Office of Inspector General

June 2005
Report No. 05-021

Status of Virginia Square Phase II Construction

EVALUATION REPORT

Office of Audits

Office of Audits

OIG

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Background and Purpose of Evaluation

In March 2002, the FDIC's Board of Directors authorized $106.5 million for Phase II of the Virginia Square (VASQ) development—the design and construction of a second office building and special-purpose facility to accommodate 1,119 FDIC employees currently housed in leased space.

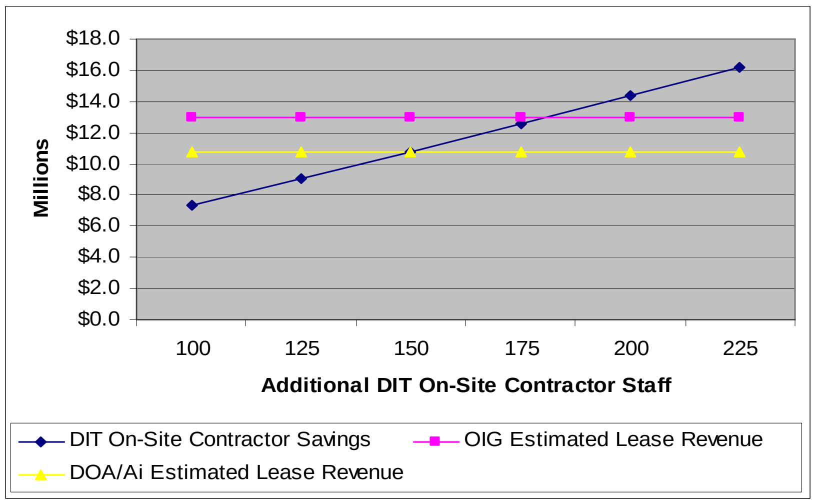
In October 2004, the Chief Operating Officer (COO) announced a decision to reduce permanent staff in several divisions. Staffs from some of the divisions were already scheduled to move to VASQ. In January 2005, the COO tasked the Division of Administration (DOA) to evaluate space utilization of FDIC-owned office buildings in light of corporate downsizing.

The objective of our evaluation was to determine whether: (1) the VASQ Phase II project costs are within budget and tasks are being completed on schedule, (2) the FDIC is following its established project control framework, and (3) DOA has planned for space utilization in light of corporate downsizing.

Results of Evaluation

The VASQ Phase II project costs are within budget and that tasks are being completed on schedule. Also, the FDIC is effectively following its established project control framework. Further, DOA is planning for space utilization in light of corporate downsizing and has analyzed several options for disposition of vacant space at VASQ. We validated the reasonableness of most of the assumptions used in those options. However, the cost-benefit of one of the options was, in part, dependent on a sufficient number of contractors performing work at VASQ. While we validated the per capita savings estimates from moving Division of Information Technology (DIT) contractors on-site under this option, we could not determine with certainty the number of contractors the Corporation planned to move on-site or whether that number would fluctuate over time.

Breakeven Analysis of Savings From Moving Additional DIT Contractor Personnel On-Site (10-Year Net Present Value)



Source: OIG analysis.

As shown, from a financial standpoint, DIT will need to house a minimum of 150 to 175 additional contractor staff currently located off-site to break even under Option III in comparison to the options that involve leasing space. Further, the DIT contractors would need to remain on site for the full 10-year period covered by the analysis. However, there are non-monetary factors related to IT security, access/communication, and equipment standardization that should be considered. This report makes no recommendations, but we encouraged DOA and DIT to continue to work together to develop more precise estimates of anticipated contractor staffing on-site at VASQ to help ensure that DOA selected the space utilization option that provides the greatest operational and financial benefits.

Management Response

DIT provided additional reasons why future DIT contractor personnel numbers cannot be definitively determined including contractor consolidation schedules, the effect of changing IT requirements on contractor workload, and fluctuations in contractor personnel as new vendors take on new tasks from old vendors or implement best practices which result in personnel efficiencies. We incorporated this additional information into our final report where appropriate.

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FDIC
Federal Deposit Insurance Corporation
801 17th Street NW, Washington, DC 20429

Office of Audits
Office of Inspector General

DATE: June 10, 2005

MEMORANDUM TO: Arleas Upton Kea, Director
Division of Administration

FROM: Russell A. Rau [Original signed by Stephen M. Beard for Russell A. Rau]
Assistant Inspector General for Audits

SUBJECT: *Status of Virginia Square Phase II Construction*
(Report No. 2005-021)

This report presents our evaluation of the status of Virginia Square Phase II Construction. The objectives of this evaluation were to determine whether: (1) the Virginia Square Phase II project costs are within budget and tasks are being completed on schedule, (2) the FDIC is following its established project control framework, and (3) the Division of Administration (DOA) has planned for space utilization in light of corporate downsizing. Additional details on our objective, scope, and methodology are provided in Appendix I.

