



OFFICE of
INSPECTOR GENERAL

UNITED STATES DEPARTMENT OF
HOUSING AND URBAN DEVELOPMENT

The Puerto Rico Department of Housing's Contracting Method for Program Management Services for the R3 program

Audit Report Number: 2023-AT-1002

March 31, 2023

Date: March 31, 2023

To: Claudia I. Monterrosa
Deputy Assistant Secretary, Office of Deputy Assistant Secretary for Grant Programs, DG

From: *//signed//*
Kilah S. White
Assistant Inspector General for Audit, Office of Inspector General, GA

Subject: The Puerto Rico Department of Housing's Contracting Method For Program Management Services for the R3 program

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our expenditure review of the Puerto Rico Department of Housing's Home Repair, Reconstruction, or Relocation program.

HUD Handbook 2000.06, REV-4, sets specific timeframes for management decisions on recommended corrective actions. For each recommendation without a management decision, please respond and provide status reports in accordance with the HUD Handbook. Please furnish us copies of any correspondence or directives issued because of the audit.

The Inspector General Act, as amended, requires that OIG post its reports on the OIG website. Accordingly, this report will be posted at <https://www.hudoig.gov>.

If you have any questions or comments about this report, please do not hesitate to call Nikita N. Irons, Audit Director, at (404) 331-3369.

Highlights

THE PUERTO RICO DEPARTMENT OF HOUSING'S CONTRACTING METHOD FOR PROGRAM MANAGEMENT SERVICES FOR THE R3 PROGRAM | 2023-AT-1002

What We Audited and Why

We audited the Puerto Rico Department of Housing's (PRDOH) Home Repair, Reconstruction, or Relocation (R3) program. We initiated this audit as part of our commitment to helping the U.S. Department of Housing and Urban Development (HUD) support effectiveness and accountability in long-term disaster recovery.

Our objective was to determine whether PRDOH followed applicable program requirements when spending R3 program funds.

What We Found

During our audit of PRDOH's R3 program funds, we determined that PRDOH generally followed applicable program requirements; however, we identified four contracts where PRDOH may have used the prohibited cost plus a percentage of cost (CPPC) contracting method to acquire program management services. Specifically, there were multiple indicators that all four of its program management services contracts could be considered CPPC contracts. PRDOH itself was concerned that these agreements were prohibited CPPC contracts and amended three of the contracts "in order to clarify that the agreement is not a 'cost-plus-percentage-of-cost' contract." However, we believed that the amendments did not completely remove the question of whether these agreements violate the CPPC contracting prohibition. At our request, HUD obtained a legal opinion from its Office of General Counsel which opined that the contracts in question did not constitute a CPPC contract.

What We Recommend

This report contains no recommendations. However, we are troubled by the manner in which PRDOH handled these four contracts, especially in their formation and administration prior to HUD's 2019 monitoring review. We believe additional monitoring of PRDOH's contracting actions is prudent to ensure they are compliant with HUD requirements.

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Background and Objectives

In September 2017, Hurricanes Irma and Maria caused catastrophic damage to Puerto Rico. Although Hurricane Irma's eyewall did not hit Puerto Rico directly, it still caused widespread power outages, flooding, and wind damage. Two weeks after Hurricane Irma barely missed Puerto Rico, Hurricane Maria struck the island directly as a strong category 4 hurricane with sustained winds of 155 miles per hour. Hurricane Maria caused catastrophic flooding and damage, and it destroyed the power grid. According to the Housing Damage Assessment and Recovery Strategies Report (June 29, 2018),¹ the Federal Emergency Management Agency (FEMA) inspections following Hurricanes Irma and Maria identified more than 307,000 homes as having moderate or major damage or as destroyed.

In February and April 2018, HUD announced that it had awarded \$19.9 billion in Community Development Block Grant Disaster Recovery (CDBG-DR) funds to Puerto Rico to recover from the hurricanes. On September 20, 2018, HUD signed the first grant agreement for the use \$1.5 billion² of these funds. As part of the first grant agreement, HUD required the Puerto Rico Department of Housing (PRDOH) to consider and address its unmet housing recovery needs.

