OFFICE OF INSPECTOR GENERAL

Audit Report 2015-FMIC-C-012

CFPB Headquarters Construction Costs Appear Reasonable and Controls Are Designed Appropriately

On September 14, 2015, the Office of Inspector General reissued this report to reflect changes to the cost information used in our analysis. Figures in table 5 and in the narrative on page 11 describing the table have been revised accordingly. The finding and conclusions in the original report have not changed.

July 31, 2015

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
CONSUMER FINANCIAL PROTECTION BUREAU

Report Contributors

James Keegan, OIG Manager
Lindsay Mough, Project Lead
Jackie Ogle, Auditor
Jennifer Ksanznak, Auditor
Cynthia Gray, Senior OIG Manager for Financial Management and Internal Controls
Melissa Heist, Associate Inspector General for Audits and Evaluations

Abbreviations

A/E	architecture and engineering
CFPB	Consumer Financial Protection Bureau
CO	contracting officer
Dodd-Frank Act	Dodd-Frank Wall Street Reform and Consumer Protection Act
GAO	U.S. Government Accountability Office
GSA	U.S. General Services Administration
IRB	Investment Review Board
LEED	Leadership in Energy and Environmental Design
MOU	memorandum of understanding
OCC	Office of the Comptroller of the Currency
OIG	Office of Inspector General
OTS	Office of Thrift Supervision
RWA	reimbursable work authorization
Treasury	U.S. Department of the Treasury

Executive Summary:

CFPB Headquarters Construction Costs Appear Reasonable and Controls Are Designed Appropriately

2015-FMIC-C-012 **July 31, 2015**

Purpose

Our objectives were to (1) evaluate the reasonableness of the overall estimated and proposed costs for the Consumer Financial Protection Bureau's (CFPB) headquarters renovation and (2) assess the effectiveness of the CFPB's processes and controls for approving, managing, and documenting headquarters renovation costs and project decisions.

Background

In June 2014, we completed a review and issued a letter to address a request from the Chairman of the Subcommittee on Oversight and Investigations, House Committee on Financial Services, regarding the CFPB's headquarters renovation budget. That review included an evaluation of the budgeting and approval process, the scope and justification for estimates, and the use of competitive procedures for the renovation project. As a continuation of that work, we conducted this audit of the CFPB's renovation costs.

Finding

We determined that construction costs appear reasonable based on comparisons to an independent cost estimate and the costs of two comparable building renovations identified by the U.S. General Services Administration. We also determined that potential renovation costs are below the amount previously budgeted and obligated for the renovation. In addition, we conducted a life cycle analysis to compare the costs of renting and renovating the building to leasing comparable space over a 30-year period. We determined that the reasonableness of this decision is highly dependent on the growth in commercial lease rates. Therefore, we identified the approximate growth rate at which our analysis shifts from favoring leasing space to favoring renting and renovating the building. This rate falls within the range of projected growth rates for commercial leases at the time the CFPB agreed to occupy the building.

Current controls for approving, managing, and documenting renovation costs and project decisions are designed appropriately; however, because most construction cost-management control activities have not yet begun, we did not have the opportunity to test the operating effectiveness of those controls. In addition, we noted that the initial renovation decision predated controls for documenting project costs and decisions.

The construction contract awarded in December 2014 includes two options that would result in additional costs to the CFPB if exercised. As we previously reported, the CFPB did not fully comply with the Investment Review Board (IRB) guidance for approving renovation costs. Therefore, the CFPB should prepare and submit a final, complete business case to the IRB for the optional investments prior to obligating funds.

On June 22, 2015, the CFPB provided us with an IRB business case with preliminary cost information for one of these options. As the business case was provided after the conclusion of our fieldwork and may still be updated, we will evaluate the final business case as part of our audit follow-up process.

Recommendation

Our report contains a recommendation designed to provide the CFPB with assurance that additional investments related to the renovation are sound business decisions. The CFPB can accomplish this by preparing and submitting a final, complete business case to the IRB for approval prior to obligating funds. In its response to our draft report, the CFPB concurs with our recommendation.

Summary of Recommendation, OIG Report No. 2015-FMIC-C-012

Rec. no.	Report page no.	Recommendation	Responsible office
1	18	Prepare and submit a complete business case to the Investment Review Board for approval prior to obligating funds if the CFPB plans to exercise the facilities operations and maintenance services option or finalize the retail tenant buyout agreement.	Office of the Chief Administrative Officer

OFFICE OF INSPECTOR GENERAL

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

CONSUMER FINANCIAL PROTECTION BUREAU

July 31, 2015

MEMORANDUM

TO: Sartaj Alag
Chief Operating Officer
Consumer Financial Protection Bureau

FROM: Melissa Heist
Associate Inspector General for Audits and Evaluations

SUBJECT: OIG Report No. 2015-FMIC-C-012: *CFPB Headquarters Construction Costs Appear Reasonable and Controls Are Designed Appropriately*

The Office of Inspector General (OIG) has completed its final report on the subject audit. We conducted this audit to (1) evaluate the reasonableness of the overall estimated and proposed costs for the Consumer Financial Protection Bureau's (CFPB) headquarters renovation and (2) assess the effectiveness of the CFPB's processes and controls for approving, managing, and documenting headquarters renovation costs and project decisions.

We provided you with a draft of our report for review and comment. In your response, you concur with our recommendation. We have included your response as appendix C in our report.

We appreciate the cooperation that we received from CFPB staff members during our audit. Please contact me if you would like to discuss this report or any related issues.

cc: Suzanne Tosini, Chief Administrative Officer
Stephen Agostini, Chief Financial Officer
J. Anthony Ogden, Deputy Inspector General

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Introduction

Objectives

In June 2014, we completed a review and issued a letter to address a request from the Chairman of the Subcommittee on Oversight and Investigations, House Committee on Financial Services, regarding the Consumer Financial Protection Bureau's (CFPB) headquarters renovation budget.[1] That review included an evaluation of the budgeting and approval process, the scope and justification for estimates, and the use of competitive procedures for the renovation project. As a continuation of that work, we conducted this audit of the CFPB's renovation costs.