Background

In 1997, the FDIC Board of Directors directed that the DOA develop a long term strategy for future headquarters housing requirements. FDIC established a task force in August 1997 to identify and evaluate options and propose a cost-effective, long-range housing plan. The task force recommended that the FDIC construct another building at Virginia Square to accommodate future office space requirements for 1,119 permanent employees and 155 contractor staff housed in leased space. From 1998 through March 2002, the FDIC selected a project team leader, established cost and time constraints, evaluated funding sources, and determined the oversight structure for the project.

In March 2002, the FDIC Board of Directors authorized $106.5 million for Phase II of the Virginia Square development—the design and construction of a second office building and a special-purpose facility to be completed in December 2005. The FDIC established an FDIC project team and contracted with three primary contractors: David Orr Partners—Development Manager; Ellstreet Corporation (Ai)—Architecture and Engineering firm, and Turner Construction Company—General Contractor. The FDIC also contracted with Heery International to be a Disbursements Advisor and to provide independent review and consulting services. Groundbreaking for the new building occurred in September 2003, and the FDIC anticipates relocating employees from its Washington, D.C., offices to the new Virginia Square office building starting in December 2005.

FDIC oversight of the project is provided by the Corporation's Board of Directors, the Executive Oversight Committee (EOC), and an FDIC Project Team. The Board of Directors authorized the project, provides funding, and monitors the project through quarterly progress reports. The EOC is composed of the FDIC Deputies to the Chairman and is responsible for monitoring adherence to the project budget, schedule, and internal controls over construction activities. The EOC also approves change orders in excess of $100,000 and receives updates from the project team and the contractors. The project team is composed of FDIC employees who are also the oversight managers and technical monitors for the four major contracts and is headed by a DOA Associate Director who also oversees the work of the General Contractor. The project team works closely with the contractors and meets weekly with them to discuss progress and issues. The Development Manager provides a monthly status report (Progress Report) to the project team and provides monthly briefings to the EOC.

Evaluation Results

We found that the Virginia Square Phase II project costs are within budget and that tasks are being completed on schedule. Also, the FDIC is effectively following its established project control framework. In that regard, DOA's contract management has been instrumental to ensuring project goals are met. Finally, DOA is also planning for space utilization in light of corporate downsizing and has analyzed several options for disposition of vacant space at VASQ. We were able to validate the reasonableness of most of the assumptions used in those options. However, we could not determine with certainty the number of contractors that the Corporation actually planned to move on-site under an option to house contractors in the vacant space or whether that number would fluctuate or stay constant over time. The cost/benefit of housing DIT contractors at Virginia Square is, in part, dependent on a sufficient number of FDIC contractor personnel actually performing work on-site at Virginia Square.

Project Costs and Schedule

We concluded that project costs are within budget and that tasks are generally being completed on schedule. As of March 31, 2005, budget commitments on the project totaled $102 million and remaining projected costs totaled $4.5 million, within the original $106.5 million project budget. Further, the March 31, 2005 Progress Report estimated a February 8, 2006 construction completion date. The current Turner contract calls for a January 19, 2006 completion date.

The Turner contract is a firm fixed-price contract. Under this type of contract, the FDIC is committed to paying the contractor the total contract amount subject to contract change orders. However, the contractor is also committed to completing the work within the amount specified. The project budget of $106.5 million includes a contingency allowance of $4.9 million. As of March 31, 2005, the FDIC had not committed any of the contingency allowance on the contract. The March 31, 2005 Progress Report indicated that contract expenditures were within budgeted amounts and projected an overall project savings of $1.4 million, not including any balance that may remain in the contingency allowance when the project is completed.

The DOA Associate Director who heads the FDIC project team and FDIC's Disbursement Advisor reported to us that the project is generally on schedule and under budget. These comments were consistent with the March 31, 2005 Progress Report which indicated that the project completion date had only slipped 20 days from the original schedule. The additional time was the result of FDIC-approved change orders which impacted final occupancy dates.