PRDOH was created by Act No. 97 of June 10, 1972. Through a secretary appointed by the governor, PRDOH is engaged in implementing the government's policy related to public housing. PRDOH has been appointed by the governor of Puerto Rico as the responsible agency for the administration of the CDBG-DR grant program. Before becoming the grantee for the disaster funds, PRDOH administered HUD's Housing Choice Voucher Program and Continuum of Care Program.

According to Amendment 8 of PRDOH's action plan, effective February 25, 2022, PRDOH allocated \$2.95 billion for its R3 program. This program provides assistance to eligible homeowners to repair damaged homes or rebuild substantially damaged homes in non-hazardous areas. Eligible homeowners with damaged homes in a hazard zone will be offered relocation assistance. Under the R3 program, applicants must prove both property ownership and primary residency at the time of the storm to receive assistance. Secondary or vacation homes are not eligible for assistance. Participants in homes that may not be rebuilt due to legal, engineering, or environmental constraints are offered relocation options.

According to HUD's Disaster Recovery Grant Reporting (DRGR) system,³ as of September 12, 2022, PRDOH had drawn down more than \$1.11 billion in disaster funds, of which more than \$573 million (about 52 percent) was charged to its Home Repair, Reconstruction, or Relocation (R3) program.

Our objective was to determine whether PRDOH followed applicable program requirements when spending R3 program funds.

¹ Following the devastation caused by Hurricanes Irma and Maria, FEMA activated the Housing Recovery Support Function under the National Disaster Recovery Framework to support response and recovery efforts in Puerto Rico. HUD is the coordinating agency, and in this role collaborates with FEMA and other Federal partners to support the housing recovery priorities established by the Commonwealth of Puerto Rico. As part of these efforts, HUD and Housing Recovery Support Function partners collaborated on the Puerto Rico Damage Assessment and Recoveries Strategies Report (<http://spp-pr.org/wp-content/uploads/downloads/2018/07/HUD-Housing-Damage-Assessment-Recovery-Strategies-6-29-18.pdf>).

² Congress appropriated \$1,507,179,000 through Public Law 115-56.

³ The DRGR system is primarily used by grantees to access grant funds and report performance accomplishments for grant-funded activities.

Results of Audit

PRDOH'S CONTRACTING METHOD FOR PROGRAM MANAGEMENT SERVICES FOR ITS R3 PROGRAM

During our audit of PRDOH's R3 program, we identified four contracts where PRDOH may have used the prohibited cost plus a percentage of cost (CPPC) contracting method to acquire program management services. Specifically, there were multiple indicators that all four of its program management services contracts could be CPPC contracts. PRDOH told us that it too was concerned that these agreements were prohibited CPPC contracts and amended three of the contracts "in order to clarify that the agreement is not a 'cost-plus-percentage-of-cost' contract." However, we were concerned that the amendments did not completely remove the question of whether these agreements violate the CPPC contracting prohibition. At our request, HUD obtained a legal opinion from its Office of General Counsel which opined that the contracts in question did not constitute a CPPC contract.

PRDOH's Program Management Services Contracts Arguably Met the Comptroller General's Four-Part Test

The Comptroller General⁴ developed a four-part test to determine whether contracts can be considered "cost plus a percentage of cost" contracts, or CPPC. According to 24 Code of Federal Regulations (CFR) 570.489(g) and Federal Court decisions, States (including Puerto Rico) are prohibited from using CPPC contracts because contractors are penalized for efficient and economical performance and rewarded for non-economical performance. The criteria used to identify a CPPC structure are (1) payment is on a predetermined percentage rate, (2) the percentage rate is applied to actual performance costs (as opposed to estimated or target performance costs determined at the outset), (3) the contractor's entitlement is uncertain at the time of award, and (4) the contractor's entitlement increases commensurately with increased performance costs. Generally, a CPPC contract is one that is structured to pay the contractor actual costs incurred on the contract plus a fixed percent for profit or overhead (that is not audited/adjusted) and which is applied to actual costs incurred.

The contracts arguably met all of the above criteria, as follows:

Criterion 1 - Payment is on a predetermined percentage rate. The four program management contracts provided compensation for hourly billing rates plus overhead costs at a fixed percentage of the total billable rates and profit at a fixed percentage of total billable hours and overhead, all of which varied by contractor. Based on the original program manager services contracts, it appeared that the overhead and profit rates were fixed in advance, so that PRDOH was bound to pay actual costs plus a predetermined rate for overhead and profit, which met the first criterion of a CPPC contract.

