



Department of Homeland Security Office of Inspector General

Review of Costs Invoiced by the City of San Francisco Relating to the Terminal 2 Checked Baggage Screening Project at San Francisco International Airport Under Other Transaction Agreement Number HSTS04-09-H-REC123



American Recovery and Reinvestment Act of 2009



Homeland
Security

August 24, 2011

Preface

The Department of Homeland Security (DHS) Office of Inspector General (OIG) was established by the *Homeland Security Act of 2002* (Public Law 107-296) by amendment to the *Inspector General Act of 1978*. This is one of a series of audits, inspections, and special reports prepared as part of our oversight responsibilities for programs, grants, and projects administered by the department under the *American Recovery and Reinvestment Act of 2009* (Recovery Act).

This report presents the results of our audit of the costs invoiced for reimbursement by the City of San Francisco under an agreement funded by the Recovery Act from the Transportation Security Administration. The purpose of the agreement was to finance a portion of the costs of modifications to San Francisco International Airport to accommodate a checked baggage inspection system.

The recommendations herein have been developed to the best knowledge available to our office, and have been discussed in draft with those responsible for implementation. We trust this report will result in more effective, efficient, and economical operations. We express our appreciation to all of those who contributed to the preparation of this report.

A handwritten signature in cursive script that reads "Anne L. Richards".

Anne L. Richards
Assistant Inspector General for Audits

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Abbreviations

CBIS	Checked Baggage Inspection System
DHS	Department of Homeland Security
OIG	Office of Inspector General
OMB	Office of Management and Budget
TSA	Transportation Security Administration

OIG

*Department of Homeland Security
Office of Inspector General*

Executive Summary

The Transportation Security Administration entered into an Other Transactional Agreement with the City of San Francisco to fund a portion of the costs to modify Terminal 2 at the San Francisco International Airport to incorporate a checked baggage inspection system. Under the agreement, the Transportation Security Administration agreed to reimburse the city up to \$15,346,800 for designing, managing, and building the project. At the time of our audit, the Transportation Security Administration had paid the city \$12,837,196 on the basis of invoices submitted through January 31, 2011.

We conducted our audit to determine whether invoiced costs were allowable, allocable, and reasonable according to the funding agreement and applicable federal requirements.

We concluded that costs of \$303,474 invoiced for construction management were questionable for reimbursement because they were not adequately supported by the city's accounting records. Also, we believe that the Transportation Security Administration needs to ensure that the city complied with the requirement for buying goods purchased/manufactured in America.

The Transportation Security Administration agreed with our two recommendations to resolve these matters. It concluded that the city should repay \$142,633 of the unsupported costs and said that the contracting officer will verify whether the city's vendors qualify under the Buy American requirement.

Background

On February 17, 2009, Congress enacted the *American Recovery and Reinvestment Act of 2009* (Recovery Act), in part to preserve and create jobs, promote economic recovery, and invest in transportation, environmental protection, and other infrastructure that will provide long-term economic benefits. The Recovery Act appropriated \$1 billion to the Transportation Security Administration (TSA) for “procurement and installation of checked baggage explosive detection systems and checkpoint explosives detection equipment. . . .” Of that amount, TSA awarded \$574,023,483 to 29 airport organizations for modifying facilities to accommodate new baggage-screening equipment.

On March 5, 2009, TSA notified the City of San Francisco that it was considering the city’s in-line explosive detection system matrix for Recovery Act funding. At that point, the city had already awarded a contract for renovation of Terminal 2 of San Francisco International Airport that included a \$32,105,580 subcontract for the baggage-handling system renovation. Subsequently, the city estimated that TSA’s Checked Baggage Inspection System (CBIS) project represented about \$17,052,000 of the total cost. Negotiations with TSA resulted in the award of Recovery Act funds of \$15,346,800, which represented 90% of the \$17,052,000. City officials told us that the Recovery Act funding allowed them to use money previously committed to CBIS for other airport projects.

The terms and conditions for the funding are set forth in Other Transaction Agreement No. HSTS04-09-H-REC123 between TSA and the city, dated June 11, 2009. The agreement period is from May 1, 2009, through September 30, 2011, and requires the city to submit invoices for reimbursement of project costs. The eligibility of project costs for reimbursement is based on the scope of the agreement; Office of Management and Budget (OMB) Circular A-87, as revised, *Cost Principles for State, Local and Indian Tribal Governments* (May 10, 2004); and TSA publication *Reimbursable and Non-Reimbursable Costs for the Electronic Baggage Screening Program, version 1.0* (June 2008). As of January 31, 2011, the city had invoiced \$12,837,196 for construction (\$12,533,722) and for construction management (\$303,474), which it incurred from June 2009 to August 2010. Those costs represented 90% of costs incurred. The agreement also includes requirements for complying with OMB Circular A-133, as revised,

Audits of States, Local Governments, and Non-Profit Organizations, and Recovery Act provisions for submitting quarterly recipient reports to the federal funding agency; paying prevailing wages as determined by the Secretary of Labor; and using American¹ iron, steel, and manufactured goods.

