



DEPARTMENT OF DEFENSE

AUDIT REPORT

NAVY REGIONAL DATA AUTOMATION CENTER,
WASHINGTON, D.C., PROCUREMENT OF
AUTOMATIC DATA PROCESSING EQUIPMENT

No. 90-103

August 24, 1990

*Office of the
Inspector General*





INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-2884

August 24, 1990

**MEMORANDUM FOR ASSISTANT SECRETARY OF THE NAVY (FINANCIAL
MANAGEMENT)**

**SUBJECT: Final Report on the Audit of Navy Regional Data
Automation Center, Washington, D.C., Procurement of
Automatic Data Processing Equipment (Report No. 90-103)**

This is our final report on the Audit of the Navy Regional Data Automation Center, Washington, D.C. (NARDAC, Washington), Procurement of Automatic Data Processing Equipment. Comments on a draft of this report were considered in preparing the final report. We made the audit from November 1989 through January 1990 in response to an allegation from six vendors that NARDAC, Washington used World Computer Systems, Inc. (World Computer Systems), a firm qualified under the Small Business Administration's Section 8(a) Program, to buy two International Business Machines (IBM) Model 3745 communication processors without full and open competition. Specifically, it was believed that NARDAC had specified to World Computer Systems the specific make and model of a communication system it desired, and by so doing, had precluded other competing firms from participation in the procurement. The procurement was valued at \$924,336. Our audit objective was to determine whether the allegation had merit. A secondary objective was to determine whether internal controls were adequate to make sure that competitive procedures were used for procurements of automatic data processing equipment. Appendix C identifies the activities visited or contacted during the review.

The audit disclosed that the vendors' allegation had merit. NARDAC, Washington did not use the required competitive procedures for purchasing automatic data processing equipment and, as a result, prevented other competing firms from participating in the procurement. In addition, NARDAC violated the Walsh-Healey Act because World Computer Systems was neither a manufacturer nor a regular dealer of the equipment. Also, World Computer Systems violated the Small Business Administration (SBA) regulation precluding brokers from participation in the Section 8(a) Program. We reported the violation of the Walsh-Healey Act to the Department of Labor, and we reported the violation of the SBA regulation to the SBA. Furthermore, internal controls were lacking; however, after the vendors' allegation was made, the Commander of the Naval Data Automation Command (NAVDAC), NARDAC's parent command, took immediate action to improve internal controls and ensure that future NARDAC procurements are conducted in full and open competition. The results of the audit are

summarized in the following paragraphs, and the details, audit recommendations, and management comments are in Part II of this report.

NARDAC, Washington circumvented requirements for full and open competition when it precluded certain vendors from participating in the procurement. As a result, the acquisition violated laws and procurement regulations and resulted in the loss of significant cost savings because of the lack of full and open competition. We recommended that functional specifications be used to maximize full and open competition for all future automatic data processing equipment procurements. If functional specifications are not appropriate, then specifications should be developed in order of precedence as outlined in the Federal Information Resource Management Regulation, section 201-24.212 (page 7).

The Walsh-Healey Act (United States Code, title 41, sec. 35(a)) was violated when NARDAC, Washington used World Computer Systems as a broker to buy its communication processors. Also, World Computer Systems violated the SBA regulation (Title 13, Code of Federal Regulations, section 124.109) that prevents brokers from participating in the Section 8(a) Program. Using the Section 8(a) contractor as a broker in the procurement resulted in unnecessary costs of \$50,429, the brokerage fee paid to World Computer Systems. We recommended that NAVDAC inform its regional data centers that using brokers to acquire automatic data processing equipment violates the Walsh-Healey Act as implemented by the Federal Acquisition Regulation, subpart 22.6 (page 17).

The audit identified internal control weaknesses as defined by Public Law 97-255, Office of Management and Budget Circular A-123, and DoD Directive 5010.38. Controls were not established or effective to ensure that acquisition regulations were being followed. Specifically, NAVDAC and the Assistant Secretary of the Navy (Shipbuilding and Logistics), now the Assistant Secretary of the Navy (Research, Development and Acquisition), did not adequately monitor contracting actions by NARDAC, Washington; requirements for full and open competition were circumvented when NARDAC mislabeled a specific make and model request as competitive and used World Computer Systems to conduct the acquisition; NARDAC violated the Walsh-Healey Act's restrictions on Government use of brokers to obtain supplies; and NARDAC's General Counsel did not adequately review the basic contract or the delivery order for the communication processors. Such weaknesses resulted in an action that violated laws and regulations. Recommendations A., B., and C.1. of this report, if implemented, will correct the weaknesses (page 21).

On May 17, 1990, a draft of this report was provided to the Assistant Secretary of the Navy (Financial Management). Comments from the Assistant Secretary of the Navy (Research, Development and Acquisition) (ASN (R,D&A)) were received on July 20, 1990. ASN (R,D&A) generally agreed with our findings and recommendations but took exception to our Finding B. on the Walsh-Healey Act. ASN (R,D&A) did not believe that NARDAC, Washington had violated the Walsh-Healey Act, and because the other NARDAC centers had relatively low contracting authority, did not believe that they had failed to comply with the Walsh-Healey Act. Nevertheless, the Navy issued a policy that restricted the acquisition of equipment under ADP services contracts. The management responses to a draft of this report conformed to the provisions of DoD Directive 7650.3. No unresolved issues existed on the audit recommendations, internal control deficiencies, or potential monetary benefits. Accordingly, additional management comments on the final report are not required. The complete text of management comments is provided in Appendix A.

This report quantifies no potential monetary benefits; however, other benefits will be realized by implementing the recommendations (see Appendix B). A copy of the report will be provided to the senior official responsible for internal controls within the Navy.

The courtesies extended to the audit staff are appreciated. If you have any questions about this audit, please contact Mr. Terry L. McKinney at (202) 693-0430 (AUTOVON 223-0430) or Mr. Kent E. Shaw at (202) 693-0440 (AUTOVON 223-0440). We will give you a formal briefing on the results of audit within 15 days of the date of this memorandum, should you desire it. A list of audit team members is in Appendix D. Copies of this report are being provided to the activities listed in Appendix E.



Edward R. Jones
Deputy Assistant Inspector General
for Auditing

Enclosure

cc:
Secretary of the Navy

REPORT ON THE AUDIT OF NAVY REGIONAL DATA
AUTOMATION CENTER, WASHINGTON, D.C., PROCUREMENT OF
AUTOMATIC DATA PROCESSING EQUIPMENT

TABLE OF CONTENTS

	<u>Page</u>
TRANSMITTAL MEMORANDUM/EXECUTIVE SUMMARY	i
PART I - INTRODUCTION	
Background	1
Objectives and Scope	3
Internal Controls	4
Prior Audit Coverage	5
Other Matters of Interest	6
PART II - FINDINGS AND RECOMMENDATIONS	
A. Competition	7
B. Walsh-Healey Act	17
C. Review and Oversight of Procurement	21
APPENDIX A - Management Comments	29
APPENDIX B - Summary of Potential Monetary and Other Benefits Resulting from Audit	35
APPENDIX C - Activities Visited or Contacted	37
APPENDIX D - Audit Team Members	39
APPENDIX E - Final Report Distribution	41

Prepared by:
Financial Management Directorate
Project OFE-0029

REPORT ON THE AUDIT OF NAVY REGIONAL DATA
AUTOMATION CENTER, WASHINGTON, D.C., PROCUREMENT OF
AUTOMATIC DATA PROCESSING EQUIPMENT

PART I - INTRODUCTION

Background

The Navy Regional Data Automation Center, Washington, D.C. (NARDAC, Washington), is the largest of nine regional data automation centers operated by the Naval Data Automation Command (NAVDAC). The regional data centers are service bureaus that support Naval activities, on a reimbursable basis, in the design, development, implementation, and operation of management information systems. NARDAC, Washington operates three computer processing centers and a remote computer operations center. NARDAC, Washington provides automated support to 164 Navy and non-Navy customers. Major Navy customers include the Chief of Naval Operations, the Navy System Commands, the Military Sealift Command, the Comptroller, the Naval Military Personnel Command, and the Navy Regional Finance Center. NARDAC, Washington and other regional data centers were initially funded by appropriations from Congress and charge user fees for the services they provide. For FY's 1988 and 1989, NARDAC, Washington's revenues and costs were about \$90 million. NARDAC, Washington employs 847 civilians and 90 military personnel. NARDAC, Washington uses computer systems manufactured by IBM, Amdahl, and National Advanced Systems. The total cost of these systems was about \$29.2 million.