Criterion 2 - The percentage rate is applied to actual performance costs (as opposed to estimated or target performance costs determined at the outset). The four program management services contracts

⁴ 55 Comp. Gen. 554, 562 (1975); see also: *Urban Data Sys., Inc. v. United States*, 699 F.2d 1147 (Fed. Cir. 1983) (adopting criteria developed by the Comptroller General at 55 Comp. Gen. 554, 562 (1975)) and *Muschany v. United States*, 324 U.S. 49, 62, 65 S. Ct. 442, 89 L. Ed. 744 (1945) and 55 Comp.Gen. 554, 562 (1975.)

provided for percentage rates of overhead and profit to be applied directly to the actual labor costs for a specific month. This process results in the contract price paid being the costs actually incurred each month plus a fixed percentage of those costs for overhead and an additional fee of total costs and overhead for profit. Although the percentage of overhead that may be compensated was determined, what could be deemed overhead by each entity was not, which resulted in significant rate variations among contractors. Further, the percentage rate was not determined based on an estimate of expected or actual overhead costs. Therefore, overhead was not a fixed amount and could vary monthly. PRDOH indicated that the reason overhead rates varied significantly among contractors was that program managers were inconsistent in determining what to include as overhead and could not provide sufficient support regarding how the contractors calculated their overhead rates.

Criterion 3 - The contractor's entitlement is uncertain at the time of award. The four program management contractors' entitlement depended on the number of billable hours per month up to the cap of 200 hours, and the amount billed would rise or fall based on the actual billable hours. Therefore, combined with the uncertainty of the undefined overhead, it could be argued the contractor's entitlement was uncertain at the time of contracting. Although the number of billable hours per month was capped at 200 hours per employee, establishing a maximum fee amount in a contract does not necessarily eliminate it from being considered a CPPC contract.⁵

Criterion 4 - The contractor's entitlement increases commensurately with increased performance costs. The four program management contractors' entitlement depended on the number of hours billed for a specific month; therefore, the amount billed would increase as actual billable hours increased.

We also identified indicators that led us to be concerned that the program management contracts were CPPC contracts. For example, PRDOH amended the program management services contracts. Three of the four contracts included language that the cost structure for the program management and administrative task "is amended in order to clarify that the agreement is not a 'cost-plus-percentage-of-cost' contract." This language implies that PRDOH was aware that someone reviewing the contracts could consider them to be CPPC contracts. PRDOH provided documentation showing that it amended the contracts as a result of a HUD monitoring review to remove any misinterpretation concerning the type of contract. As shown in table 1, the amendments did not appear to resolve the CPPC issue because the amendments incorporated the previous overhead and profit percentages into the amount paid per hour, which did not change the total amount paid to the contractor. Therefore, we were concerned that the amendments did not address the concern that someone reviewing contract could potentially view it as being a CPPC contract.

⁵ Urban Data Systems, Inc., v. United States, 699 F.2d 1114, 1152 (Fed. Cir. 1983) ("There is nothing in the statute, or its background or objectives, to distinguish a 'cost-plus-a-percentage-of-cost-up-to-a-designated-limit' system of contracting from an unlimited cost-plus-a-percentage-of-cost system."); Cf. 38 Comp. Gen. 38, 40 (1958) (cost limitations are not sufficient to save such contracts from violating the prohibition.).

Table 1

Original and amended rates for program management services*				
Original rates**	Per hour	Overhead %	Profit %	Total
AECOM	\$122.89	182.50	8.00	\$374.94
Alliance for the Recovery of Puerto Rico	86.12	103.04	9.00	190.60
ICF, Incorporated, LLC	240.75	8.69	4.00	272.15
Innovative Emergency Management, Inc.	92.31	73.00	10.00	175.67
Amended rates	Per hour \$	Overhead %	Profit %	Total
AECOM***	\$122.89	182.50	8.00	\$374.94
Alliance for the Recovery of Puerto Rico	190.60	0	0	190.60
ICF, Incorporated, LLC	272.15	0	0	272.15
Innovative Emergency Management, Inc.	175.66	0	0	175.66
*List only includes the program manager position for each program manager.				
**Calculated by HUD OIG, rounded to the next cent.				
***PRDOH did not amend AECOM’s contract.				