Project Control Framework

The FDIC has established and is following a project control framework for the management of the Virginia Square Phase II construction project.[1] Adherence to the project control framework has contributed to the project being completed on schedule and within budget. The project control framework includes continuous monitoring of the project, formal documentation of change orders and contract modifications, comparison of updated cost and budget information with the original cost and budget estimates, and continuous communication between the FDIC and contractors to ensure that issues are addressed in a timely manner.

To evaluate whether FDIC was following its control framework, we interviewed the project's contracting officer, oversight managers, technical monitors, and contractor personnel. We also reviewed contract files, meeting minutes, and Progress Reports. We found that the current status and progress of the Virginia Square Phase II project are continuously monitored and documented in the monthly Progress Reports. These reports include a time line to track planned and actual progress and document requests for information among the project team and contractors. The Progress Reports also include a comparison of updated cost and budget estimates with the original cost and budget estimates.

FDIC project team and contractor representatives hold weekly meetings to discuss current progress and issues. The Development Manager's monthly progress report contains minutes of these weekly meetings along with Task Lists to track task assignment and due dates. In addition, all Requests for Information are documented and tracked in the Progress Report. Further, the FDIC Technical Monitor and contractor representatives conduct a monthly walk-through of the project site and discuss the General Contractor's request for a progress payment in relation to the physical evidence of the progress. Finally, the FDIC and Disbursement Advisor have further strengthened the project control framework by thoroughly reviewing all invoices and adjusting them as necessary prior to payment.

<u>Change Orders:</u> The original Board case budgeted a project change order allowance of $3,939,799 and a contingency allowance of $4,918,632 intended to cover costs for unanticipated events occurring during design and construction, such as escalating building costs involving site conditions and equipment. Change orders are written orders authorizing and directing the contractor to charge for work not included in the contract's original scope of work.

As of March 31, 2005, Turner Construction had requested 50 project change orders totaling $2.2 million and the FDIC had approved 37 of the change orders totaling $1.2 million. The Development Manager told us that the number of change orders on this project was very low relative to other similar construction projects. Change order increases ranged in price from $4,000 to $270,000, and only two change orders were in excess of $100,000. Of the 37 change

[1] We issued a report, *Control Framework for the Virginia Square Phase II Project* (Report No. 04-018, dated April 22, 2004), which concluded that FDIC had established an adequate control framework for monitoring construction of the building.

orders approved by the FDIC, only three were approved for the original price submitted by Turner. The FDIC had negotiated a lower price on all other change orders after reviewing the original change order request. The Development Manager was involved in the review process on all change orders and provided an evaluation of the change order requests to the FDIC.

The change orders generally resulted from unexpected design deviations encountered once construction on the project began. For example, on the Virginia Square Phase II project, comments from the Arlington County Fire Marshall on the plans submitted for the Building Permit required structural changes and additional concrete reinforcement to the fire lanes. The original plans were designed to be within the Arlington County code when they were submitted; however, Arlington County is in the process of revising the requirements to provide necessary support for fire equipment in the event of an emergency. This required a number of change orders to the structure and the amount of concrete used in constructing the fire lanes.

We examined the FDIC's process for review and approval of change orders and selected a sample of six change orders to verify that they had been reviewed and approved in a timely manner. We found that the file for each change order contained support for the change order amount, a description of the change order, and evidence that the change order had been reviewed by FDIC officials and the Development Manager within the requested timeframe. We concluded that the number and dollar amount of change orders were supported and within the original budgeted estimates. Further, we verified that none of the $4.9 million project contingency allowance had been used.

Permits: We verified that all permits that the FDIC was required to obtain for the Virginia Square Phase II project were obtained and approved by Arlington County within required project timeframes. The construction project required the FDIC to obtain five permits, which had been approved within the timeframes required for the project to be completed on schedule. No delays have occurred on the Virginia Square Phase II construction as a result of the permit-approval process. Arlington County approved the FDIC's final permit on February 4, 2005.

Space Utilization

DOA is in the process of conducting a space utilization analysis to evaluate several options for the disposition of vacant space at Virginia Square resulting from corporate downsizing. We validated the reasonableness of most of the cost assumptions related to staffing and leasing used in DOA's space utilization analysis. However, we could not determine with certainty the number of contractors the Division of Information Technology (DIT) planned to move on-site or whether that number would fluctuate over the time period covered in DOA's analysis.

In October 2004, the Chief Operating Officer (COO) announced a decision to reduce permanent staff in several divisions. Staff from these divisions were already scheduled to move to Virginia Square upon completion of Phase II construction. In January 2005, the COO tasked DOA with evaluating space utilization of FDIC-owned office buildings in light of corporate downsizing.