One of the Washington centers was obtained from the Department of Agriculture. The Department of Agriculture (USDA) transferred its staff, computer equipment, and other resources needed to run the center to the Navy because USDA was moving its computer processing workload to its Kansas City, Missouri, Computer Center and no longer needed the Washington, D.C., Computer Center. Simultaneously, NARDAC, Washington needed to increase its computer processing capacity to support expanding customer requirements. The transfer was approved by the General Services Administration on September 23, 1987, and the transfer was effective on October 1, 1987.

Eight months after the transfer of the computer center and at the request of NARDAC, the Department of Agriculture entered into contract number 54-3142-8-101RS with World Computer Systems, Inc. (World Computer Systems), of Laurel, Maryland. The contract was transferred 7 days later to NARDAC. World Computer Systems was established in 1983 under the name World Computer Systems Services Associates. In 1984, it was admitted to the Small Business Administration's Section 8(a) Program. The goal of the Section 8(a) Program, which was authorized by the Small Business Act of 1953, is to foster business ownership by socially and

economically disadvantaged individuals through Government procurement assistance and other means. The company was incorporated in Maryland on August 26, 1985, as World Computer Systems Service Associates, Inc. On August 10, 1988, the company changed its name to World Computer Systems, Inc. The company provides a variety of services, including computer programming, data processing facilities management, and systems integration. About 60 percent of World Computer Systems' business is with the Federal Government. World Computer Systems has branch offices in Oak Ridge, Tennessee; Huntsville, Alabama; Orlando, Florida; and St. Louis, Missouri.

The World Computer Systems contract was an indefinite-quantity contract under which the Government issued delivery orders for each project. The contract stated that World Computer Systems would:

... Provide automatic data processing (ADP) related services to include, but not limited to, designing, developing, and analyzing software, ADP hardware and software acquisition and maintenance and other ADP services as more specifically described in subsequent tasking statements.

The contract was for 1 year from the award date, with an option to extend the contract for 4 more years. However, NARDAC did not extend the contract, and it expired in May 1989. During the year that the contract was in force, NARDAC issued 23 orders, totaling \$3,510,056, against the contract. Eight of the orders were for systems development work; 10 were for technical support; and 5 were for systems enhancements (purchases of computer hardware and software). The largest of these orders (delivery order 7U13, dated September 15, 1988) was valued at \$924,336 and involved the purchase of IBM communication processors, software, and engineering services (i.e., installation of the software and hardware). Our audit focused on this delivery order.

NARDAC, Washington is one of five NARDAC's that have been granted contracting authority by the Assistant Secretary of the Navy (Shipbuilding and Logistics) (ASN(S&L))^{1/}. The Head of the Contracts Department reports directly to the Commanding Officer of NARDAC for contracting matters and to the Deputy Director of NARDAC for administrative matters. The Contracts Department has 31 civilian and 3 military employees, 4 of which have contracting authority. Contracting authority for computer equipment, software, and related services is limited to \$100,000. Unlimited

^{1/} The Assistant Secretary of the Navy (Shipbuilding and Logistics) was recently reorganized and is now the Assistant Secretary of the Navy (Research, Development and Acquisition).

Administrative Contracting Officer authority exists for contracts assigned to NARDAC by the Automatic Data Processing Selection Office and other contracting organizations.

Objectives and Scope

Our audit was made in response to an allegation that NARDAC, Washington had used World Computer Systems to buy two IBM Model 3745 communication processors without full and open competition. The allegation stated that NARDAC had specified to World Computer Systems the specific make and model of communication processors it desired, and by so doing, had precluded other competing firms from participating in the procurement. Our audit objective was to determine whether the allegation had merit. A secondary objective was to determine whether internal controls were adequate to ensure that competitive procedures were used for procurements of automatic data processing equipment. The audit was performed from November 1989 through January 1990. This program audit was made in accordance with auditing standards issued by the Comptroller General of the United States as implemented by the Inspector General, DoD, and accordingly included such tests of internal controls as were considered necessary.

Our review focused on the procurement of the two IBM Model 3745 communication processors by World Computer Systems for NARDAC, Washington. This procurement was valued at \$924,336. During our review we interviewed individuals from NARDAC, Washington; NAVDAC, the parent command for NARDAC; and World Computer Systems. At NARDAC, we interviewed the technical staff members who initiated the requirement, contracting officers, and the center's Competition Advocate. We also interviewed the former Commanding Officer of NARDAC. We were unable to interview the former head of NARDAC's Contracts Department because he is retired and lives outside the United States. This individual played a major role in the award of the World Computer Systems contract and in the procurement of the IBM processors. At NAVDAC, we interviewed the legal counsel who reviewed and approved the procurement. We also interviewed the former Director of NAVDAC and a former NAVDAC attorney who had approved the procurement. We also talked to representatives of Amdahl Corporation and NCR Comten. Both companies manufacture and market communication processors that compete with the IBM communication processor. Finally, we interviewed a contracting officer and the Acting Director of Information Resources Management for USDA. Our discussions with USDA were coordinated with USDA's Office of the Inspector General. Appendix C identifies the activities visited or contacted during the review.

We reviewed all available documentation developed from June 1988 to May 1989. We examined justifications and procurement records maintained by NARDAC and World Computer Systems. We compared the

procurement process used by NARDAC to criteria specified by the Federal Acquisition Regulation (FAR) and the Federal Information Resources Management Regulation (FIRMR) (Title 41, Code of Federal Regulations). Acquisitions of ADP equipment are required to follow both the FAR and the FIRMR. We also consulted Datapro Reports on Data Communications, which describes and provides specifications for competing communication processors. We also examined NARDAC and NAVDAC internal controls for procurement of ADP resources.

Internal Controls

The audit identified internal control weaknesses as defined by Public Law 97-255, Office of Management and Budget Circular A-123, and DoD Directive 5010.38. Controls were not established or effective when the procurement was made to ensure that acquisition regulations were followed. In response to a vendor complaint on the procurement, the Commander, NAVDAC took several corrective actions that should result in improved internal controls. The corrective actions include:

- Requiring that all NARDAC delivery orders for equipment be approved by its Competition Advocate;
- Requiring that all delivery orders for equipment valued at greater than \$5,000, or 10 percent of the total cost of the delivery order, also be approved by the NAVDAC Competition Advocate;
- Revising NAVDAC Instruction 5231.1, "Competition Advocacy Program," to give a clearer definition of "competition"; and
- Prohibiting further orders on the World Computer Systems contract until the scope of the contract was clearly defined by the Navy Regional Contracting Center (NRCC), Washington. Because of the NRCC review, the option to extend the contract was not exercised.

We also made a number of recommendations which we believe would improve internal controls. We recommended that the regional data centers develop functional specifications to meet their procurement needs to the maximum extent possible; that NAVDAC instruct its regional data centers not to use brokers to acquire automatic data processing equipment; and that the Commander of NAVDAC establish a policy that legal counsel review all transferred contracts before contracting actions are made against them. Recommendations A., B., and C.1. in this report, if implemented, will correct the weaknesses. This report quantifies no potential monetary benefits; however, other benefits are described in Appendix B. A copy of this report will be provided to the senior official responsible for internal controls within the Navy.

Prior Audit Coverage

This is our second audit in response to allegations made by six vendors that the Navy was steering contracts to IBM. Two reports were issued during our first audit: "Naval Military Personnel Command Planned Procurement of Automated Data Processing Equipment" (Report 90-019, December 15, 1989), and "Quick-Reaction Report on the Review of Naval Military Personnel Command (NMPC) Planned Procurement of Automated Data Processing Equipment" (Report 89-073, May 9, 1989).

These two reports concluded that NMPC's attempt to buy a communication processor was biased toward IBM. NMPC attempted to use a firm that was qualified under the Small Business Administration's (SBA) Section 8(a) Program to buy the processor. We concluded that the NMPC violated the Walsh-Healey Act when it attempted to use the 8(a) contractor. The Navy generally agreed with our recommendations and has taken appropriate corrective actions.

On June 21, 1989, the General Accounting Office (GAO) issued "Navy Improperly Restricted Competition for Its Civilian Pay System," Report No. GAO/IMTEC 89-61 (OSD case number 8041). That report was also in response to the vendors' allegations of Navy favoritism toward IBM. The report focused on a procurement by the Navy Standard Civilian Pay System (NAVSCIPS). GAO found that the Navy did not follow accepted practices for systems development in making several key technical decisions. Specifically, the Navy selected a data base management system, hardware, and the 10 sites where the system would run, without conducting the proper studies and developing adequate support.