We requested payroll documentation from PRDOH for all four program managers, such as employee wages, deductions, fringe benefits, net pay, etc., to support the amounts charged. In its response, PRDOH stated that the four program manager contracts were time and materials contracts for which such documentation was not required. PRDOH also stated that requesting payroll documentation and then applying the percentages would produce a CPPC contract, which is prohibited. PRDOH never provided the payroll data for our analysis.

HUD’s Office of General Counsel Opined On PRDOH’s R3 Program Management Contracts

In response to a draft of this report, HUD’s Office of General Counsel (OGC) provided a legal opinion to OIG stating that PRDOH had not used prohibited “cost-plus-a-percentage of cost” (CPPC) contracts in procuring services with CDBG-DR funds from four program management (PM) contractors for Puerto Rico’s Home Repair, Reconstruction, or Relocation Program (R3). OGC determined that the R3 PM services contracts were not CPPC contracts because the plain language of the contract before it was amended indicates that it was a permissible cost-plus-fixed-fee contract. The contractor’s entitlement was a fixed amount per month, and the contractor could bill less than the fixed amount in any given month if the contractor was paid the full fixed entitlement over the life of the contract. Further, since the contract was amended before it ended, it is impossible to know whether PRDOH would have impermissibly administered the contract as a CPPC over the life of the contract. OGC further stated that whether PRDOH violated the prohibition on CPPC contracts is moot from the date of the amendment of each PM services contract because PRDOH amended each PM services contract for the remaining contract period into a permissible labor-hours contract, removing profit as a separate cost item. Moreover, since the contracts were amended before billing concluded, OGC saw no basis to conclude with certainty that the PM contracts were prohibited CPPC contracts.

Conclusion

HUD's OGC opined that PRDOH's program management contracts were not impermissible CPPC contracts. Additionally, HUD provided technical assistance to PRDOH staff regarding its contracting in 2020 after concluding its prior monitoring review. Therefore, this report contains no recommendations.

However, we are troubled by the manner in which PRDOH handled these four contracts, especially in their formation and administration prior to HUD's 2019 monitoring review. We believe additional monitoring of PRDOH's contracting actions is prudent to ensure they are compliant with HUD requirements.

Scope and Methodology

We conducted our audit work from July 2020 to September 2022 in San Juan, PR. Our audit period was from July 2019 through November 2020.

To accomplish our audit objective, we

- Reviewed relevant criteria, including public laws and Federal Register notices.
- Interviewed program staff at HUD and PRDOH.
- Reviewed PRDOH policies and procedures with a focus on program expenditures.
- Reviewed PRDOH's action plans and amendments.
- Reviewed the 2018 and 2020 CDBG-DR grant agreements between HUD and PRDOH.
- Reviewed the three most recent independent auditor reports for the periods ending June 30, 2017, June 30, 2018, and June 30, 2019.
- Reviewed HUD monitoring reports.
- Reviewed internal PRDOH monitoring reports and audit reports.
- Reviewed PRDOH quarterly performance reports.
- Reviewed financial reports from HUD's DRGR system to obtain grant drawdown information for the audit period.
- Reviewed financial reports from PRDOH, such as its disbursement register, trial balances, general ledger, bank accounts, and procurement register.

We selected and reviewed a sample of drawdowns from HUD's DRGR system to ensure that transactions were allowable and properly supported and verified the accuracy and completeness of the accounting records for the period July 1, 2019, through November 30, 2020.

HUD's DRGR system showed PRDOH's R3 program expenditures of more than \$36 million in 111 DRGR vouchers for the period July 1, 2019, through June 30, 2020. Using a nonstatistical sampling plan,⁶ we reviewed three DRGR vouchers that totaled more than \$6.7 million (or 18.3 percent of the amount drawn during the review period) to determine whether PRDOH spent CDBG-DR funds for the R3 program in accordance with its action plan and applicable program requirements. These vouchers included expenditure transactions of all four contracted program managers.⁷

In addition, we obtained PRDOH's disbursement register for the expanded audit period of July 1, 2019, through November 30, 2020.⁸ It included 77 transactions related to program management services, totaling nearly \$35 million. We selected all 77 transactions related to the program management services and reviewed the supporting documentation for each transaction to perform our expenditure review to

⁶ Due to the small number of vouchers, we did not conduct statistical sampling.