In January 2005, DOA issued a Task Order to Ai to evaluate space utilization alternatives which stated:

> Ai will develop a study to determine space utilization at FDIC's three owned properties (550 17th Street, 1776 F Street & VA Sqr.) and alternates for disposition of unoccupied vacant space recommending the most cost efficient option based on a cost benefits analysis. The study should consider existing and projected population, organization, and existing and projected space availability, effective first quarter 2006, but with minimal reconfiguration of existing facilities, and minimal impact on the current budget and schedule of the Virginia Square Phase II project. The study should be based on four options, if viable:
>
> - Leasing 1776 F Street
> - Sell 1776 F Street
> - Lease Va Sqr. Phase II South Tower
> - House [DIT] Contractors – Va Sqr. Phase II North Tower

Following task order award, DOA removed from consideration the second option, to sell the FDIC-owned building at 1776 F Street, because there was not enough vacant space in FDIC-owned Washington, D.C., buildings to warrant the sale.

DOA provided Ai with DOF-prepared future FDIC employee staffing estimates to assist with the analysis. In late January 2005, DIT provided an estimate of cost savings that the FDIC could achieve by providing office space at Virginia Square for contract personnel currently housed off-site. DIT based its estimates (shown in Table 1) on contractor rates from a sample of existing contracts and calculated per capita annual cost averages based on 174 current DIT off-site contractors.

Table 1: DIT Per Capita On-Site Contractor Analysis

Cost Item	Cost
Contractor rate reduction from housing contractors on-site	$9,100
Annual external IT security monitoring costs avoided by housing contractors on-site	1,609
Equipment and connectivity charges at vendor sites.	1,057
Less: Computer and telephone support necessary for contractors on-site.	(2,434)
Annual Savings Per On-Site Contractor Employee	***$9,332***

Source: DIT.

Note: DIT's analysis also included a cost factor of $3,000 for the revenue lost from not leasing Virginia Square. We removed this amount from the DIT calculation because it is addressed in DOA's space utilization analysis.

As shown in Table 1, DIT estimated an annual cost savings of $9,332 per contract employee by providing these contractors with space in the Virginia Square facility because contractors generally provide discounted rates when their personnel work on-site. DIT determined that its existing contractors offered on-site rates which were, on average, 6.3 percent less than the contractors' off-site rates. DIT also provided that in addition to the cost savings associated with on-site contractors, there are a number of non-monetary benefits related to security, access/communication, and equipment usage. These benefits as described by DIT are detailed in Table 2.

Table 2: DIT Non-Monetary Benefits of Housing Contractors On-Site

Security	Access/Communication	Equipment/Hardware/Software
• Cost avoidance of ensuring IT security at off-site locations • Uniform, consistent implementation of Security policies • Only FDIC approved hardware connected to the infrastructure • Immediate reaction to a Security breach • Enhanced physical security as opposed to commercial leasing of extra space	• Immediate face-to-face availability with FDIC staff • Avoid delays incurred by travel to and from meetings • Immediate first hand information exchanged between parties • Familiarity with customers, and technical environment • Same test facilities and environment • Improved access to helpdesk support	• Ensure use of the same version of software • Ensure that all equipment is in accordance with FDIC specifications • Immediate replacement/repair of malfunctioning hardware • Ensure that technical upgrades are uniformly available

Source: DIT.

DOA provided Ai with DIT's January analysis and instructed Ai to assume a future DIT on-site contracting need of 174 contractors.

DOA provided us a draft report on Ai's analysis in April 2005 and Ai's final report in May 2005. The analysis presented three options and calculated net present value (NPV) revenue/savings estimates under 5-year and 10-year periods. Each option was based on different configurations of division and office employees within FDIC headquarters-owned buildings. The options considered potential lease revenue for vacant space for Options I and II and savings from discounted on-site contractor rates for Option III. Table 3 summarizes the economic effect of each option.

Table 3: Net Present Value Cost Analysis of Real Estate Options

Options	Space Utilization	FDIC Staff Moves	Revenue or Savings	
			5 Year NPV	10 Year NPV
Option I—1776 F Street Lease: Consolidate staff in VASQ and lease F Street vacant space.	Lease 40,030 Usable Square Feet (USF) 15,041 USF vacant	286	$5,743,153	$10,708,690
Option II—VA Square Lease: Consolidate staff at 1776 F Street and VASQ Phase I and lease space in VASQ Phase II.	Lease 49,003 USF 6,068 USF vacant	311	5,750,981	10,787,532
Option III—Consolidate staff at 1776 F Street and VASQ Phase I and house DIT contractors in VASQ Phase II.	DIT Contractors occupy 38,695 USF 16,376 USF vacant	60	7,018,598	12,529,883

Source: Ai draft report dated April 8, 2005.