Our objectives were to (1) evaluate the reasonableness of the overall estimated and proposed costs for the CFPB's headquarters renovation and (2) assess the effectiveness of the CFPB's processes and controls for approving, managing, and documenting headquarters renovation costs and project decisions. Because the construction contract was awarded during the course of our audit, we assessed the costs associated with the awarded contract in lieu of proposed costs.

Background

The Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), enacted July 21, 2010, established the CFPB as an independent bureau within, but autonomous from, the Federal Reserve System. The Dodd-Frank Act prescribes that a presidentially appointed, Senate-confirmed Director is to lead the CFPB. Prior to the appointment of a CFPB Director,[2] the Dodd-Frank Act assigned to the Secretary of the Treasury certain CFPB functional responsibilities. The Secretary delegated this interim authority to the Special Advisor to the Secretary and to other U.S. Department of the Treasury (Treasury) officials who worked to stand up the CFPB.

1700 G Street NW Building

On February 18, 2011, Treasury announced that the future permanent headquarters of the CFPB would be located at 1700 G Street NW, Washington, DC. This announcement, which predated the beginning of the CFPB's operations,[3] noted that major building renovations were needed to make more efficient use of the space and to update the building to meet current energy and environmental standards.

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1. Office of Inspector General, Response to the January 29, 2014, Congressional Request Regarding the CFPB's Headquarters Renovation Project, June 30, 2014, http://oig.federalreserve.gov/reports/cfpb-congressional-request-headquarters-renovation-project-jun2014.htm.

2. The Director of the CFPB was appointed by the President on January 4, 2012, and confirmed by the Senate on July 16, 2013.

3. The CFPB began operations in July 2011.

The building at 1700 G Street NW had been used by the Office of Thrift Supervision (OTS) as its headquarters. When the Dodd-Frank Act abolished OTS, its interests in the building transferred to the Office of the Comptroller of the Currency (OCC) effective July 21, 2011.[4] Prior to the building's transfer to the OCC, a Treasury official, acting on behalf of the CFPB, signed a letter of intent with the OCC in January 2011 for the CFPB to occupy the building. The major points of the letter include the following:

- The CFPB would lease the entire building from the OCC as is.
- The OCC and the CFPB would mutually agree on the terms and conditions of the lease for the building and on a rental payment at a market rate, including a market escalation over the term of the lease.
- The CFPB would retain the childcare center in the building and establish an agreement with the center for use of space in the building.

The CFPB moved into the building on October 1, 2011, under an interim agreement with the OCC. On February 10, 2012, the U.S. General Services Administration (GSA) provided the OCC with a delegation of authority to charge rent for the building, and on February 17, 2012, the OCC and the CFPB entered into an occupancy agreement. The agreement includes terms that the CFPB (1) will pay fair market rent,[5] (2) will be responsible for the cost of any building improvements, (3) will obtain the OCC's approval prior to taking any action that may affect the retail tenants, and (4) will ensure that the normal business operations of the retail tenants are not disrupted by alterations or improvements to the premises made by the CFPB. The occupancy agreement includes a base period of 20 years, which the CFPB can opt to extend for two additional 5-year periods. The OCC can cancel this agreement only if the CFPB fails to pay rent or fails to comply with other material terms of the agreement.

Renovation Project Contracts and Agreements

As of January 2015, three major contracts had been awarded for the CFPB headquarters building renovation: an architecture and engineering (A/E) contract, a construction management contract, and a construction contract. The CFPB awarded the A/E contract for design services and subsequently executed a memorandum of understanding (MOU) and a reimbursable work authorization (RWA) with GSA for the renovation of the building. Pursuant to the MOU, GSA awarded the construction management and construction contracts on behalf of the CFPB.

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4. As noted in the Treasury Office of Inspector General report *OCC's Leasing Activities Conformed With Applicable Requirements; Issues With the Former OTS Headquarters Building Need to Be Resolved*, the OCC Chief Counsel's Office reviewed documentation related to ownership of the former OTS headquarters building, as well as applicable laws and regulations related to the transfer and ownership of the building, and concluded that the OCC owns the building. As of May 2015, the U.S. Government Accountability Office is reviewing whether the OCC has the legal authority to retain the rent.

5. The OCC and the CFPB agreed to a $34-per-square-foot rental rate, escalated at 2 percent per year over the life of the occupancy agreement. We noted that in 1998, the U.S. Department of Housing and Urban Development also paid $34 per square foot, to OTS, for the use of space in the 1700 G Street NW building.

Architecture and Engineering Contract

In September 2012, the CFPB awarded a contract for A/E design services for a not-to-exceed amount of $12 million in support of the renovation project. The CFPB used the competitive procedures outlined in subpart 36.6 of the *Federal Acquisition Regulation*. These procedures include using an evaluation board to evaluate and rank firms based on technical qualifications prior to the contracting officer (CO) beginning price negotiations. The negotiations resulted in the award of an indefinite-delivery, indefinite-quantity contract providing for the issuance of task orders throughout the contract period. As of January 2015, the CFPB had awarded four task orders against the A/E contract and obligated $9.5 million.[6]

Agreements With GSA

In September 2013, the CFPB signed an MOU and an RWA with GSA for the renovation of the building.[7] The MOU established responsibilities for GSA related to project management, including procurement, design review services, construction, and contract administration for the renovation of the building. The MOU specified that the project involves the modernization of the overall building, including significant improvements to the building site, structure, interior finishes, and major systems.

In September 2013, the CFPB executed an RWA with GSA to obligate $145.1 million for the building renovation. This funding amount is inclusive of construction, construction management, contingencies, and fees and is based on an estimate prepared by GSA in July 2013.[8] While GSA subsequently revised the $145.1 million estimate to $139.1 million to reflect the CFPB's decision to exclude construction of a seventh floor, the funding obligated by the CFPB under the RWA remains at $145.1 million. Pursuant to the MOU and within the funding limitations of the RWA, GSA awarded construction management and construction contracts.