The objective of this audit was to determine whether costs invoiced by the city are allowable, allocable, and reasonable according to the funding agreement and applicable federal requirements.

Results of Review

We determined that costs of \$12,533,722 invoiced for construction were allowable, allocable, and reasonable, and that costs of \$303,474 invoiced for construction management were questionable for reimbursement because they were not adequately supported by the accounting records. Also, we concluded that the city complied with the requirements for submitting quarterly reports and for paying prevailing wages. Regarding the requirement for buying goods purchased/manufactured in America, we are recommending that TSA examine the relevant project documents to ensure that 95% of the project was built with American products.

Unsupported Construction Management Costs

The city assigned construction management costs of \$303,474 for the baggage-handling system solely to the Recovery Act portion of the project. The costs are for personnel services (\$276,624) plus fees (\$26,850) provided by the city's construction management services firm. The baggage-handling system project consists of facilities to support the CBIS and other baggage-handling system facilities not eligible for reimbursement.

The time records supporting the personnel services costs indicated, however, that the individual who performed baggage handling duties worked on the entire terminal renovation. In that regard, the specialist who performed these duties told us that his time should have been allocated between the CBIS project and the remaining baggage-handling system activities. The TSA site lead confirmed that the specialist's time was not limited to the CBIS project.

¹ On October 13, 2009, TSA issued a waiver to the Buy American requirements. The waiver specifies that at least 95% of each project be built with American-produced products and allows up to 5% of total project costs to be used for non-American products.

OMB Circular A-87 says that “a cost is allocable to a particular cost objective if the goods or services involved are chargeable or assignable to such cost objective in accordance with relative benefits received.” In addition, Article IV of the agreement specifically required that the reimbursable costs be associated with the CBIS project. Because fees are based on a percentage of personnel services costs and the supporting records do not identify the amount of personnel services costs that should be allocated to CBIS, we classified the entire \$303,474 for construction management services as unsupported.

City officials agreed that the construction management services costs had not been allocated. They also said that they used a conservative approach for identifying and billing of costs related to the CBIS project. In addition, city officials believed that they had incurred other eligible construction management costs that had not been invoiced and that are sufficient to offset the questionable costs. At the exit conference, the city informed us that it was working with TSA to determine an equitable basis for distributing the baggage-handling construction management costs.

Use of American Iron, Steel, and Manufactured Goods

Section 1605 of the Recovery Act requires the use of American iron, steel, and manufactured goods in the construction, alteration, maintenance, or repair of Recovery Act projects. The Recovery Act also authorizes the head of a Federal agency to waive the requirement under certain circumstances, such as when there are insufficient quantities of goods. Under TSA’s waiver of the requirement, up to 5% of total project costs may be from non-American sources. However, the support to demonstrate compliance with the requirement to use American goods was in some cases unclear or incomplete.

The general contractor on the project, Turner Construction Company, obtained 20 letters from vendors regarding the source of the mechanical and control components and the electrical components the subcontractor used for the CBIS project. Most of the letters indicated that the goods were purchased, manufactured, and assembled in the United States. However, four letters indicated that some of the goods could have been made in foreign countries.

- The first letter stated that some of the goods were purchased from Germany and Asia but that “every carton, box, package, or pallet that they ship has ‘U.S. Made’ or ‘USA Performed’ content.”

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- The second letter stated that (1) some of the finished components used in the conveyors were imported and (2) some of the bulk conveyor belt materials used in manufacturing may have been imported.
 - The third letter stated that “all products manufactured in [our] U.S. facilities meet the criteria to be included in qualified ARRA projects. Additionally, depending on the funding agency, products manufactured in our Mexican facilities may also meet the criteria and should be evaluated on a project by project basis.”
 - The fourth letter came from a catalog page and stated that “All Parts, Materials, and/or Articles in this catalog in black type may or may not comply with the Buy American ACT and the Buy American Improvement ACT of 2005, if necessary please check with the factory.”

City officials also provided us a summary calculation showing that about 99.7% of all of the equipment and material components used in the CBIS project were made in America. Although the city’s calculation was taken from the schedule of values for the CBIS project, the schedule of values did not include the name of the vendors that provided the goods for the various work activities. As a result, we could not readily validate the city’s calculation.

TSA officials have not examined the city’s compliance with the requirement to use American goods. However, on February 3, 2011, TSA published an administration checklist to aid contracting officials in determining Buy American compliance. TSA’s Director, Security Technology Acquisition Division, told us that TSA is developing procedures to implement the checklist.