The GAO recommended that the Assistant Secretary of the Navy (Financial Management) stop further hardware and software orders under the contract; conduct a cost-benefit analysis for the full range of site alternatives; recompute the NAVSCIPS requirements using functional specifications; and determine whether to continue the contract, limit orders to the minimum required, or terminate the contract for the convenience of the Government and award a new contract. The Comptroller, Department of Defense, responded to the recommendations. The Comptroller generally agreed with the recommendations and has taken appropriate corrective actions.

In August 1986, the ASN (S&L) made a procurement management review at NARDAC, Washington. The purpose of the review was to determine whether NARDAC's Contracts Department was complying with established procurement policies and procedures. The reviewer examined recent delivery orders for four contracts and conducted interviews with contracting staff, legal counsel, and one contracting officer's technical representative. The

resulting report contained several adverse findings on the organizational placement of the contracting office, the training of contracting officers, the potential lack of independence because contractor staff were on-site, the relationship with NAVDAC legal counsel, and the general quality of contracting. Because of the review, the Assistant Secretary reduced NARDAC's procurement authority to the issuance of orders under existing contracts and recommended to NAVDAC that it conduct significant procurement training and increase its review and oversight of NARDAC.

The Assistant Secretary made a follow-up review during May 1987. The follow-up review concluded that NARDAC had fully complied with the intent of the recommendations and had significantly improved the quality of its procurement office. Despite improved conditions noted in the ASN (S&L) follow-up review, our audit found that NARDAC's Contracts Department still needed improvement.

Other Matters of Interest

During the audit, we found that World Computer Systems violated Section 124.109 of the Small Business Administration (SBA) regulation (Title 13, Code of Federal Regulations). This section states that brokers are ineligible to take part in the Section 8(a) Program, since brokers do not satisfy the definition of a manufacturer or regular dealer. We concluded that World Computer Systems was neither a manufacturer nor a regular dealer, as defined by the SBA regulation, of the computer equipment it sold to the Navy; therefore, World Computer Systems had acted as a broker. In addition, World Computer Systems violated its contract's Small Business Concern Representation clause (FAR 52.219-01). In Section K.8 of the contract, World Computer Systems represented and certified that it is a small business concern and that all end items to be furnished will be manufactured or produced by a small business concern. The IBM processors purchased for NARDAC were the end items under this delivery order. IBM does not meet the definition of a small business. We brought the violations to the attention of the Administrator and the Inspector General of the Small Business Administration.

Likewise, we found that the NARDAC procurement through World Computer Systems violated the Walsh-Healey Act (U.S.C., title 41, section 35(a)) as implemented by FAR subpart 22.6. The Walsh-Healey Act provides that the Government can procure its supplies only from the manufacturer or a regular dealer of the supplies. This violation was brought to the attention of the Department of Labor, which is responsible for enforcing the Act. Both the violation of the SBA regulation and the violation of the Walsh-Healey Act are discussed in greater detail in Finding B.

PART II - FINDINGS AND RECOMMENDATIONS

A. Competition

FINDING

The Navy Regional Data Automation Center, Washington, D.C. (NARDAC, Washington), circumvented requirements for full and open competition and showed bias toward International Business Machines Corporation (IBM) when it purchased communication processors through World Computer Systems, Inc. (World Computer Systems). The delivery order precluded two competing vendors, Amdahl and NCR Comten, from participating in the procurement. Since the delivery order was not synopsisized in the Government's Commerce Business Daily, the vendors were not aware of the procurement. The specifications also cited a requirement for a specific make and model of processor manufactured only by IBM. NARDAC favored the IBM processor because its staff concluded that only IBM could meet their requirements and that the IBM communication processors were technologically superior to competing products. NARDAC circumvented the requirements for full and open competition because:

- the solicitation was mislabeled as a "competitive contract" instead of a sole-source procurement;
- internal controls to detect and prevent the mislabeled procurement were not in place,
- legal loopholes existed that do not require full and open competition when a contractor buys supplies for the Government; and
- NARDAC believed that the Section 8(a) firm could obtain the processor faster than the Naval Regional Contracting Center.

The buy through World Computer Systems violated laws and procurement regulations and resulted in the loss of potential cost savings that would have resulted from full and open competition.

DISCUSSION OF DETAILS

Background. The Government's procurement goal is full and open competition through competitive procedures that allow all responsible sources to submit offers. Agencies are to award contracts based on the lowest overall cost to the Government. Acquisition of automatic data processing (ADP) equipment, supplies, and services must follow both the Federal Acquisition Regulation (FAR) and the Federal Information Resources Management Regulation (FIRMR).

ADP specifications should reflect an agency's requirements and should be based on need and circumstances. Office of Management and Budget Circular A-109 and FIRMR parts 201-11, 201-20, and 201-30 emphasize the development of specifications to enhance competition. FIRMR section 201-30.013, "Specifications and Purchase Descriptions," identifies five types of specifications allowable for ADP procurements. The five specification types and their order of precedence for use are as follows: functional ADP specifications, equipment performance specifications, software and equipment plug-to-plug compatible functionally equivalent specifications, brand name or equal specifications, and specific make or model specifications.

One of the first four specification types is required for a competitive award. FIRMR section 201-2.001, states that a specific make or model specification is considered noncompetitive:

Noncompetitive (sole source) requirement means that the Government's requirement is set forth in the form of necessary specifications so restrictive that (a) there is only one known supplier capable of satisfying the Government's requirement or (b) the acquisition is based on specific make and model specifications/purchase descriptions, notwithstanding the existence of adequate price competition.

If a specific make and model specification is used, formal justifications and approvals are required. The FAR 6.303 and 6.304, describe the requirements for sole-source justifications and approval authority. The FAR requires that a contracting officer not enter into a sole-source contract unless he or she justifies such actions in writing. Each justification must contain enough facts and a rationale to justify the circumstances requiring other than full and open competition (FAR 6.303), and each justification must be approved at various levels based on the proposed contract value (FAR 6.304). According to NAVDAC Instruction 5230.3B, "Information System Project Actions," the Commander of NAVDAC must approve noncompetitive requests exceeding \$50,000.

Requirement for Communication Processors. NARDAC recognized a requirement for new communication processors in 1987. At one of NARDAC's Computer Centers at the Washington Navy Yard, the Amdahl Model 4705 communication processors were about 5 years old. NARDAC managers told us that the processors could no longer support NARDAC's growing customer requirements. New processors were also needed to accommodate increased wordloads at its Washington Navy Yard Centers.

NARDAC management had initially hoped to obtain the processors as part of its Data Processing Installation Phase III (DPI Phase III) procurement. The DPI Phase III was an attempt by the NAVDAC to buy IBM-compatible equipment to satisfy NARDAC's growing customer requirements. The DPI Phase III procurement was to be a major procurement with an estimated value of \$150 million. The procurement, however, was delayed and ultimately suspended after protests by NCR Comten and PacifiCorp Capital, who contended that the request for proposals favored IBM. During December 1988, in response to PacifiCorp's protest, the General Services Administration Board of Contract Appeals agreed with PacifiCorp that the solicitation provided for less than full and open competition, and ordered the Navy to rewrite and reissue the contract solicitation. The House of Representatives Government Operations Committee also took an interest in the DPI Phase III procurement. On August 29, 1989, at the request of the Committee, the General Services Administration formally withdrew its delegation of procurement authority for the buy. The Navy must resubmit an agency procurement request before proceeding with the DPI Phase III program.

Following the termination of the DPI Phase III procurement, NARDAC management decided to obtain the communication processors through other channels. According to NARDAC technical managers responsible for getting the new processors, they wanted the latest model of communication processors available. The technical managers generally regarded IBM as the industry leader for communication processors. The managers initially wanted to buy the IBM Model 3725 communication processor. The IBM Model 3725 was also used as the brand name or equal processor under the DPI Phase III program. But during March 1988, IBM began delivery of a newer communication processor, the Model 3745. After deliveries began, NARDAC, with the help of IBM representatives, took steps to get the IBM Model 3745.

IBM Assistance. NARDAC technical managers relied on their IBM representatives to help them determine what was needed to replace the Amdahl Model 4705's with IBM Model 3745 communication processors. IBM provided NARDAC with a detailed list of equipment, software, and IBM product numbers that would be needed to make the processor work. The NARDAC technical manager who initiated the request told us that he relied heavily upon the IBM representative because he did not fully understand what the IBM items did or why they were needed.