Construction Management Activities

In July 2014, GSA awarded a firm-fixed-price construction management contract for $4.4 million using the best value tradeoff process[9] included in subpart 15.101 of the *Federal Acquisition Regulation*. This contract requires the construction management company to provide services, including cost management, schedule development and maintenance, change management, quality control, quality assurance, reporting, value engineering, and design reviews for the building renovation.

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6. Where necessary, we rounded dollar figures in the text of the report to the relevant decimal point.

7. The MOU with GSA was not fully executed until October 2013 due to the partial closure of the federal government.

8. The estimate was prepared using a cost modeling worksheet that uses historical data to generate costs for major building systems based on the gross area of the project and major building systems quality levels.

9. The best value tradeoff process is a competitive acquisition strategy designed to permit tradeoffs between price and nonprice factors. Under this acquisition strategy, the solicitation must identify the relationship between these factors used for evaluation of proposals.

Construction management activities have also included the development of an independent cost estimate by a third-party project management firm with construction expertise. This project management firm based the independent cost estimate on the A/E contractor's design documents and provided the estimate to GSA in July 2014.

Construction Contract

In December 2014, GSA awarded a firm-fixed-price construction contract for $99.4 million[10] using the two-phase design-build selection process[11] described in subpart 36.3 of the *Federal Acquisition Regulation*. The contract is structured as a base contract for the full renovation of the building and includes 10 options for additional supplies or services that can be exercised unilaterally by the CFPB at any time during the contract's period of performance. The contract also established unit prices for materials or services that can be added or deducted from the contract price if the required scope of work is increased or decreased. See table 1 for a description of the base contract, options, and unit prices.

10. The contract value is solely for construction costs and does not include the contingency, fees, overhead, and construction management costs included in the $145.1 million RWA.

11. The two-phase process includes a phase I request for qualifications followed by a phase II request for proposals. During phase I, proposals are evaluated and the government selects the most highly qualified offerors to submit proposals for phase II. The phase II request for proposals results in the selection of the construction contractor whose offer provides the best value to the government.

Table 1: Summary of Construction Contract Elements and Costs[a]

Contract elements	Description	Cost ($ millions)
Base	To turn over a complete and functional building for the renovation of the CFPB headquarters.	$97.7
Option 1: Childcare center	Construction of the childcare center pursuant to the contract documents. In the event that this is not exercised, Option 10 is to be performed.	$4.1
Options 2–8: Construction of retail space	Construction of retail space, including demolition, storefronts, skylights, and interior fit-out.	Not applicable[b]
Option 9: Facilities operations and maintenance services	Provide a three-year service contract for operating and maintaining the building on construction completion.	$6.2
Option 10: Operational retail	In the event that Option 1 is not exercised, this option provides for an alternative scope of work based on the continued operation of the retail tenant that currently occupies the space where the childcare center would be located.	$1.8
Unit prices	Prices per unit of measurement for materials or services for room construction and fit-out, HAZMAT testing and reporting, and stone and concrete repair work. For each of the unit price categories, the contractor's proposal contains estimated quantities and total cost for each unit price. These are totaled for total unit price offers.	To be determined[c]

Source: OIG summary of contract elements.

[a]The costs in the table are rounded.
[b]The costs of retail construction are the responsibility of the OCC, not the CFPB.
[c]As unit prices can be added or deducted from the contract price if the scope of work changes, we did not include the associated costs in our summary of contract elements.

GSA initially awarded the base contract plus Option 10. The remaining options, including Option 1, can be awarded at any time during the contract's period of performance, while unit prices can be added or deducted from the contract price at any time during the design phase. In the event that the CFPB exercises Option 1, Option 10 will no longer be performed because it provides for an alternative scope of work only in the event that Option 1 is not exercised. In June 2015, the CFPB directed GSA to exercise Option 1.

Results of Analysis: Renovation Costs

We found that (1) the CFPB followed required processes in evaluating the price reasonableness of A/E costs, (2) construction costs appear reasonable based on comparisons to an independent cost estimate and the costs of two comparable building renovations, and (3) potential renovation costs are below the amount previously budgeted and obligated for the renovation. In addition, we conducted a life cycle analysis to compare the costs of renting and renovating the building to leasing comparable space over a 30-year period. We determined that the reasonableness of the decision is highly dependent on the growth in commercial lease rates. Therefore, we identified the approximate growth rate at which our analysis shifts from favoring leasing space to favoring renting and renovating the building. This rate falls within the range of projected growth rates for commercial leases at the time the CFPB agreed to occupy the building.

The CO Followed the *Federal Acquisition Regulation* in Determining the Price Reasonableness of the A/E Contract

The CFPB awarded an indefinite-delivery, indefinite-quantity contract for A/E design services for a not-to-exceed amount of $12 million. This contract type provides for the issuance of task orders throughout the contract period. As of January 2015, the CFPB had awarded four task orders against the A/E design services contract and obligated $9.5 million.[12] As described below, we reviewed the CO's price reasonableness determination for the overall contract fee for the A/E contract, as well as for individual task orders and modifications above $500,000,[13] and we found that the CO followed the required processes outlined in the *Federal Acquisition Regulation* to determine price reasonableness.

Overall Contract Fee

Subpart 36.6 of the *Federal Acquisition Regulation* states that negotiations for A/E contracts should be conducted in accordance with part 15 of the *Federal Acquisition Regulation*. These negotiations begin with the most preferred firm as ranked by the evaluation board, based on technical qualifications. Subpart 15.4 of the *Federal Acquisition Regulation* prescribes cost and price negotiation policies for pricing negotiated prime contracts. Under subpart 15.404-1 of the *Federal Acquisition Regulation*, the CO is responsible for evaluating the reasonableness of offered prices.