We believe that TSA should use the checklist to help determine whether the city complied with the Buy American requirement for the CBIS project. At the exit conference, TSA’s Contracting Officer told us that the TSA site lead may be able to do a further analysis of the city’s schedule of values to determine the source of the goods used in the CBIS project.

Recommendations

We recommend that TSA’s Contracting Officer:

Recommendation #1: Resolve the \$303,474 of unsupported costs.

Recommendation #2: Review the iron, steel, and manufactured goods used in the CBIS project to determine whether the city fully complied with applicable Buy American requirements.

Management Comments and OIG Analysis

TSA Comments to Recommendation #1:

TSA Concur: Based on TSA's share of the cost of construction, it determined that \$160,841 of the unsupported construction management costs of \$303,474 were allocable to TSA. TSA said that the \$142,633 balance will be deducted from a future invoice from the city.

OIG Analysis:

The TSA decision sufficiently responds to the recommendation. However, the recommendation will remain unresolved until TSA provides us with a copy of the invoice with the \$142,633 reduction.

TSA Comments to Recommendation #2:

TSA Concur: TSA said that the contracting officer will verify that the goods used by the city complied with the Buy American requirements.

OIG Analysis:

The TSA decision sufficiently responds to the recommendation. However, the recommendation will remain unresolved until TSA provides us with evidence that it has completed the verification.

Appendix A

Purpose, Scope, and Methodology

The objective of the audit was to determine whether invoiced costs are allowable, allocable, and reasonable according to the funding agreement and applicable federal requirements. Our audit covered invoiced costs of \$12,837,196 for the period June 2009 to August 2010. This represents the total amount invoiced as of January 31, 2011.

Our tests and procedures included the following:

- Reviewing TSA project files, the award agreement and modifications, the Recovery Act, and TSA and OMB guidelines;
- Interviewing TSA officials to obtain an understanding of project operations;
- Examining city accounting records supporting amounts invoiced;
- Interviewing city officials to obtain an understanding of project management, accounting, procurement, and invoicing;
- Inspecting the CBIS project;
- Performing fraud detection procedures; and
- Reviewing the working papers of the certified public accountant firm that performed the Single Audit of the San Francisco International Airport for fiscal year ending June 30, 2010.

The Single Audit of the airport was performed by KPMG and included Recovery Act-funded CBIS project costs of \$12,224,567 (or 95% of invoiced costs). The Single Audit report classified the CBIS as a major program and assessed the airport as a low risk.² The Single Audit report did not identify any questionable costs related to the CBIS, but reported that (1) the contractor's statements of compliance with the *Davis-Bacon Act* were submitted late and (2) the city did not appear to be in conformity with the Recovery Act (Section 1512) reporting requirements. The Single Audit did not classify either of these findings as a material weakness.

We also tested city records supporting costs invoiced to determine compliance with OMB Circular A-87 and with other terms and

² A low-risk assessment results from the preceding two annual Single Audits with unqualified opinions on the entity's financial statements and the schedule of expenditures of federal awards, and no deficiencies in internal controls which were identified as material weaknesses under the requirements of generally accepted government auditing standards.

Appendix A
Purpose, Scope, and Methodology

conditions of the agreement. We considered the Single Audit and the city's internal controls over the administration of TSA funds in determining our audit procedures.

We conducted this performance review between February 15, 2011 and April 6, 2011, pursuant to the *Inspector General Act of 1978*, as amended, and according to 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 upon our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based upon our audit objectives. We appreciate the cooperation of City of San Francisco and TSA officials in providing the information and access necessary to accomplish this review.

Appendix B Management Comments to the Draft Report

U.S. Department of Homeland Security
601 South 12th Street
Arlington, VA 20598



Transportation
Security
Administration

JUL 15 2011

INFORMATION

MEMORANDUM FOR: Charles Edwards
Acting Inspector General
Department of Homeland Security

FROM: John S. Pistole *John Pistole*
Administrator

SUBJECT: The Transportation Security Administration's (TSA) Response to the Department of Homeland Security (DHS) Office of Inspector General's *Draft Letter Report: Review of Costs Invoiced by the City of San Francisco Relating to the Terminal 2 Checked Baggage Screening Project at San Francisco International Airport Under Other Transaction Agreement Number HSTS04-09-H-REC123, For Official Use Only*

Purpose

This memorandum constitutes TSA's formal Agency response to DHS Office of Inspector General (OIG) draft letter report entitled, *Draft Letter Report: Review of Costs Invoiced by the City of San Francisco Relating to the Terminal 2 Checked Baggage Screening Project at San Francisco International Airport Under Other Transaction Agreement Number HSTS04-09-H-REC123 - For Official Use Only*, OIG Project No. 11-112-AUD-TSA, dated June 9, 2011. TSA appreciates the opportunity to review and provide comments to your draft report.

