup>76</sup> In addition, each delegation memorandum to CORs reviewed for this audit emphasized that the COR is prohibited from approving any actions that would result in additional charges to the U.S. government. Nonetheless, OIG identified 14 constructive changes that resulted in unauthorized commitments because the changes affected the contract price without the approval of the CO. As the U.S. government’s authorized agent for working with contractors, the CO has sole authority to solicit proposals and negotiate, award, administer, modify, or terminate contracts.<sup>77</sup> Table 2 provides the executed amount for each REA related to the identified constructive changes that resulted in unauthorized commitments.

**Table 2: Cost of Constructive Changes Resulting in Unauthorized Commitments**

Construction Project	REA	Award Amount <sup>a</sup>	Project Sub-Total
NEC Asuncion <sup>b</sup>	REA 080	\$128,590	\$197,542
	REA 121	\$68,952	
NEC Beirut	REA 052	\$75,285	\$75,285
	REA 003	\$725,509	
NCC Hyderabad	REA 019	\$77,404	\$938,077
	REA 027	\$107,170	
	REA 030	\$27,994	
NCC Lagos	REA 005	\$8,655 <sup>c</sup>	\$8,655
	REA 026	\$138,192	
NEC Tegucigalpa	REA 027	\$168,478	\$1,203,852
	REA 028	\$106,990	
	REA 043	\$291,516	
	REA 047	\$396,663	
	REA 085	\$102,013	
<b>Total</b>			<b>\$2,423,411</b>

<sup>a</sup> Award amount is the total amount awarded to the contractor for the REA based on contract modifications.

<sup>b</sup> The PD for the NEC Asuncion project had a \$25,000 CO warrant; which would provide the authority to make changes within that limit. However, the award amounts for REA 080 and REA 121 exceeded that limit.

<sup>c</sup> REA 005 was submitted by the contractor for reimbursement of monthly internet service for the on-site OBO office for the duration of the project. The Department subsequently awarded a contract modification for a lower amount for the reimbursement of the internet services.

**Source:** OIG-generated based on data obtained from OBO and AQM.

### Unauthorized Commitments Were Not Ratified as Required

According to the Department of State Acquisition Regulation, “All [Department] unauthorized commitments in excess of \$1,000 shall be submitted to the [Department] Procurement

<sup>76</sup> FAR 1.602-2(d)(5).

<sup>77</sup> 14 FAH-2 H-141(a).

Executive for ratification.”<sup>78</sup> According to the FAR, “ratification” is the act of approving an unauthorized commitment by an official who has the authority to do so.<sup>79</sup> However, an AQM management official stated that none of the unauthorized commitments identified by OIG were submitted to the Procurement Executive for ratification. Thus, the COs executed contract modifications in violation of the FAR and Department policy.

To address the deficiencies identified with the constructive changes, which led to REAs and ultimately resulted in unauthorized commitments that were not properly ratified, OIG is offering the following recommendations.

**Recommendation 1:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, update the Foreign Affairs Handbook (14 FAH-2 H-535) to include guidance on how to avoid improper technical direction that could initiate a constructive change for construction contracts. At a minimum, the update should include guidance on reviewing requests for information and other methods of communication to contractors.

**Management Response:** The Bureau of Administration did not concur with the recommendation, stating that it is “developing a COR Handbook that will become a stand-alone document separate from the FAH.” The bureau’s response also stated that “the inclusion of construction information may be too specific for an overall guidance document that addresses the Department’s worldwide portfolio of commodities and services.”

**OIG Reply:** On the basis of the Bureau of Administration’s nonconcurrence with the recommendation, OIG considers this recommendation unresolved and will pursue resolution of the recommendation during the audit compliance process. Specifically, the recommendation will be considered resolved when the Bureau of Administration provides a plan of action for addressing the recommendation or provides an acceptable alternative that fulfills the intent of the recommendation. This recommendation will be closed when OIG receives documentation demonstrating that the Bureau of Administration, in coordination with OBO, has developed and implemented guidance on how to avoid improper technical direction that would initiate a constructive change for construction contracts.

**Recommendation 2:** OIG recommends that the Bureau of Overseas Buildings Operations develop and communicate a Construction Alert reminding Project Directors and Construction Executives to review and follow the guidelines detailed in the Foreign Affairs Handbook (14 FAH-2 H-535) regarding preventing constructive changes to contracts.

**Management Response:** OBO stated that it would concur with the recommendation if OIG removed “regarding preventing constructive changes to the contract.” OBO also stated that

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<sup>78</sup> Department of State Acquisition Regulation, 601.602-3(b)(2)(ii), “Ratification of unauthorized commitments.”

<sup>79</sup> FAR 1.602-3(a).

it will develop and communicate a Construction Alert reminding PDs and Construction Executives to follow 14 FAH-2 H-535.

**OIG Reply:** OIG did not modify the recommendation as requested by OBO because the FAH section cited in the recommendation relates to constructive changes, including how to avoid them. Therefore, removing the phrase “regarding preventing constructive changes” alters the intent of the recommendation. In addition, although OBO stated that it did not concur with the recommendation language, it stated that it planned to implement the recommendation. Therefore, on the basis of OBO’s planned actions, OIG considers this recommendation resolved, pending further action. This recommendation will be closed when OIG receives documentation demonstrating that OBO has developed and communicated a Construction Alert reminding PDs and Construction Executives to review and follow the guidelines detailed in 14 FAH-2 H-535.

**Recommendation 3:** OIG recommends that the Bureau of Overseas Buildings Operations (OBO), in coordination with the Bureau of Administration, develop and implement a process for management to review and monitor documents referenced in contractor requests for equitable adjustment, such as requests for information and requests for design clarification, to identify improper technical direction initiated by Project Directors or other OBO personnel.

**Management Response:** OBO did not concur with the recommendation, stating that the Department has a process to review and monitor documents to identify improper technical direction prior to responding to an RFI. Furthermore, OBO stated that it “has a different fundamental understanding of what constitutes ‘improper technical direction’” than OIG. Based on its own definition, OBO does not believe that OIG presented findings that OBO failed to identify improper technical direction. In addition, OBO disagreed that ratification of technical direction is needed, “as this would create a chilling effect to make any response by a COR that ‘could’ be referenced in a subsequent modification.” According to OBO, this would also “undermine the delegations and limits on authority set forth in the FAR.” OBO stated that it would work with the Bureau of Administration and the Department’s Office of the Legal Adviser to reinforce the current contractual language on the limitations of COR authority.

**OIG Reply:** OIG’s finding related to constructive changes used the FAR, ASBCA cases, and Department policy as authoritative criteria. OBO should be using the same criteria for identifying constructive changes. Finding A of this report provides details of some of the constructive changes that OIG identified during the audit. For example, a contractor submitted an RFI asking if the government wanted to include fire protection monitoring, which was not included in the contract. In response, the PD stated in writing that the monitoring would be a benefit and recommended it be incorporated. The contractor construed the PD’s response as having the effect of a change order and submitted an REA for compensation. The Department subsequently paid the contractor for the constructive change. OBO did not provide any documentation to contradict the findings in this report.

Additionally, as noted in the finding, the Department of State Acquisition Regulation and FAR require unauthorized commitments to be ratified by someone authorized to approve contractual changes. An experienced PD should recognize the difference between valid technical direction and communication that would lead to an unauthorized commitment. Therefore, recommending that OBO comply with federal and Department guidance should not have a “chilling effect” on PDs’ ability to perform their duties. The recommendation also would not “undermine” delegations established in the FAR because OIG is recommending compliance with FAR requirements.

On the basis of OBO’s nonconcurrence with the recommendation, OIG considers this recommendation unresolved and will seek resolution during the audit compliance process. The recommendation will be considered resolved when OBO provides a plan of action for addressing the recommendation or provides an acceptable alternative that fulfills the intent of the recommendation. This recommendation will be closed when OIG receives documentation demonstrating that OBO, in coordination with the Bureau of Administration, has developed and implemented a process for management to review and monitor documents referenced in contractor REAs, such as RFIs and requests for design clarification, to identify improper technical direction initiated by PDs or other OBO personnel.

**Recommendation 4:** OIG recommends that the Bureau of Administration develop and implement a communications strategy to direct Contracting Officers to review requests for equitable adjustment for unauthorized commitments and to resolve unauthorized commitments in accordance with the ratification process.

**Management Response:** The Bureau of Administration did not concur with the recommendation, stating that “the current process of reviewing [REAs] already inherently adjudicates any perceived commitments and anything that is not to be authorized would not be approved as part of the equitable adjustment.” The Bureau of Administration also stated that the “contract states that, if the contractor does any such work without the proper direction of the CO, they are doing the work at their own risk.” Furthermore, the Bureau of Administration stated that adding the ratification process to existing procedures and controls would “inhibit the Department from following timelines” prescribed by the FAR.

**OIG Reply:** The Bureau of Administration did not demonstrate during the audit that it reviewed and adjudicated the unauthorized commitments identified in Finding A of this report. Although OBO’s contracts include language related to the contractor accepting risk for performing work that is not included in the contract, OIG found that the Department generally approved the REAs reviewed for this audit after a constructive change occurred. Additionally, the ratification process is required by the Department of State Acquisition Regulation and the FAR, so it would not inhibit the Department’s efforts to comply with the FAR.

On the basis of the Bureau of Administration’s nonconcurrence with the recommendation, OIG considers this recommendation unresolved. The recommendation will be considered

resolved when the Bureau of Administration provides a plan of action for addressing the recommendation or provides an acceptable alternative that fulfills the intent of the recommendation. This recommendation will be closed when OIG receives documentation demonstrating that the Bureau of Administration has developed and implemented a communications strategy to direct COs to review REAs for unauthorized commitments and to resolve unauthorized commitments in accordance with the ratification process.

### ***Evaluation and Resolution of REAs***

OIG found that PDs and COs did not evaluate and resolve the REAs reviewed for this audit in accordance with the FAR and Department guidance. Specifically, OIG found that PDs did not always comply with requirements to determine the merit of REAs, prepare sufficient IGCEs, prepare negotiation memoranda, receive CO authorization before beginning negotiations, or perform required cost analyses. Additionally, OIG found that the Department allowed contractors to improperly use two different bases for indirect cost allocation and did not resolve REAs in a timely manner.

#### ***PDs Did Not Always Perform Required Merit Determination Activities***

According to the OBO Construction Management Guidebook, after receiving all necessary documents to analyze the REA, the PD should provide the Construction Executive with a written analysis and recommendations about the merit of the REA. The written analysis should include contract references and backup documentation.<sup>80</sup> The Construction Executive is responsible for reviewing the PD's analysis and transmitting it to the CO for decision.<sup>81</sup>

OIG found that PDs did not always comply with the requirements outlined in the OBO Construction Management Guidebook to determine the merit of REAs. PDs interviewed for this audit stated that they included their analyses and recommendations related to REAs in a "Findings of Fact" document, which they included in prenegotiation memoranda sent to COs. Therefore, OIG reviewed the prenegotiation memoranda for the 30 REAs selected for testing<sup>82</sup> to determine if the document included a written analysis of the REA, a recommendation about the merit of the REA, contract references, and backup documentation. Based on its review, OIG determined that PDs serving as CORs did not perform all required merit determination activities for 25 of 30 (83 percent) of the REAs selected for testing.

For example, for REA 027,<sup>83</sup> the PD prepared a 1-page price acceptance memorandum that included a 1-sentence description of the REA. Specifically, the memorandum stated that the contractor installed shading canopies where needed. No other information was included, and no backup documentation was provided to assist management in making a merit

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<sup>80</sup> OBO, "Construction Management Guidebook," 3.2.12.13(B)(5), page 3-56.

<sup>81</sup> Ibid., 3.2.12.14, page 3-59.

<sup>82</sup> Appendix A provides details of the sample selected.

<sup>83</sup> REA 027 was submitted by the contractor for the NCC Hyderabad construction project.

determination. Even though detailed information on the REA was not provided, the CO approved the REA valued at \$107,170.

In another example, for REA 059,<sup>84</sup> the PD prepared a 1-page prenegotiation memorandum that included a brief description of the REA. Specifically, the memorandum stated that the REA was for “low-water surcharges.”<sup>85</sup> No other information was included, and no backup documentation was provided. Even though detailed information was not provided, the CO approved the REA valued at \$80,071. The REA was approved even though the contract, which was firm-fixed price, stated that “the contractor is responsible for paying all charges incurred in obtaining materials that must be imported for the project and in transporting the materials to the construction site.” 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. That contract type places upon the contractor the full responsibility for all costs and resulting profit or loss.<sup>86</sup>

In a third example, for REA 080,<sup>87</sup> the PD submitted a 1-page prenegotiation memorandum that included a 1-sentence description of the REA. Specifically, the memorandum stated that the REA was for signage size changes and language translations. No other information was included, and no backup documentation was provided. Even though detailed information was not provided, the CO approved the REA valued at \$128,590.

#### *PDs Did Not Always Prepare Sufficient IGCEs*

Proper development of IGCEs is an important part of the REA evaluation process. According to the FAH, an IGCE is the U.S. government's estimated cost or price of the proposed acquisition. In addition, IGCEs serve as a basis for comparing costs or prices proposed by offerors and as an objective basis for determining price reasonableness.<sup>88</sup> According to the Overseas Procurement Guide, the government must prepare an IGCE for proposed contract modifications and assess any time extension that may be justified, and the estimate must be detailed enough to permit a cost analysis of the contractor's proposal.<sup>89</sup> For construction contracts, the FAR<sup>90</sup> requires an IGCE for each contract modification anticipated to exceed the simplified acquisition threshold.<sup>91</sup> OBO guidance requires an IGCE for construction contract modifications that exceed \$25,000.<sup>92</sup>

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<sup>84</sup> REA 059 was submitted by the contractor for the NEC Asuncion construction project.

<sup>85</sup> The contractor claimed in its REA that it was unable to transport material using a barge because of low water levels on a nearby river. Therefore, the contractor changed the mode of transportation to overland transport and claimed the additional costs for shipments.

<sup>86</sup> FAR 16.202-1.

<sup>87</sup> REA 080 was submitted by the contractor for the NEC Asuncion construction project.

<sup>88</sup> 14 FAH-2 H-351(a).

<sup>89</sup> OPE, “Overseas Procurement Guide,” Chapter 8, “Contract Modification/Contract Closeout,” Section VI, “Backup Supporting Contract Modifications/Delivery Orders/Task Orders,” C, “Pricing of Adjustments.”