We found that the CO conducted negotiations with the most preferred firm and prepared a negotiation memorandum. The negotiation memorandum detailed the events and rationale that led

12. On February 23, 2015, the CFPB issued task order 5 for $2.2 million. Because this task order was awarded after the conclusion of our fieldwork, it was not included in our analysis.

13. Modifications to task orders included extending the period of performance, changing key personnel, and adding funds for additional work. For our price reasonableness analysis, we only reviewed modifications to add funds.

to the award of the A/E contract and documented the CO's determination that the overall contract fee was fair and reasonable. In making this determination, the CO used technical assistance from reports provided by two project management firms specializing in construction design, as permitted by the *Federal Acquisition Regulation*.

Both reports included analyses and comments on the contractor's overall proposed fee and indicated that a lower fee should be negotiated based on other similar projects. In addition, one report provided specific comments and recommendations related to labor rates, escalation, overhead, and profit. The CO used the reports' recommendations to set a negotiation objective for the overall fee and as discussion points during negotiations. As a result of negotiations, the CO was able to achieve savings on key aspects of the contract, including a reduction of $3.6 million in the proposed overall fee. In addition, the CO found the proposed labor rates to be fair and reasonable based on research and analysis.

Task Orders

In addition to reviewing the reasonableness of offered prices, subpart 15.404-1 of the *Federal Acquisition Regulation* states that the CO should request that personnel having specialized knowledge or experience perform an analysis of proposed resources, and that at a minimum, the analysis should examine the need for the types and quantities of labor hours and the labor mix. This analysis should be performed to ensure that the level of effort is appropriate.

As of January 2015, the CFPB had awarded four task orders against this A/E design services contract. We found that the CO determined that the level of effort for each task order and modification we reviewed was reasonable. In making each determination, the CO used sources with specialized knowledge. Specifically, the CO used a project management firm specializing in construction design to provide technical assistance in analyzing the price reasonableness of task order 1. For all subsequent task orders and modifications within our scope, we reviewed documentation provided by the CO showing that the CFPB project manager reviewed and approved the level of effort prior to award.

In reviewing memorandums to the file, we noted that the CO stated the price proposals reflected the contract labor rates previously found to be fair and reasonable. We analyzed the accepted pricing sheets and confirmed that the correct contract labor rates were proposed.[14] We also noted that the project manager provided the CO with the results of the level of effort reviews. For task order 2, the project manager considered the level of effort to be excessive based on a review of proposed labors hours. Through negotiations, the CO obtained a $350,645 reduction to the task order price.

14. In analyzing profit and overhead, we noted nonmaterial errors with the application of profit on subcontractor costs. We have brought this to the attention of the CFPB.

Construction Costs Are Consistent With an Independent Cost Estimate and the Cost of Comparable Projects

To evaluate the reasonableness of the construction costs, we compared these costs to an independent cost estimate and the costs of two comparable renovations provided by GSA. We found the construction costs to be consistent with these benchmarks and concluded that the construction costs appear reasonable. We also determined that potential renovation costs are below the amount previously budgeted and obligated for the renovation. In addition, we compared the life cycle costs of renting and renovating the building to leasing comparable space over a 30-year period.[15] We determined that the reasonableness of the decision is highly dependent on the growth in commercial lease rates. Therefore, we used a range of growth rates to identify the approximate point at which our analysis shifts from favoring leasing space to favoring renting and renovating the building.

Appendix B describes our calculations of awarded construction costs, potential construction costs, and potential renovation costs that we used in our comparative analyses as well as potential all-in costs that we used in our life cycle analysis.

Comparison of Awarded Construction Costs to an Independent Cost Estimate

The construction contract was initially awarded for $99.4 million and included the costs of the base contract for the building renovation and Option 10 for operational retail.[16] To evaluate these awarded construction costs, we identified the costs of these same elements in a cost estimate independently prepared by a third-party project management firm[17] and compared them to the construction contract award amount. As shown in table 2, we determined that the awarded construction costs were $24.3 million below the independent cost estimate for the same contract elements.

15. The CFPB does not have leasing authority. However, we use this term to differentiate between the scenarios outlined in our analysis.

16. In June 2015, the CFPB directed GSA to exercise Option 1 for construction of the childcare center. We performed the analysis in table 2 using the construction costs initially awarded. In updating costs to reflect the exercise of Option 1, we determined that the awarded construction costs would be $26.2 million below the independent cost estimate. For our remaining analyses, we already accounted for Option 1 by using the highest cost combination of options.

17. This estimate is based on the A/E contractor's design documents.

Table 2: Difference Between the Independent Cost Estimate and Construction Contract Award Amount

Independent cost estimate ($ million)	Contract award ($ million)	Difference ($ million)	Percent difference
123.8	99.4	24.3	21.8

Source: OIG analysis of awarded construction costs and independent cost estimate.

Note: Calculations may differ slightly due to rounding.

Comparison of Potential Construction Costs to Other Building Construction Costs

GSA identified two building renovations comparable to the CFPB renovation and provided us with construction costs per gross square foot for each. To determine whether the CFPB's potential costs are consistent with these renovations, we compared those costs to the construction cost figures provided by GSA.[18] To account for the potential construction costs the CFPB could incur, we added the highest cost combination of options[19] included in the construction contract, all unit price offers,[20] and other costs, such as a construction contingency, to the base contract for a total of $128.6 million. We then divided these costs by the gross square footage in the independent cost estimate[21] to calculate the CFPB's potential construction costs per gross square foot. As shown in table 3, we calculated the CFPB's potential construction costs as $285.32 per gross square foot, which is $3.46 and $41.42 per gross square foot less than the comparable renovations.

18. It was necessary to conduct this analysis on a per-square-foot basis to account for the difference in size of the buildings.

19. As shown in table 1, the costs of Options 2–8 would be borne by the OCC and, therefore, were not included in our calculation. In addition, we included Option 1 in lieu of Option 10, as it is the more costly alternative. Further, to be conservative in our analyses, we included Option 9 in our calculation, even though it is for maintenance services rather than construction.