In late May 2005, the DOA Associate Director proposed Option III to the EOC as the best course of action for FDIC. The EOC accepted DOA's proposal. The Associate Director stated that his decision was based not only on the greater economic benefit that would be achieved as shown in Table 3 above, but also on the non-monetary benefits to the FDIC related to housing DIT contractors on-site.

OIG Analysis of DOA Estimates

To validate the reasonableness of DOA estimates, we focused on three areas: (1) future permanent staffing levels and space requirements, (2) current lease rates in the Virginia Square area, and (3) future DIT contracting needs, on-site rates, and intangible benefits from on-site DIT contractors.

Future Permanent Staffing Levels: The 2002 Board of Directors' decision to build VASQ Phase II was based on a DOA Long-Term Housing Study (LTHS) updated in August 2001. The LTHS estimated office space needs based on a factor of 332.5 rentable square feet (RSF) per employee.[2] The LTHS identified a requirement for 372,068 square feet to accommodate 1,119 headquarters staff.

We analyzed DOF-estimated staffing projections and concluded that the downsizing effort will result in a total of 197 fewer permanent employees at VASQ—78 employees in the existing structure (Phase I) and 119 employees in the new structure (Phase II). These staffing estimates were the same as those estimates used in the Ai analysis.

As discussed earlier, DOA removed from consideration the option to sell the FDIC-owned F Street building because there was not enough vacant space to warrant the sale. We reviewed DOF staffing projections and confirmed that downsizing plans will result in 10 fewer staff being housed in the F Street building. DOA and Ai projected 9,769 usable square feet (USF) of vacant space out of 120,414 USF available in the F Street building. FDIC also plans to close the Child Development Center in the F Street building which will leave an additional 6,607 USF vacant on the ground-floor level. Because over 85 percent of the F Street building will be occupied, and because it is prudent to retain a small amount of space to absorb periodic staffing changes, we concluded it was reasonable to remove the option to sell the F Street building from consideration.

Virginia Square Lease Rates: We obtained current leasing rates for the Virginia Square area of Arlington County, Virginia, and estimated what the FDIC could earn from leasing vacant space at VASQ using the 332.5 RSF per employee factor and the DOF downsizing estimates. We estimated the net present value of a 10-year lease for the RSF available at about $13 million net of operating expenses as shown in Table 4.

Table 4: Preliminary Estimates on Impact of Downsizing

VASQ Phase	Employee Downsizing	Rentable Square Feet (332.5 per person)	10-year lease NPV
Phase I (old structure)	78 staff	25,935 RSF	$5.16 million
Phase II (new structure)	119 staff	39,567 RSF	$7.87 million
Total	197 staff	65,502 RSF	$13.03 million

Source: OIG Analysis.
Note: Analysis based on $35 per square foot (psf) less $10 psf operating expenses with a 4 percent annual rent escalation. The calculation also includes a 6 percent lease commission and a $45 psf tenant improvement allowance.

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[2] Rentable Square Foot reflects individual office or cubicle space plus a 30 percent factor for circulation space and a 15 percent loss factor. For an employee with a 250 square foot office, the RSF calculation would be (250 x 1.3) x 1.15 = 374 RSF.

Our estimate resulted in a 10-year NPV that was $2.24 million higher than Ai's Option II ($10.8 million) presented in Table 3. The primary reason for this difference is that our calculation used 65,502 *rentable* square feet, while DOA/Ai's used 55,071 *usable* square feet (with 6,068 square feet of that amount remaining vacant). RSF represents the area on which a rental payment is based; USF is the area that a tenant can actually utilize. The difference between the two is called a loss factor and is usually expressed as a percentage of USF (usually a 15-20 percent loss factor is used in the real estate industry). Applying a 15-percent loss factor to DOA/Ai's USF amount yields 63,332 RSF which approximates our estimate of 65,502 RSF.

Further, our calculation is somewhat theoretical and based on the original LTHS per employee space allocation, while DOA's calculation is situational and considers the practical realities of configuring office space; locating divisions and offices to achieve operational efficiencies; and providing adequate "swing space" to accommodate periodic staffing fluctuations. We concluded that DOA/Ai's Option II leasing estimates and our leasing estimate provided a reasonable range for potential revenue from leasing space at VASQ.