Background

As part of the American Recovery and Reinvestment Act of 2009 (Recovery Act), TSA was appropriated \$1 billion for "procurement and installation of checked baggage explosives detection systems and checkpoint explosives detection equipment." TSA has awarded more than \$500 million in Recovery Act funding to airport organizations for modifying facilities to accommodate new baggage-screening equipment through the Electronic Baggage Screening Program (EBSF).

**Review of Costs Invoiced by the City of San Francisco Relating to the
Terminal 2 Checked Baggage Screening Project at San Francisco International Airport
Under Other Transaction Agreement Number HSTS04-09-H-REC123**

Appendix B Management Comments to the Draft Report

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One Recovery Act award was to the City of San Francisco (the City) for a Checked Baggage Inspection System (CBIS) at San Francisco International Airport (SFO) through an Other Transaction Agreement (OTA) dated June 11, 2009. The City had previously awarded a terminal renovation project at SFO in which TSA was not involved that included a \$32,105,580 subcontract for the baggage-handling system renovation. Through the OTA, TSA was able to provide Recovery Act funding for the CBIS portion of the project. The City estimated that the CBIS project represented approximately \$17,052,000 of the total cost. As of January 31, 2011, the City had invoiced \$12,837,196 for construction (\$12,533,722) and construction management (\$303,474).

Discussion

The results of the audit determined that approximately 2 percent of the costs invoiced by the City were questionable because they were not adequately supported by accounting records. Specifically, while the \$12,533,722 invoiced for construction was allowable, the \$303,474 invoiced for construction management costs (personnel services and fees) was not allocated between the Recovery Act funded CBIS project and the larger terminal renovation project. To resolve this issue, TSA will work with the City to pro-rate these costs based on the percentage of actual costs of the \$17 million CBIS project compared to the total cost of the larger terminal renovation project, \$32 million. Based on this, \$160,841 of the questioned construction management costs (\$303,474) could be allocated to the CBIS project, with \$142,633 being allocated to the larger terminal renovation project. This adjustment will be attained by TSA receiving a future invoice from the City reflective of a \$142,633 reduction in costs.

The audit also determined that TSA officials did not examine the City's compliance with the Buy American Act. While most of the letters obtained by the general contractor indicated that the goods were Buy American Act compliant, four letters indicated that some could have been manufactured in foreign countries. While City officials provided OIG with a summary calculation from a schedule of values "showing that about 99.7% of all of the equipment and material components used in the CBIS project were made in America," the schedule did not include the names of the vendors that provided these goods. As a result, OIG was not able to validate the City's use of Buy American Act compliant materials. To verify that the goods used are Buy American Act compliant, TSA will conduct further analysis to ensure that the schedule of values includes the names of the specific vendors who provided those materials.

TSA concurs with both of the recommendations made in the subject draft report and will take the actions necessary to resolve these issues.

Recommendation 1: TSA's Contracting Officer resolve the \$303,474 of unsupported costs.

TSA Concurs: As indicated above, TSA will work with the City to pro-rate the \$303,474 of unsupported construction management costs based on the percentage of actual costs of the \$17 million CBIS project compared to the total cost of the larger terminal renovation project, \$32 million. Based on this, \$160,841 of the questioned construction management costs (\$303,474) could be allocated to the CBIS project, with \$142,633 being allocated to the larger

Appendix B

Management Comments to the Draft Report

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terminal renovation project. This adjustment will be attained by TSA receiving a future invoice from the City reflective of a \$142,633 reduction in total reimbursable CBIS costs.

Recommendation 2: TSA's Contracting Officer review the iron, steel, and manufactured goods used in the CBIS project to determine whether the city fully complied with applicable Buy American requirements.

TSA Concurs: While City officials provided the OIG with a summary calculation from a schedule of values showing that approximately 99.7 percent of all of the equipment and material components used in the CBIS project were made in America, the Contracting Officer will work with the TSA site lead to ensure that the schedule of values includes the names of the specific vendors who provided those materials in order to verify that the goods used are compliant with Buy American Act requirements.

Additionally, TSA's Office of Acquisition has developed a checklist to assist acquisition workforce staff in assessing and monitoring Recovery Act recipient compliance with Buy American Act compliance. TSA intends to implement use of this checklist within 90 days. This checklist was previously provided to OIG in an update to *OIG-11-07, Final Report, Use of American Recovery and Reinvestment Act Funds by the TSA for the Electronic Baggage Screening Program (November 12, 2010)*.

Appendix C
Major Contributors to this Report

Roger LaRouche, Director
Robert Leonard, Audit Manager
Karl Gallagher, Audit Manager

Appendix D
Report Distribution

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