NARDAC's technical manager copied IBM's product list onto a proposed statement of work. This statement of work was then attached to a NARDAC Information System Project Action Approval Request Form. Technical staff members prepare this form to begin an ADP acquisition.

When we asked NARDAC's technical managers whether communication processors manufactured by vendors other than IBM could also meet NARDAC's requirements, we were told that only the IBM Model 3745 could satisfy NARDAC's technical requirements. This was mainly due to the fact that, at the time of the procurement, only the IBM Model 3745 could operate IBM's latest software (Network Control Program version 5), which NARDAC considered necessary to meet its future customer needs. The technical managers told us that they decided to purchase IBM after they analyzed industry documentation and literature for three vendors' products: IBM, Amdahl, and NCR Comten. Amdahl and NCR Comten are the only vendors that make communication processors comparable to the IBM Model 3745. Both Amdahl and NCR Comten told us that they were not contacted about the procurement and were not aware that the procurement was being made. At the time of the procurement, NARDAC managers had little documentation for their contention that only an IBM Model 3745 could support NARDAC's requirements.

We believe that NARDAC showed favoritism during this procurement by discussing the procurement only with IBM. The FAR 3.101 requires that Government business be conducted in a manner above reproach, with complete impartiality, and with preferential treatment for none. However, we do not believe that NARDAC has shown a systematic bias in favor of IBM. To the contrary, at the time of the procurement, IBM made up only eight percent of NARDAC's processing power. Amdahl Corporation and National Advanced Systems made up 56 percent and 36 percent, respectively. Nevertheless, we believe the procurement gives the appearance of bias in IBM's favor because the two other competing vendors were not given the opportunity to discuss their solutions to NARDAC's technical requirements.

Mislabeled Procurement. The FAR subpart 6.5 and NAVDAC Instruction 5231.1, "Competition Advocacy Program," require that the Competition Advocate challenge barriers to competition, including unnecessarily restrictive statements of need. However, at the time of the procurement, NAVDAC required that its Competition Advocate review only acquisitions labeled as sole-source. Although the statement of work for the procurement of the communication processor specified an IBM model, the Information System Project Action Approval Request Form inappropriately indicated that the procurement was competitive. Therefore, the NARDAC Competition Advocate did not review the procurement, and the necessary approval process for a sole-source procurement was bypassed.

NAVDAC instructions required signature approvals from the technical managers and the NARDAC Commanding Officer. The technical managers and the Commanding Officer of NARDAC approved the request on the day it was submitted, July 18, 1988.

The technical manager who prepared the request form told us that he labeled the acquisition as competitive because he mistakenly believed that the World Computer Systems contract, which was to be used to procure the ADPE, had been awarded competitively. The contracting officer considered the acquisition to be competitive because he intended to direct World Computer Systems to ask for bids from IBM and its dealers. He believed that since World Computer Systems would get multiple bids, the acquisition would meet the requirements for competition. However, the FIRMR, section 201-2.001, states that a procurement that specifies make and model specifications is considered sole-source, regardless of whether there is adequate price competition. In our opinion, the contracting officer either lacked the training necessary to be a contracting officer for ADP resources or used very poor judgment in approving the acquisition as competitive. Likewise, we believe that the Commanding Officer of NARDAC used poor judgment in approving World Computer Systems to make the procurement. Our concerns are discussed in greater detail in Finding C, "Review and Oversight of Procurement."

One of our prior audit reports, "Defense Logistics Agency Contracts for Data Processing Equipment and Services" (Report 85-113, September 5, 1985), showed that competitive acquisitions can result in cost savings. The audit analyzed prices paid for the same items under four contracting methods (commercial, GSA Schedule, sole-source, and competitive). The analysis showed that competitive acquisitions can cost as much as 42 percent less than sole-source acquisitions.

Contracting Method. Before the NARDAC technical manager requested the communication processors, NARDAC's technical managers and the former head of NARDAC's Contracts Department met to discuss the procurement. The NARDAC contracting officer told us that after the meeting, he was directed by the former head of the Contracts Department to use World Computer Systems to conduct the procurement. This was because the technical managers believed that World Computer Systems could buy the equipment faster than the Naval Regional Contracting Center (NRCC), Washington. The NRCC is responsible for procuring NARDAC's ADP equipment, supplies, and services costing under \$10 million. One NARDAC official told us that some procurements through the NRCC had taken up to 18 months to complete. According to an NRCC memorandum of January 4, 1988, a minimum lead time of 210 days is required for the NRCC to award a negotiated or sealed bid contract costing more than \$100,000.

Purchase of Processors by World Computer Systems. Representatives from World Computer Systems were confused when they received NARDAC's delivery order to buy the processors competitively. The contract statement of work stated, "The ADPE . . . must be competitively acquired. Documentation to support the fact that competition was conducted . . . is required."

Yet World Computer Systems' staff concluded that only the IBM Model 3745 could meet the NARDAC specifications. Accordingly, competition could not be obtained. On August 23, 1988, the Director of Contracts for World Computer Systems wrote to the NARDAC contracting officer:

In regard to obtaining competition for this requirement, WCSSA [World Computer Systems Services Associates] reviewed the requirements of NARDAC, when competing this requirement WCSSA discovered that currently only the IBM 3745 system meets all of those requirements.

In a letter dated August 29, 1988, the head of NARDAC's Contracts Department responded, stating:

World Computer Systems has misinterpreted the request for competition. NARDAC Washington was not requiring World Computer Systems to seek alternate systems but ensure that the IBM 3745 system to be purchased is being bought at the lowest price available.

The NARDAC contracting officer then instructed World Computer Systems to get price quotes from IBM dealers to satisfy the requirement for competition. World Computer Systems followed that advice. In September 1988, World Computer Systems awarded a contract to IBM for its processors. IBM bid prices identical with its General Services Administration Multiple Award Schedule contract.

When a contractor buys materials, supplies, articles, or equipment for the Government, the contractor is not required to solicit and select sources according to the same standards and rules applicable to the Government. For example, a contractor does not have to meet the same level of competition as the Government when conducting procurements. Government agencies must follow the Competition in Contracting Act of 1984 (Public Law 98-369), which requires full and open competition, meaning that all responsible sources are permitted to submit offers and receive consideration. Agencies must advertise their procurements in the Commerce Business Daily, as required by the FAR 5.301. The Commerce Business Daily is a Government publication that summarizes the Government's solicitations. The requirements of the Competition in Contracting Act, however, do not extend to Government contractors who, instead, must follow requirements stated in the contract. Contractors are also not required to advertise their solicitations in the Commerce Business Daily. If the solicitation had been published in the Commerce Business Daily, it is our opinion that competing vendors would have protested the competitive classification and demanded the elimination of IBM bias in the procurement or demanded that the

procurement be justified as sole-source. Additionally, because the processors were bought through a contractor instead of directly by the Navy, potential offerors could not file protests with the Government. A protest is a written objection by an interested party to a solicitation or award. An interested party is an actual or potential offeror with an economic interest in the award. Procurements made directly by the Government enable a potential offeror to file a protest with:

- the procuring agency (FAR subpart 33.1),
- the General Accounting Office (U.S.C., title 31, sec. 3551),
- the General Services Board of Contract Appeals (U.S.C., title 40, sec. 759 (h)),
- the United States District Courts (U.S.C., title 5, sec. 702 and sec. 28), or
- the United States Claims Court (U.S.C., title 28, sec. 1491 (a)(1) and (3)).

Procurements made by a contractor, however, do not allow disappointed offerors to use these forums of appeal. These forums are unlikely to entertain protests because subcontractors have no contractual relationship with the Government or because a subcontractor's protest may not be within the jurisdiction of these forums.

Vendor Interest. NCR Comten learned of the NARDAC procurement shortly after the IBM communication processors had been delivered. On February 27, 1989, a senior marketing representative from NCR Comten met with the Director of the Navy's Information Resource Management Office to complain about NARDAC's procedures for buying the processors. Because of the complaint, the Commander of NAVDAC investigated the procurement. He concluded that:

- the original justification for the IBM 3745 was superficial, but some NARDAC staff members still believed that IBM processors were the only alternative; and
- true competition did not exist in the procurement.

NAVDAC took the following corrective actions:

- all NARDAC delivery orders for equipment are now to be approved by its Competition Advocate;
- all delivery orders for equipment valued at greater than \$5,000, or 10 percent of the total value of the delivery

order, are now also to be approved by the NAVDAC Competition Advocate;

- NAVDAC Instruction 5231.1, "Competition Advocacy Program," was revised to define "competition" more clearly; and

- further orders from the World Computer Systems contract were prohibited until the Naval Regional Contracting Center, Washington clearly defined the contract's scope. Because of that review, the contract was not renewed.