<u>Future DIT Contracting Requirements</u>: To validate DIT's analysis of potential savings from moving contractors on-site at VASQ, we verified information about the number of current off-site DIT contractors, plans for replacing or consolidating existing contracts, differences between on and off-site rates, and the validity of non-monetary benefits of having contractors on-site.

DIT based its per capita cost savings estimates on 174 contractor staff. In early April 2005, we researched FDIC's Outlook database and identified 213 DIT off-site contractors.[3] We accessed the Contract Management Information System and worked with DIT to determine contractor information, including the expiration year of each vendor's contract(s) and whether there would be a continuing need for each vendor's contract(s) or whether the contract(s) would be consolidated into DIT's Information Technology Application Services (ITAS) contract.[4] We also verified with DIT that most existing contracts offer lower on-site rates and that the contractors would be required to begin billing on-site rates immediately in the event that the contractors were moved on-site at VASQ (i.e., no contract modification would be required to receive on-site rates). Table 5 presents our analysis of DIT existing contractor staff sorted by contract expiration year.

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[3] In its analysis, DIT initially concluded that one contractor, Pinkerton, had lower off- than on-site rates. Thus DIT excluded 41 Pinkerton off-site contractor employees from its analysis. DIT later determined that Pinkerton's on-site rates were lower than their off-site rates.

[4] ITAS is a multiple award contract valued at $550 million over a 10-year period of performance. ITAS will consolidate a number of existing contracts and award future task orders to four pre-approved contractors for application development and maintenance support.

Table 5: Existing On and Off-Site DIT Contractors

Company	Staff Currently Off-Site	Staff On-Site at VASQ	Expiration Year of Contract(s) [(a)]	Planned Replacement of Contract
IBM	5	5	2005	Consolidated into ITAS
Janus	0	4	2005	Consolidated into ITAS
Unisys	0	10	2005	Consolidated into ITAS
Z. Inc	8	5	2005	Consolidated into ITAS
ATS	6	1	2006	Consolidated into ITAS
STSI	16	0	2006	Consolidated into ITAS
Bearing Point	26	21	2007	Contract will be renewed, competed and/or consolidated into ITAS.
CIBER	26	7	2007	Consolidated into ITAS
COMSO	13	4	2007	Consolidated into ITAS
Pinkerton	41	20	2007	Consolidated into ITAS
Accenture	20	35	2009	Consolidated into ITAS
Impact Innovations	3	36	2009	Consolidated into ITAS
SRA[(b)]	9	162	2009	Will not be consolidated
Deloitte Consulting	13	1	2012	Consolidated into ITAS
Booze Allen	5	1	2015	Consolidated into ITAS
Misc.	22	36	Various	N/A
Total	**213**	**348**		

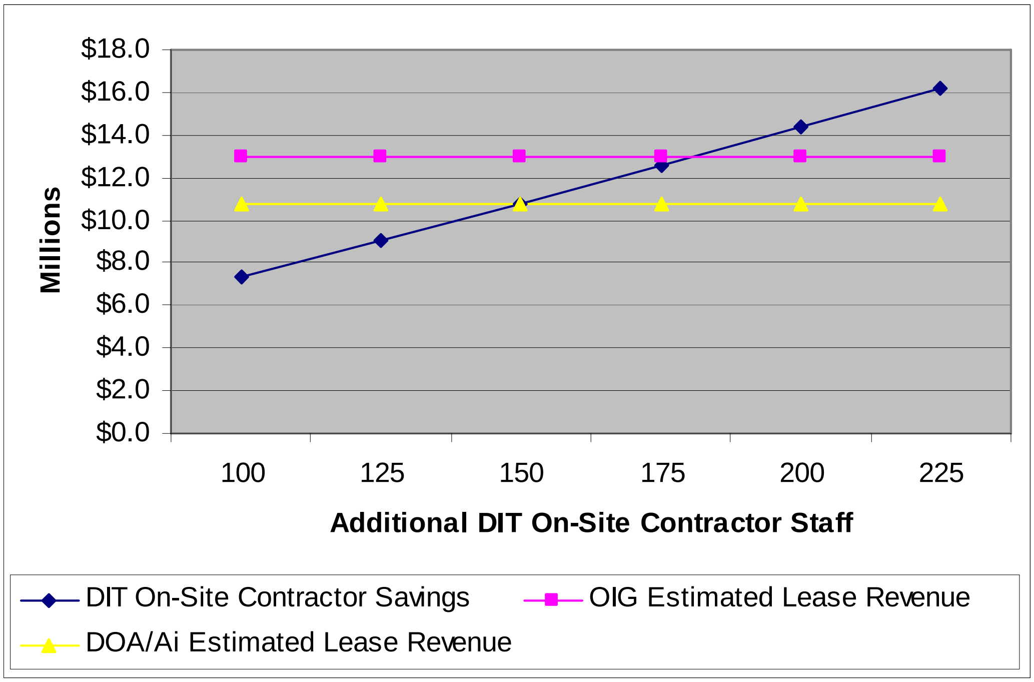
Source: OIG Analysis and DIT contractor information.
Notes:
(a) Some vendors have multiple contracts. For each vendor we used the contract with the latest expiration date.
(b) SRA is the vendor for the Infrastructure Services Contract which consolidated existing infrastructure support contracts. DIT does not intend to consolidate the Infrastructure Services Contract into ITAS.