⁷ Program managers are responsible for operational support to PRDOH, applicant intake, eligibility determinations, duplication of benefits analysis, performing damage assessments, and everyday management of the different tasks performed by PRDOH's other contractors and consultants, among other tasks. PRDOH contracted AECOM, Alliance for the Recovery of Puerto Rico, Innovative Emergency Management, Inc, and ICF, Incorporated, LLC, as program managers.

⁸ The audit period was expanded to include additional transactions related to program manager services expenditures. The original review period was July 1, 2019, through June 30, 2020.

determine whether costs were allowable and properly supported and to quantify the questioned amounts, if any. Finally, we reviewed the disbursement register to determine whether PRDOH correctly classified program expenditures in DRGR and whether activity delivery costs⁹ contributed to the objectives and the intended benefits of the R3 program.

The results of this audit apply only to the expenditures reviewed and cannot be projected to the universe of activities. We relied in part on computer-processed data contained in PRDOH's systems and HUD's DRGR system to achieve our audit objectives. Although we did not perform a detailed assessment of the reliability of the data, we performed a minimal level of testing and found the data to be adequately reliable for our purposes. The tests for reliability included but were not limited to comparing computer-processed data to drawdown support documents, expenditure support documents, and bank statements.

We conducted the audit 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 objective(s). We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective(s).

⁹ Activity delivery costs are costs incurred by a grantee or subrecipient directly related to delivery of a specific CDBG-DR project or service to a beneficiary. They are not required to be tied to a specific address but must be tied to delivering CDBG-DR-eligible project or units.

Appendixes

APPENDIX A - AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation – Auditee Comments



February 14, 2023

Nikita N. Irons
Regional Inspector General for Audit
Office of Audit, Region 4
U.S. Department of Housing and Urban Development
75 Ted Turner Drive, Room 330
Atlanta, GA 30303

Via email: eyala@hudoia.gov

RE: PRDOH Response Worksheet – HUD OIG Audit Report No. 2023-AT-100X

Dear Ms. Irons,

On February 7, 2023, the Puerto Rico Department of Housing (PRDOH) received a Draft Audit Report No. 2023-AT-100X from the U.S. Department of Housing and Urban Development – Office of Inspector General (HUD OIG), which includes a draft Finding from their review of the Home Repair, Reconstruction, or Relocation (R3) Program conducted on July 2020. As requested by HUD OIG, PRDOH hereby submits its comments in a response worksheet to be included in the final audit report.

HUD OIG Statement_1	<i>"PRDOH's Program Management Services Contracts Arguably Met the Comptroller General's Four-Part Test"</i>
PRDOH Response_1	<p>PRDOH disagrees with HUD OIG's interpretation of the R3 Program Manager (PM) contracts as cost-plus-percentage-of-costs (CPPC) contracts.</p> <p>A CPPC contract is a contracting method under which the Government contracts and is bound to pay costs undetermined at the time the contract is made and to be incurred in the future, plus a commission based on a percentage of these future costs. See <i>Muschany et al. v. United States; Andrews et al. v. Same</i>, 324 US 49 (1945). For a CPPC situation to present itself the U.S. Government Accountability Office (GAO) has established a four-pronged test in which all of the following criteria must be present: (1) payment is at a predetermined percentage rate; (2) the rate is applied to actual performance costs; (3) the contractor's entitlement is uncertain at the time of</p>