20. The contract established unit prices for materials or services that can be added or deducted from the contract price if the required scope of work is increased or decreased. The contractor's proposal contains estimated quantities and total cost for each unit price. We totaled these to arrive at the total unit price offers that we used in our calculations.

21. The gross square footage includes the gross square footage of the base building, including the basement, the garage, and the potential childcare center, but excludes the retail space and courtyard.

Table 3: Difference Between Comparable Construction Costs and CFPB Potential Construction Costs per Gross Square Foot[a]

Comparable renovations	Comparable construction costs[b]	CFPB potential construction cost	Difference	Percent difference
Building 1	$288.78	$285.32	$3.46	1.2
Building 2	$326.74	$285.32	$41.42	13.5

Source: OIG analysis of contract pricing compared to GSA comparable renovations.

[a]The figures in the table are rounded.
[b]Comparable construction costs per gross square foot were calculated by GSA.

Comparison of Potential Renovation Costs to the CFPB's Renovation Budget

In addition to construction costs, the CFPB's $145.1 million renovation budget includes construction management costs and GSA fees. Therefore, to estimate potential renovation costs, we added the costs associated with construction management and GSA fees to the potential construction costs described in the previous section. We then compared the potential renovation costs to the $145.1 million to determine whether the CFPB is within its renovation budget. As shown in table 4, we calculated potential renovation costs to be $6.4 million below the amount budgeted and obligated for the renovation.

Table 4: Difference Between Renovation Budget and Potential Renovation Costs[a]

CFPB renovation budget ($ million)	Potential renovation costs ($ million)	Difference ($ million)	Percent difference
145.1	138.7	6.4	4.5

Source: OIG analysis of contract pricing and RWA.

[a]The figures in the table are rounded.

Analysis of Renovating Versus Leasing Comparable Space

The CFPB decided to rent and renovate the 1700 G Street NW building (renovating scenario) rather than lease a building of a similar size (leasing scenario). To evaluate the CFPB's decision to renovate, we compared the net present value of the renovating scenario to the net present value of the leasing scenario over the CFPB's 30-year occupancy agreement period.[22] To estimate the cost of the renovating scenario, we included all obligations and budgeted costs associated with renovating, as well as the cost to rent the building over the 30-year occupancy agreement. To calculate the cost of the leasing scenario, we included potential rent using GSA's projected rate

22. As noted in our June 30, 2014, response letter to the congressional request, CFPB officials provided us with a ballpark analysis intended to make sure that the decision to renovate made sense. We noted certain renovation cost elements were not included in the analysis. Therefore, we conducted our own life cycle analysis.

for a fully serviced lease in Washington, DC; estimated tenant improvement costs; estimated security costs; and the GSA fee. Our analysis does not consider qualitative factors.[23]

We determined that the reasonableness of the decision to renovate is highly dependent on growth in commercial lease rates. Therefore, we used a range of growth rates in the leasing scenario to determine the approximate growth rate at which the financial analysis shifts from favoring a leasing scenario to favoring a renovating scenario. As shown in table 5, when we escalated lease rates at 3.75 percent and 4 percent annually, the cost to lease would be lower, and at 4.25 percent and 4.5 percent annually, the cost to renovate would be lower. Therefore, the approximate point at which the financial analysis shifts from favoring a leasing scenario to favoring a renovating scenario is between 4 percent and 4.25 percent.

Table 5: Summary of Net Present Value Analysis[a]

Leasing scenario growth rate (%)	Difference of net present value scenarios ($ million)	Scenario supported by net present value calculation
3.75	-23.4	Leasing
4.00	-6.5	Leasing
4.25	11.2	Renovating
4.50	29.7	Renovating

Source: OIG summary of results of net present value analysis.

[a]The costs in the table are rounded.

We noted that at the time the CFPB signed the occupancy agreement for the building, effective rent rates for commercial office space in the Washington, DC, market were projected to increase between 2.3 percent and 4.5 percent annually for the following five years. The growth rate at which our analysis shifts from favoring leasing to favoring renovating falls within this range. We also noted that as of fourth quarter 2014, effective rent rates were projected to increase 3.7 percent to 4.5 percent annually for the following five years, indicating that commercial lease rates are still projected to grow.

23. Revised Office of Management and Budget Circular A-94, *Guidelines and Discount Rates for Benefit-Cost Analysis of Federal Programs*, states that "all future benefits and costs, including nonmonetized benefits and costs, should be discounted" in a net present value analysis. In cases in which monetary values of some benefits and costs cannot be determined, "a comprehensive enumeration of the different types of benefits and costs, monetized or not, can be helpful in identifying the full range of program effects."

Results of Analysis: Processes and Controls

Overall, we found that the CFPB's processes and controls appear to be designed appropriately for approving, managing, and documenting headquarters renovation costs and project decisions. However, as most construction cost-management control activities have not yet begun, we did not have the opportunity to test the operating effectiveness of those controls. In addition, we noted that the initial renovation decision predated controls for documenting project costs and decisions.

Controls Are in Place to Approve Renovation Costs

The CFPB has a formal process to review major investments. Major investments include those with an estimated value of $500,000 or more, or a life cycle cost of $2.5 million or more over five years. These investments must be reviewed by the CFPB's Investment Review Board (IRB), an executive advisory body chaired by the Chief Financial Officer. To obtain IRB approval, program offices must complete an IRB business case that outlines and supports the investment. If the IRB approves the business case, the program office may submit a control sheet for approval to obligate funds. This process is an important funding control because funds are not available for obligation or expenditure until the IRB approves the investment. As previously reported and further discussed in the Finding section of this report, we noted that the approval of funding for the renovation was not in accordance with the CFPB's policy for major investments.