<sup>90</sup> FAR 36.203(a).

<sup>91</sup> The simplified acquisition threshold is \$250,000.

<sup>92</sup> OBO, “Construction Management Guidebook,” 3.2.12.8, page 3-50.

OBO officials were required to prepare an ICGE for 19 of 30 REAs selected for review.<sup>93</sup> OIG found that OBO officials did not prepare IGCEs for 5 of 20 (26 percent) REAs. In addition, 11 of 14 (79 percent) of the IGCEs prepared by OBO did not sufficiently demonstrate they were independent estimates. For example, two of the IGCEs reviewed for the NEC Asuncion project included the exact amount of the contractor's proposed direct costs. Similarly, one of the IGCEs reviewed for the NEC Beirut project attached the contractor's REA pricing to the spreadsheet used by the Department to develop the IGCE.<sup>94</sup>

*PDs Did Not Always Prepare Negotiation Memoranda or Receive CO Authorization Before Negotiation Occurred*

According to the OBO Construction Management Guidebook, the PD must prepare and send the prenegotiation memorandum to the CO for approval, via the Construction Executive. In addition, the OBO Construction Management Guidebook states that "if the REA has merit, the CO will negotiate the cost with the [c]ontractor (or authorize PD/COR in writing to negotiate on their behalf)." Furthermore, the PD must negotiate only after receiving the authorization by the CO in writing. The PD must send a record of the negotiation memorandum to the CO with the result of the negotiations.<sup>95</sup> Lastly, the FAR states that the CO shall establish prenegotiation objectives before the negotiation of any pricing action.<sup>96</sup>

Of the 30 REAs selected for review,<sup>97</sup> 11 were negotiated.<sup>98</sup> However, OIG found that PDs either did not prepare the required prenegotiation memoranda before beginning negotiations or did not obtain CO authorization in writing for any of those 11 REAs. Specifically, prenegotiation memoranda were not prepared for 8 of 11 (73 percent) REAs that were negotiated. Furthermore, the three prenegotiation memoranda that were prepared were not signed by the CO prior to negotiations as required. In these 11 instances, the PD started negotiations either prior to developing a prenegotiation memorandum or prior to the CO approving that memorandum to authorize the PD to negotiate on the CO's behalf. For example, for REA 019, OBO staff started negotiations with the contractor the day after receiving the REA, prior to

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<sup>93</sup> Six of the selected REAs were each less than \$25,000, which means that OBO officials were not required to prepare IGCEs. Additionally, OBO rejected four REAs, which eliminated the need for negotiations; therefore, IGCEs were not prepared.

<sup>94</sup> A similar issue was reported in the OIG report, *Audit of Select Contract Administration Processes Related to the Construction of New Embassy Compound Mexico City* (AUD-CGI-24-09, January 2024), page 17. OIG included a recommendation in that report (Recommendation 2) intended to address this issue. As of December 2024, that recommendation is unresolved. Because the recommendation remains unresolved, OIG is not including additional recommendations in this report related to this issue.

<sup>95</sup> OBO, "Construction Management Guidebook," 3.2.12.13(B)(8), page 3-56.

<sup>96</sup> FAR 15.406-1(b).

<sup>97</sup> Appendix A provides details of the sample selected.

<sup>98</sup> Negotiations were not conducted for 19 of 30 REAs selected for review. According to OBO's "P&PD Cost 01: Cost Estimate Preparation and Review," page 4, "contractor prices within 10 percent of the [IGCE] are considered reasonable." PDs agreed that they complied with this guidance and did not conduct formal negotiations when the amount of the REA was within 10 percent of the IGCE. Additionally, OBO rejected four REAs before the negotiation phase.

developing a prenegotiation memorandum or obtaining authorization from the CO to negotiate on their behalf.

*PDs Did Not Perform Required Cost Analyses*

The FAR defines cost analysis as “the review and evaluation of any separate cost elements and profit or fee in an offeror’s or contractor’s proposal, as needed to determine a fair and reasonable price.”<sup>99</sup> A cost analysis would be required for REAs. The OBO Construction Management Guidebook requires OBO officials to perform a cost analysis to address each cost element and fee.<sup>100</sup> The government can use various cost analysis techniques, including verification of cost data or pricing data, to determine the necessity and reasonableness of proposed costs.<sup>101</sup> Additionally, the government can compare the costs proposed by the contractor for individual cost elements with the IGCE.<sup>102</sup>

For 15 of 30 (50 percent) REAs selected for review, OIG found that PDs did not properly evaluate all costs submitted by contractors to determine the necessity, or the possible duplication, of costs. For example, for the NEC Asuncion project, the contractor submitted REA 059 to request compensation for costs related to changing the manner in which material was transported to the jobsite (e.g., shipping, surcharges, and marine insurance). The contractor selected the original mode of material transportation to the jobsite and the contract was a firm-fixed price contract that stated, “the contractor is responsible for paying all charges incurred in obtaining materials that must be imported for the project and in transporting the materials to the construction site.” Therefore, the PD should have questioned the contractor’s additional shipping costs in the REA. Moreover, the contractor included marine insurance in the REA despite electing to use overland transport for the materials to the jobsite.

OIG also found that OBO officials did not always properly assess the necessity of items approved in the contract that would normally be included in overhead costs.<sup>103</sup> Nine of 30 (30 percent) REA proposals reviewed for this audit included costs that were related to overhead (e.g., small tools, expendables, and supervision). These contracts included a field overhead rate. The Department did not provide documentation demonstrating that the responsible PDs or COs determined whether those costs were contractually covered by the contractor’s field overhead rate. Additionally, OIG found that seven REAs related to the NEC Beirut project included a request for reimbursement for preparing the REA. However, the PD did not verify that REA preparation costs were necessary, and the Department did not provide documentation demonstrating that the PD decided the cost was justified.

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<sup>99</sup> FAR 15.404-1(c)(1), “Proposal Analysis Techniques.”

<sup>100</sup> OBO, “Construction Management Guidebook,” 3.2.12.15, “Execution of Change,” page 3-62.

<sup>101</sup> FAR 15.404-1(c)(2).

<sup>102</sup> FAR 15.404-1(c)(2)(iii).

<sup>103</sup> Overhead costs, also known as indirect costs, are those costs that are not directly related to the production of a product or service. These include costs such as rent, utilities, administrative costs and salaries, and insurance.

The Department had an independent external auditor review the contractor's indirect<sup>104</sup> (overhead) rates for the NEC Asuncion project.<sup>105</sup> The independent external auditor found that the contractor's detailed cost breakdown for previous modifications contained overlapping costs, including labor supervision,<sup>106</sup> totaling \$417,895. This finding resulted in a government credit for that amount and a reduction of various rates. However, OIG identified other cost elements in this audit that should have been reviewed for necessity and possible cost duplication, as shown in Table 3.

**Table 3: Cost Elements Not Evaluated by Project Directors**

Construction Project	REA Number	Small Tools	Expendables	Other Costs	Subtotal
NEC Asuncion	059			\$80,071	<b>\$80,113</b>
	121			\$42 <sup>a</sup>	
NEC Beirut	052	\$328	\$585	\$270 <sup>b</sup>	<b>\$5,887</b>
	082			\$90 <sup>b</sup>	
	083			\$360 <sup>b</sup>	
	084			\$2,700 <sup>b</sup>	
	085			\$90 <sup>b</sup>	
	086			\$900 <sup>b</sup>	
	088	\$258	\$36	270 <sup>b</sup>	
	026	\$243	\$1,060		
NEC Tegucigalpa	027	\$160	\$1,240		<b>\$25,663</b>
	028	\$636	\$837		
	043	\$852	\$2,369		
	047	\$15,182	\$1,936		
	085	\$1,043	\$105		
<b>TOTAL</b>		<b>\$18,444</b>	<b>\$15,204</b>	<b>\$84,365</b>	<b>\$111,663</b>

<sup>a</sup> Labor supervision costs.

<sup>b</sup> REA preparation costs that were not charged on other projects.

**Source:** OIG-generated based on data obtained from OBO and AQM.

By not properly evaluating each cost submitted by contractors to determine its necessity and avoid the duplication of costs, the government potentially paid for unnecessary services or duplicated payments of overhead costs. Consequently, OIG considers the costs for REA 059 and the labor supervision costs for REA 121 for the NEC Asuncion project to be unsupported costs totaling \$80,113. In addition, OIG considers all small tools, expendables, and REA preparation costs for the REAs tested for the NEC Beirut project to be unsupported costs totaling \$5,887.

<sup>104</sup> The terms indirect and overhead were used interchangeably in documents provided by OBO and AQM.

<sup>105</sup> Five of seven NEC Asuncion REAs reviewed during this audit were resolved prior to the independent external auditor's review.

<sup>106</sup> The Department allowed the contractor to continue to charge the labor supervision rate, although the consultant identified an overlap with other cost elements, without providing any justification.

Furthermore, OIG considers all small tools and expendable costs for the REAs tested for the NEC Tegucigalpa project to be unsupported costs totaling \$25,663.

### Contractors Were Allowed To Use Two Bases for Allocating Overhead

According to the FAR, contractors must choose one accounting method for allocating overhead costs and apply it consistently.<sup>107</sup> A contractor may choose any acceptable distribution base for allocating its jobsite overhead pool to particular cost objectives, but no more than one.<sup>108</sup> For instance, the contractor can select either a *per diem rate*, where overhead would be treated as a direct cost and applied as a set price per day; for example, \$19,000 per day for each day of delay. Alternatively, the contractor can apply a *percentage rate* to all direct costs associated with a change. For example, 3 percent of direct costs for allocating its jobsite overhead pool to particular cost objectives.

For construction contracts, the FAR states that costs incurred at the jobsite incident to performing the work are allowable as direct<sup>109</sup> or indirect costs,<sup>110</sup> provided the accounting method used is in accordance with the contractor's established and consistently followed cost accounting practices for all work.<sup>111</sup> Thus, a contractor may choose any acceptable distribution base (e.g., per diem rate or percentage of direct costs) for allocating its jobsite overhead pool to particular cost objectives, but no more than one. Allowing contractors to use two methods to allocate overhead costs could result in double recovery of those overhead costs. This violation would impact all contract modifications regardless of the process that led to the modification, including those approved through the RFP process.

Other government agencies and contractors have turned to the Armed Services Board of Contract Appeals (ASBCA)<sup>112</sup> regarding accounting practices to allocate indirect costs. For example, in 1998, the ASBCA held that a contractor's practice of switching between a time distribution base (per diem rate) and a direct cost distribution base (percentage of direct costs) for allocating jobsite overhead costs to changes violated the FAR requirement for a single overhead distribution base.<sup>113</sup> The decision was reaffirmed in two similar opinions in 1999<sup>114</sup>

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<sup>107</sup> FAR 31.105(d)(3), "Construction and Architect-Engineer Contracts."

<sup>108</sup> M.A. Mortenson Co., ASBCA No. 40750 et al., 98-1 BCA paragraph 29,658, 146,946 (Senior Deciding Group).

<sup>109</sup> FAR 2.101 states that direct cost means any cost that is identified specifically with a particular final cost objective. Direct costs are not limited to items that are incorporated in the end product as material or labor. Costs identified specifically with a contract are direct costs of that contract.

<sup>110</sup> FAR 2.101 states that indirect cost means any cost not directly identified with a single final cost objective but identified with two or more final cost objectives or with at least one intermediate cost objective.

<sup>111</sup> FAR 31.105(d)(3).

<sup>112</sup> The ASBCA hears and decides post-award contract disputes between contractors and certain government agencies, including the Department of Defense. The ASBCA functions under the Contract Disputes Act (41 United States Code §§ 7101-7109).

<sup>113</sup> M.A. Mortenson Co., ASBCA No. 40750 et al., 98-1 BCA paragraph 29,658, 146,946 (Senior Deciding Group).

<sup>114</sup> Caddell Construction Co., Inc., ASBCA No. 49333, 2000-1 BCA paragraph 30,702.

and 2022.<sup>115</sup> Specifically, in the 2022 opinion, the ASBCA stated, “The plain language of our holding in *Mortenson*, however, does not allow recovering [Field Office Overhead] on a percentage basis in [modifications] and per diem basis in an REA any more than it allows switching between the two distribution bases from [modification to modification]. This is reflective of FAR 31.203(d), which states ‘[o]nce an appropriate base for allocating indirect costs has been accepted, the contractor shall not fragment the base by removing individual elements.’”<sup>116</sup>

OIG found that the Department allowed contractors to use two different bases for allocating jobsite overhead costs in violation of the cost principle requirements of the FAR.<sup>117</sup> Specifically, for the NEC Beirut and NEC Tegucigalpa construction projects, the Department allowed contractors to charge jobsite or field office costs using two different methods. The contractor used a per diem method for modifications that extended the contract’s time of performance and a percentage of direct costs method for modifications that did not extend the time of performance.

For example, for the NEC Beirut project, the contractor allocated indirect costs as a percentage of direct costs if the REA did not include an extension of time. However, for REA 081, the contractor requested to allocate overhead costs at a per diem rate of \$119,742 for 51 compensable days, totaling \$6,003,323.<sup>118</sup> Ultimately, the CO executed a contract modification “to pay the contractor for half of the proposal amount and approve the [period of performance] extension of 51 days” for REA 081 in the amount of \$3,066,045. OIG noted similar actions for other NEC Beirut REAs.

Similarly, for the NEC Tegucigalpa project, the contract included a provision to establish field office overhead using a proposed allocation rate of 22 percent of direct costs. However, the contractor also proposed that, for a change involving a time impact attributable to the government, equitable adjustment would include an allocation of indirect costs charged daily. Table 4 shows costs questioned by OIG because contractors used two methods to allocate their overhead costs.

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<sup>115</sup> *Pave-Tech Inc.*, ASBCA No. 61879, 2022 ASBCA LEXIS 20 (March 23, 2022).

<sup>116</sup> FAR 31.203, “Indirect Costs.”

<sup>117</sup> Although this issue was identified during a review of select REAs, other modifications to the related contracts would also be impacted. Therefore, OIG’s recommendations related to this topic include any modifications to the related contracts.

<sup>118</sup> A September 30, 2020, letter from the contractor for the REA requested \$6,003,323; however, an email from the contractor on December 14, 2021, requested \$6,132,089.