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	<p>contracting; and (4) it increases commensurately with increased performance costs. If any of the four (4) points are not present, then there is no CPPC. In the context of the R3 PM contracts, two out of the four criteria are not met, therefore they are not CPPC contracts.</p> <p>The R3 PM contracts were structured using a combination of two (2) contract types and pricing structures. The first is a labor-hour portion included as the Program Management and Administration task to compensate the eventual Program Managers for the high-level management and administrative personnel required for the services. The second portion of the contract is a fixed fee per unit pricing for milestone tasks covering application-specific services, for specific tasks to be performed by contractors while processing program applications. This is the R3 Application Per Unit Tasks and Other Tasks. The independent cost estimate (ICE) was also prepared using these pricing structures and taking into consideration the R3 Program needs at that time.</p> <p>Criterion 3 of the CPPC test requires the contractor's entitlement to be uncertain at the time of contracting. In IEM's specific example, the entitlement for the Program Manager position is \$92.31 plus \$67.39 for overhead ($\\$67.39 = \\$92.31 \times 73\%$) and \$15.97 for profit ($\\$15.97 = (\\$92.31 + \\$15.97) \times 10\%$), for a total of \$175.67 for each hour of work by the position. Rates for all other positions can also be determined using the same methodology where each hour of work is a fixed fee. Therefore, since the contractor's entitlement was ascertainable at the time of contracting the contract does not constitute a CPPC situation.</p> <p>Criterion 4 of the CPPC test requires that the contractor's entitlement increase commensurate to increased performance costs. In each of the PM contracts the PRDOH established a billable cap of 200 monthly hours for each position in the Program Management and Administration Task. Therefore, contractors cannot increase their entitlement beyond the established monthly cap for the positions, even if such positions were employed in excess of 200 hours for any specific month. PRDOH, when it accepted this offer agreed to pay the set amount per hour, up to the 200 hours cap, and no more. The contract contains no provision allowing adjustment of price based on possible future indeterminate expenses. See <i>Muschany, supra</i>.</p>
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	<p>During the Request for Proposals (RFP) process the PRDOH provided responses to questions and requests for clarifications from Proposers. Specifically, question no. 68 submitted by ICF Incorporated, LLC requested clarification as follows:</p> <p><i>"The Cost Form requires offerors to provide an overhead rate for program management. Can you please clarify whether that rate should include:</i></p> <ul style="list-style-type: none"><i>• fringe benefits?</i><i>• G&A (general and administrative)?</i><i>• overhead costs (office space, communications, computers, etc.)?</i><i>• travel?</i><i>• other direct costs associated with the project?"</i><p>The PRDOH responded to this request for clarification with the following:</p><p><i>"Exhibit J (Cost Form), in the Programs Management and Administration (Maximum Per Month) section, requires the Proposer to provide the overhead rate related to the positions reference in the said section. In that instance the overhead includes all cost related to accomplish the required services. This cost may include fringe benefits, travel, general and administrative, among other overhead costs."</i> (Emphasis provided.)</p><p>Federal Acquisition Regulations (FAR) Part 16, Section 16.601(b), defines a time and materials contract (T&M) as follows:</p><p><i>(b) Description. A time-and-materials contract provides for acquiring supplies or services on the basis of –</i></p><p><i>(1) Direct labor hours at specified fixed hourly rates that include wages, overhead, general and administrative expenses, and profit; [...].</i></p><p>In <i>Muschany Et Al, v. United States; Andrews Et Al, v. Same,</i> supra, the U.S. Supreme Court established:</p><p><i>... Congress certainly did not intend to prevent a party who was merely submitting a bid to the Government from computing the amount of his bid by taking into consideration his costs and then adding a certain percentage of the cost as his profit, the resulting sum bid being fixed in amount and not subject to change. Congress, by changing the original prohibition in the act from one outlawing any "cost-plus" system of contracting</i></p>
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	<p>so as to expressly authorize use of a "cost-plus-a-fixed-fee" form of contract, indicated it did not care how the contractor computed his fee or profit so long as the fee or profit was finally and conclusively fixed in amount at the time when the Government became bound to pay it by its acceptance of the bid. By eliminating the risk of loss and permitting the guarantee of a satisfactory but fixed fee, Congress sought prompt performance and lower over-all expenditures for contracts in a rising labor and commodity market than would be offered by contractors who were compelled themselves to assume the risk of these unpredictable costs." (Emphasis provided.)</p> <p>From the answers to questions and requests for clarifications, and from the U.S. Supreme Court's decision, it is evident that the Program Management and Administration Task included in the PM contracts does not constitute a CPPC situation. PRDOH used the percentages included in the task during negotiations to establish the fixed amount that PRDOH became bound to pay by its acceptance of the bids. The percentages, along with the base rates included in the contracts, also fall within the definition of fixed hourly rates for a time-and-materials contract, which includes labor hours. As an example, IEM's fixed fee for the Program Management position of \$175.67 (resulting by combining the base rate, the overhead rate, and the profit rate) includes wages, overhead, general, and administrative expenses, and profit.</p>
<p>HUD OIG Statement_1A</p>	<p>"In addition, we identified other indications supporting that program management contracts were CPPC contracts. For example, PRDOH amended the program management services contracts. Three of the four contracts stated that the cost structure for the program management and administrative task "is amended in order to clarify that the agreement is not a 'cost-plus-percentage-of-cost' contract." This language implies that PRDOH was aware that the contracts arguably were or could be considered CPPC contracts. PRDOH provided documentation showing that it amended the contracts as a result of a HUD monitoring review to remove any misinterpretation concerning the type of contract. However, as shown in table 1, the amendments did not resolve the CPPC issue as the amendments merely incorporated the previous overhead and profit percentages into the amount paid per</p>