In addition, the current head of NARDAC's Contracts Department required all contracting personnel to attend a 2-week training class, "Defense Contracting for Information Resources Management," and is developing procurement training for NARDAC technical personnel.

The actions taken by NAVDAC and NARDAC should promote full and open competition in its ADP procurements; however, we also recommend that NAVDAC require its regional data centers to use functional specifications or other specifications in the order of precedence prescribed by the FIRMR, section 201-24.212.

RECOMMENDATION FOR CORRECTIVE ACTION

We recommend that the Commander, Naval Data Automation Command require that its regional data centers develop, where applicable, functional specifications to maximize full and open competition. If functional specifications are not appropriate, develop specifications in the order of precedence as required by the Federal Information Resource Management Regulation, section 201-24.212.

MANAGEMENT COMMENTS

The Navy concurred with our recommendation and stated that NARDAC, Washington was developing new procedures to ensure that where applicable, functional specifications are used to maximize full and open competition. Within 6 months the Naval Computer and Telecommunications Command (NCTC, NARDAC's newly-formed parent command) will direct all NARDAC's to develop similar procedures for NCTC review and approval.

The Navy believed, however, that the finding contained a misinterpretation of applicable regulations. The Navy stated that the report's discussion of "Mislabelled Procurement" assumed that a procurement under the 8(a) Program would normally be subject to review and challenge by competition advocates, and that the report further assumed that this procurement escaped such a challenge because it was mislabeled as competitive when it should have been labeled as sole-source. The Navy contended that the proper label should have been "not available for

competition." This label would have been appropriate because the contract was under the SBA's 8(a) Program, and Navy competition advocates are not expected or encouraged to scrutinize 8(a) procurements for competitive opportunities (except for contracts in excess of \$3,000,000, as delineated in FAR 19.805, effective November 30, 1989).

AUDIT RESPONSE TO MANAGEMENT COMMENTS

The competition advocate is responsible for challenging barriers to and promoting full and open competition by spotting competitive opportunities in the acquisition of supplies and services (FAR 6.502). The Brooks Act treats specific make and model specifications as noncompetitive, regardless of the number of responsible sources (U.S.C., title 40, sec. 759 (g)). No distinction is made in the Brooks Act (or in FIRMR, subsection 201-11.002, which implements this portion of the Act) between Section 8(a) and non-8(a) contractors. Accordingly, we believe that this procurement should have been labeled as a sole-source procurement, and that if it had been labeled properly, it would have been reviewed by the NARDAC Competition Advocate.

FAR 19.805, which the Navy cites, was not in effect at the time of the procurement, and is not applicable to this procurement. FAR subpart 19.8 was revised to implement sections 303(b) and 303(d) of the Business Opportunity Development Reform Act of 1988, Public Law 100-856. Section 303(b) of the Act requires that acquisitions offered for award under section 8(a) of the Small Business Act be awarded on the basis of competition restricted to eligible 8(a) Program participants if:

- there is a reasonable expectation that at least two eligible program participants will submit offers and that the award can be made at a fair market price, and

- the anticipated award price of the contract will exceed \$5,000,000 in the case of a contract opportunity assigned a standard industrial classification code for manufacturing, and \$3,000,000 in the case of all other contract opportunities.

This revision was effective on November 30, 1989, over a year after the NARDAC procurement was initiated on July 18, 1988.

The intent of the Business Development Reform Act was to promote competition between Section 8(a) firms. FAR 19.805 applies to situations where the Government is conducting its own procurement. In the procurement through World Computer Systems, the 8(a) contractor was conducting the procurement on behalf of the Government. World Computer Systems was soliciting offers from three firms that made no representation as to their Section 8(a) status. For these reasons, we do not believe that FAR 19.805, as revised, is relevant.

Management comments to the recommendation satisfy the intent of the report. Further reply to the recommendation is not required.

B. Walsh-Healey Act

FINDING

NARDAC, Washington violated the Walsh-Healey Act (the Act) (U.S.C., title 41, sec. 35(a)) when it used World Computer Systems as a broker to buy its communication processors. World Computer Systems also violated SBA regulation (Title 13, Code of Federal Regulations, Section 124.109), which precludes brokers from participating in the Section 8(a) Program. As a result, NARDAC incurred unnecessary costs of \$50,429 when it paid World Computer Systems its brokerage fee; the buy could have been made through the NRCC at no additional cost to NARDAC. NARDAC's contracting officer told us that he was unaware of the Walsh-Healey Act restrictions on using brokers.

DISCUSSION OF DETAILS

Walsh-Healey Act and SBA Regulations. The Walsh-Healey Act applies to contracts and subcontracts that exceed \$10,000 under Section 8(a) of the Small Business Act, for the manufacture or furnishing of supplies within the United States, Puerto Rico, or the Virgin Islands. The Walsh-Healey Act requires that any contract entered into by an executive agency for the manufacture or furnishing of materials, supplies, articles, and equipment in any amount exceeding \$10,000 shall include a representation that the contractor is the manufacturer of or a regular dealer in the materials, supplies, articles or equipment to be manufactured or used in the performance of the contract. The SBA regulation (Title 13, Code of Federal Regulations, Section 124.109) states that brokers are ineligible to take part in the Section 8(a) Program since brokers do not satisfy the definition of a manufacturer or regular dealer. The FAR subpart 22.6 implements the Walsh-Healey Act and gives specific definitions for both manufacturers and regular dealers:

'Manufacturer' ... means a person that owns, operates, or maintains a factory or establishment that produces on the premises the materials, supplies, articles, or equipment required under the contract and of the general character described by the specifications.

'Regular dealer' ... means a person that owns, operates, or maintains a store, warehouse, or other establishment in which the materials, supplies, articles, or equipment of the general character described by the specifications and required under the contract are bought, kept in stock, and sold to the public in the usual course of business.

For each solicitation that may be subject to the Act, the contracting officer must obtain representations from prospective contractors that they are manufacturers or regular dealers of the supplies offered (FAR 22.608-1). NARDAC's contracting officer told us that he was not aware of the Walsh-Healey Act provisions; therefore, he had not determined whether placing an order under the contract with World Computer Systems to obtain the processors would violate the Act.

World Computer Systems does not manufacture computer processors, nor does it stock and sell computer processors to the public. The company merely ordered the processors from IBM, which delivered and installed the processors in the Navy's facility. World Computer Systems incurred little risk and performed no substantive task except to order the processors from IBM. Accordingly, we believe that World Computer Systems was acting as a broker.

We have referred the violation of the SBA regulation to both the Administrator of the SBA and the SBA's Inspector General. We have referred the violations of the Walsh-Healey Act to the Department of Labor, which is responsible for enforcing the Act.

Additional Cost. The Navy unnecessarily increased its purchase costs by at least \$50,429 when it used World Computer Systems to buy the processors. The increased costs represented a brokerage fee paid to World Computer Systems for making the procurement. We calculated this additional cost by subtracting World Computer Systems' cost from NARDAC's cost:

ADDITIONAL COSTS INCURRED BY NARDAC BY
USING A BROKER TO PROCURE COMMUNICATION PROCESSORS

	<u>World Computer Systems Cost</u>	<u>NARDAC Cost</u>	<u>Additional Cost (Difference)</u>
IBM Processors	\$658,248	\$698,401	\$40,153
Software Lease	143,458	152,206	8,748
Proprietary Software Lease	12,800	14,328	1,528
IBM System Engineering	58,806	58,806	0
World Computer Systems Program Manager	<u>595</u>	<u>595</u>	<u>0</u>
Totals	<u>\$873,907</u>	<u>\$924,336</u>	<u>\$50,429</u>

This additional cost represents general and administrative expense applied as a percentage of cost to the equipment and software rather than the effort used to obtain the processors.

These costs would not have been incurred if NARDAC had used the NRCC to obtain the processors.

RECOMMENDATION FOR CORRECTIVE ACTION

We recommend that the Naval Data Automation Command inform its regional data centers that using brokers to obtain automatic data processing equipment violates the Walsh-Healey Act, as implemented by the Federal Acquisition Regulation subpart 22.6.

MANAGEMENT COMMENTS

The Navy partially concurred with our recommendation, and stated that NAVDAC (now NCTC) has issued a policy that restricts the acquisition of equipment under ADP service contracts. The Navy believed that its policy met the intent of the recommendation to ensure that ADP is not bought at unnecessarily high prices from brokers.