Since most of the existing contracts will be consolidated into the ITAS contract, we analyzed ITAS contract pricing schedules to calculate the difference between on- and off-site rates. The ITAS contract has four prime and a number of subcontractors that have been prequalified to receive contract work through the award of task orders. Each contractor offered differing on- and off-site rates. We concluded that, on average, the on-site rates were about 6.7 to 9 percent less than the off-site rates. Accordingly, we concluded that DIT's assumption of a 6.3 percent savings from on-site rates was reasonable.

Another benefit cited by FDIC for having IT contractor personnel in Virginia Square is that this arrangement provides for increased security for FDIC systems. We agree that there are security-related benefits to having contractor personnel on-site as presented in Table 2.

However, we could not determine with certainty the number of contractor personnel that DIT actually planned to move on-site or whether that number would fluctuate over time. We also could not determine with certainty, as existing contracts are consolidated into ITAS, whether DIT will replace departing contractor personnel on a one-for-one basis with on-site ITAS contractor personnel or achieve contractor personnel reductions. The following figure presents the breakeven point between our and DOA/Ai's leasing analyses and savings achieved from moving various additional levels of DIT contractor staff on-site over a 10-year period.

Breakeven Analysis of Savings from Moving Additional DIT Contractor Personnel On-Site (10-Year NPV)



Source: OIG analysis.

As shown, from a financial standpoint, DIT will need to house a minimum of 150 additional contractor staff currently located off-site for savings to exceed the revenues from DOA/Ai's Option II—Virginia Square Lease (as presented in Table 3) and about 176 additional contractor staff currently located off-site for the savings to exceed our Virginia Square leasing revenue estimate (as presented in Table 4). Further, the DIT contractors would need to remain on-site for the full 10-year period of analysis. The Corporation has developed several large corporate systems over the past few years and thus needed significant contractor resources to support those initiatives. However, the Chief Information Officer has indicated that the number of major system development projects will decrease going forward. Thus, there is some uncertainty about whether FDIC will have sufficient future system development activity to sustain the current level of contractor staffing.

In response to a draft of this report, DIT provided additional explanation for why it is difficult to estimate the future number of DIT contractors. In addition to the consolidation of existing contracts into ITAS over time (as discussed above in Table 5), DIT's response noted that contactor workloads can fluctuate significantly with changing IT requirements and contractor personnel numbers can fluctuate as new vendors take on tasks from old vendors and as new vendors identify and implement best practices across the enterprise, thereby increasing contractor personnel efficiencies.

Conclusion

DOA's project management of the Virginia Square Phase II construction is keeping the project generally on schedule and within budget. DOA has maintained compliance with its project control framework and has an effective project management team in place. DOA is also planning for space utilization in light of corporate downsizing. We were able to validate the reasonableness of most of the assumptions used in the options being considered, as well as the non-monetary benefits associated with housing contractor personnel in the Phase II tower. However, DOA needed to work with DIT to develop more precise projections of anticipated on-site contractor staffing at Virginia Square to help ensure that DOA selected the space utilization option that provides the greatest operational and financial benefits.

Corporation Comments and OIG Evaluation

We issued a draft of this report dated May 24, 2005. DOA elected not to provide a written response. DIT provided a written response dated June 7, 2005 to provide additional information regarding why future DIT contractor personnel numbers cannot be definitively determined. We incorporated this additional information into our final report where appropriate. DIT's response is included in its entirety as Appendix II.

Objective, Scope and Methodology

The objectives of this evaluation were to determine whether: (1) the Virginia Square Phase II project costs are within budget and tasks are being completed on schedule, (2) the FDIC is following its established project control framework, and (3) DOA has planned for space utilization in light of corporate downsizing. We performed our evaluation from March 2005 through May 2005 in accordance with generally accepted government auditing standards.