	<p>hour, which did not change the total amount paid to the contractor. Therefore, we question whether the amendments changed the potential CPPC nature of the contract as the amounts paid per hour were the same."</p>
<p>PRDOH Response_1A</p>	<p>HUD performed a monitoring visit to PRDOH from November 13-15, 2019, in which it reviewed the Alliance, AECOM, ICF, and IEM contracts for program management services. As part of that review, HUD requested clarification regarding the contract type and provided technical assistance to PRDOH regarding clarification to certain provisions to prevent misinterpretation.</p> <p>In its formal monitoring report provided to PRDOH on February 7, 2020, and after HUD review of the aforementioned contracts and information provided by PRDOH to HUD on December 3, 2019, HUD did not issue a Finding related to the PM contracts. Instead, HUD included the following concern:</p> <p><i>The Compensation Schedule in Attachment D was adapted from the pricing schedule the contractors included in their submissions in response to the Request for Proposals. The form was requested by the grantee in its RFPs and appears designed to allow the grantee to consider profit as a separate element of price and to compare the pricing across the submissions of all qualified proposers. By disaggregating the hourly labor rates to show profit as a percentage, the Compensation Schedule could be misinterpreted to represent a prohibited form of contract. (Emphasis added.)</i></p> <p>Following HUD's guidance and feedback, PRDOH amended the contracts to clarify the language regarding the lump sum and so that the use of a percentage did not lead to misinterpretation by future reviewers. After thoroughly reviewing the contracts and their provisions to their satisfaction, on November 18, 2020, HUD issued a determination stating that "[t]he grantee ha[d] closed all Findings issued as part of this monitoring review."</p> <p>Since the PM contracts were never a CPPC contract but a time and materials contract, the amendments did not change their intrinsic nature. The amendments were executed at HUD's request to clarify the language included and remove any ambiguity to avoid misinterpretation by future reviewers.</p>

<p>HUD OIG Statement_1B</p>	<p><i>"We requested payroll documentation from PRDOH for all four program managers, such as employee wages, deductions, fringe benefits, net pay, etc., to support the amounts charged. In its response, PRDOH stated that the four program manager contracts were time and materials contracts for which such documentation was not required and stated that requesting payroll documentation and then applying the percentages would produce a CPPC contract, which is prohibited. PRDOH never provided the payroll data for our analysis."</i></p>
<p>PRDOH Response_1B</p>	<p>From HUD OIG's statement, it is unclear as to which specific interaction they are referring to. However, PRDOH maintains that the R3 PM contracts are time-and-materials contracts, which include labor hours at a fixed rate. This type of contract is validated with submitted invoices and supporting timesheets, not with payroll documentation.</p>
<p>HUD OIG Statement_2</p>	<p>"PRDOH Lacked Understanding of CPPC Contract Requirements"</p> <p><i>While PRDOH certified that it had in place proficient procurement processes, it lacked an understanding of the criteria of a CPPC contract. For example, PRDOH did not believe criterion number 3 and 4 were met because (1) the entitlement for the program manager positions were set as a fixed rate per hour and (2) they established a billable cap of 200 monthly hours for each, position, respectively. However, PRDOH ignored that the contractor's entitlement depended upon the hours charged each month, thereby arguably meeting criterion 3 and 4. Further, establishing a maximum fee or cap does not necessarily remove the CPPC structure.</i></p> <p><i>Throughout the response, PRDOH claimed the contracts to be time and materials in some instances and labor hours in other instances. In addition, it used criteria related to another type of contract, cost plus a fixed fee, to support the allowability of the program management services contracts. It appeared that PRDOH was unsure of what constituted each type of contract and did not understand the exact nature of its program management services contracts."</i></p>
<p>PRDOH Response_2</p>	<p>PRDOH disagrees with HUD OIG's statement as to PRDOH staff "lack[ing] an understanding of the criteria of a CPPC contract". After a thorough review of the facts, PRDOH maintains that the R3 PM contracts are a time-and-materials contract and do not constitute a CPPC situation. PRDOH welcomes any</p>