Controls Are in Place to Manage Renovation Costs

We noted that the CFPB has controls in place to manage the renovation's overall budget and costs. These controls include the RWA and the MOU with GSA that establish overall budget controls. In addition, the construction and construction management contracts include cost management controls specific to managing costs throughout the design and construction phases of the renovation project.

Controls to Manage the Renovation Budget

The CFPB's controls for the management of the overall renovation budget include the RWA and the MOU with GSA. The RWA established funding of $145.1 million for the renovation project, and the CFPB included this amount in its budget. The RWA also serves as an overall cost control because it requires GSA to seek an amendment from the CFPB for additional funding prior to incurring costs above the RWA amount. As noted in the Results of Analysis: Renovation Costs section, we calculated the CFPB's potential renovation costs to be $6.4 million below the original RWA amount. While the RWA serves as a control over funding, controls to manage construction costs are necessary, as discussed in the Controls to Manage Construction Costs section below.

In addition, the CFPB entered into an MOU with GSA that lays out the respective responsibilities of both parties. The document establishes that the CFPB has overall responsibility and approval

authority for all aspects of the renovation project, including the renovation budget. The MOU reiterates that GSA must request additional funding from the CFPB prior to awarding any contracts over the RWA amount. The MOU also requires GSA to (1) receive the CFPB's written authorization prior to any procurements made on the CFPB's behalf and (2) provide written notification to the CFPB when the costs incurred and outstanding commitments reach 80 percent of the estimated total project costs. These provisions in the MOU give the CFPB additional oversight and control of the overall renovation budget.

Controls to Manage Construction Costs

With the award of the construction contract, the need for controls expanded from the overall budget, which has been established, to ongoing management of construction costs within that budget. The RWA and the MOU remain important controls throughout the life cycle of the renovation project; however, GSA notes in its cost-estimating and cost-management criteria document that effective cost management is needed throughout the design and construction phases to ensure that costs are within scope and budget. We found that both the construction and construction management contracts for the CFPB renovation provide important cost management controls.

Construction Contract

The construction delivery method can affect cost management practices. The CFPB selected the design/build-bridging delivery method for the renovation project, and both the MOU and construction contract specified the use of this method. The design/build-bridging method is a blend of traditional design and design-build methods, in which the project owner produces limited drawings and specifications through a bridging architect, leaving finalization of these documents and construction to a follow-on design-builder who will become the architect-of-record. Both GSA and the Construction Management Association of America note advantages to using the design/build-bridging method, including the project owner's additional control over the design and corresponding costs and the improved ability to meet stringent schedule requirements.

The objective of cost controls in construction is to complete the contracts within budget, and the type of construction contract selected can help accomplish this objective. The construction contract for the CFPB renovation project was awarded as a firm-fixed-price contract. According to the *Federal Acquisition Regulation*, subpart 16.202-1, a firm-fixed-price contract provides for a price that is not subject to any adjustment on the basis of the contractor's cost experience in performing the contract and provides maximum incentive for the contractor to control costs and perform effectively. After the award of a firm-fixed-price contract, the contractor becomes responsible for completing the work at the fixed price unless the contract is amended to alter the price. A firm-fixed-price contract can help ensure that the renovation costs remain within the budget and can be an important cost management control.

Construction Management Contract

With the award of the firm-fixed-price construction contract, the focus of cost control shifts to managing changes to the contract so that the original award amount and agreed-upon changes are within the construction budget. We reviewed the construction management contract to identify specific processes and controls in place to manage costs. The contract states that the construction management firm is responsible for managing the design/build-bridging construction project with an emphasis on meeting goals relating to schedule, budget, scope, and quality.

The construction management contract contains provisions for design reviews and value engineering.[24] Specifically, the construction management firm is responsible for coordinating all design reviews and reconciling any conflicting review comments. The construction management firm is also responsible for ensuring that all comments have been incorporated or otherwise addressed and documenting any unresolved comments in the design review report. The U.S. Government Accountability Office (GAO) considers design reviews to be a useful practice for managing costs. The construction management firm is also required to conduct value engineering workshops during the design phase of the project and provide a value engineering expert as well as independent experts to conduct these workshops. Designed building features, systems, equipment, and material selections are to be analyzed through value engineering prior to the selection of final design features. In discussing specific design features, GSA officials explained that in addition to cost, functionality and aesthetics should also be considered. For example, a design feature may help the CFPB meet Leadership in Energy and Environmental Design (LEED) standards,[25] be used for maintenance considerations, or have a higher upfront cost that could result in cost savings over the life of the item. The Office of Management and Budget and GAO note the importance of value engineering as a recognized technique for reducing costs while maintaining or improving productivity and quality. Both value engineering and design reviews serve as valuable tools for managing renovation costs.

The construction management contract also requires the construction management firm to provide a finance manager. The finance manager's responsibilities include (1) providing financial management expertise, (2) monitoring all obligations and costs expended, (3) making recommendations for decisions relevant to the project's budgeting and expenditures, (4) providing advice and monitoring whether the project is being designed within budget, (5) tracking overall project costs to determine whether they are within the available funding authority, and (6) providing monthly status reports. The finance manager's expertise will be critical in managing renovation costs during the design and construction phases.

In addition, the construction management firm is required to prepare independent cost estimates for all design submissions and any change orders, compare the estimates with those prepared by the contractor, and reconcile cost differences. Further, the firm is required to attend preinvoice payment meetings with the GSA project team and the CFPB before submitting payment requests. The purpose of these meetings is to discuss the amounts of prospective payments and the supporting documentation required and to reach agreements on the amounts payable to the construction contractor. These meetings enable the CFPB to stay informed of the project costs on an ongoing basis. The construction contract also contains a provision for preinvoice payment

24. Value engineering is used to identify alternative design solutions that can lower life cycle costs while maintaining or enhancing essential functions.

25. GSA requires all substantial renovations to achieve a LEED Gold rating.

meetings that give the CFPB the opportunity to review and approve invoices for construction costs.