**Table 4: NEC Beirut and NEC Tegucigalpa Overhead Costs Questioned by OIG**

Construction Project	Per Diem Rate	Percentage of Direct Costs	Total
<b>NEC Beirut</b>			
REA 052		\$9,905	
REA 081	\$3,066,045		
REA 088		\$2,221	
<b>Subtotal</b>			<b>\$3,078,171</b>
<b>NEC Tegucigalpa</b>			
REA 026		\$20,323	
REA 027		\$24,776	
REA 028		\$15,734	
REA 043		\$41,646	
REA 047		\$56,667	
REA 085		\$14,574	
<b>Subtotal</b>			<b>\$173,720</b>
<b>Total</b>			<b>\$3,251,891</b>

Source: OIG-generated based on data obtained from OBO and AQM.

Allowing contractors to use two methods to allocate overhead costs could result in double recovery of those overhead costs. As a result, OIG considers \$3,078,171 to be questioned (i.e., unallowable) costs for the NEC Beirut project. In addition, OIG considers all jobsite overhead costs for the REAs tested for the NEC Tegucigalpa project, totaling \$173,720, to be questioned (i.e. unallowable) costs.

#### ***Department Did Not Resolve REAs in a Timely Manner***

According to the OBO Construction Management Guidebook, OBO's goal is to resolve REAs within 90 days.<sup>119</sup> The Guidebook also states that the CO will issue a contract modification within 30 days after completion of the REA negotiations.<sup>120</sup> However, OIG found that 20 of 30 (67 percent) of the REAs selected for testing were not evaluated and resolved within OBO's 90-day goal. Specifically, the timeframe for resolving (i.e., from REA submission through issuance of the applicable contract modification) these 20 REAs ranged from 96 to 869 days. Table 5 shows the elapsed days until resolution for each REA tested.

<sup>119</sup> OBO, "Construction Management Guidebook," 3.2.12.13, page 3-55.

<sup>120</sup> Ibid., 3.2.12.13(B)(9), page 3-56.

**Table 5: Days Elapsed Between REA Submission and Contract Modification**

<b>Construction Project</b>	<b>REA</b>	<b>Elapsed Days</b>
NEC Asuncion	REA 059	98
	REA 062	869
	REA 065	75
	REA 080	86
	REA 102	127
	REA 107	83
	REA 121	359
NEC Beirut	REA 052	805
	REA 081	699
	REA 082	651
	REA 083	68
	REA 084	82
	REA 085	96
	REA 086	65
	REA 088	63
NCC Hyderabad	REA 003	601
	REA 019	125
	REA 027	164
NCC Lagos	REA 030	133
	REA 001	293
	REA 002	34
	REA 004	101
	REA 005	270
NEC Tegucigalpa	REA 026	166
	REA 027	154
	REA 028	154
	REA 043	153
	REA 047	358
	REA 068	42
	REA 085	56

**Source:** OIG-generated based on data obtained from OBO and AQM.

By delaying the resolution of the additional time requested by the contractor, the government made it difficult to determine what actions impacted the change and what time was owed for each specific change. OIG found that delays in the REA resolution process complicated decision making, especially at the end of the process. For example, for REA 003 for the NCC Hyderabad project, the original PD assigned to the construction project questioned the merit of the REA in a letter to the contractor and requested additional information to review the merit of the REA. However, no additional actions were taken by the PD or the contractor to resolve the REA for

509 days, until a new OBO Construction Manager arrived at the construction site.<sup>121</sup> The new Construction Manager commenced negotiations with the contractor without the CO confirming the merit of the REA. The CO ultimately awarded a \$725,509 contract modification 601 days after the REA was submitted, even though the concerns regarding the merit of the REA noted in the original letter from the PD had not been addressed. Because the initial merit questions were never addressed, OIG is questioning the unsupported costs of \$725,509 for this contract modification.

### ***Causes of the Deficiencies Identified***

According to the *Standards for Internal Control in the Federal Government*, management should implement control activities through policies<sup>122</sup> and periodically review policies, procedures, and related control activities for continued relevance and effectiveness in achieving the entity's objectives or addressing related risks.<sup>123</sup> Additionally, management should monitor internal controls as part of the normal course of operations. Ongoing monitoring includes regular management and supervisory activities, comparisons, reconciliations, and other routine actions.<sup>124</sup>

The deficiencies identified in this report occurred primarily because PDs and COs did not follow established Department policies and procedures for evaluating and resolving REAs. Additionally, COs did not ensure that PDs performed required REA activities and did not request additional information when documents related to the REA lacked required information. For the REAs reviewed during the audit, COs generally accepted PDs' recommendations rather than requesting sufficient documentation to make informed decisions. Furthermore, OIG found that OBO and AQM management had not established a sufficient process to determine whether PDs and COs have adhered to requirements and processes outlined in federal and Department policies concerning evaluating, resolving, and monitoring REAs or ensuring REAs are completed in a timely manner. In addition, although OBO had REA-related policies and procedures, AQM did not have specific procedures for evaluating and resolving REAs. Furthermore, existing Department policies did not provide sufficient guidance to PDs and COs on how to evaluate each contractor-billed cost element or how to allocate jobsite overhead costs for construction projects. Some PDs and COs interviewed for this audit also indicated that they did not understand the cost principle requirements for construction contracts outlined in the FAR.

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<sup>121</sup> REA 003 for the NCC Hyderabad construction project was evaluated and resolved in 601 days, largely due to the REA remaining dormant for 509 days after the original PD questioned the merit of the REA. The OBO Construction Manager directs and coordinates the daily activities of the professional engineering staff and is responsible for investigating and resolving specific technical issues and making a valid recommendation or giving options to the PD. The successor PD resolved the REA sometime after arriving at the construction project site.

<sup>122</sup> Government Accountability Office, *Standards for Internal Control in the Federal Government* (GAO-14-704G, September 2014), § 12.01.

<sup>123</sup> *Ibid.*, § 12.05

<sup>124</sup> *Ibid.*, § 16.05.

***The Department Does Not Have Reasonable Assurance That REAs Had Merit and Were Settled at Fair and Reasonable Prices***

Until the Department acts to fully comply with the FAR and Department guidance governing REAs, it will not have reasonable assurance that REAs are settled in a fair and reasonable manner, nor will it be able to prevent paying contractors multiple times for the same indirect costs. Additionally, until COs require PDs to provide adequate written analysis and recommendations that include contract references, adequate IGCEs, complete prenegotiation memoranda, and accurate cost analysis to show how merit was determined and to establish a negotiating position, the Department cannot be assured that REAs have been properly evaluated and resolved. As a result, the Department will not be ready to properly negotiate with contractors and may incur additional costs. Furthermore, contract modifications resulting from REAs that take an excessive time to finalize may negatively impact the project's schedule accuracy and create delays in reimbursing contractors for work they have already completed.

Overall, OIG is questioning \$837,172 in unsupported costs and \$3,251,891 in unallowable costs associated with 17 of the 30 REAs OIG reviewed for this audit. Appendix B provides a summary of these questioned costs. OIG is offering the following recommendations to address the issues identified during the audit.

**Recommendation 5:** OIG recommends that the Bureau of Overseas Buildings Operations (OBO) develop and communicate a Construction Alert to remind Project Directors and Construction Executives to review and follow the guidelines and steps developed in OBO's Construction Management Guidebook pertaining to requests for equitable adjustment, including documenting contract references and providing backup documentation to link changes to the contract.

**Management Response:** OBO concurred with the recommendation.

**OIG Reply:** On the basis of OBO's concurrence with the recommendation, OIG considers this recommendation resolved, pending further action. This recommendation will be closed when OIG receives documentation demonstrating that OBO has developed and communicated a Construction Alert to remind PDs and Construction Executives to review and follow the guidelines and steps developed in OBO's Construction Management Guidebook pertaining to REAs, including documenting contract references and providing backup documentation to link changes to the contract.

**Recommendation 6:** OIG recommends that the Bureau of Overseas Buildings Operations, in coordination with the Bureau of Administration, develop and implement a process to periodically assess activities related to evaluating, resolving, and monitoring requests for equitable adjustment to ensure Project Directors and Contracting Officers adhere to federal and Department of State requirements.

**Management Response:** OBO did not concur with the recommendation, stating that it has processes in place related to the recommendation.

**OIG Reply:** Although OBO stated that it has processes in place related to the recommendation, OIG found that these processes did not ensure that PDs or COs adhered to federal and Department requirements, as described in Finding A of this report. On the basis of OBO's nonconcurrency with the recommendation, OIG considers this recommendation unresolved and will pursue resolution of the recommendation during the audit compliance process. The recommendation will be considered resolved when OBO provides a plan of action for addressing the recommendation or provides an acceptable alternative that fulfills the intent of the recommendation. This recommendation will be closed when OIG receives documentation demonstrating that OBO, in coordination with the Bureau of Administration, has developed and implemented a sufficient process to assess activities related to evaluating, resolving, and monitoring REAs to ensure PDs and COs adhere to federal and Department requirements.

**Recommendation 7:** OIG recommends that the Bureau of Administration develop, implement, and communicate policies and procedures directing Contracting Officers to obtain from the responsible Project Director all required documentation related to requests for equitable adjustment for construction contracts and to document their review of all findings of fact, written request for equitable adjustment analyses, and prenegotiation memoranda provided by Project Directors to assist Contracting Officers in making merit determinations.

**Management Response:** The Bureau of Administration concurred with the recommendation.

**OIG Reply:** On the basis of the Bureau of Administration's concurrence with the recommendation, OIG considers the recommendation resolved, pending further action. This recommendation will be closed when OIG receives documentation demonstrating that the Bureau of Administration has developed, implemented, and communicated policies and procedures directing COs to obtain from the responsible PD all required documentation related to REAs for construction contracts and to document their review of all findings of fact, written REA analyses, and prenegotiation memoranda provided by PDs to assist COs in making merit determinations.

**Recommendation 8:** OIG recommends that the Bureau of Administration develop, implement, and communicate policies and procedures for resolving requests for equitable adjustment.

**Management Response:** The Bureau of Administration concurred with the recommendation.

**OIG Reply:** On the basis of the Bureau of Administration's concurrence with the recommendation, OIG considers the recommendation resolved, pending further action. This recommendation will be closed when OIG receives documentation demonstrating that the Bureau of Administration has developed, implemented, and communicated policies and procedures for resolving REAs.

**Recommendation 9:** OIG recommends that the Bureau of Overseas Buildings Operations, in coordination with the Bureau of Administration, develop, implement, and communicate a process for Project Directors and Contracting Officers to evaluate all cost elements submitted by contractors to determine necessity, reasonableness, and allowability. Additionally, the process should require that cost element evaluations be included in the independent government cost estimate and prenegotiation memoranda.

**Management Response:** OBO concurred with the recommendation, stating that it will coordinate with the Bureau of Administration and the Office of the Legal Adviser to address cost evaluations in current and future contracts.

**OIG Reply:** On the basis of OBO's concurrence with the recommendation and planned actions, OIG considers this recommendation resolved, pending further action. This recommendation will be closed when OIG receives documentation demonstrating that OBO, in coordination with the Bureau of Administration, has developed, implemented, and communicated a process for PDs and COs to evaluate all cost elements submitted by contractors to determine necessity, reasonableness, and allowability. Additionally, the process should require that cost element evaluations be included in the IGCE and prenegotiation memoranda.

**Recommendation 10:** OIG recommends that the Bureau of Overseas Buildings Operations, in coordination with the Bureau of Administration, develop, implement, and communicate policies and procedures for Project Directors and Contracting Officers to comply with the cost principle requirements for construction contracts in Federal Acquisition Regulation 31.203.

**Management Response:** OBO concurred with the recommendation, stating that OBO and the Bureau of Administration's procedures for reviewing and approving contract modifications are sufficient once FAR 31.203 is properly understood and incorporated.

**OIG Reply:** On the basis of OBO's concurrence with the recommendation, OIG considers the recommendation resolved, pending further action. This recommendation will be closed when OIG receives documentation demonstrating that OBO, in coordination with the Bureau of Administration, has developed, implemented, and communicated policies and procedures for PDs and COs to comply with the cost principle requirements for construction contracts in FAR 31.203.

**Recommendation 11:** Once Recommendation 10 has been implemented, OIG recommends that the Bureau of Overseas Buildings Operations (OBO), in coordination with the Bureau of Administration, develop and implement training for OBO staff and Contracting Officers on the policies and procedures related to cost principles.

**Management Response:** OBO concurred with the recommendation.

**OIG Reply:** On the basis of OBO's concurrence with the recommendation, OIG considers this recommendation resolved, pending further action. This recommendation will be closed

when OIG receives documentation demonstrating that OBO, in coordination with the Bureau of Administration, has developed and implemented training for OBO staff and COs on the policies and procedures related to cost principles.

**Recommendation 12:** OIG recommends that the Bureau of Overseas Buildings Operations (OBO) develop and implement a process to identify delays in responding to contractors' requests for equitable adjustment. At a minimum, the process should include controls that would trigger OBO management action after a specified period of time without resolution.

**Management Response:** OBO did not concur with the recommendation, stating that it has a process for leadership to review delayed REAs. OBO also stated that OIG reviewed REAs that occurred during the pandemic. The pandemic led to "extraordinary delays on some REAs" and created a "misleading assertion that the Bureau needs additional oversight related to this issue."

**OIG Reply:** As detailed in Appendix A of this report, OIG excluded all COVID-19 related REAs because of the predictable impact that the pandemic had on construction management, including disruptions to the construction materials and equipment supply chain and diminished labor productivity. Additionally, during the audit, OIG met with various OBO PDs and Bureau of Administration officials. Although some mentioned the impact that COVID-19 had on construction schedules, none provided feedback indicating that the deficiencies that OIG identified resulted from the COVID-19 pandemic.

On the basis of OBO's nonconurrence with the recommendation, OIG considers the recommendation unresolved and will seek resolution of the recommendation during the audit compliance process. The recommendation will be considered resolved when OBO provides a plan of action for addressing the recommendation or provides an acceptable alternative that fulfills the intent of the recommendation. This recommendation will be closed when OIG receives documentation demonstrating that OBO has developed and implemented a process to identify delays in responding to contractors' REAs.

**Recommendation 13:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, take the following actions: (1) determine whether the questioned costs of \$80,113, which were considered unsupported, for three requests for equitable adjustment for the New Embassy Compound Asuncion, Paraguay, construction contract (SAQMMA17C0082) were supported and (2) recover any costs determined to be unsupported, as shown in Table B.1.