The Navy believed that the finding inaccurately stated that the NARDAC, Washington was guilty of violating the Walsh-Healey Act. The Navy contends that Walsh-Healey Act determinations are required before contract award, and because the Navy did not award the contract, it was not the Navy's responsibility to determine compliance with the Walsh-Healey Act. However, since the matter has been referred to the Department of Labor for review, the Navy believed that further comment on the finding would be premature.

AUDIT RESPONSE TO MANAGEMENT COMMENTS

The Navy's policy concerning the use of ADP service contracts to purchase ADP meets the intent of the recommendation. However, we still believe that the Navy violated the Walsh-Healey Act.

We agree that the awarding Agency had a responsibility, under FAR 22.602(b) and 22.608, to make a determination concerning the requirements of the Walsh-Healey Act before contract award. However, we do not believe that this omission by the USDA relieved the Navy of correcting contract deficiencies when the Navy received the contract and before the order was placed. Furthermore, the actual purchase of the supplies occurred under the Navy's contract tenure when the Navy ordered World Computer Systems to purchase equipment for which it was not a regular dealer or manufacturer. The Department of Labor, where we referred the Navy's violation, should make final determination of any violations of the Walsh-Healey Act.

C. Review and Oversight of Procurement

FINDING

NAVDAC did not adequately monitor contracting actions taken by NARDAC, Washington. This occurred because NAVDAC's General Counsel did not adequately review the basic contract or the delivery order for the communication processors. As a result, NARDAC circumvented its contracting authority limits by having a contracting officer of the Department of Agriculture contract on NARDAC's behalf. NARDAC also circumvented the requirements to justify a sole-source procurement when it mislabeled a request for specific make and model hardware as a competitive procurement. NARDAC circumvented the requirements for full and open competition when it used World Computer Systems to buy communication processors on its behalf and provided the company with restrictive specifications. NARDAC also violated the Walsh-Healey Act's restrictions on Government use of brokers to obtain supplies.

DISCUSSION OF DETAILS

Background. The FAR subpart 1.6 describes the responsibilities and the authority of a contracting officer. Contracting officers are generally responsible for ensuring performance of all necessary actions for effective contracting, ensuring compliance with the terms of the contract, and safeguarding the interests of the United States in its contractual relationships. The FAR subpart 1.6 prohibits contracting officers from entering into any contract until all requirements of law, regulations, and other applicable procedures have been met. Additionally, contracting officers are required to make sure that contractors receive impartial, fair, and equitable treatment. A contracting officer is to be appointed in writing and selected based on an assessment of the candidate's experience, training, and knowledge of acquisition policies and procedures.

NARDAC, Washington is one of five NARDAC's that has been granted contracting authority by the Assistant Secretary of the Navy (Shipbuilding and Logistics) (ASN (S&L)). NARDAC's Contracts Department has 31 civilian and 3 military employees, 4 of whom have contracting authority. Contracting authority for computer equipment, software, and related services is limited to \$100,000. Unlimited administrative contracting officer authority exists for contracts assigned to the NARDAC by the Navy's Automatic Data Processing Selection Office (ADPSO) and other contracting organizations.

During August 1986, the ASN (S&L) made a procurement management review at NARDAC, Washington. DoD Directive 5126.34, "Defense Procurement Management Review Program," requires that procurement management reviews of procurement organizations be performed

periodically. The purpose of the review was to determine whether NARDAC's Contracts Department was complying with established procurement policies and operating procedures. The reviewer examined recent delivery orders for four contracts and conducted interviews with contracting staff, legal counsel, and one contracting officer's technical representative. The resulting report contained several adverse findings on the organizational placement of the contracting office, the training of its contracting officers, its potential lack of independence because contractor staff were on-site, its relationship with NAVDAC legal counsel, and the overall quality of contracting. Because of the review, the ASN (S&L) reduced NARDAC's procurement authority to the issuance of orders under existing contracts and recommended to NAVDAC that it conduct significant procurement training and increase its review and oversight of NARDAC.

The ASN (S&L) performed a follow-up review during May 1987. The follow-up review concluded that NARDAC had fully complied with the intent of the recommendations and had significantly improved the quality of its procurement office. On April 1, 1990, the Naval Supply Systems Command took over from the ASN (S&L) as NARDAC's Head of Contracting Activity.

NARDAC Contracting Actions. NARDAC contracting officers did not fulfill their responsibilities under FAR subpart 1.6 because they:

- did not detect that obtaining the processors through World Computer Systems would violate the Walsh-Healey Act,

- did not challenge the specific make and model specification used in the request form for acquiring the processors, and

- mislabeled the sole-source contract as a competitive contract.

The contracting officer who signed the contracting action told us that he was not comfortable with approving the document, but that he felt pressure from his supervisor, the former head of the Contracts Department, to approve it. He told us that he was not aware of the Walsh-Healey Act restrictions on the use of brokers to acquire Government supplies (see Finding B). Contracting officers are given wide latitude in exercising their contracting responsibilities, but they are expected to act independently and to use good judgment. In this procurement, we do not believe that the contracting officer used good judgment.

Contracting Authority. NARDAC, in effect, circumvented the limits of its contracting authority when it asked the U.S. Department of Agriculture (USDA) to execute a contract with World Computer Systems on NARDAC's behalf. Since NARDAC's

contracting authority was limited to \$100,000, the former head of NARDAC's Contracts Department asked USDA contracting officers to let a contract for computer equipment, software, and related services to support NARDAC's newly-owned Washington Computer Center. The Washington Computer Center had been transferred effective October 1, 1987, from the USDA to NARDAC. The contract was awarded on June 6, 1988, and was transferred to NARDAC for administration 7 days later.

The contracting officer at USDA told us that the former head of NARDAC's Contracts Department asked him to award the contract because of NARDAC's limited contracting authority and because the head of the Contracts Department believed that the Navy was too slow in awarding contracts. The USDA contracting officer responded by negotiating and awarding the indefinite quantity contract to World Computer Systems through the SBA 8(a) Program. The USDA contracting officer said that he awarded the contract in good faith to help NARDAC with the operation of its computer center.

Although the contract was made to support the operation of the Washington Computer Center, NARDAC did not use it solely for that center. Of the 23 orders placed by NARDAC during the contract's 1-year life, World Computer Systems told us that only 2 were for support of the Washington Computer Center.

Because the contract was awarded by another agency and because the contract's scope was broadly defined, we believe it created an opportunity for NARDAC to circumvent its own contracting authority. The acquisition of IBM communication processors, which was not made in support of the Washington Computer Center, was valued at \$924,336, which is more than nine times NARDAC's contracting authority of \$100,000.

The circumvention of NARDAC's contracting authority occurred because NARDAC was able to rely on its successor Procurement Contracting Officer (PCO) authority granted by the ASN (S&L). Successor PCO authority enables a contracting officer to assume the responsibilities normally retained by the procurement contracting officer once the contract has been delegated to him or her. However, according to an ASN (S&L) official, the successor PCO authority was intended only for contracts awarded by the Navy's ADPSO. The successor PCO authority memorandum stated, "NARDAC, Washington may exercise successor PCO authority to the extent that this is authorized by the cognizant procuring contracting officer." Because the authorization did not specifically mention ADPSO contracts, the authority was left open to any "cognizant procuring contracting officer"; therefore, NARDAC was able to take advantage of this oversight.

USDA award of the contract for NARDAC also was not in accordance with the Articles of Agreement for the transfer of USDA's computer center to NARDAC. The Articles of Agreement were approved in September 1987 by the Assistant Secretary of the Navy for Financial Management and by the Assistant Secretary of Agriculture for Administration, and were effective on October 1, 1987. The agreement stated:

USDA will provide contract administration support to the Navy for all [WCC] contracts in effect as of October 1, 1987. A transition schedule will be developed to phase out this support with all existing contracts to be completely turned over to the Navy no later than October 1989. All new contract actions beginning on or after October 1, 1987 will be the direct responsibility of and funded by the Navy.

Based on conversations with USDA's Acting Director of the Office of Information Resources Management and the Technical Director of NARDAC, we believe that any contracts needed to support the Washington Computer Center after October 1, 1987, should have been awarded by the Navy in accordance with the Articles of Agreement. USDA awarded the contract for NARDAC in June 1988, 8 months later than specified in the agreement.

Legal Review. NAVDAC's legal counsel did not review the basic contract with World Computer Systems or adequately review the subsequent delivery order to procure the communication processors. The basic contract was not reviewed because no formal policy required externally generated contracts to be reviewed by counsel.