Both the construction and construction management contracts play important roles in the management of the renovation costs. The firm-fixed-price construction contract and design/build-bridging method help to ensure that the budget is not exceeded and give the CFPB additional control over the design and corresponding costs. The construction management contract includes specific controls for managing costs throughout the design and construction phases of the renovation project so that the renovation budget is not exceeded. The existence of these controls indicates that measures have been taken to ensure that the renovation budget and costs are managed throughout the renovation project's life cycle. Because the construction contract was recently awarded, activities that fall under these controls had not yet begun at the time we conducted our fieldwork. As such, we did not have the opportunity to test the effectiveness of these cost management controls.

Controls Have Been Implemented to Document Project Costs and Decisions

The CFPB was unable to locate documentation of the original decision to fully renovate the building or provide support that an analysis was performed prior to the decision being made. Based on our interviews with CFPB officials and our review of legacy documents,[26] we concluded that this decision was made prior to the beginning of CFPB operations in July 2011.

The CFPB now has processes and controls in place for the documentation of renovation project decisions. Specifically, an IRB business case is required for all major investment decisions. Based on our review of CFPB guidance, the business case should include an alternatives analysis section, which requires a description of alternatives, a comparison of the costs and benefits of alternatives, and the rationale for choosing the investment over the alternatives. If completed in accordance with the CFPB's current policies, the IRB business case will serve as documentation and support for major investment decisions

In addition, the CFPB now has a records management policy that establishes guidelines under which the CFPB manages federal records throughout their life cycle and is based on federal guidelines on record management. The policy outlines the Chief Administrative Officer's responsibilities regarding recordkeeping, which include establishing an agency-wide records management policy and related procedures. We noted that file plans[27] that detail processes for maintaining records were distributed to the Office of the Chief Financial Officer and the Office of the Chief Operating Officer. Both offices have responsibilities associated with the renovation costs and project decisions.

26. These legacy documents included a December 2010 memorandum from an OTS official to a Treasury official that stated the CFPB would be the primary tenant of the building and would be responsible for the building's renovation. Further, the January 2011 Letter of Intent and a February 2011 Treasury press release provide further support that the decision to renovate predated the beginning of CFPB operations.

27. These file plans are based on the National Archives and Records Administration's General Records Schedules.

We noted that the construction management contract also includes requirements for the documentation of renovation project decisions. The construction manager is required to maintain files, such as documentation of significant clarifications and decisions, progress reports, and monthly status reports. The project status reports are provided monthly to GSA and the CFPB and include a summary of issues resolved and decisions reached. Based on our review of these reports, we noted that the construction management firm meets with the CFPB and GSA biweekly to discuss critical project risks and issues that could affect the project budget or schedule. The meetings and the actions taken to resolve the identified risks are documented by the project management firm and are included in the monthly progress reports.

Our review of the CFPB's current IRB process and records management policy found that they were implemented in fiscal year 2013. As discussed, the decision to renovate was made prior to July 2011, which predates the establishment of these controls. Given that the CFPB now has policies and procedures in place to document ongoing and future renovation decisions, we are not making any recommendations at this time.

Finding: The CFPB Should Submit Optional Renovation Costs to the IRB for Approval

Our review of the construction contract awarded in December 2014 and related documents identified costs for an optional facilities maintenance contract and estimated costs associated with buying out a retail tenant in the event that the childcare center option is exercised. Each of these costs individually exceeds the IRB's threshold of a major investment and was not included in the previous IRB business case. CFPB policy requires program offices to complete a business case to obtain IRB approval for major investments. As previously reported, the IRB approved an incomplete business case for the headquarters building renovation in September 2013. CFPB officials stated that the IRB approved the original business case without complete information because funding approval was viewed as a formality given that the decision to proceed with the renovation had already been made. While the overall funding has already been approved, the costs of the optional facilities maintenance contract and buying out a retail tenant require additional investments not originally anticipated by the CFPB. Therefore, the IRB should review and approve these investments to provide the CFPB with assurance that these investments are sound business decisions.

Optional Renovation Costs Qualify as Major Investments

The construction contract includes two options that the CFPB can exercise that would result in additional cost to the CFPB. One option is for a facilities operations and maintenance services contract. The other option is for the construction of a childcare center, which would require the CFPB to incur costs for a retail tenant buyout. The costs associated with the facilities maintenance contract and buying out the retail tenant were not separately identified in the original business case for the renovation and therefore were not individually analyzed.

The CFPB requires program offices to prepare and submit a business case for IRB approval prior to obligation or expenditure of funds. The CFPB's IRB charter and internal training documents provide specific guidance for making a sound business case for an investment. Both of these optional costs qualify as major investments under IRB guidance and would require the preparation and submission of a business case to the IRB for approval if pursued. The IRB is responsible for ensuring that business cases fully support how the investment aligns with the CFPB's mission, vision, and strategic goals and is a sound business decision. According to IRB guidance, a major investment requires a business case submission at the onset and when any changes are made to an existing investment's scope, approach, or budget after initial IRB approval.

When the business case was initially approved, the cost breakdown was based on the $145.1 million cost estimate prepared by GSA for the building renovation and did not include costs associated with buying out a retail tenant. In addition, the initial business case did not separately identify the option for facilities operations and maintenance services. This option was not separately identified until the construction procurement phase of the project.

These two optional costs have not been individually analyzed and require additional investments not originally anticipated by the CFPB. As we previously reported and discussed with CFPB officials, the initial renovation funding was approved without a complete business case analysis. Therefore, if the CFPB decides to pursue these optional investments, conducting a complete analysis and obtaining IRB approval would help the CFPB ensure that these investments are sound business decisions.

In February 2015, we discussed our recommendation with CFPB officials, who concurred with the recommendation and stated that they planned to submit the optional investments to the IRB for approval. On June 22, 2015, the CFPB provided us with an IRB business case for the retail tenant buyout. The CFPB noted that this business case included preliminary cost information and may be updated in the coming weeks based on ongoing discussions. Because the business case was provided after the conclusion of our fieldwork and could be updated, we will evaluate the final business case as a part of our audit follow-up process.