	recommendations HUD OIG may have on how to improve the language in the contracts to avoid any misunderstandings from future reviewers.
HUD OIG Statement_3	<p><i>"Funds May Have Been Spent on Prohibited Contracting Practice"</i></p> <p><i>We performed an analysis of the profit and overhead amounts charged by the program managers between July 1, 2019, and November 30, 2020, based on the rates presented in table 1 of this report. The amounts charged by the program managers are presented in table 2. Based on our review of the program management contracts and addendums, and the CPPC criteria, the amounts were charged using a potentially prohibited contracting method."</i></p>
PRDOH Response_3	PRDOH disagrees with this statement. Please refer to PRDOH's response to HUD OIG Statement_1.
Recommendation_1A	<i>"Seek a legal opinion from the Office of General Counsel to determine whether PRDOH awarded CPPC contracts for its four program management services. If it is determined that the contracts are prohibited, the Deputy Assistant Secretary should seek remedy under 2 CFR 200.339-343.6."</i>
PRDOH Response_4	Recommendation 1A is not addressed to PRDOH. However, as mentioned in our response to HUD OIG's Statement_1A, we wish to emphasize the fact that HUD already performed a monitoring review of the R3 PM contracts in November 2019. After a thorough review of the submitted documentation HUD did not issue any finding of CPPC. Instead, HUD recommended PRDOH "update its standard form contract language to eliminate ambiguity for future contracts" and "clarify the ambiguities for contractors under existing contracts". PRDOH followed HUD's guidance and amended the contracts to clarify the language included to avoid misinterpretation by future reviewers.
Recommendation_1B	<i>"Instruct PRDOH to provide recurring training to program staff to ensure that it understands and follows Federal procurement requirements; specifically, 24 CFR 570.489(g), which establishes that States (including Puerto Rico) are prohibited from contracting using a CPPC structure. In addition, HUD should ensure that PRDOH complies with the training and provide evidence of completion."</i>

PRDOH Response_5	PRDOH disagrees with HUD OIG's statement as to its staff "lack[ing] an understanding" of the applicable procurement requirements. However, HUD already provided training and technical assistance to PRDOH staff to ensure compliance with 24 C.F.R. § 570.489(g), as evidenced in HUD's Monitoring Report from the November 2019 monitoring event issued on February 7, 2020: "Technical assistance with respect to contract language, vendor education and outreach, internal auditor vs. monitoring role and process, RFQ to RFP process, Minority-owned Business Enterprise/Women-owned Business Enterprise requirements, and geographic preferences was provided." (HUD Monitoring Report 2/7/20).
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PRDOH appreciates the opportunity provided by HUD OIG to clarify the items included in the draft audit report, as done so in the response worksheet. Should you have any questions about the submitted responses, please feel free to contact me.

Sincerely,



Marezle Díaz Sánchez, Esq.
Disaster Recovery Deputy Secretary
Puerto Rico Department of Housing

OIG Evaluation of Auditee Comments

In response to our draft audit report, PRDOH provided comments on February 14, 2023, stating its disagreement with the characterization of the use of CPPC contracting methods for its four program management services. Additionally, in response to recommendation 1A, HUD's Office of General Counsel's (OGC) provided a legal opinion to HUD OIG on March 3, 2023. OGC concluded that the contracts did not meet the criteria of a CPPC contract. Based on the legal opinion, we have made revisions throughout the report to reflect the decision and to remove the proposed recommendations.