The contract with World Computer Systems had several procedural flaws that we believe would have been identified if NAVDAC's legal counsel had reviewed the contract before contract administration functions were exercised beginning in June 1988. An April 5, 1989, memorandum from NAVDAC's legal counsel observed:

As received, the contract did not meet definitional FAR requirements for a true contract. In particular, there was no semblance of a pricing mechanism (no rates, no ceiling, no labor categories, no man hour or cost estimates, no minimum)

Under federal acquisition principles, the World Computer arrangement comes closest to a Basic Ordering Agreement (BOA). FAR 16.703. A BOA contains (i) prescribed clauses, (ii) a statement of work as specific as practicable, and (iii) a method for

determining prices. A BOA itself is not considered a contract: each BOA order is treated as [a] contract and must be based on competition or an appropriate non-competitive justification and approval. In my view, the world [World Computer Systems] arrangement does not even meet the definition of a BOA, much less a contract, because the work statement is too broad and the pricing mechanism is missing.

The delivery order to procure the processors was dated September 15, 1988, and was reviewed and approved by an inexperienced junior attorney in NAVDAC's General Counsel office. The attorney had not been trained adequately or provided with any formal procedures for reviewing delivery orders.

Approval by NARDAC's Commanding Officer. The decision to procure the two IBM communication processors was approved by the Commanding Officer of NARDAC. The Commanding Officer's approval was the last approval required for the acquisition to be made, and the Commanding Officer had a responsibility to ensure that the acquisition was consistent with laws, regulations, and Navy policies. In our opinion, the Commanding Officer did not use good judgment in approving the procurement.

Remedial Actions. As a result of the NCR Comten complaint about the procedures used by NARDAC to buy the processors, the Director of the Navy Information Resources Management office directed the Commander of NAVDAC to perform an investigation. A report was issued to the Information Resources Management Office during May 1989. The NAVDAC Commander recommended to the Information Resources Management Office that official letters of reprimand be sent to the former Commanding Officer of NARDAC and to NAVDAC legal counsel. The NAVDAC Commander believed the NAVDAC legal counsel had not adequately supervised the staff members who had approved the delivery order. However, no personnel actions have been taken against any of the individuals who were responsible for the procurement. Also, NAVDAC did not take exception to the NARDAC Contracting Officer's approval of the procurement.

The actions taken by NARDAC's contracting officers and the subsequent approval of the actions by its Commanding Officer on this contract raise serious questions about the competency and judgment of some of NARDAC's contracting staff and the judgment of NARDAC's former Commanding Officer. Our review, however, focused only on one transaction and one contract. Therefore, we recommend that the Commander, Naval Supply Systems Command perform a more comprehensive review of NARDAC's Contracting Department. If, as a result of that review, the Commander concludes that the NARDAC contracting officers are not meeting their responsibilities under FAR subpart 1.6, we recommend that contracting authority for NARDAC, Washington be rescinded.

RECOMMENDATIONS FOR CORRECTIVE ACTION

1. We recommend that the Commander, Naval Data Automation Command:

a. establish formal policy to ensure that all transferred contracts are given a legal review before the contracts are executed, and

b. establish formal procedures for legal reviews of contracting actions.

2. We recommend that the Commander, Naval Supply Systems Command perform a comprehensive review of contracting actions taken by the Naval Regional Data Automation Center, Washington to determine whether:

a. Federal procurement regulations are being followed and all acquisitions are subject to full and open competition,

b. contracting officers have sufficient experience, training, and knowledge of acquisition policies and procedures to fulfill their responsibilities under Federal Acquisition Regulation 1.602-2, and

c. contracting actions do not exceed the dollar thresholds authorized.

3. If significant deviations from Federal procurement regulations are identified during the review (Recommendation 2.), we recommend that the Commander, Naval Supply Systems Command rescind contracting authority for the Navy Regional Data Automation Center, Washington and that all future contracting actions for NARDAC, Washington be assumed by the Naval Regional Contracting Center, Washington.

4. We recommend that the Director of the Office of Information Resources Management take appropriate disciplinary actions against those personnel responsible for approving procurement procedures used in the acquisition of the communication processors for the Naval Regional Data Automation Center, Washington.

MANAGEMENT COMMENTS

The Navy concurred with Recommendations C.1., C.2., C.3., and partially concurred with Recommendation C.4. The Navy stated that the Naval Supply Systems Command (NAVSUP), which is now the source of procurement authority for all NARDAC's, has regulations in place that require legal review of all significant contracting

actions. Additionally, the NAVSUP has clarified NARDAC, Washington's procurement authority so that only contracts from the Navy's ADPSO can be accepted for administration (Recommendation C.1.).

The NAVSUP's, Contracting Management Directorate has scheduled a review of the NARDAC, Washington for the fourth quarter of FY 1990. The review will cover areas for which NARDAC, Washington has been granted contracting authority by NAVSUP (Recommendation C.2.). Based on the results of the review of NARDAC, appropriate actions will be determined. NAVSUPINST 4200.28, "Procurement Management Review of the Navy Field Contracting System," addresses actions to be taken when performance is considered unsatisfactory, including revocation, adjustment, or suspension of contracting authority (Recommendation C.3.).

The Navy partially concurred with Recommendation C.4., stating that although it did not agree with all of the report's conclusions regarding the Navy's alleged violations, it did agree that an abuse of the procurement process occurred. Accordingly, disciplinary action had been considered and taken where appropriate.

AUDIT RESPONSE TO MANAGEMENT COMMENTS

The Navy's comments and proposed corrective actions are responsive to the report. Further reply to the final report is not required.



THE ASSISTANT SECRETARY OF THE NAVY
(Research, Development and Acquisition)
WASHINGTON, D.C. 20350-1000

19 JUL 1990

MEMORANDUM FOR THE DEPARTMENT OF DEFENSE ASSISTANT INSPECTOR
GENERAL FOR AUDITING

Subj: DRAFT REPORT ON THE AUDIT OF NAVY REGIONAL DATA AUTOMATION
CENTER, WASHINGTON, D.C., PROCUREMENT OF AUTOMATIC DATA
PROCESSING EQUIPMENT (PROJECT NO. OFE-0029) - ACTION
MEMORANDUM

I am responding to the draft audit report forwarded by TAB A
concerning the procurement of communication processors by the
Navy Regional Data Automation Center, Washington, D.C.

The Department of the Navy response is provided at TAB B.
We generally agree with the draft audit report findings and
recommendations. As outlined in the enclosed comments, the
Department has taken, or is planning to take specific actions to
ensure adequate management controls of similar procurements in
the future.

A handwritten signature in cursive script, appearing to read "G. Cann", is positioned above the printed name.

Gerald A. Cann

TAB A - DODIG Memo of 7 May 90

TAB B - DON Response to Draft Audit Report

Department of the Navy Response
to
DODIG Draft Report of May 7, 1990
on

Navy Regional Data Automation Center, Washington, D.C.
Procurement of Automatic Data Processing Equipment
Project No. OFE-0029

Finding A:

The Navy Regional Data Automation Center (NARDAC), Washington, D.C. circumvented requirements for full and open competition and showed bias toward IBM when it purchased communication processors through World Computer Systems, Inc. NARDAC circumvented the requirement for full and open competition because:

- the solicitation was mislabeled as a "competitive contract" instead of a sole-source procurement;
- internal controls to detect and prevent the mislabeled procurement were not in place;
- legal loopholes existed that do not require full and open competition when a contractor buys supplies for the Government; and
- NARDAC believed that the Section 8(a) firm could obtain the processor faster than the Naval Regional Contracting Center.

Recommendation A:

We recommend that the Commander, Naval Data Automation Command (NAVDAC) require that its regional data centers develop, where applicable, functional specifications to maximize full and open competition. If functional specifications are not appropriate, develop specifications in the order of precedence as required by Federal Information Resource Management Regulation section 201-24.212.

DON Position - Finding A: Concur

We concur in the facts set forth in this finding, but believe it contains a misstatement in its interpretation of applicable regulations. The discussion of "Mislabeled Procurement" assumes that procurements under the 8(a) program would normally be subject to review and challenge by competition advocates. It further assumes that this particular procurement escaped such challenge because it was mislabelled "competitive" when it should have been labelled "sole source". The correct label would have been "not available for competition". Competition advocates are not expected or encouraged to scrutinize 8(a) procurements for competitive opportunities (except for contracts in excess of \$3,000,000 as delineated in FAR 19.805, effective 30 Nov 89).