In performing this evaluation we interviewed FDIC and contractor personnel including the:

- Contracting Officer, Oversight Manager, and Technical Monitor for the Turner Construction Contract
- Vice President, Orr Partners, Virginia Square Phase II Development Manager
- DIT Deputy Director, Business Administration Branch
- DOF Manager, Program Administration Branch
- FDIC Oversight Manager, Heery International
- DOA Assistant Director, Leasing
- DOA Chief, Space Planning and Design

We also reviewed various documents related to the Virginia Square Phase II project including:

- The March 22, 2002 FDIC Board Memorandum approving the Phase II construction.
- The contracts between the FDIC and Turner, Orr, Ai, and Heery.
- Turner contract modifications 1 through 10.
- Change orders to the Turner Contract.
- Permits obtained for the Virginia Square Phase II construction.
- The Development Manager's Monthly Progress Reports from January 2004 to March 2005 including Budget, Change Order Logs, Construction Schedules, Meeting Minutes, Task Lists, and Request for Information submittals.
- Notes from Executive Oversight Committee meetings during 2004 and 2005.
- DIT's On-site/Off-site Contractor Analysis dated February 1, 2005.
- FDIC Cost Analysis of Real Estate Options as of April 11, 2005.
- Washington on-site employees and DOF contractor staffing schedules.
- Negotiated labor rates for DIT contracts.
- Prior OIG audit reports related to the Virginia Square Phase II project.

We also conducted analysis of various real estate alternatives based on information obtained from an independent real estate firm familiar with the Northern Virginia area. We used this analysis to evaluate the reasonableness of DOA space utilization assumptions.

We relied on information from FDIC's Microsoft Outlook employee and contractor database and DOA's Contract Management Information System to estimate the number of on-site and off-site DIT contractors and expiration dates for DIT contracts. We examined the data for obvious errors or missing entries and interviewed officials knowledgeable about the data who regularly use the data for evaluation. We concluded the data were sufficiently reliable for the purposes of this assignment.

Corporation Comments

Federal Deposit Insurance Corporation
3501 N. Fairfax Drive, Arlington, VA 22226

Division of Information Technology

June 7, 2005

MEMORANDUM TO: Stephen M. Beard
Deputy Assistant Inspector General for Audits
Office of Inspector General

FROM: Michael E. Bartell, CIO and Director
Division of Information Technology

[Electronically produced version; original signed by Michael E. Bartell]

SUBJECT: Response to the Draft Report Entitled, *Status of Virginia Square Phase II Construction* (Assignment No. 2005-021)

Thank you for the opportunity to review and comment on the Office of Inspector General's (OIG) subject draft evaluation report dated May 24, 2005. The Division of Information Technology (DIT) recognizes that subsequent to this draft report, the FDIC Chief Operating Officer (COO) and Chief Financial Officer (CFO) approved the Division of Administration's Option III plan to consolidate staff at the 1776 F Street and Virginia Square Phase (VASQ) I locations while housing DIT contractors in the VASQ Phase II location.

In reviewing the draft report, DIT appreciates the OIG's recognition of the reasonableness of our assumed savings estimates and is pleased that the OIG agrees that there are security-related benefits to having contractor personnel on-site. DIT does, however, have one general concern that we believe should be addressed in the final report. On four occasions in the eleven-page draft, it is stated that the OIG, "could not determine with certainty the number of contractor personnel that DIT actually planned to move on-site or whether the number would fluctuate over time." Recognizing that this evaluation report will be published and available to the public in final form, DIT is concerned that the draft report's repetitive treatment of the estimates of future DIT contractor personnel may raise undue concern on the part of a casual reader if it is not placed in the proper context. As such, DIT requests that the OIG include additional language in the final report that recognizes the following key reasons why future DIT contractor personnel numbers cannot be definitively determined:

- Contracts being consolidated under ITAS are being phased in over time;
- Contractor workload can fluctuate significantly with changing IT requirements;
- Contractor personnel numbers fluctuate as new vendors take on tasks from former vendors, i.e., ramp up typically involves a larger number of contractor staff initially and then trails off to a smaller figure as the vendor becomes familiar with the task; and finally,
- Contractor personnel numbers fluctuate as the new vendors identify and implement best practices across the enterprise, thereby increasing contractor personnel efficiencies.

If you have any questions regarding this response, please contact Rack Campbell, DIT Audit Liaison on 516x1422.

cc: Steven P. Anderson, DIT
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