**Management Response:** The Bureau of Administration did not concur with the recommendation, stating that it is difficult to recover costs that might be considered unallowable from a firm-fixed-price contract. The Bureau of Administration also stated that "[a]bsent fraud on the part of the contractor, it will not be possible to undo a bilateral modification due to a later review that disputes an individual cost element of the overall modification amount."

**OIG Reply:** As discussed in Finding A of this report, an independent audit of the Asuncion project identified cost overlaps included in indirect cost rates. The contractor provided a credit for the amount of unallowable costs identified. Based on this example, the Department can, and has, disputed an individual cost element from a previous contract modification and recovered those costs.

On the basis of the Bureau of Administration's nonconcurrency with the recommendation, OIG considers this recommendation unresolved and will seek resolution during the audit compliance process. The recommendation will be considered resolved when the Bureau of Administration provides a plan of action for addressing the recommendation or provides an acceptable alternative that fulfills the intent of the recommendation. This recommendation will be closed when OIG receives documentation demonstrating that the Bureau of Administration, in coordination with OBO, took the following actions: (1) determined whether the questioned costs of \$80,113, which were considered unsupported, for three REAs for the NEC Asuncion construction contract (SAQMMA17C0082) were supported and (2) recovered any costs determined to be unsupported.

**Recommendation 14:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations (OBO), take the following actions: (1) determine whether the questioned costs of \$5,887, which were considered unsupported, for seven requests for equitable adjustment for the New Embassy Compound Beirut, Lebanon, construction contract (SAQMMA17C0079) were supported and (2) recover any costs determined to be unsupported, as shown in Table B.2.

**Management Response:** The Bureau of Administration did not concur with the recommendation, stating that it is difficult to recover costs that might be considered unallowable from a [firm-fixed-price] contract. The Bureau of Administration also stated that "[a]bsent fraud on the part of the contractor, it will not be possible to undo a bilateral modification due to a later review that disputes an individual cost element of the overall modification amount."

**OIG Reply:** As discussed in Finding A of this report, an independent audit of the Asuncion project identified cost overlaps included in indirect cost rates. The contractor provided a credit for the amount of unallowable costs identified. Based on this example, the Department can, and has, disputed an individual cost element from a previous contract modification and recovered those costs.

On the basis of the Bureau of Administration's nonconcurrency with the recommendation, OIG considers this recommendation unresolved and will seek resolution of the recommendation during the audit compliance process. The recommendation will be considered resolved when the Bureau of Administration provides a plan of action for addressing the recommendation or provides an acceptable alternative that fulfills the intent of the recommendation. This recommendation will be closed when OIG receives documentation demonstrating that the Bureau of Administration, in coordination with OBO, took the following actions: (1) determined whether the questioned costs of \$5,887, which

were considered unsupported, for seven REAs for the NEC Beirut construction contract (SAQMMA17C0079) were supported and (2) recovered any costs determined to be unsupported.

**Recommendation 15:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations (OBO), take the following actions: (1) determine whether the questioned costs of \$25,663, which were considered unsupported, for six requests for equitable adjustment for the New Embassy Compound Tegucigalpa, Honduras, construction contract (19AQMM19C0223) were supported and (2) recover any costs determined to be unsupported, as shown in Table B.3.

**Management Response:** The Bureau of Administration did not concur with the recommendation, stating that it is difficult to recover costs that might be considered unallowable from a firm-fixed-price contract. The Bureau of Administration also stated that “[a]bsent fraud on the part of the contractor, it will not be possible to undo a bilateral modification due to a later review that disputes an individual cost element of the overall modification amount.”

**OIG Reply:** As discussed in Finding A of this report, an independent audit of the Asuncion project identified cost overlaps included in indirect cost rates. The contractor provided a credit for the amount of unallowable costs identified. Based on this example, the Department can, and has, disputed an individual cost element from a previous contract modification and recovered those costs.

On the basis of the Bureau of Administration’s nonconcurrence with the recommendation, OIG considers this recommendation unresolved and will seek resolution during the audit compliance process. The recommendation will be considered resolved when the Bureau of Administration provides a plan of action for addressing the recommendation or provides an acceptable alternative that fulfills the intent of the recommendation. This recommendation will be closed when OIG receives documentation demonstrating that the Bureau of Administration, in coordination with OBO, took the following actions: (1) determined whether the questioned costs of \$25,663, which were considered unsupported, for six REAs for the NEC Tegucigalpa construction contract (19AQMM19C0223) were supported and (2) recovered any costs determined to be unsupported.

**Recommendation 16:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, take the following actions: (1) determine whether the questioned costs of \$3,078,171, which were considered unallowable, for two requests for equitable adjustment for the New Embassy Compound Beirut, Lebanon, construction contract (SAQMMA17C0079) were allowable and (2) recover any costs determined to be unallowable, as shown in Table B.4.

**Management Response:** The Bureau of Administration did not concur with the recommendation, stating that it is difficult to recover costs that might be considered unallowable from a firm-fixed-price contract. The Bureau of Administration also stated that

“[a]bsent fraud on the part of the contractor, it will not be possible to undo a bilateral modification due to a later review that disputes an individual cost element of the overall modification amount.”

**OIG Reply:** As discussed in Finding A of this report, an independent audit of the Asuncion project identified cost overlaps included in indirect cost rates. The contractor provided a credit for the amount of unallowable costs identified. Based on this example, the Department can, and has, disputed an individual cost element from a previous contract modification and recovered those costs.

On the basis of the Bureau of Administration’s nonconcurrency with the recommendation, OIG considers this recommendation unresolved and will seek resolution during the audit compliance process. The recommendation will be considered resolved when the Bureau of Administration provides a plan of action for addressing the recommendation or provides an acceptable alternative that fulfills the intent of the recommendation. This recommendation will be closed when OIG receives documentation demonstrating that the Bureau of Administration, in coordination with OBO, took the following actions: (1) determined whether the questioned costs of \$3,078,171, which were considered unallowable, for two REAs for the NEC Beirut construction contract (SAQMMA17C0079) were allowable and (2) recovered any costs determined to be unallowable.

**Recommendation 17:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, take the following actions: (1) determine whether the questioned costs of \$173,720, which were considered unallowable, for six requests for equitable adjustment for the New Embassy Compound Tegucigalpa, Honduras, construction contract (19AQMM19C0223) were allowable and (2) recover any costs determined to be unallowable, as shown in Table B.5.

**Management Response:** The Bureau of Administration did not concur with the recommendation, stating that it is difficult to recover costs that might be considered unallowable from a firm-fixed-price contract. The Bureau of Administration also stated that “[a]bsent fraud on the part of the contractor, it will not be possible to undo a bilateral modification due to a later review that disputes an individual cost element of the overall modification amount.”

**OIG Reply:** As discussed in Finding A of this report, an independent audit of the Asuncion project identified cost overlaps included in indirect cost rates. The contractor provided a credit for the amount of unallowable costs identified. Based on this example, the Department can, and has, disputed an individual cost element from a previous contract modification and recovered those costs.

On the basis of the Bureau of Administration’s nonconcurrency with the recommendation, OIG considers this recommendation unresolved and will seek resolution during the audit compliance process. The recommendation will be considered resolved when the Bureau of Administration provides a plan of action for addressing the recommendation or provides an

acceptable alternative that fulfills the intent of the recommendation. This recommendation will be closed when OIG receives documentation demonstrating that the Bureau of Administration, in coordination with OBO, took the following actions: (1) determined whether the questioned costs of \$173,720, which were considered unallowable, for six REAs for the NEC Tegucigalpa construction contract (19AQMM19C0223) were allowable and (2) recovers any costs determined to be unallowable.

**Recommendation 18:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, (1) review all contract modifications for the New Embassy Compound Tegucigalpa, Honduras, construction contract (19AQMM19C0223) to identify all costs associated with violations of the cost principle requirements in Federal Acquisition Regulation 31.203, which govern the selection of a distribution base for allocating indirect costs, and (2) recover any costs determined to be unallowable.

**Management Response:** The Bureau of Administration concurred with the recommendation, stating that it will review all future contract modifications for this contract for violations of cost principles and include the recovery of unallowable costs as part of future outstanding negotiations.

**OIG Reply:** The intent of the recommendation was for the Bureau of Administration, in coordination with OBO, to review all completed contract modifications for the NEC Tegucigalpa construction contract, not future contract modifications. Therefore, on the basis of the Bureau of Administration's response, OIG considers the recommendation unresolved and will pursue resolution of the recommendation during the audit compliance process. The recommendation will be considered resolved when the Bureau of Administration provides a plan of action for addressing the recommendation or provides an acceptable alternative that fulfills the intent of the recommendation. This recommendation will be closed when OIG receives documentation demonstrating that the Bureau of Administration, in coordination with OBO, (1) reviewed all contract modifications for the NEC Tegucigalpa construction contract (19AQMM19C0223) to identify all costs associated with violations of the cost principle requirements in FAR 31.203, which govern the selection of a distribution base for allocating indirect costs, and (2) recovered any costs determined to be unallowable.

**Recommendation 19:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, (1) review all contract modifications for the New Embassy Compound Beirut, Lebanon, construction contract (SAQMMA17C0079) to identify all costs associated with violations of the cost principle requirements in Federal Acquisition Regulation 31.203, which govern the selection of a distribution base for allocating indirect costs, and (2) recover any costs determined to be unallowable.

**Management Response:** The Bureau of Administration concurred with the recommendation, stating that it will review all future contract modifications for violations of

cost principles and include the recovery of unallowable costs as part of future outstanding negotiations.

**OIG Reply:** The intent of the recommendation was for the Bureau of Administration, in coordination with OBO, to review all completed contract modifications for the NEC Beirut construction contract, not future contract modifications. Therefore, on the basis of the Bureau of Administration's response, OIG considers the recommendation unresolved and will seek resolution of the recommendation during the audit compliance process. The recommendation will be considered resolved when the Bureau of Administration provides a plan of action for addressing the recommendation or provides an acceptable alternative that fulfills the intent of the recommendation. This recommendation will be closed when OIG receives documentation demonstrating that the Bureau of Administration, in coordination with OBO, (1) reviewed all contract modifications for the NEC Beirut construction contract (SAQMMA17C0079) to identify all costs associated with violations of the cost principle requirements in FAR 31.203, which govern the selection of a distribution base for allocating indirect costs, and (2) recovered any costs determined to be unallowable.

**Recommendation 20:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations (OBO), take the following actions: (1) determine whether the questioned costs of \$725,509, which were considered to be unsupported, for request for equitable adjustment 003 for the New Consulate Compound Hyderabad, India, construction contract (SAQMMA16C0274), were supported and (2) recover any costs determined to be unsupported, as shown in Table B.6.

**Management Response:** The Bureau of Administration did not concur with the recommendation, stating that it is difficult to recover costs that might be considered unallowable from a firm-fixed-price contract. The Bureau of Administration also stated that "[a]bsent fraud on the part of the contractor, it will not be possible to undo a bilateral modification due to a later review that disputes an individual cost element of the overall modification amount."

**OIG Reply:** As discussed in Finding A of this report, an independent audit of the Asuncion project identified cost overlaps included in indirect cost rates. The contractor provided a credit for the amount of unallowable costs identified. Based on this example, the Department can, and has, disputed an individual cost element from a previous contract modification and recovered those costs.

On the basis of the Bureau of Administration's nonconcurrency with the recommendation, OIG considers this recommendation unresolved and will seek resolution during the audit compliance process. The recommendation will be considered resolved when the Bureau of Administration provides a plan of action for addressing the recommendation or provides an acceptable alternative that fulfills the intent of the recommendation. This recommendation will be closed when OIG receives documentation demonstrating that the Bureau of Administration, in coordination with OBO, took the following actions: (1)

determined whether the questioned costs of \$725,509, which were considered to be unsupported, for REA 003 for the NCC Hyderabad construction contract (SAQMMA16C0274) were supported and (2) recovered any costs determined to be unsupported.

## RECOMMENDATIONS

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**Recommendation 1:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, update the Foreign Affairs Handbook (14 FAH-2 H-535) to include guidance on how to avoid improper technical direction that could initiate a constructive change for construction contracts. At a minimum, the update should include guidance on reviewing requests for information and other methods of communication to contractors.

**Recommendation 2:** OIG recommends that the Bureau of Overseas Buildings Operations develop and communicate a Construction Alert reminding Project Directors and Construction Executives to review and follow the guidelines detailed in the Foreign Affairs Handbook (14 FAH-2 H-535) regarding preventing constructive changes to contracts.

**Recommendation 3:** OIG recommends that the Bureau of Overseas Buildings Operations (OBO), in coordination with the Bureau of Administration, develop and implement a process for management to review and monitor documents referenced in contractor requests for equitable adjustment, such as requests for information and requests for design clarification, to identify improper technical direction initiated by Project Directors or other OBO personnel.

**Recommendation 4:** OIG recommends that the Bureau of Administration develop and implement a communications strategy to direct Contracting Officers to review requests for equitable adjustment for unauthorized commitments and to resolve unauthorized commitments in accordance with the ratification process.

**Recommendation 5:** OIG recommends that the Bureau of Overseas Buildings Operations (OBO) develop and communicate a Construction Alert to remind Project Directors and Construction Executives to review and follow the guidelines and steps developed in OBO's Construction Management Guidebook pertaining to requests for equitable adjustment, including documenting contract references and providing backup documentation to link changes to the contract.

**Recommendation 6:** OIG recommends that the Bureau of Overseas Buildings Operations, in coordination with the Bureau of Administration, develop and implement a process to periodically assess activities related to evaluating, resolving, and monitoring requests for equitable adjustment to ensure Project Directors and Contracting Officers adhere to federal and Department of State requirements.

**Recommendation 7:** OIG recommends that the Bureau of Administration develop, implement, and communicate policies and procedures directing Contracting Officers to obtain from the responsible Project Director all required documentation related to requests for equitable adjustment for construction contracts and to document their review of all findings of fact, written request for equitable adjustment analyses, and prenegotiation memoranda provided by Project Directors to assist Contracting Officers in making merit determinations.

**Recommendation 8:** OIG recommends that the Bureau of Administration develop, implement, and communicate policies and procedures for resolving requests for equitable adjustment.

**Recommendation 9:** OIG recommends that the Bureau of Overseas Buildings Operations, in coordination with the Bureau of Administration, develop, implement, and communicate a process for Project Directors and Contracting Officers to evaluate all cost elements submitted by contractors to determine necessity, reasonableness, and allowability. Additionally, the process should require that cost element evaluations be included in the independent government cost estimate and prenegotiation memoranda.