Recommendation

We recommend that the Chief Administrative Officer

1. Prepare and submit a complete business case to the IRB for approval prior to obligating funds if the CFPB plans to exercise the facilities operations and maintenance services option or finalize the retail tenant buyout agreement.

Management's Response

The CFPB concurs with our recommendation and will obtain IRB approval prior to obligating funds in connection with the facilities operations and maintenance services option or retail tenant buyout.

OIG Comment

We believe that the actions described by the CFPB are responsive to our recommendation. The OIG intends to follow up on the CFPB's actions to ensure that the recommendation is fully addressed.

Appendix A
Scope and Methodology

To evaluate the reasonableness of the renovation costs, we reviewed the CO's price reasonableness determination for the A/E contract. We also compared construction costs to an independent cost estimate and the cost of two comparable building renovations and compared overall renovation costs to the amount previously budgeted and obligated for the renovation. In addition, we performed a life cycle analysis comparing the total potential costs of renovating the building to the cost of leasing comparable space over the period of the 30-year occupancy agreement.

To assess the effectiveness of the CFPB's processes and controls, we reviewed the CFPB's internal policies and processes for approving major investments. Specifically, we reviewed the CFPB's IRB charter and internal IRB guidance to understand the process and specific requirements for completing business cases for major investments. We also evaluated the IRB business case and respective control sheet related to the CFPB's headquarters renovation. In addition, we reviewed the MOU and the RWA with GSA, as well as the construction management and construction contracts to identify controls in place to manage renovation costs. We interviewed cognizant CFPB officials and reviewed relevant documentation regarding current CFPB processes for documenting renovation costs and project decisions. Our scope included estimated, budgeted, and actual renovation costs and the contracts for A/E design services, construction management, and construction awarded in support of the CFPB's headquarters renovation.

We conducted this performance audit from July 2014 through February 2015 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix B
Summary of Cost Elements Included in Levels of Cost Calculations

The Results of Analysis: Renovation Costs section describes a series of cost analyses conducted to assess the reasonableness of the renovation costs. Three of these analyses compared CFPB costs to various points of reference. To conduct our analyses, it was necessary to calculate various levels of costs to ensure appropriate comparisons to the various points of reference. Therefore, we identified the cost elements included in the various points of reference and calculated comparable levels of CFPB costs using those same elements. We also conducted a life cycle analysis of the renovation project, for which we calculated an additional level of cost that included all potential remaining costs associated with renovating the building. The elements included in the levels of costs are described below and in table B-1.

- **Awarded construction costs.** This is the amount initially awarded for the construction contract and includes the base contract and Option 10.

- **Potential construction costs.** Because the awarded construction costs do not include all options and unit prices, we added the highest cost combination of options, unit price offers, and other costs such as a construction contingency, to the base contract to determine the potential construction costs.

- **Potential renovation costs.** In addition to construction costs, the CFPB's $145.1 million renovation budget includes construction management costs and GSA fees. Therefore, we added the construction management costs and GSA fees to the potential construction costs to determine the potential renovation costs.

- **Potential all-in costs.** The CFPB's decision to rent and renovate the 1700 G Street NW building also results in additional costs to the CFPB, such as the A/E contract and the rent and other expenses for swing space. Therefore, we added these costs to the total potential renovation costs to determine the potential all-in costs.

Table B-1: Summary of Cost Elements Included in Levels of Cost Calculations

Cost element	Cost ($ million)	Awarded construction costs	Potential construction costs	Potential renovation costs	Potential all-in costs
Base contract	97.7	✓	✓	✓	✓
Option 1: Childcare center	4.1		✓	✓	✓
Option 9: Facilities operations and maintenance	6.2		✓	✓	✓
Option 10: Operational retail	1.8	✓			
Estimated unit price offers[a]	8.4		✓	✓	✓
Estimated contingency and other costs[a]	12.3		✓	✓	✓
Construction management contract	4.4			✓	✓
Estimated GSA fee and overhead[a]	5.6			✓	✓
Estimated additional costs[a,b]	67.3				✓
Total ($ million)		**99.4**	**128.6**	**138.7**	**206.9**

Source: OIG summary of renovation costs.

Note: Totals may differ slightly due to rounding.

[a]We calculated estimated costs because actual figures have not been determined. For estimated unit price offers, we aggregated the three unit price offers estimated by the construction contractor. We calculated estimated contingency and other costs and estimated GSA fee and overhead using standard percentages and fees used by GSA. We calculated estimated additional costs using obligations and budget numbers provided by the CFPB.

[b]Estimated additional costs include the cost of the A/E contract and the rent and other expenses for swing space. We did not include the cost of rent and other expenses for the headquarters building over the term of the lease, as these are rental costs that would be incurred regardless of whether the CFPB chose to renovate the building.

Appendix C
Management's Response

1700 G Street N.W., Washington, DC 20552

July 30, 2015

Ms. Melissa Heist
Associate Inspector General for Audits and Evaluations
Board of Governors of the Federal Reserve System and
Consumer Financial Protection Bureau
20th and Constitution Avenue
Washington, DC 20551

Dear Ms. Heist,

We have reviewed your draft report entitled *CFPB Headquarters Construction Costs Appear Reasonable and Controls are Designed Appropriately*, and appreciate the opportunity to respond.

We are pleased that the report found that the construction costs for the Bureau's headquarters renovation appear reasonable and that we have designed and implemented appropriate controls for approving, managing, and documenting renovation costs and project decisions. As detailed in the report, we concur with your recommendation to obtain Investment Review Board approval before obligating funds related to the two construction options that, if exercised, would result in additional costs to the Bureau.

As the renovation progresses, we remain committed to proceeding in a responsible and transparent manner and welcome your ongoing review.

Sincerely,

Stephen J. Agostini

Stephen Agostini
Chief Financial Officer

consumerfinance.gov

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