DON Position - Recommendation A: Concur

NARDAC Washington is already developing procedures to ensure that the use of functional specifications are used where applicable to maximize full and open competition. Naval Computer and Telecommunications Command (NCTC) will issue, within six months, direction to all NARDACs to develop similar procedures for NCTC review and approval.

Finding B:

NARDAC, Washington violated the Walsh-Healey Act when it used World Computer Systems, Inc. as a broker to buy its communication processors. NARDAC incurred unnecessary cost of \$50,429 in brokerage fees.

Recommendation B:

We recommend that the Naval Data Automation Command inform its regional data centers that using brokers to obtain automated data processing equipment violates the Walsh-Healey Act, as implemented by the Federal Acquisition Regulation subpart 22.6.

DON Position - Finding B: Do Not Concur

The report is inaccurate in stating that NARDAC, Washington is guilty of a Walsh-Healey violation, if one occurred. Walsh-Healey determinations are required before contract award and therefore before the contract was transferred to NARDAC, Washington. However, since this matter has been referred to the Department of Labor, the proper forum for resolution, further comment on the finding would be premature.

DON Position - Recommendation B: Partially Concur

NAVDAC (now NCTC) has issued policy restricting the acquisition of equipment under ADP services contracts. We believe this meets the intent of the recommendation and ensures that we do not buy our ADP at unnecessarily high prices from brokers. However, the recommendation appears to misunderstand the level of contracting authority at the other NARDACs. None of the other NARDACs has authority to enter into a contract over \$25,000. It is unlikely that they have any significant problem with Walsh-Healey compliance.

Finding C:

NAVDAC did not adequately monitor contracting actions taken by NARDAC, Washington. NAVDAC's General Counsel did not adequately review the contract or delivery order, allowing NARDAC to circumvent its contracting authority limits by using Department of Agriculture's Contracting Officer to contract on NARDAC's behalf.

DON Position - Finding C: Concur

Recommendation C-1:

We recommend that the Commander, Naval Data Automation Command:

a. establish formal policy to ensure that all transferred contracts are given a legal review before the contracts are executed, and

b. establish formal procedures for legal reviews of contracting actions.

DON Position - Recommendations C-1: Concur

Although we concur with the intent of the recommendation, NAVDAC no longer exists. The Naval Supply Systems Command (NAVSUP) is now the source of procurement authority for all NARDACs. NAVSUP has in place regulations and procedures which require legal review of all significant contracting actions. NAVSUP has also clarified NARDAC, Washington's procurement authority so that only contracts from the Navy's ADP Selection Office can be accepted for administration. Under the more structured NAVSUP procedures, abuses of the sort identified in the report will not be possible. Accordingly, additional procedures envisioned by the report are considered unnecessary.

Recommendation C-2:

We recommend that the Commander, Naval Supply Systems Command perform a comprehensive review of contracting actions taken by the Navy Regional Data Automation Center (NARDAC), Washington to determine whether:

a. Federal procurement regulations are being followed and all acquisitions are subject to full and open competition;

b. contracting officers have sufficient experience, training, and knowledge of acquisition policies and procedures to fulfill their responsibilities under FAR subsection 1.602-2; and

c. contracting actions do not exceed the dollar thresholds authorized.

DON Position - Recommendation C-2: Concur

A review of NARDAC, Washington will be conducted by personnel of the Naval Supply Systems Command (NAVSUP), Contracting Management Directorate. This review will be scheduled for the fourth quarter of fiscal year 1990. The review will focus on the areas for which NARDAC, Washington has been granted authority by NAVSUP. It is noted that the scope of contracting authority granted to NARDAC, Washington by NAVSUP is significantly less than NARDAC previously held.

Recommendation C-3:

If significant deviations from Federal procurement regulations are identified during the review (Recommendation 2), we recommend that the Commander, Naval Supply Systems Command rescind contracting authority for the Navy Regional Data Automation Center, Washington and that all future contracting actions for NARDAC Washington be assumed by the Navy Regional Contracting Center, Washington.

DON Position - Recommendation C-3: Concur

Based on the results of the NAVSUP review of NARDAC, a determination will be made in accordance with NAVSUPINST 4200.82 as to what specific action is necessary and appropriate. NAVSUPINST 4200.28, "Procurement Management Review of the Navy Field Contracting System," sets forth the procedures which NAVSUP follows when conducting reviews of contracting offices. It addresses actions to be taken when performance is considered unsatisfactory, including revocation, adjustment, or suspension of contracting authority.

Recommendation C-4:

We recommend that the Director of the Office of Information Resources Management take appropriate disciplinary actions against those personnel responsible for approving procurement procedures used in the acquisition of the communication processors for the Navy Regional Data Automation Center, Washington.

DON Position - Recommendation C-4: Partially Concur

Although we do not agree with all of the conclusions of the report regarding alleged Navy violations of law and regulation, we do agree that an abuse of the procurement process occurred. Disciplinary action has been considered and taken where appropriate.

**SUMMARY OF POTENTIAL MONETARY AND
OTHER BENEFITS RESULTING FROM AUDIT**

<u>Recommendation Reference</u>	<u>Description of Benefit</u>	<u>Amount and/or Type of Benefit</u>
A.	Compliance with the Federal Information Resources Management Regulation on computer hardware acquisitions.	Nonmonetary; improve competitiveness in computer hardware specifications.
B.	Compliance with Federal Acquisition Regulation and the Walsh-Healey Act.	Nonmonetary; ensure compliance with laws and regulations.
C.1.	Improve internal controls by requiring legal review of transferred contracts.	Nonmonetary; ensure that contracts are legally sound and comply with applicable regulations.
C.2.	Improve internal controls and help ensure compliance with Federal Acquisition Regulation.	Nonmonetary; ensure that NARDAC contracting staff fulfill their responsibilities.
C.3.	Improve internal controls and help ensure compliance with Federal Acquisition Regulation.	Nonmonetary; ensure that that NARDAC contracting staff fulfill their responsibilities.
C.4.	Provide for accountability of actions by procurement personnel.	Nonmonetary; ensure that NAVDAC and NARDAC procurement personnel fulfill their required responsibilities.

ACTIVITIES VISITED OR CONTACTED

Office of the Secretary of Defense

Comptroller of the Department of Defense,
Washington, DC

Department of the Navy

Assistant Secretary of the Navy (Research, Development and
Acquisition), Washington, DC
Office of Information Resources Management,
Washington, DC
Naval Data Automation Command, Washington, DC
Navy Regional Data Automation Center, Washington, DC
Naval Air Systems Command, Washington, DC
Naval Supply Systems Command, Arlington, VA
Naval Telecommunications Command, Washington, DC

Non-DoD Activities

Department of Agriculture, Washington, DC
House Committee on Government Operations, Washington, DC
Small Business Administration, Washington, DC

Non-Government Activities

World Computer Systems, Inc., Laurel, MD
Amdahl Corporation, Washington, DC
NCR Comten, Rockville, MD

AUDIT TEAM MEMBERS

Nancy L. Butler, Director, Financial Management Directorate
Terry L. McKinney, Program Director, Automated Systems Division
Kent E. Shaw, Project Manager
Joseph Boyce, Team Leader
Richard Hanley, Auditor
Douglas Saunders, Auditor
Susanne B. Allen, Editor

FINAL REPORT DISTRIBUTION (Continued)

Non-DoD Activities

Department of Agriculture
Department of Labor
Department of State
General Accounting Office
 Information Management and Technology Division
 NSIAD Technical Information Center
General Services Administration
Office of Management and Budget
Small Business Administration

Congressional Committees:

Senate Committee on Appropriations
Senate Subcommittee on Defense, Committee on Appropriations
Senate Committee on Armed Services
Senate Committee on the Budget
Senate Committee on Governmental Affairs
Senate Subcommittee on Oversight of Government Management,
 Committee on Governmental Affairs
House Committee on Appropriations
House Subcommittee on Defense, Committee on Appropriations
House Ranking Minority Member, Committee on Appropriations
House Committee on Armed Services
House Committee on the Budget
House Committee on Energy and Commerce
House Subcommittee on Commerce, Consumer Protection, and
 Competitiveness, Committee on Energy and Commerce
House Subcommittee on Readiness, Committee on Armed Services
House Committee on Government Operations
House Subcommittee on Legislation and National Security,
 Committee on Government Operations
House Committee on Small Business
House Subcommittee on SBA, the General Economy, and Minority
 Enterprise Development, Committee on Small Business