**Recommendation 10:** OIG recommends that the Bureau of Overseas Buildings Operations, in coordination with the Bureau of Administration, develop, implement, and communicate policies and procedures for Project Directors and Contracting Officers to comply with the cost principle requirements for construction contracts in Federal Acquisition Regulation 31.203.

**Recommendation 11:** Once Recommendation 10 has been implemented, OIG recommends that the Bureau of Overseas Buildings Operations (OBO), in coordination with the Bureau of Administration, develop and implement training for OBO staff and Contracting Officers on the policies and procedures related to cost principles.

**Recommendation 12:** OIG recommends that the Bureau of Overseas Buildings Operations (OBO) develop and implement a process to identify delays in responding to contractors' requests for equitable adjustment. At a minimum, the process should include controls that would trigger OBO management action after a specified period of time without resolution.

**Recommendation 13:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, take the following actions: (1) determine whether the questioned costs of \$80,113, which were considered unsupported, for three requests for equitable adjustment for the New Embassy Compound Asuncion, Paraguay, construction contract (SAQMMA17C0082) were supported and (2) recover any costs determined to be unsupported, as shown in Table B.1.

**Recommendation 14:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations (OBO), take the following actions: (1) determine whether the questioned costs of \$5,887, which were considered unsupported, for seven requests for equitable adjustment for the New Embassy Compound Beirut, Lebanon, construction contract (SAQMMA17C0079) were supported and (2) recover any costs determined to be unsupported, as shown in Table B.2.

**Recommendation 15:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations (OBO), take the following actions: (1) determine whether the questioned costs of \$25,663, which were considered unsupported, for six requests for equitable adjustment for the New Embassy Compound Tegucigalpa, Honduras, construction contract (19AQMM19C0223) were supported and (2) recover any costs determined to be unsupported, as shown in Table B.3.

**Recommendation 16:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, take the following actions: (1) determine whether the questioned costs of \$3,078,171, which were considered unallowable, for two requests for equitable adjustment for the New Embassy Compound Beirut, Lebanon, construction contract (SAQMMA17C0079) were allowable and (2) recover any costs determined to be unallowable, as shown in Table B.4.

**Recommendation 17:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, take the following actions: (1) determine whether the questioned costs of \$173,720, which were considered unallowable, for six requests for equitable adjustment for the New Embassy Compound Tegucigalpa, Honduras, construction contract (19AQMM19C0223) were allowable and (2) recover any costs determined to be unallowable, as shown in Table B.5.

**Recommendation 18:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, (1) review all contract modifications for the New Embassy Compound Tegucigalpa, Honduras, construction contract (19AQMM19C0223) to identify all costs associated with violations of the cost principle requirements in Federal Acquisition Regulation 31.203, which govern the selection of a distribution base for allocating indirect costs, and (2) recover any costs determined to be unallowable.

**Recommendation 19:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, (1) review all contract modifications for the New Embassy Compound Beirut, Lebanon, construction contract (SAQMMA17C0079) to identify all costs associated with violations of the cost principle requirements in Federal Acquisition Regulation 31.203, which govern the selection of a distribution base for allocating indirect costs, and (2) recover any costs determined to be unallowable.

**Recommendation 20:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations (OBO), take the following actions: (1) determine whether the questioned costs of \$725,509, which were considered to be unsupported, for request for equitable adjustment 003 for the New Consulate Compound Hyderabad, India, construction contract (SAQMMA16C0274), were supported and (2) recover any costs determined to be unsupported, as shown in Table B.6.

## APPENDIX A: PURPOSE, SCOPE, AND METHODOLOGY

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The Office of Inspector General (OIG) conducted this audit to determine whether the process used by the Department of State (Department) to reach equitable adjustments with selected construction contractors responsible for large construction contracts complied with the Federal Acquisition Regulation and Department guidance.

OIG conducted this audit from October 2023 to September 2024 in the Washington, DC, metropolitan area. The scope of this audit was completed requests for equitable adjustment (REA) related to New Embassy Compound (NEC) and New Consulate Compound (NCC) construction projects that were processed from October 1, 2020, through June 30, 2023. The audit scope excluded all COVID-19 related REAs because of the predictable impact that the pandemic had on construction management, including disruptions to the construction materials and equipment supply chain and diminished labor productivity. OIG conducted this performance audit in accordance with generally accepted government auditing standards. These standards require that OIG plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for the findings and conclusions based on the audit objective. OIG believes that the evidence obtained provides a reasonable basis for the findings and conclusions based on the audit objective.

To obtain background information for this audit, OIG reviewed federal laws and regulations and Department policies and procedures. Specifically, OIG reviewed the Federal Acquisition Regulation; the Foreign Affairs Manual; the Foreign Affairs Handbook; the Department of State Acquisition Regulation; applicable Bureau of Administration, Office of the Procurement Executive, guidance; and applicable Bureau of Overseas Buildings Operations (OBO) guidance related to construction projects.

During audit fieldwork, OIG interviewed key OBO and Bureau of Administration, Office of the Procurement Executive, Office of Acquisitions Management (AQM),<sup>1</sup> officials associated with the process to reach equitable adjustments for construction projects. Additionally, OIG reviewed and analyzed the NEC Asuncion, Paraguay, construction contract (SAQMMA17C0082); NEC Beirut, Lebanon, construction contract (SAQMMA17C0079); NCC Hyderabad, India, construction contract (SAQMMA16C0274); NCC Lagos, Nigeria, construction contract (19AQMM21C0156); and NEC Tegucigalpa, Honduras, construction contract (19AQMM18C0223). Furthermore, OIG reviewed REA supporting documentation and contract modification documentation. Specifically, OIG reviewed the REA submissions from construction contractors for selected projects, including the Project Directors' analyses, independent government cost estimates, time impact analyses (if applicable), Contracting Officers' decisions of merit, prenegotiation memoranda, negotiation summaries, and price acceptance memoranda.

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<sup>1</sup> After the completion of audit fieldwork, the Bureau of Administration implemented a reorganization of its offices and realigned their acquisitions expertise within OPE under the Deputy Assistant Secretary for Global Acquisitions.

## Data Reliability

OIG used computer-processed data provided by OBO, from its eData database,<sup>2</sup> to identify the universe of REAs submitted by contractors for large overseas construction contracts from October 1, 2020, through June 30, 2023. To assess the completeness and accuracy of the universe of submitted REAs, OIG used data from nonautomated sources provided by AQM and compared the data with the data provided by OBO. Overall, OIG concluded that the combined data were sufficiently reliable for selecting the REAs to review and for the purpose of fulfilling the audit objective.

## Work Related to Internal Control

During the audit, OIG considered a number of factors, including the subject matter of the project, to determine whether internal control was significant to the audit objective. Based on its consideration, OIG determined that internal control was significant for this audit. OIG then considered the components of internal control and the underlying principles included in the *Standards for Internal Control in the Federal Government*<sup>3</sup> to identify internal controls that were significant to the audit objective. Considering internal control in the context of a comprehensive internal control framework can help auditors to determine whether underlying internal control deficiencies exist.

For this audit, OIG concluded that two of five internal control components from the *Standards for Internal Control in the Federal Government*—Information and Communication and Monitoring—were significant to the audit objective. The Information and Communication component relates to the quality of information that management and personnel communicate and use to support the internal control system. The Monitoring component relates to activities that management establishes and operates to assess the quality of performance over time and promptly resolve the findings of audits and other reviews. OIG also concluded that two of the principles related to the selected components were significant to the audit objective, as described in Table A.1.

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

Components	Principles
Information and Communication	Management should internally communicate the necessary quality information to achieve the entity's objectives.
Monitoring	Management should establish and operate monitoring activities to monitor the internal control system and evaluate the results.

**Source:** Generated by OIG from an analysis of internal control components and principles from the Government Accountability Office, *Standards for Internal in the Federal Government* (GAO-14-704G, September 2014).

<sup>2</sup> eData is a data collection tool, using Excel, that serves as the consolidated location for project information.

<sup>3</sup> Government Accountability Office, *Standards for Internal Control in the Federal Government* (GAO-14-704G, September 2014).

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

- Analyzed a sample of REAs and supporting documentation to determine whether the Project Directors, acting as Contracting Officer’s Representatives, completed REA merit determination activities, prepared prenegotiation documentation, documented negotiations with the contractors, and provided the results of the negotiations to the Contracting Officers and Construction Executives prior to approval in accordance with applicable requirements.
- Analyzed contract modification documentation associated with the REAs selected for testing to determine whether the Contracting Officers executed the contract modifications, including both cost and construction schedule changes, in accordance with applicable regulations.

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

**Sampling Methodology**

OIG’s sampling objective was to select a sample of REAs, associated with NEC and NCC construction projects, for testing. From a universe of 440 REAs processed from October 1, 2020, through June 30, 2023, OIG selected 30 REAs from 5 overseas construction projects for review. See below for additional details.

***Construction Project Selection Methodology***

OIG identified 82 construction projects with 900 associated REAs, totaling \$589,224,208, submitted by construction contractors from October 1, 2020, through June 30, 2023. OIG excluded all COVID-19 related REAs because of the predictable impact that the pandemic had on construction management, including disruptions to the construction materials and equipment supply chain and diminished labor productivity. Of the 82 construction projects, 29 were related to NEC and NCC construction projects. The 29 NEC and NCC construction projects had 440 associated REAs, totaling \$245,327,940, submitted by construction contractors during the scope period. From the 29 projects, OIG judgmentally selected 5 of the most significant construction projects for testing. Details of the five selected construction projects are shown in Table A.2.

**Table A.2: Construction Projects Selected for Review**

<b>Construction Project</b>	<b>Contract</b>	<b>Contract Award Amount</b>	<b>Number of REAs</b>	<b>Amount of REAs</b>
NEC Asuncion	SAQMMA17C0082	\$165,823,000	115	\$12,363,443
NEC Beirut	SAQMMA17C0079	\$586,061,860	31	\$39,571,642

NCC Hyderabad	SAQMMA16C0274	\$203,114,000	29	\$11,773,568
NCC Lagos	19AQMM21C0156	\$319,027,389	7	\$13,564,440
NEC Tegucigalpa	19AQMM18C0223	\$244,544,274	98	\$14,534,201
<b>Total</b>		<b>\$1,518,570,523</b>	<b>280</b>	<b>\$91,807,294</b>

Source: OIG-generated based on data obtained from OBO and AQM.

### **REA and Contract Modification Selection Methodology**

From the universe of 280 REAs associated with the 5 selected construction projects, OIG selected a nonstatistical sample of 30 REAs for review, totaling \$21,428,992. OIG also reviewed the 27 executed contract modifications,<sup>4</sup> totaling \$8,764,977, that were associated with the 30 selected REAs.

#### *Selection of REAs Associated With NEC Asuncion Construction Project (Contract SAQMMA17C0082)*

OIG identified 115 REAs, totaling \$12,363,443, submitted during the scope period for the NEC Asuncion contract. OIG selected a judgmental sample of the seven REAs, totaling \$6,847,781, that had the highest values and that had completed the evaluation and resolution process. Details of the seven REAs selected for review and the associated contract modifications are shown in Table A.3.

**Table A.3: REA Selection for the NEC Asuncion Construction Project (Contract SAQMMA17C0082)**

REA Number	Submitted Amount	Modification Number	Executed Amount
REA 059	\$80,071	P00023	\$80,071
REA 062	\$6,397,273	P00038	\$966,652
REA 065	\$8,705	P00023	\$8,705
REA 080	\$128,590	P00024	\$128,590
REA 102	\$80,351	N/A*	\$0*
REA 107	\$83,839	N/A*	\$0*
REA 121	\$68,952	P00039	\$68,952
<b>Total</b>	<b>\$6,847,781</b>		<b>\$1,252,970</b>

\* A contract modification was not executed because the REA was rejected.

Source: OIG-generated based on data obtained from OBO and AQM.

<sup>4</sup> Three of the 30 REAs were rejected, resulting in 27 contract modifications being executed.

*Selection of REAs Associated With NEC Beirut Construction Project (Contract SAQMMA17C0079)*

OIG identified 31 REAs, totaling \$39,571,642, submitted during the scope period for the NEC Beirut contract. OIG selected a judgmental sample of the eight REAs, totaling \$5,523,698, that had the highest values and that had completed the evaluation and resolution process. Details of the eight REAs selected for review and the associated contract modifications are shown in Table A.4.

**Table A.4: REA Selection for the NEC Beirut Construction Project (Contract SAQMMA17C0079)**

REA Number	Submitted Amount	Modification Number	Executed Amount
REA 052	\$75,285	P00041	\$75,285
REA 081	\$6,003,323	P00051	\$3,066,045
REA 082	\$(196,913)*	P00039	\$(196,913)
REA 083	\$6,827	P00034	\$6,827
REA 084	\$235,765	P00036	\$235,765
REA 085	\$(125,277)*	P00043	\$(125,277)
REA 086	\$(492,195)*	P00042	\$(492,195)
REA 088	\$16,883	P00047	\$16,883
<b>Total</b>	<b>\$5,523,698</b>		<b>\$2,586,420</b>

\* REA, which decreased cost, was submitted for a substitution of materials.

**Source:** OIG-generated based on data obtained from OBO and AQM.

*Selection of REAs Associated With NCC Hyderabad Construction Project (Contract SAQMMA16C0274)*

OIG identified 29 REAs, totaling \$11,773,568, submitted during the scope period for the NCC Hyderabad contract. OIG selected a judgmental sample of the four REAs, totaling \$1,130,463, that had the highest values and that had completed the evaluation and resolution process. Details of the four REAs and the associated contract modifications selected for review are shown in Table A.5.

**Table A.5: REA Selection Associated With NCC Hyderabad Construction Project (Contract SAQMMA16C0274)**

REA Number	Submitted Amount	Modification Number	Executed Amount
REA 003	\$853,578	P00013	\$725,509
REA 019	\$86,271	P00028	\$77,404
REA 027	\$121,573	P00028	\$107,170
REA 030	\$69,041	P00028	\$27,994
<b>Total</b>	<b>\$1,130,463</b>		<b>\$938,077</b>

**Source:** OIG-generated based on data obtained from OBO and AQM.

*Selection of REAs Associated With NCC Lagos Construction Project (Contract 19AQMM21C0156)*

OIG identified seven REAs, totaling \$13,564,440, submitted during the scope period for the NCC Lagos contract. OIG selected a judgmental sample of the four REAs, totaling \$4,713,630, that had the highest values and that had completed the evaluation and resolution process. Details of the four REAs and the associated contract modifications selected for review are shown in Table A.6.

**Table A.6: REA Selection Associated With NCC Lagos Construction Project (Contract 19AQMM21C0156)**

REA Number	Submitted Amount	Modification Number	Executed Amount
REA 001	\$1,225,671	P00005	\$452,988
REA 002	\$3,166,857	N/A*	\$0*
REA 004	\$312,447	P00005	\$312,447
REA 005	\$8,655	P00008	\$8,655
<b>Total</b>	<b>\$4,713,630</b>		<b>\$774,090</b>

\* A contract modification was not executed because the REA was rejected.

Source: OIG-generated based on data obtained from OBO and AQM.

*Selection of REAs Associated With NEC Tegucigalpa Construction Project (Contract 19AQMM18C0223)*

OIG identified 98 REAs, totaling \$14,534,201, submitted during the scope period for the NEC Tegucigalpa contract. OIG selected a judgmental sample of the seven REAs, totaling \$3,213,420, that had the highest values and that had completed the evaluation and resolution process. Details of the seven REAs and the associated contract modifications selected for review are shown in Table A.7.

**Table A.7: REA Selection Associated With NEC Tegucigalpa Construction Project (Contract 19AQMM18C0223)**

REA Number	Submitted Amount	Modification Number	Executed Amount
REA 026	\$138,192	P00011	\$138,192
REA 027	\$168,478	P00011	\$168,478
REA 028	\$106,990	P00011	\$106,990
REA 043	\$291,516	P00014	\$291,516
REA 047	\$396,663	P00017	\$396,663
REA 068	\$2,009,568	P00020	\$2,009,568
REA 085	\$102,013	P00019	\$102,013
<b>Total</b>	<b>\$3,213,420</b>		<b>\$3,213,420</b>

Source: OIG-generated based on data obtained from OBO and AQM.

## **Prior Office of Inspector General Reports**

In January 2024, OIG reported,<sup>5</sup> among other issues, that neither OBO nor AQM executed contract modifications for the NEC Mexico City construction contract in accordance with requirements. OIG made six recommendations to address issues identified. As of December 2024, the six recommendations remained resolved, pending further action.

In April 2023, OIG reported<sup>6</sup> that OBO and AQM did not assess time for the NEC Mexico City, Mexico, project as part of the independent government cost estimate process. Without a complete independent government cost estimate that includes an assessment of time, the Department is not fully prepared to determine whether the contractor's proposal is fair and reasonable and whether a time extension, as presented in the time impact analysis prepared by the contractor, is justified. OIG made four recommendations to address the deficiencies identified. As of December 2024, three recommendations were implemented and closed, and one recommendation remained resolved, pending further action.

In September 2020, OIG reported<sup>7</sup> that major systems were not fully commissioned at NEC London, at least in part, because OBO personnel did not perform adequate quality assurance to identify and address potential causes for schedule delays and the effect these delays had on the commissioning of major building systems. The major delaying events were generally attributed to incomplete design documents, evolving security requirements, and flaws in OBO's secure material procurement program. The contractor submitted an REA. The request included an additional 259 days of performance to complete the project and a mitigation amounting to \$82,708,652. The Department negotiated a settlement and issued two contract modifications granting an additional 279 days to the schedule and more than \$18 million. OIG made 11 recommendations, all of which have been implemented and closed.

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<sup>5</sup> OIG, *Audit of Select Contract Administration Processes Related to the Construction of New Embassy Compound Mexico City, Mexico* (AUD-CGI-24-09, January 2024).

<sup>6</sup> OIG, *Management Assistance Report: Actions To Address Ongoing Construction Schedule Delays at New Embassy Compound Mexico City Are Needed* (AUD-CGI-23-16, April 2023).

<sup>7</sup> OIG, *Audit of the Bureau of Overseas Buildings Operations Process To Execute Construction Closeout Procedures for Selected Capital Construction Projects* (AUD-CGI-20-43, September 2020).

## APPENDIX B: QUESTIONED COSTS IDENTIFIED DURING THE AUDIT

During the audit, the Office of Inspector General (OIG) selected for testing 30 requests for equitable adjustment (REA) related to New Embassy Compound (NEC) and New Consulate Compound (NCC) construction projects that were submitted from October 1, 2020, through June 30, 2023.<sup>1</sup> From the 30 REAs, OIG identified issues related to 17 REAs, totaling \$837,172, that were not properly supported and \$3,251,891 that were unallowable, as shown in Tables B.1 through B.6. OIG considers the unsupported and unallowable amounts to be questioned costs.<sup>2</sup>

**Table B.1: Unsupported Costs for NEC Asuncion, Paraguay (Cost Elements)**

Construction Project	REA Number	Value of REAs Reviewed	Unsupported Costs
NEC Asuncion	REA 059	\$80,071	\$80,071
NEC Asuncion	REA 121	\$68,952	\$42
<b>Total</b>			<b>\$80,113</b>

**Source:** OIG-generated based on a review of REAs for the selected construction projects and the results of audit testing for the sample of REAs selected.

**Table B.2: Unsupported Costs for NEC Beirut, Lebanon (Cost Elements)**

Construction Project	REA Number	Value of REAs Reviewed	Unsupported Costs
NEC Beirut	REA 052	\$75,285	\$1,183
NEC Beirut	REA 082	(\$196,913)	\$90
NEC Beirut	REA 083	\$6,827	\$360
NEC Beirut	REA 084	\$235,765	\$2,700
NEC Beirut	REA 085	(\$125,277)	\$90
NEC Beirut	REA 086	(\$492,195)	\$900
NEC Beirut	REA 088	\$16,883	\$564
<b>Total</b>			<b>\$5,887</b>

**Source:** OIG-generated based on a review of REAs for the selected construction projects and the results of audit testing for the sample of REAs selected.

<sup>1</sup> Appendix A provides details of the sample selected.

<sup>2</sup> The Inspector General Act of 1978, 5 United States Code § 405(a)(4),(7), "Reports," indicates that a questioned cost may be questioned because of (a) an alleged violation of a provision of a law, contract, grant, cooperative agreement, or other agreement or document governing the expenditure of funds; (b) a finding that, at the time of the audit, such cost is not supported by adequate documentation (also known as an unsupported cost); or (c) a finding that the expenditure of funds for the intended purpose is unnecessary or unreasonable.

**Table B.3: Unsupported Costs for NEC Tegucigalpa, Honduras (Cost Elements)**

<b>Construction Project</b>	<b>REA Number</b>	<b>Value of REAs Reviewed</b>	<b>Unsupported Costs</b>
NEC Tegucigalpa	REA 026	\$138,193	\$1,303
NEC Tegucigalpa	REA 027	\$168,478	\$1,400
NEC Tegucigalpa	REA 028	\$106,990	\$1,473
NEC Tegucigalpa	REA 043	\$291,516	\$3,221
NEC Tegucigalpa	REA 047	\$396,663	\$17,118
NEC Tegucigalpa	REA 085	\$102,013	\$1,148
<b>Total</b>			<b>\$25,663</b>

**Source:** OIG-generated based on a review of REAs for the selected construction projects and the results of audit testing for the sample of REAs selected.

**Table B.4: Unallowable Costs for NEC Beirut (Per Diem and Percentage of Direct Costs)**

<b>Construction Project</b>	<b>REA Number</b>	<b>Value of REAs Reviewed</b>	<b>Unallowable Costs</b>
NEC Beirut	REA 052	\$75,285	\$9,905
NEC Beirut	REA 081	\$6,133,080	\$3,066,045*
NEC Beirut	REA 088	\$16,883	\$2,221
<b>Total</b>			<b>\$3,078,171</b>

\* Although the contractor requested \$6,133,080, the Contracting Officer ultimately approved payment in the amount of \$3,066,045.

**Source:** OIG-generated based on a review of REAs for the selected construction projects and the results of audit testing for the sample of REAs selected.

**Table B.5: Unallowable Costs for NEC Tegucigalpa (Percentage of Direct Costs)**

<b>Construction Project</b>	<b>REA Number</b>	<b>Value of REAs Reviewed</b>	<b>Unallowable Costs</b>
NEC Tegucigalpa	REA 026	\$138,193	\$20,323
NEC Tegucigalpa	REA 027	\$168,478	\$24,776
NEC Tegucigalpa	REA 028	\$106,990	\$15,734
NEC Tegucigalpa	REA 043	\$291,516	\$41,646
NEC Tegucigalpa	REA 047	\$396,663	\$56,667
NEC Tegucigalpa	REA 085	\$102,013	\$14,574
<b>Total</b>			<b>\$173,720</b>

**Source:** OIG-generated by OIG based on a review of REAs for the selected construction projects and the results of audit testing for the sample of REAs selected.

**Table B.6: Unsupported Costs for NCC Hyderabad, India (Delays Determining Merit)**

<b>Construction Project</b>	<b>REA Number</b>	<b>Value of REAs Reviewed</b>	<b>Unsupported Costs</b>
NCC Hyderabad	REA 003	\$725,509	\$725,509
<b>Total</b>			<b>\$725,509</b>

**Source:** OIG-generated based on a review of REAs for the selected construction projects and the results of audit testing for the sample of REAs selected.

## APPENDIX C: BUREAU OF OVERSEAS BUILDINGS OPERATIONS RESPONSE

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**United States Department of State**

*Washington, D.C. 20520*

UNCLASSIFIED

February 19, 2025

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

**FROM:** OBO – Patricia Lacina, Director *PAL*

**SUBJECT:** OBO Response to OIG draft Audit of Selected Contractor Requests for Equitable Adjustment Related to Bureau of Overseas Buildings Operations Construction Projects

This response memo consists of three sections: 1. Overall feedback; 2. Action office responses; and 3. Technical comments.

#### **1. OVERALL FEEDBACK**

OBO appreciates the OIG’s continued interest in OBO construction projects. OIG and OBO share many common goals, such as improving operations and providing safe, secure, functional, and resilient facilities to enable U.S. foreign policy. However, this audit report reflects several significant fundamental misalignments between the OIG and OBO about the standard, purpose, and process of Requests for Equitable Adjustment (REA) in overseas construction contracts.

OBO had concerns as early as December 12, 2024, when the OIG shared the Audit “Highlights and Recommendations” summary and repeatedly provided feedback and requested to meet with the OIG to discuss technical corrections. The OIG informed OBO that it would not make any changes to the report following a discussion. To that end, OBO has outlined the full extent of its concerns in this memo.

OBO plans, designs, and executes overseas diplomatic construction projects around the world in unpredictable environments which are often faced with rapidly changing security risks, political and civil unrest, evolving natural hazard threats, and malign influence. OBO’s Office of Construction Management endeavors to conduct their work with a reasonable standard of care to fulfill their

responsibilities to their organization. While the Bureau understands that the OIG aimed to detect every instance when an employee did not comply with requirements, the reality of construction professionals in any sector is that it is unrealistic to establish and expect absolutes. As the Government Accountability Office's Standards for Internal Control in the Federal Government (known as the "Green Book") describes, "Internal control is a process effected by an entity's oversight body, management, and other personnel that provides reasonable assurance that the objectives of an entity will be achieved." OBO has achieved its objectives and provided this reasonable assurance. Should the OIG expect 100 percent compliance, OBO notes that it does not have the resources to staff the organization to achieve it, nor does it anticipate the ability to increase staffing in the near term.

Related to OBO's concerns with the report's "absolute" versus "reasonable" standard of care, the report provides some misleading conclusions due to lack of context. For example, the OIG states that it is "questioning \$837,172 in unsupported costs," for the total combined values of all REAs reviewed in the audit. This amount only represents 4 percent of the approximately \$21.4 million combined values. In other words, OBO properly adjudicated 96 percent of the evaluated REAs. Further, of the \$837,172 the OIG noted, \$725,509 is for one single REA for a change in the sun screen design as part of the Hyderabad New Consulate Compound project, which OBO does consider to be a supported change. With the removal of the Hyderabad REA from the OIG's "unsupported costs" estimate, the \$111,663 in unsupported costs represents 0.5 percent of the combined value of all REAs audited.

Another fundamental disagreement, as evidenced in the draft report, is that OBO does not consider responses to a Request for Information (RFI) to be a commitment or a change to the contract. The USG, as generally accepted in the construction industry, has an obligation to provide timely responses to technical questions to avoid uncertainty and potential costly corrective work. Therefore, OBO does not consider technical direction in response to an RFI to be a potential unauthorized commitment with personal liability implications, nor improper technical direction even if referenced in a subsequent modification. OBO contracts stipulate that when technical direction is provided, for example via an RFI, the response does not change the terms of the contract nor does anyone other than the Contracting Officer (CO) have the authority to make changes to the terms of the contract. The contract states that, if the contractor does any such work without proper direction from the CO, they are doing the work at their own

risk. OBO does not aim to prevent REAs, but rather considers the process to be a valuable tool for ensuring fair and reasonable resolution of contract issues.

OBO also notes that the period the OIG covered was both during and directly following the COVID-19 pandemic, an unprecedented event that had rippling effects on staffing, global supply chains, price escalation and resulting impacts on overseas construction projects. Such factors bias the OIG's sample and, as a result, OBO does not believe that many of the OIG's findings based on REAs from this period – even if correct – should result in recommendations to adjust the entire construction program. OBO will present more specific examples in the recommendation responses below.

Finally, OBO thanks the OIG for noting in its report that the Department allowed contractors to use two different bases for allocating jobsite overhead costs in violation of the cost principle requirements of the FAR. The Department became aware of this independently of the OIG's audit and is working with its Office of the Legal Adviser to resolve. OBO notes that the OIG's reported "\$3,251,891 in unallowable costs" is associated with two REAs that directly related to this issue.

## **2. ACTION OFFICE RESPONSES**

OBO responds to the OIG's recommendations issued to the Bureau in **bold** text.

**Recommendation 2:** OIG recommends that the Bureau of Overseas Buildings Operations develop and communicate a Construction Alert reminding Project Directors and Construction Executives to review and follow the guidelines detailed in the Foreign Affairs Handbook (14 FAH-2 H-535) regarding preventing constructive changes to contracts.

**OBO Response:** OBO requests that the recommendation language remove "regarding preventing constructive changes to contracts." With that, OBO concurs with the recommendation. OBO will develop and communicate a Construction Alert reminding PDs and CEs to follow 14 FAH-2 H-535.

**Recommendation 3:** OIG recommends that the Bureau of Overseas Buildings Operations (OBO), in coordination with the Bureau of Administration, develop

and implement a process for management to review and monitor documents referenced in contractor requests for equitable adjustment, such as requests for information and requests for design clarification, to identify improper technical direction initiated by Project Directors or other OBO personnel.

**OBO Response: OBO does not concur with this recommendation. Through OBO's rOBO application, review of documents related to Requests for Contract Action (RFCA) occur through the approval process. This process is then repeated through the Ariba system process in which funding is "sent" to A/GA for processing into a contract modification. Any review more in depth as suggested by the OIG would require resources and time that are not available to the Department.**

**The Department has a process to review and monitor documents to identify improper technical direction. Reviews occur prior to responding to the RFI and are captured in OBO's ProjNet system. Further, as discussed in the "overall feedback" section above, OBO has a different fundamental understanding of what constitutes "improper technical direction" than the OIG's report and, based on OBO's definition, the OIG did not present findings that OBO failed to identify improper technical direction.**

**The OIG suggests requiring ratification for providing technical direction. OBO disagrees, as this would create a chilling effect to make any response by a COR that "could" be referenced in a subsequent modification. Further, this would undermine the delegations and limits on authority set forth in the FAR. This would also severely impact the USG obligation to provide timely responses to contractor inquiries to "avoid claims that the contractor was delayed by the U.S. Government inaction or that constructive acceptance has occurred" as referenced in 14 FAH-2 H-535 d (4).**

**OBO will work with A Bureau and confirm with L to include specific language in RFI interpretation to reinforce the current contractual language of the limitations of the COR authority.**

**Recommendation 5:** OIG recommends that the Bureau of Overseas Buildings Operations (OBO) develop and communicate a Construction Alert to remind Project Directors and Construction Executives to review and follow the guidelines and steps developed in OBO's Construction Management Guidebook pertaining to

requests for equitable adjustment, including documenting contract references and providing backup documentation to link changes to the contract.

**OBO Response: OBO concurs with this recommendation.**

**Recommendation 6:** OIG recommends that the Bureau of Overseas Buildings Operations, in coordination with the Bureau of Administration, develop and implement a process to periodically assess activities related to evaluating, resolving, and monitoring REAs to ensure Project Directors and Contracting Officers adhere to federal and Department of State requirements.

**OBO Response: OBO does not concur with this recommendation. OBO already has processes in place, such as those in its Service Level Agreement and the RFCA process.**

**Recommendation 9:** OIG recommends that the Bureau of Overseas Buildings Operations, in coordination with the Bureau of Administration, develop, implement, and communicate a process for Project Directors and Contracting Officers to evaluate all cost elements submitted by contractors to determine necessity, reasonableness, and allowability. Additionally, the process should require that cost element evaluations be included in the independent government cost estimate and prenegotiation memoranda.

**OBO Response: OBO concurs with this recommendation and will coordinate with A/GA and L to address cost evaluations in current and future contracts.**

**However, OBO notes that, given the iterative process between the Department and the contractor for REA adjustment, completing the actions outlined in this recommendation before negotiation may not be feasible nor practical. Also, cost evaluations often include more than individual cost elements to determine reasonableness. As such, other methodologies such as parametric estimating, market analysis, may also be included in developing Independent Government Cost Estimates and pre-negotiation memoranda.**

**Recommendation 10:** OIG recommends that the Bureau of Overseas Buildings Operations, in coordination with the Bureau of Administration, develop,

implement, and communicate policies and procedures for Project Directors and Contracting Officers to comply with the cost principle requirements for construction contracts in Federal Acquisition Regulation 31.203.

**OBO Response: OBO concurs with the recommendation to develop and communicate the policy of complying with FAR 31.203. OBO and A/GA's current procedures for reviewing and approving contract modifications are sufficient once the policies of 31.203 are properly understood and incorporated.**

**Recommendation 11:** Once Recommendation 10 has been implemented, OIG recommends that the Bureau of Overseas Buildings Operations (OBO), in coordination with the Bureau of Administration, develop and implement training for OBO staff and Contracting Officers on the policies and procedures related to cost principles.

**OBO Response: OBO concurs with this recommendation.**

**Recommendation 12:** OIG recommends that the Bureau of Overseas Buildings Operations (OBO) develop and implement a process to identify delays in responding to contractors' requests for equitable adjustment. At a minimum, the process should include controls that would trigger OBO management action after a specified period of time without resolution.

**OBO Response: OBO does not concur with this recommendation. OBO already has a process in place for leadership for review of delayed REAs. As discussed in the "overall feedback" section above, the OIG reviewed REAs during the pandemic, resulting in extraordinary delays on some REAs and creating a misleading assertion that the Bureau needs additional oversight related to this issue.**

**Further, the report's evaluation of time to resolution through modification does not take into consideration the iterative process between the Department and the contractor for REA adjustment. Therefore, while timely REA resolution is a general best practice, the measurement of REA submission to contract modification is not meaningful.**

**3. TECHNICAL COMMENTS**

- All financial information about ongoing contracts is Sensitive But Unclassified.
- On the Introduction page the report states, “In addition, OIG found that PDs and Contracting Officers (CO) did not evaluate and resolve REAs in accordance with the FAR and Department guidance.”
  - OBO requests that the OIG clarify the statement with, “In addition, OIG found in several cases that PDs and Contracting Officers (CO) did not evaluate and resolve REAs...”
- On Page 4 the report states, “For OBO construction projects, the PD is responsible for preparing the IGCE using input from OBO’s staff assigned to the project.”
  - OBO requests that the OIG clarify the statement with, “For OBO construction projects, the PD is responsible for preparing the IGCE using input from OBO’s staff or resources assigned to the project.”
- On Page 13, footnote 72 states, “An RFI is generally a situation in which a contractor asks the government for clarification of contract requirements. RFIs are submitted by the contractor using a software application available to OBO and AQM staff.”
  - OBO notes that this is a targeted definition and not a general one. In general, an RFI is a process which allows the contractor to obtain clarification about project requirements or intent.
- On Page 18, the report references to REAs by number only. Since there are multiple projects with the same REA numbers, we request that the project and ideally a brief description of the REA be included in this section for ease of reference.

## APPENDIX D: BUREAU OF ADMINISTRATION RESPONSE

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United States Department of State

Washington, D.C. 20520

UNCLASSIFIED

February 19, 2025

### MEMORANDUM

TO: OIG/AUD – Melissa Bauer

FROM: A/GA/AMD – Ramona E. Watts-Sutton, HCA Acting Vincent J. Sanchez Digitally signed by Vincent J. Sanchez  
Date: 2025.02.21  
18:41:26 -05'00'

SUBJECT: Draft Report – Audit of Selected Contractor Requests for Equitable Adjustment Related to Bureau of Overseas Buildings Operations Construction Projects (AUD-CGI-25-XX)

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

**Recommendation 1:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, update the Foreign Affairs Handbook (14 FAH-2 H-535) to include guidance on how to avoid improper technical direction that could initiate a constructive change for construction contracts. At a minimum, the update should include guidance on reviewing requests for information and other methods of communication to contractors.

**Management Response to Draft Report (02/19/25):** The Bureau of Administration, Global Acquisition, Acquisition Policy Directorate (A/GA/APD) does not concur with this recommendation. Currently, A/GA/APD is developing a COR Handbook that will become a stand-alone document separate from the FAH. The inclusion of construction information may be too specific for an overall guidance document that addresses the Department's worldwide portfolio of commodities and services.

**Recommendation 4:** OIG recommends that the Bureau of Administration develop and implement a communications strategy to direct Contracting Officers to review requests for equitable adjustment for unauthorized commitments and to resolve unauthorized commitments in accordance with the ratification process.

**Management Response to Draft Report (02/19/25):** The Bureau of Administration, Global Acquisition, Acquisition Management Directorate (A/GA/AMD) non-concurs with this recommendation. The current process of reviewing requests for equitable adjustment already inherently adjudicates any perceived commitments and anything that is not to be authorized would not be approved as part of the equitable adjustment. Only the Contracting Officer (CO) has the authority to make changes to the terms of the contract. The contract states that, if the contractor does any such work without proper direction from the CO, they are doing the work at their own risk. Further, the Department has effective procedures in place to prevent

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unauthorized commitments and OBO has internal controls for reviewing RFIs and their technical direction, as described in OBO's response to Recommendation 3. Adding the ratification process to these existing procedures and controls would also inhibit the Department from following timelines as prescribed in the FAR (52.243-4 Changes clause and 52.233-1 Disputes clause) with regards to equitable adjustments and claims.

**Recommendation 7:** OIG recommends that the Bureau of Administration develop, implement, and communicate policies and procedures directing Contracting Officers to obtain from the responsible Project Director all required documentation related to requests for equitable adjustment for construction contracts and to document their review of all findings of fact, written request for equitable adjustment analyses, and prenegotiation memoranda provided by Project Directors to assist Contracting Officers in making merit determinations.

**Management Response to Draft Report (02/19/25):** The Bureau of Administration, Global Acquisition, Acquisition Management Directorate (A/GA/AMD) concurs with this recommendation to develop, implement, and communicate supporting organizational policies and procedures, as defined in the Department of State Acquisition Manual (DOSAM) 601.104-80(f), to ensure COs document receipt and review of all required documentation related to REAs to support its merit determinations.

**Recommendation 8:** OIG recommends that the Bureau of Administration develop, implement, and communicate policies and procedures for resolving requests for equitable adjustment.

**Management Response to Draft Report (02/19/25):** The Bureau of Administration, Global Acquisition, Acquisition Management Directorate (A/GA/AMD) concurs and will develop, implement, and communicate supporting organizational policies and procedures, as defined in the Department of State Acquisition Manual (DOSAM) 601.104-80(f), for resolving equitable adjustments.

**Recommendation 13:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, take the following actions: (1) determine whether the questioned costs of \$80,225, which were considered unsupported, for three requests for equitable adjustment for the New Embassy Compound Asuncion, Paraguay, construction contract (SAQMMA17C0082) were supported and (2) recover any costs determined to be unsupported, as shown in Table B.1.

**Management Response to Draft Report (02/19/25):** The Bureau of Administration, Global Acquisition, Acquisition Management Directorate (A/GA/AMD) non-concurs. While Part 31 cost principles apply to negotiation of modifications to FFP contracts, this does not allow us to treat FFP contracts like cost contracts. FAR 31.102 puts a gloss on using the cost principles in FFP modifications, saying that the amount agreed to in a modification is not necessarily based on the individual cost elements in the total amount. This would make it difficult to pull back amounts now determined to be unallowable. Absent fraud on the part of the contractor, it will

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not be possible to undo a bilateral modification due to a later review that disputes an individual cost element of the overall modification amount.

**Recommendation 14:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, take the following actions: (1) determine whether the questioned costs of \$5,887, which were considered unsupported, for seven requests for equitable adjustment for the New Embassy Compound Beirut, Lebanon, construction contract (SAQMMA17C0079) were supported and (2) recover any costs determined to be unsupported, as shown in Table B.2.

**Management Response to Draft Report (02/19/25):** The Bureau of Administration, Global Acquisition, Acquisition Management Directorate (A/GA/AMD) non-concurs. While Part 31 cost principles apply to negotiation of modifications to FFP contracts, this does not allow us to treat FFP contracts like cost contracts. FAR 31.102 puts a gloss on using the cost principles in FFP modifications, saying that the amount agreed to in a modification is not necessarily based on the individual cost elements in the total amount. This would make it difficult to pull back amounts now determined to be unallowable. Absent fraud on the part of the contractor, it will not be possible to undo a bilateral modification due to a later review that disputes an individual cost element of the overall modification amount.

**Recommendation 15:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, take the following actions: (1) determine whether the questioned costs of \$25,663, which were considered unsupported, for six requests for equitable adjustment for the New Embassy Compound Tegucigalpa, Honduras, construction contract (19AQMM19C0223) were supported and (2) recover any costs determined to be unsupported, as shown in Table B.3.

**Management Response to Draft Report (02/19/25):** The Bureau of Administration, Global Acquisition, Acquisition Management Directorate (A/GA/AMD) non-concurs. While Part 31 cost principles apply to negotiation of modifications to FFP contracts, this does not allow us to treat FFP contracts like cost contracts. FAR 31.102 puts a gloss on using the cost principles in FFP modifications, saying that the amount agreed to in a modification is not necessarily based on the individual cost elements in the total amount. This would make it difficult to pull back amounts now determined to be unallowable. Absent fraud on the part of the contractor, it will not be possible to undo a bilateral modification due to a later review that disputes an individual cost element of the overall modification amount.

**Recommendation 16:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, take the following actions: (1) determine whether the questioned costs of \$3,078,171, which were considered unallowable, for two requests for equitable adjustment for the New Embassy Compound Beirut, Lebanon, construction contract (SAQMMA17C0079) were allowable and (2) recover any costs determined to be unallowable, as shown in Table B.4.

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**Management Response to Draft Report (02/19/25):** The Bureau of Administration, Global Acquisition, Acquisition Management Directorate (A/GA/AMD) non-concurs. While Part 31 cost principles apply to negotiation of modifications to FFP contracts, this does not allow us to treat FFP contracts like cost contracts. FAR 31.102 puts a gloss on using the cost principles in FFP modifications, saying that the amount agreed to in a modification is not necessarily based on the individual cost elements in the total amount. This would make it difficult to pull back amounts now determined to be unallowable. Absent fraud on the part of the contractor, it will not be possible to undo a bilateral modification due to a later review that disputes an individual cost element of the overall modification amount.

**Recommendation 17:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, take the following actions: (1) determine whether the questioned costs of \$173,720, which were considered unallowable, for six requests for equitable adjustment for the New Embassy Compound Tegucigalpa, Honduras, construction contract (19AQMM19C0223) were allowable and (2) recover any costs determined to be unallowable, as shown in Table B.5.

**Management Response to Draft Report (02/19/25):** The Bureau of Administration, Global Acquisition, Acquisition Management Directorate (A/GA/AMD) non-concurs. While Part 31 cost principles apply to negotiation of modifications to FFP contracts, this does not allow us to treat FFP contracts like cost contracts. FAR 31.102 puts a gloss on using the cost principles in FFP modifications, saying that the amount agreed to in a modification is not necessarily based on the individual cost elements in the total amount. This would make it difficult to pull back amounts now determined to be unallowable. Absent fraud on the part of the contractor, it will not be possible to undo a bilateral modification due to a later review that disputes an individual cost element of the overall modification amount.

**Recommendation 18:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, (1) review all contract modifications for the New Embassy Compound Tegucigalpa, Honduras, construction contract (19AQMM19C0223) to identify all costs associated with violations of the cost principle requirements in Federal Acquisition Regulation 31.203, which govern the selection of a distribution base for allocating indirect costs, and (2) recover any costs determined to be unallowable.

**Management Response to Draft Report (02/19/25):** The Bureau of Administration, Global Acquisition, Acquisition Management Directorate (A/GA/AMD) concurs and will review all future contract modifications for this contract for violations of cost principals and include the recovery of unallowable costs as part of future outstanding negotiations.

**Recommendation 19:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, (1) review all contract modifications for the New Embassy Compound Beirut, Lebanon, construction contract (SAQMMA17C0079) to identify all costs associated with violations of the cost principle requirements in Federal

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Acquisition Regulation 31.203, which govern the selection of a distribution base for allocating indirect costs, and (2) recover any costs determined to be unallowable.

**Management Response to Draft Report (02/19/25):** The Bureau of Administration, Global Acquisition, Acquisition Management Directorate (A/GA/AMD) concurs and will review all future contract modifications for this contract for violations of cost principles and include the recovery of unallowable costs as part of future outstanding negotiations.

**Recommendation 20:** OIG recommends that the Bureau of Administration, in coordination with the Bureau of Overseas Buildings Operations, take the following actions: (1) determine whether the questioned costs of \$725,509, which were considered to be unsupported for request for equitable adjustment 003 for the New Consulate Compound Hyderabad, India, construction contract (SAQMMA16C0274), were supported and (2) recover any costs determined to be unsupported, as shown in Table B.6.

**Management Response to Draft Report (02/19/25):** The Bureau of Administration, Global Acquisition, Acquisition Management Directorate (A/GA/AMD) non-concurs. While Part 31 cost principles apply to negotiation of modifications to FFP contracts, this does not allow us to treat FFP contracts like cost contracts. FAR 31.102 puts a gloss on using the cost principles in FFP modifications, saying that the amount agreed to in a modification is not necessarily based on the individual cost elements in the total amount. This would make it difficult to pull back amounts now determined to be unallowable. Absent fraud on the part of the contractor, it will not be possible to undo a bilateral modification due to a later review that disputes an individual cost element of the overall modification amount.

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## APPENDIX E: OIG'S REPLY TO TECHNICAL COMMENTS FROM THE BUREAU OF OVERSEAS BUILDINGS OPERATIONS

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In addition to responding to the recommendations offered in a draft of this audit report, the Bureau of Overseas Buildings Operations (OBO) provided technical comments regarding the audit findings that did not directly relate to the Office of Inspector General's (OIG) recommendations (see Appendix C). A synopsis of OBO's most significant technical comments and OIG's reply to each are presented below:

**OBO Comment:** OBO stated that it "had concerns as early as December 12, 2024, when the OIG shared the Audit 'Highlights and Recommendations' summary and repeatedly provided feedback and requested to meet with the OIG to discuss technical corrections." OBO also stated that "OIG informed OBO that it would not make any changes to the report following a discussion."

**OIG Reply:** On December 12, 2024, OIG provided OBO and the Bureau of Administration with a document that included an overview of OIG's audit findings and anticipated recommendations. The intent of the document was to facilitate a constructive conversation at the audit exit conference that was subsequently held on December 17, 2024. During the exit conference, OBO officials requested additional information related to OIG's findings, which OIG responded to during the meeting. For example, one OBO official questioned why OIG used the phrase "did not always" in the summary document, opining that "reasonable care" or "reasonable assurance" would be more appropriate. OIG explained that it identified instances in which OBO did not comply with requirements and other instances in which OBO complied with requirements, which OIG summarized as "did not always."

On December 20, 2024, OBO officials notified OIG that OBO and the Bureau of Administration had additional questions and comments for OIG's consideration. OIG advised OBO officials that the draft report, which OIG anticipated issuing for comment in January, included additional details related to OIG's findings and should address OBO's questions. OIG also indicated that it would be willing to hold additional meetings with OBO and the Bureau of Administration to answer questions. The draft report was issued on January 22, 2025. Comments from OBO and the Bureau of Administration were due on February 5, 2025. On January 30, 2025, OBO and the Bureau of Administration requested a 2-week extension (i.e., until February 19, 2025) to respond to the draft report, which OIG granted. On February 13, 2025, OBO requested to meet with OIG, one day before comments were due. OIG stated that it would meet to discuss the report at OBO's convenience; however, OIG would not be able to authorize an additional extension to the deadline to respond to the draft report. OBO responded that instead of scheduling a meeting, it would focus on providing a response to the draft report.

**OBO Comment:** OBO stated that it "plans, designs, and executes overseas diplomatic construction projects around the world in unpredictable environments[,] which are often faced with rapidly changing security risks, political and civil unrest, evolving natural hazard threats, and malign influence." OBO also stated that it "endeavors to conduct [its] work with a

reasonable standard of care.” OBO indicated that “OIG aimed to detect every instance when an employee did not comply with requirements, [but] the reality of construction professionals in any sector is that it is unrealistic to establish and expect absolutes.” OBO cited the Government Accountability Office’s *Standards for Internal Control in the Federal Government*,<sup>3</sup> which describes internal control as a “process effected by an entity’s oversight body, management, and other personnel that provides reasonable assurance that the objectives of an entity will be achieved.” OBO stated that it has “achieved its objectives and provided this reasonable assurance.” According to OBO, if OIG expects 100 percent compliance, OBO “does not have the resources to staff the organization to achieve it.”

**OIG Reply:** In accordance with professional auditing standards, OIG selected samples of items to test (as described in Appendix A), performed the testing, and accurately reported the results. Specifically, OIG tested 30 requests for equitable adjustment (REA) and identified 14 (47 percent) constructive changes, none of which had been ratified as required. OIG also found Project Directors (PD) did not perform all required merit determination activities for 25 (83 percent) of 30 REAs. Additionally, OIG found OBO did not prepare independent government cost estimates (IGCE) for 5 (26 percent) of 20 REAs and that 11 (79 percent) of 14 IGCEs were insufficient. Furthermore, OIG found prenegotiation memoranda were not prepared for 8 (73 percent) of 11 REAs that were negotiated. OIG also found that PDs did not properly evaluate all costs for 15 (50 percent) of 30 REAs reviewed. Finally, OIG found that 20 (67 percent) of 30 REAs were not evaluated and resolved in accordance with OBO’s established goals. Based on the work performed, as reported in Finding A of this report, OIG concluded that OBO “will not have reasonable assurance that REAs are settled in a fair and reasonable manner.” The Government Accountability Office defines reasonable assurance as a “high degree of confidence, but not absolute confidence.”<sup>4</sup> Had OIG identified a lower percentage of errors during its testing, it would have characterized its conclusions differently. However, the significant percentage of errors identified during OIG’s testing demonstrates that OBO did not develop an internal control structure that provides a reasonable assurance (i.e., a high degree of confidence) that its objectives will be achieved.

**OBO Comment:** OBO stated that OIG’s “report provides some misleading conclusions due to lack of context.” As an example, OBO noted that OIG questioned \$837,172 in unsupported costs for the REAs reviewed. According to OBO, this represented four percent of the selected REAs’ \$21.4 million combined value. Furthermore, of the \$837,172, \$725,509 was for one REA related to a change in the sunscreen design for the Hyderabad, India, New Consulate Compound (NCC). OBO stated that it considers this to be a supported change. OBO stated that if that amount is removed, the amount of unsupported costs would be \$111,663, representing 0.5 percent of the combined value of the REAs audited.

**OIG Reply:** The purpose of OIG’s audit was not specifically to identify questioned costs. OIG’s objective was to determine whether the process used to reach equitable adjustments with

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<sup>3</sup> GAO-14-704G, September 2014.

<sup>4</sup> *Ibid.*, page 78.

selected construction contractors responsible for large construction contracts complied with the Federal Acquisition Regulation and Department guidance. OIG performed audit work to fulfill that objective and provided details of its testing results in Finding A of this report. One effect of the deficiencies identified was identified unsupported costs. However, the most significant effect is that the Department does not have reasonable assurance that REAs are settled in a fair and reasonable manner and cannot be assured that REAs have been properly evaluated and resolved. As a result, the Department is not positioned to properly negotiate with contractors and may incur additional costs. Furthermore, delays in contract modifications can negatively impact projects' schedules and create delays in reimbursing contractors for work that they have completed. With respect to OBO's comment that it considered the change in design for the Hyderabad NCC to be a supported change, OBO did not provide OIG any documentation that supported this statement or conclusion.

**OBO Comment:** OBO stated that it "does not consider responses to a Request for Information (RFI) to be a commitment or a change to the contract." OBO notes that it has an obligation to provide timely responses to technical questions "to avoid uncertainty and potential costly corrective work." Therefore, OBO states that it "does not consider technical direction in response to an RFI to be a potential unauthorized commitment . . . nor improper technical direction even if referenced in a subsequent modification." OBO added that its contracts "stipulate that when technical direction is provided, . . . the response does not change the terms of the contract nor does anyone other than the Contracting Officer (CO) have the authority to make changes to the terms of the contract." OBO also stated that the contract states that "if the contractor does any such work without proper direction from the CO, they are doing the work at their own risk." Finally, OBO stated that "OBO does not aim to prevent REAs, but rather considers the process to be a valuable tool for ensuring fair and reasonable resolution of contract issues."

**OIG Reply:** OIG agrees that when handled correctly, a technical response to an RFI would not be considered a commitment or a change to a contract. However, as detailed in Finding A of this report, in certain cases, OBO officials responded, either orally or in writing, to RFIs in a manner that was construed by the contractor as having the same effect as a change order, which did not comply with federal or Department guidance. OBO officials allowed contractors to proceed in accordance with OBO's direction and without ensuring the CO issued a contract modification. Contractors submitted REAs for the work, and the Department paid the contractors for the constructive changes. In fact, in three responses to RFIs, the PD informed the contractor that a request for proposal (RFP) would be issued for the changes that were agreed to, demonstrating that the PD recognized the response changed the contract requirements. However, no RFPs or contract modifications were provided. The work was completed and the contractor was paid for the work using the REA process.

OIG recognizes that OBO's contracts include language stating that contractors accept the risk for performing work that is not approved by a CO. However, OIG found that the Department generally approved REAs requested by contractors after a constructive change. Such actions can be construed by contractors as permission to change contract requirements without risk to

them and to add costs to government contracts without prior CO approval. For example, during a preconstruction conference, an OBO official reminded a contractor that the CO is the only one with authority to make decisions that affect the contract. The contractor acknowledged the CO's authority, but stated that it would often need to act in the project's best interest and proceed without official CO direction. The contractor added it will often proceed "at risk" with work approved unofficially and would take it on good faith that the CO will ultimately support the work performed. With respect to OBO's statement that it "does not aim to prevent REAs," many of the REAs reviewed for this audit were caused by constructive changes that, according to the Overseas Procurement Guide,<sup>5</sup> should be avoided.

**OBO Comment:** OBO stated that the scope period of OIG's audit was both during and directly following the COVID-19 pandemic, "an unprecedented event that had rippling effects on staffing, global supply chains, price escalation and resulting impacts on overseas construction projects. Such factors bias the OIG's sample and, as a result, OBO does not believe that many of the OIG's findings based on REAs from this period—even if correct—should result in recommendations to adjust the entire construction program."

**OIG Reply:** During the audit planning process, OIG considered the impact of COVID-19 on the REA process and the objectives of the audit. Therefore, as detailed in Appendix A of this report, OIG excluded all COVID-19 related REAs because of the predictable impact that the pandemic had on construction management, including disruptions to the construction materials and equipment supply chain and diminished labor productivity. Additionally, during the audit, OIG met with various OBO Project Directors and Bureau of Administration officials. Although some mentioned the impact that COVID-19 had on construction schedules, none provided feedback indicating that the deficiencies that OIG identified resulted from the COVID-19 pandemic.

**OBO Comment:** OBO stated that all financial information about ongoing contracts is Sensitive But Unclassified.

**OIG Reply:** On February 20, 2025, OIG requested that OBO provide specificity regarding what portions of a draft of this report it believed were Sensitive But Unclassified. OBO responded that nothing in the report was Sensitive But Unclassified.

**OBO Comment:** OBO requested that OIG clarify a statement in the Highlights page of the draft report that stated, "OIG found that PDs and Contracting Officers (CO) did not evaluate and resolve REAs in accordance with the [Federal Acquisition Regulation] and Department guidance."

**OIG Reply:** In the final report, OIG clarified the statement by indicating that OIG found that PDs and COs did not evaluate and resolve selected REAs in accordance with guidance.

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<sup>5</sup> Bureau of Administration, "Overseas Procurement Guide," Chapter 8, Section II, "Original Signed Contract and Modifications," E, "Constructive Changes."

**OBO Comment:** OBO requested that OIG clarify a statement in the Background section of the draft report that stated, “For OBO construction projects, the PD is responsible for preparing the [independent government cost estimate] using input from OBO’s staff or resources assigned to the project.”

**OIG Reply:** OIG modified the language in the Background section to clarify the statement, as requested.

**OBO Comment:** OBO stated that footnote 72 of the draft report was a “targeted” definition and requested a more “general” definition.

**OIG Reply:** OIG modified the language in footnote 72 to a general definition, as requested.

**OBO Comment:** OBO requested that OIG include more details of some of the REAs (rather than just including the REA numbers).

**OIG Reply:** As requested, OIG added details of REAs in footnotes on pages 18–19 of this report.

## ABBREVIATIONS

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AQM	Office of Acquisitions Management
ASBCA	Armed Services Board of Contract Appeals
CM	Office of Construction Management
CO	Contracting Officer
COR	Contracting Officer's Representative
FAH	Foreign Affairs Handbook
FAM	Foreign Affairs Manual
FAR	Federal Acquisition Regulation
IGCE	Independent Government Cost Estimate
NCC	New Consulate Compound
NEC	New Embassy Compound
OBO	Bureau of Overseas Buildings Operations
OIG	Office of Inspector General
OPE	Office of the Procurement Executive
PD	Project Director
REA	Request for Equitable Adjustment
RFI	Request for Information
RFP	Request for Proposal

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